HEARING TO REVIEW THE STATE OF THE CROP INSURANCE INDUSTRY

HEARING

BEFORE THE

SUBCOMMITTEE ON
GENERAL FARM COMMODITIES
AND RISK MANAGEMENT

OF THE

COMMITTEE ON AGRICULTURE
HOUSE OF REPRESENTATIVES

ONE HUNDRED TENTH CONGRESS

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HEARING TO REVIEW THE STATE OF THE CROP INSURANCE INDUSTRY

TUESDAY, MAY 1, 2007

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON GENERAL FARM COMMODITIES AND RISK MANAGEMENT,
COMMITTEE ON AGRICULTURE,
Washington, D.C.

The Subcommittee met, pursuant to call, at 10:02 a.m., in Room 1300 of the Longworth House Office Building, Hon. Bob Etheridge [Chairman of the Subcommittee] presiding.

Members present: Representatives Etheridge, Scott, Marshall, Salazar, Boyda, Herseth Sandlin, Space, Pomeroy, Peterson (*ex officio*), Moran, Conaway, Neugebauer, and Goodlatte (*ex officio*).

OPENING STATEMENT OF HON. BOB ETHERIDGE, A REPRESENTATIVE IN CONGRESS FROM NORTH CAROLINA

Mr. ETHERIDGE. Thank you. The hearing of the Subcommittee on General Farm Commodities and Risk Management to review the crop insurance industry will come to order.

Today this Subcommittee continues its proud tradition of thoughtful and careful oversight of one of the key components of the farm safety net—crop insurance. The last Congress, our previous Chairman, my good friend and colleague, Jerry Moran, was diligent and aggressive in this area and I hope to follow his example. Jerry will be here a little later. I understand his flight has not arrived yet. I am going to submit my opening statement for the record, because I want to move quickly to the witnesses' testimony and to the questions of Members of this Committee. In addition, another subcommittee will be holding a hearing at 1 p.m. today and I want to give staff ample time to prepare the hearing room and hopefully catch a bite of lunch myself, in the meantime, if we have an opportunity.

With that, I will yield to the Ranking Member. I was going to yield to my good friend Jerry Moran, who is not here, but I will yield to my good friend, Mr. Neugebauer, for opening comments.

OPENING STATEMENT OF HON. RANDY NEUGEBAUER, A REPRESENTATIVE IN CONGRESS FROM TEXAS

Mr. NEUGEBAUER. Well, thank you, Chairman Etheridge, for calling this hearing. As you know, I have a tremendous amount of interest in crop insurance because I believe it is an equally important safety net for producers all across the country, and I know that many of us went on some listening sessions around the country. I have traveled my district, just recently, I had three listening sessions. I heard loud and clear from my constituents that a better Crop Insurance Program, one that gives them more coverage, is a much needed piece of the safety net as we sit down and write the next farm bill. So I look forward to hearing from our witnesses. It is good to have Dr. Collins and Administrator Gould here today. I appreciate you coming and sharing your thoughts and ideas and look forward to having a dialogue here as you present your testimony.

Mr. ETHERIDGE. Thank you very much. And before we go to our witnesses, I will ask the Chairman of the full Committee, Mr. Peterson, if he has comments he would like to make.

OPENING STATEMENT OF HON. COLLIN C. PETERSON, A REPRESENTATIVE IN CONGRESS FROM MINNESOTA

Mr. PETERSON. Thank you, Mr. Chairman. I will try to be brief here, but I want to thank you and the Ranking Member for your leadership on this and thank Dr. Collins and Administrator Gould for being with us today.

You know, when we did the crop insurance overhaul we put significant new money into this program and it has accomplished part of what we tried to do. The coverage is better and certain aspects of it are working better, but we still have not accomplished one of the things that we were trying to do back then; and that is to eliminate the need for ad hoc disaster programs. And we are, as you know, dealing with another one of them right now. And if you look at the baseline spending and the different components of the farm bill, the crop insurance part of things was a significant increase from what the baseline was in 2002, and yet we still have a big hole in this safety net.

And so you know, I agree with Mr. Neugebauer, that this is something that we have got to try to figure out how to do. There has been a proposal from the Department to look at some kind of risk management or crop insurance policy to cover this. One of the things I want to know is, we haven't, I don't think, seen the details of this or seen the scoring or how it is going to work. The sooner you can get that to us the better. I have to tell you that ever since I got to Congress, given my experience trying to put something together in this area, I am skeptical about whether this can be done with crop insurance. Given the parameters that you guys have to work with and I guess I am willing to be convinced otherwise, but generally, I have some skepticism.

And the other issue that I think we are going to have to deal with are noninsured crops, which I think cause a problem in terms of building pressure for these ad hoc disasters. Somehow or other we have got to deal with them, and it just seems like it is very slow and very hard to get new crops covered and so forth. We have got to figure out some way to streamline that process and try to broaden the coverage so that we get a majority of these crops covered somehow or other under the program.

So I look forward to your testimony and look forward to working with you, but we need that information sooner rather than later, because we are about to get started here marking things up in Subcommittee and we need to know what the different options are. So thank you, Mr. Chairman.

[The prepared statement of Mr. Peterson follows:]

Rep. Collin C. Peterson
Opening Statement
Hearing to Review the crop insurance industry
Subcommittee on General Farm Commodities and Risk Management
May 1, 2007

Thank you Mr. Chairman.

The crop insurance program is an important part of American agriculture, providing a safety net for producers when prices are low and ensuring a secure and abundant supply of food and fiber for America.

Now that commodity prices are high for most crops, government farm program outlays are low. Although this means we have less money to work with as we write the new Farm Bill, it proves that the safety net is working. That is encouraging.

As we begin to write the farm bill, hearings such as this one are important since there is always room for improvement.

One of the areas I believe we need to address is the ability to transfer Actual Production History (APH) to new land. I am concerned that the way RMA has let farmers transfer APHs to new ground has created an incentive for breaking out prairie.

Another problem I have been hearing about a lot from farmers is that with the rising price of corn and other commodities, crop insurance is driving planting decisions, rather than the market.

Finally, one of my main priorities for the 2007 Farm Bill is to include a permanent disaster assistance program. We have done eight disaster bills out of the last ten years, and it's always been an uphill battle.

A permanent disaster assistance program that is tied to crop insurance would increase participation, reduce unnecessary spending and ensure that farmers get help when they need it.

I thank the Chairman for calling this hearing, and look forward to the witnesses testimony on how we can continue to improve the crop insurance program.

Mr. ETHERIDGE. Thank you, Mr. Chairman. The Chairman requests that other Members submit their opening statements for the record so the witnesses may begin their testimony and that we ensure that they have ample time for questions.

Opening Statement of Congressman Jerry Moran
Ranking Member
Subcommittee on General Farm Commodities and Risk Management

May 1, 2007 Hearing to Review the Crop Insurance Industry.

Thank you, Mr. Chairman. The crop insurance industry represents a key component of the farm safety net for agricultural producers. While many of the programs this Committee oversees operate on a macro scale, crop insurance is tailored to a producer's specific local needs. The program helps mitigate the inherent risk that is a part of agriculture and often provides the liquidity needed to endure significant crop losses. Not only does the program protect farmers and ranchers, but it provides assurance to lenders and agriculture retailers that a crop loss will not necessarily mean default.

The crop insurance program has grown tremendously over the years. It is insuring more producers and additional types of crops, while taking on larger amounts liability. Although the crop insurance industry has experienced exceptional growth and success, issues still remain. Certain crops continue to be uncovered by crop insurance policies. In addition, problems within existing crop policies continue to affect the system. For instance, in many parts of my home state of Kansas, multi-year droughts have caused declining yields and reduced the effectiveness of the many producers' policies.

In the past, changes to the crop insurance program were made separate of the Farm Bill. While it remains to be seen whether this trend will change, the United States Department of Agriculture's (USDA) 2007 Farm Bill Proposal has certainly began the discussion of whether the 2007 Farm Bill might include a crop insurance title. I have seen USDA's initial proposal and thank them for submitting their ideas. I am sure that Dr. Collins and Administrator Gould will elaborate on some of the Administrations ideas in their testimony today.

I also look forward to hearing the perspective of those involved in actual delivery of the crop insurance policies. Much debate has arisen recently regarding the amount of underwriting gains experienced by crop insurance industry and the need to encourage additional efficiency in delivery of the policies. I hope the witnesses today can help elaborate on the difference between underwriting gains and profit and provide the Committee with information to determine how a change in the share of risk on premiums might affect the industry. I also look forward to hearing any ideas the industry may have on how to improve the current crop insurance system.

For crop insurance companies to stay engaged in the delivery of agriculture policies, there must be some level of return similar to other areas of insurance. It is the Committee's job to determine the best method of keeping crop insurance companies engaged in the industry, while responsibly using taxpayer money. I look forward to all the witnesses' testimony and hope that our discussion today can yield useful information for this Committee to utilize in the coming months.

Thank you, Mr. Chairman.

Statement of Ranking Member Bob Goodlatte
House Committee on Agriculture
Subcommittee on General Farm Commodities and Risk Management
Hearing to review the crop insurance industry
May 1, 2007

I would like to thank today's witnesses for testifying at this important hearing to discuss our nation's crop insurance program.

From our first panel of witnesses, I would like a status report on how USDA continues to administer the Agriculture Risk Protection Act of 2000. One area of specific interest to me is the 508(h) submission process. How is this provision working and what evidence do you have that demonstrates the effectiveness of this provision?

I am also interested in recent advancements in the use of data mining to detect and deter waste, fraud and abuse in this program. I would appreciate a description of the administration's proposal on data mining so that I can better understand your ideas.

The Administration has also made a number of other suggestions for consideration including the frequency of renegotiating the Standard Reinsurance Agreement with the crop insurance industry, adjustments to the Administration and Operations reimbursements levels, and other suggestions to deal with program costs. I would like you to comment on how these proposals would improve the program without causing overall harm.

I am also pleased to welcome the second panel to the Agriculture Committee. Companies and agents are the delivery mechanism of crop insurance to our farmers and ranchers. I would like to hear your concerns with the current program. Any comments you have about the Administration's proposal will also be helpful so that we can better understand how changes to the program may impact you.

Once again, I thank the witnesses for attending this hearing and I look forward to your testimony and your answers to our questions.

WORD COUNT: 267

Mr. ETHERIDGE. With that, I would like to welcome to the table Dr. Keith Collins, Chief Economist, the U.S. Department of Agriculture, and Administrator Eldon Gould, Risk Management Agency, U.S. Department of Agriculture, as well. Dr. Collins, please begin when you are ready and let me remind you there are 5 minutes for opening statements and your full statements will be submitted for the record. Dr. Collins.

STATEMENT OF KEITH COLLINS, PH.D., CHIEF ECONOMIST, U.S. DEPARTMENT OF AGRICULTURE, WASHINGTON, D.C.

Dr. COLLINS. Chairman Etheridge, Chairman Peterson and other Members of the Subcommittee, thank you very much for the invitation to come up here today and join Administrator Gould and talk about the Federal Crop Insurance Program. My brief comments here are going to reflect the perspective of the Board of Directors of the Federal Crop Insurance Corporation.

I am Chairman of the Board. The Board currently consists of nine Members, three from USDA, Under Secretary Keenum, Administrator Gould and myself, as well as six Members from the private sector: four producers, a person experienced in insurance regulation and a person experienced in the insurance industry. We are very pleased that crop insurance continues to see strong growth and excellent performance.

To reiterate a few statistics you have probably seen, insured acreage increased from 182 million acres in 1998, just before we increased buy-up premium subsidies, to 242 million acres in 2006. Insured liability last year was $50 billion; that was up 80 percent from 1998. Total premiums last year were $4.6 billion; that was up 140 percent from 1998. And with the first sales of the new pasture, range and forage products this year, and the increase in major crop prices which is raising price elections, insured acreage, liability and premiums for 2007 are all going to expand sharply above the 2006 record levels. Producers also continue to increase coverage levels, with catastrophic coverage now down to only 12 percent of insured acreage.

The program continues to have no excessive losses. Indemnities averaged only 91 percent of total premiums during 2001 to 2006. This low ratio reflects a combination of things, the fact that we have more and better data; we have made steady improvements in our ability to establish rates and use the data that we have; and we have also had no major systemic weather disasters in recent years.

A key Board responsibility is to approve new products for sale. Proposed products come to us from the private sector and they come from products developed under contracts awarded by RMA. The Agricultural Risk Protection Act of 2000, ARPA, introduced the so-called 508(h) authority that permits private individuals to submit products for approval and be reimbursed for research, development and maintenance costs if the Board approves the products. Under ARPA, 70 such products have been submitted to the Board. Forty-two have been approved. The rest were disapproved, withdrawn, returned as incomplete or illegal or remain under review.

Many of these submissions became pilot programs or improved or expanded existing pilots. RMA currently administers 28 pilot programs. After a pilot program is complete, normally 3 years, there is a year of evaluation. After evaluation it comes to the Board and the Board has to determine whether the pilot should be modified and extended, made a permanent policy or terminated. Of the pilots initiated in the late 1990s and under ARPA, the Board has acted on 26 of them. We have terminated seven, we have extended six and we have made 13 permanent.

During the past year, to give you a few examples, after a completed evaluation, the Board approved continuation of the livestock price and margin plans of insurance, with a number of changes to improve them. A new lamb price insurance pilot was also approved. An evaluation report was completed on the adjusted gross revenue pilot plan of insurance, and we are making changes in that product, plus AGR-Lite, a derivative product. The Board is also very pleased to work with RMA and its contractors to develop the pasture range and forage products, which are for sale for the first time this year. One product that the Board disapproved during the past year was a so-called good experience discount. Board Members believed the product was inequitable and not in the best interests of producers.

An issue that has been of great interest to this Subcommittee has been to find a way to help producers who experience successive years of low yields. When that happens, producers' coverage declines and their premiums increase. Last week, the Board met to consider two contracted products that were developed to address the issue of declining yields. Unfortunately, most of the expert reviews, as well as RMA and the Board itself, found many concerns. The main problems were actuarial, concerns with over-insurance and adverse selection. Both products were tabled, but the Board asked RMA to assess an alternative idea for an indexed yield plug that would replace a producer's yield in a year when it falls below a certain level.

To conclude, on behalf of all Board Members, I want to say that we consider it an honor to work with RMA and within our statutory parameters to help improve the Federal Crop Insurance Program and to work with the crop insurance companies and their agents, who do a tremendous job every day in delivering this critical part of the farm safety net to America's farmers and ranchers. Thank you.

[The prepared statement of Dr. Collins follows:]

STATEMENT OF KEITH COLLINS
CHIEF ECONOMIST, UNITED STATES DEPARTMENT OF AGRICULTURE
BEFORE THE HOUSE AGRICULTURE SUBCOMMITTEE ON
GENERAL FARM COMMODITIES AND RISK MANAGEMENT

May 1, 2007

Mr. Chairman and Members of the Subcommittee, thank you for the opportunity to join Risk Management Agency (RMA) Administrator Eldon Gould today to report on the status of the Federal crop insurance program. My comments are from the perspective of the Board of Directors (Board) of the Federal Crop Insurance Corporation (FCIC), which I chair. The Board has general management responsibility for the FCIC.

I will begin by acknowledging the outstanding efforts and accomplishments of the members of the FCIC Board. In addition to myself, current voting Board members include Mark Keenum, Under Secretary for Farm and Foreign Agricultural Services; Bill Classen; a resident of Iowa with expertise in the insurance industry; Frank Jones, a cotton and cattle producer from Texas; Tim Kelleher, a rice producer from California; Luis Monterde, a blueberry producer from Mississippi; Mike Pickens, an attorney from Arkansas with expertise in insurance regulation, and Curt Sindergard, a corn and soybean producer from Iowa. RMA Administrator Gould is Manager of the FCIC and a nonvoting member of the Board. The Board also greatly benefits from the assistance of Floyd Gaibler, Deputy Under Secretary for Farm and Foreign Agricultural Services, and Brent Doane, Secretary to the Board.

Crop Insurance Today

Crop insurance began in 1938 as a pilot program covering wheat. In 1939, there were about 7 million acres enrolled in the pilot crop insurance program. Over the next 40 years, crop insurance was primarily delivered to producers by Department of Agriculture employees through a program that grew slowly and was limited in the number of crops covered. By 1979, crop insurance was available in only about half of the nation's counties. Reliance on disaster assistance and concerns about adverse effects of crop insurance, such as moral hazard and bringing higher risk land into production, led to landmark crop insurance reform legislation in 1980. The Federal Crop Insurance Improvement Act 1980 made crop insurance delivered through the private sector the primary form of disaster assistance for producers. Subsequent legislation, the Federal Crop Insurance Reform Act of 1994 and the Agricultural Risk Protection Act of 2000 (ARPA), continued program improvements, increased premium subsidies and expanded program offerings and participation.

The performance of crop insurance under ARPA may be illustrated by comparing program data for the 2006 crop year, the most complete recent year of data, with data for 1998, the year prior to the increase in premium subsidies that began first with ad hoc disaster legislation for 1999 and 2000 and then legislated through ARPA for subsequent years (table). In 2006, there were 1.15 million Federal crop insurance policies earning premiums, slightly below the 1.24 million policies earning premiums in 1998. However, by 2006, insured liability increased to about $50 billion, nearly 80 percent higher than the $28 billion liability in 1998. Insured acres increased to 242 million in 2006, up from 182 million in 1998. Total premiums increased to $4.6 billion in 2006, up over 140 percent since 1998. The sharp increases in these indicators reflect higher participation and coverage levels caused by higher premium subsidies, a pronounced shift from yield-only coverage to revenue coverage, and higher commodity prices, which have increased revenue insurance guarantees.

Since the increase in premium subsidies under ARPA and the disaster legislation in the late 1990s, more farmers are buying coverage above the catastrophic risk protection (CAT) level. In 1998, CAT coverage accounted for 34 percent of the program's insured acreage. In 2006, only 12 percent of insured acres were covered at the CAT level. For most producers, buying policies with increased buy-up coverage is necessary to manage risks more effectively and to allow them to move away from dependence on Government ad hoc disaster assistance.

While we have seen growth in insured liability for the major row crops over the past decade, we have also seen an increase in coverage for many specialty crops. Broader specialty crop coverage has resulted from pilot programs initiated in the late 1990s, programs authorized in ARPA, and the expansion of Adjusted Gross Revenue (AGR) and AGR-Lite plans of insurance. The range of new products is illustrated by Board actions the April 2007 meeting, where a new plan of insurance for honey was approved for expert review, a plan for processing pumpkins was approved, and a pilot program for cultivated clams was modified and extended.

Insurance products that offer whole farm or revenue protection have grown sharply. For example, liability insured under the Revenue Assurance, Income Protection, and Crop Revenue Coverage plans of insurance increased from $4.8 billion, or 17 percent of total program liability, in 1998 to $23.5 billion, or 47 percent of total liability, in 2006. The whole farm plans of insurance Adjusted Gross Revenue (AGR) and AGR-Lite have risen from no liability to $351 million over the same period.

The popularity of area plans of insurance have also increased very sharply in recent years. Insured liability under the Group Risk Plan (GRP) and Group Risk Income Protection (GRIP) plans of insurance increased from $0.5 billion in 1998 to $6.8 billion in 2006—more than a 12-fold increase.

The actuarial performance of Federal crop insurance has steadily improved over the years. In the 1981-1990 crop years, the loss ratio, which is total indemnities divided by total premiums, averaged 1.53. The loss ratio for 1991-2000 declined to an average of 1.07. And for 2001-2006, the loss ratio has averaged an even lower 0.91. Over time, premium rates have increased to cover expected losses. Part of the increase in premium rates was due to the assessment of historical experience and establishment of, and movement towards, target rates by RMA to cover expected losses. The increase in premium subsidies under ARPA also increased participation, drawing more low risk producers into the program, thereby reducing adverse selection and improving actuarial performance.

Federal crop insurance is delivered to producers entirely by private insurance companies. Over time, some companies have exited the business, others have merged or been acquired, and new entrants have joined the program. The Board and RMA serve as regulators of this private sector delivery structure, which must be efficient and financially healthy if the Federal crop insurance program is to succeed. Today, RMA has a Standard Reinsurance Agreement (SRA) with the 16 companies that constitute the public-private partnership for the delivery of Federal crop insurance. The SRA defines the risk sharing agreement between the government and the companies that is crucial to the efficient operation of the program. By being able to share in the underwriting gains, companies have an incentive to participate in the program and expand sales, and by sharing in the losses, they have an incentive to ensure policies are properly underwritten and loss adjusted.

The SRA also establishes the reimbursement to the companies for administrative and operating (A&O) expenses in accordance with the provisions of the Federal Crop Insurance Act (Act). For the 2006 reinsurance year, the rate at which we reimburse the companies' A&O costs has changed compared with earlier years. In 2000, the average reimbursement rate was 25.7

percent of net premium. In 2005, the average was 21.8 percent of net premium, and for the 2006-crop year, the average reimbursement is 20.7 percent.

For the 2006 insurance year, A&O reimbursements are estimated at $958 million, up from $443 million in 1998. Despite the decline in the A&O reimbursement percentage, the total dollar reimbursement is up because of the increase in premium per policy, primarily due to higher average coverage levels, greater purchase of revenue insurance, and RMA rate adjustments. Premium per policy has increased from $1,510 in 1998 to $3,989 in 2006. Underwriting gains for the companies are up as well, rising from $280 million in 1998 to $890 million estimated for 2006. The total delivery cost, A&O plus underwriting gains, have increased from about $0.72 billion in 1998 to $1.85 billion in 2006. The combined increases in A&O and underwriting gains have helped improve the financial performance of the companies since 2002, when the largest company became insolvent. The improved financial picture has also encouraged new entrants into the program.

Board Activities and Priorities

Management of the FCIC is vested in its Board of Directors, subject to the general supervision of the Secretary of Agriculture. Board members take actions necessary to protect the interests of producers, improve the actuarial soundness of the program, and apply program provisions to all companies and insured producers in a fair and consistent manner.

In the mid 1990s, when companies introduced new products, such as revenue products, they shouldered the research and development costs, and their products were immediately adopted by their competitors without compensation. ARPA provided that private entities may be reimbursed for research and development and maintenance costs for four years, if the product is submitted under section 508(h) of the Act (508(h) products) and approved by the Board for use in the Federal crop insurance program. Including our most recent meeting in April 2007, seventy 508(h) products have been submitted to the Board since mid 2000 when ARPA was enacted. Of that total, 42 have been approved by the Board, 6 have been disapproved or a notice of intent to disapprove has been issued, 13 were withdrawn by the submitter, three were returned or deemed incomplete or illegal, and 6 are in review. Approved 508(h) products range from a Livestock Risk Protection program for lambs to AGR-Lite.

The Board carries out its business through public meetings held 8-10 times per year and other working sessions among its members and has executed a detailed division of responsibilities between itself and RMA. With respect to those functions delegated to RMA, the Board regularly reviews RMA's performance. The Board also establishes the priority for RMA efforts to improve the operation of Federal crop insurance.

A continuing priority of the Board has been to work with RMA to deal with a large backlog of pilot programs. Because pilot programs are new programs, they must be continually monitored to ensure acceptable performance, and if they are not, immediate corrections must be made. Pilots generally are designed for 3 years and then must be evaluated. Based on the evaluation, the Board determines whether each pilot is then modified and continued, approved for permanent programs, or terminated. Many of these programs were initiated in the late 1990s to address perceived areas of insufficient insurance coverage, or they were authorized by ARPA. RMA currently administers 28 pilot programs for the 2007 crop year. Of the pilots initiated in the late 1990s or under ARPA, the Board has voted to terminate 7 programs, three were terminated and replaced by other pilots, 6 have been extended to gain more experience, 13 have been approved for conversion to permanent status, and 5 pilot programs are slated for evaluation during 2007-2008.

Generally, the process of going from an idea to a permanent program takes many years for an FCIC-originated product. As a result of the limitations on RMA to conduct research and development contained in the Act, the process includes a contracted feasibility study, a contracted policy development study, 3 or more years of piloting the program, a contracted evaluation study, and conversion to a permanent policy through notice and comment rulemaking.

In deciding the fate of a pilot program, as for any decision the Board makes, the Board considers whether its actions are in the interests of producers and the crop insurance program, whether such action can be implemented in an actuarially sound manner, and whether program integrity will be protected. An example of the difficulty of establishing an effective pilot program is the Florida Fruit Tree Program. The Board voted to implement numerous program improvements for 2006 for the then-existing pilot program, which was not working well for Florida citrus producers. The changes included an occurrence loss option and an option for comprehensive tree value, which covers the lost asset value of destroyed trees. While the policy also provided coverage for losses due to Asiatic Citrus Canker (ACC), indemnification was predicated on an eradication order and the destruction of the trees by the State, which was required if ACC was discovered.

However, following 2005's hurricanes, the spreading of ACC changed the assessment of expected losses on which the premium rate structure of the policy was calculated. In addition, the State' policy of requiring the destruction of the trees changed, and we found it necessary to modify the policy again. The Board met with ACC experts, and RMA worked closely with other USDA agencies to monitor the changing approach to controlling ACC in the state of Florida. Because of the difficulty in rating the plan of insurance and the vulnerability that placed on the FCIC, as well as the likelihood that an unacceptable administrative burden would be placed on the companies, the Board voted to remove ACC coverage for the 2008 and succeeding crop years in the Florida Fruit Tree Pilot Insurance Program.

Another issue of concern to the Board is implementation and maintenance cost for insurance products that do not sell well and thus offer limited benefits to the producer. The Board has requested additional information on potential sales and costs from submitters before considering a product for approval and from RMA before taking action on pilot program evaluation. The Board considers whether the product could be better structured to meet the needs of producers and improve marketability and looks closely at the program's research and development costs, maintenance costs, and administrative complexity. High costs to USDA and the companies, which include information technology costs, agent training costs, sales barriers such as product complexity, and loss adjustment costs relative to policies sold, have been factors in the Board's determination of whether approval is in the best interest of producers. When rejecting a product or terminating a pilot program, the Board also considers the availability of alternative risk management tools for producers, including products such as AGR and AGR-Lite, which cover all of the farm's income from production.

During the past year, an evaluation report was completed on AGR that identified a number of potential changes that improve its effectiveness and marketability. The Board would like to continue to improve AGR and AGR-Lite so these products may serve the large number of crop-specific programs that generate low levels of sales. RMA is now assessing how the evaluation report recommendations, as well as recommendations from the companies, may be implemented to improve product performance. The Board has already reduced the number of commodities required to be produced in order to be eligible for higher coverage levels and discontinued the 75 percent coverage level/65 percent payment rate option for these whole-farm revenue policies. In addition a study has been completed on the premium rating of these policies which appear high in some cases, and we expect to implement adjusted rates as a result. The Board also desires to combine AGR and AGR-Lite over time into one insurance plan.

There are other areas where product simplification is proceeding. For example, the Board worked with RMA to develop a proposed rule combining the many existing APH and all individual revenue insurance plans for major crops into one consolidated plan of insurance. The producer will be able to choose a yield-based or revenue-based product from the options in the combined policy according to individual needs. This combined policy is expected to be available, in conjunction with development of a new software system, for the 2009 crop.

Lack of livestock insurance products has historically been a key gap in insurance coverage. ARPA authorized pilot programs to evaluate effectiveness of risk management tools for livestock producers with an annual spending limit of $20 million. The first livestock pilot was offered in 2003 for swine in Iowa. We now have Livestock Risk Protection (LRP), which covers hog, fed cattle, and feeder cattle prices, and Livestock Gross Margin (LGM), which has covers the margin between hog prices and feed costs and was extended to fed and feeder cattle in 2006. In the 2006 crop year, these programs insured around $190 million in livestock. Both programs had very low loss ratios.

During the past year, an evaluation report was completed on the livestock price plans of insurance. The report offers many recommendations to improve the attractiveness and effectiveness of these products, ranging from permitting higher coverage levels to eliminating the prohibition on offsetting trades to moving the sales window to earlier in the day to instituting a major agent training and producer educational effort. The Board authorized RMA to develop a plan to implement the recommendations were merited. On April 27, 2007, RMA announced a number of changes effective July 2007 for LRP and LGM, which should improve their effectiveness and marketability.

For the 2007 reinsurance year, the Board also approved an LRP pilot program for lamb. This product insures a lamb price. This new product was a new challenge for the Board. The product uses econometric modeling as the basis for establishing the insurance guarantee, the first such product for FCIC. Approval of this pilot came about only after exhaustive meetings and studies to evaluate using a model's projected price to determine an insurance guarantee for those commodities for which there are no established markets to permit price discovery. If the pilot proves successful, this method could be extended to other products for which an established commodity market does not exist.

In April 2007, the Board also approved for expert review two alternative milk revenue-type plans of insurance. If ultimately approved for sale, these would be the first milk insurance plans offered by FCIC.

In August 2006, RMA announced the availability of the Pasture, Rangeland, Forage insurance products for pasture and rangeland. Addressing the needs of livestock producers has been a top priority for the Board. There are over 400 million acres of rangeland, 120 million acres of pasture, and 62 million acres of hay in the United States. However, pasture, rangeland and forage situations are so diverse across the country, so existing insurance products were limited in their usefulness because they were based on an individual's forage production or on NASS estimates of hay production. The Board culminated a several year process of development by approving two pasture, range, and forage pilot programs that are being offered for sale for the first time for the 2007 crops. The new insurance products are area based products that trigger indemnities based on indexes. One index is based on accumulated rainfall and the other is based on a temperature-adjusted measure of vegetation obtained from the National Oceanographic and Atmospheric Administration. Both products will use new technology to help solve the problem of the inability to directly measure forage production across the diverse range and pasture settings on U.S. farms and ranches. Each pilot program is offered in six states.

The Board has spent much time trying to implement a premium discount for producers. The controversy over Premium Reduction Plans led the Board to investigate the possibility of providing an experience-based discount for producers. A final submission for an experience-based discount, developed under contract, was presented to the Board last fall. The proposal called for discounts based on a producer's loss ratio compared with the loss ratio of other producers in the county. The Board believed that this proposal would have led to many inequities and was not in the best interests of producers. For example, producers with high loss ratios operating in a high loss ratio county may receive discounts, while producers with lower loss ratios in lower loss ratio counties may not. Also, it would have been possible that producers with poorer yield experiences than other producers in a county to receive discounts because their loss ratios were lower, not due to a better yield experience, but because they purchased lower coverage levels. In early 2007 the Board voted not to approve this experience-based discount proposal after expert review and much analysis by the RMA and the Board.

One of the goals of producer discounts is to provide producers with premium costs that better reflect their individual risks. The Board closely follows RMA premium rate adjustments, and RMA has extensive efforts underway to improve ratings and risk classification. The improvement in the program's loss ratio over time partly reflects a continuing effort to implement more actuarially sound premium rates. In addition, during the past year, the Board approved a new method to determine unit discounts. RMA is also updating rating models and improving reference yields. Collectively, these most recent efforts will further improve risk classification and align premium rates more closely with an individual grower's risk of loss. As these adjustments are implemented, they will obviate the need for, and benefits of, more ad hoc adjustments such as the experience-based discount that the Board rejected.

The Board has an ongoing effort to address the effects of successive years of declining yields on producers' abilities to buy sufficient insurance coverage. When such yield losses occur, producers' coverage declines and premium rates increase. Two separate development contracts were completed and sent for expert review during early 2007. One contract developed an indexed yield approach for corn, cotton, soybeans, and wheat. Another contract developed alternatives to the current APH yield methods that limit the amount yields may drop. At its April 2007 meeting, the Board tabled both products and asked RMA to assess the feasibility of a hybrid approach using concepts from each of the contracted studies and report back to the Board.

Conclusion

Federal crop insurance has advanced much in recent years. It has not, as hoped, prevented calls for ad hoc disaster assistance, and it may not have generated the volume of new product submissions from the private sector envisioned at the inception of ARPA. But, we have seen steadily more effective risk management tools become available to producers and improvement in the actuarial performance of the program. As the 2007 farm bill comes into focus, one certainty will be the continuing need to improve and make available more cost-effective risk management tools such as crop insurance. The FCIC Board will continue to diligently examine, encourage, and demand improvements in insurance products that are in the interest of producers, that are actuarially appropriate, and that protect the interests of the American taxpayer. That completes my comments.

Table--Changes in Federal Crop Insurance Program Indicators, pre and post ARPA

Item	1998	2006 Estimated
No. of policies (Mil.)	1.243	1.147
Insured liability (Bil. $)	27.9	49.9
Liability per policy ($)	22,469	43,490
Acres enrolled (Mil.)	181.8	242.1
Acres in CAT (Mil.)	61.5	28.5
Acres in buy-up (Mil.)	120.3	213.6
Loss ratio 1/	0.89	0.75
Producer loss ratio 2/	1.80	1.80
Indemnities paid (Bil. $)	1.678	3.415
Total premium (Bil. $)	1.876	4.577
Producer paid premiums (Bil. $)	0.930	1.897
Premium subsidies (Bil. $)	0.946	2.680
Premium subsidy rate for 55% coverage on an APH policy (%)	46.1	64
Premium per policy ($)	1,510	3,989
Administrative and operating expense reimbursement to AIPs (Bil. $)	0.443	0.958
Underwriting gains of AIPs (Bil. $)	0.280	0.890
Program cost (Bil. $) 3/	1.471	3.366

ARPA=Agricultural Risk Protection Act of 2000
CAT= catastrophic coverage
AIP=approved insurance provider (reinsured companies)
1/ Indemnities divided by total premiums
2/ Indemnities divided by producer paid premiums
3/ Total indemnities minus producer paid premiums plus administrative and operating expense reimbursement plus underwriting gains of AIPs (excludes RMA salaries and expenses)

Mr. ETHERIDGE. Thank you, sir. Administrator Gould?

STATEMENT OF ELDON GOULD, ADMINISTRATOR, RISK MANAGEMENT AGENCY, U.S. DEPARTMENT OF AGRICULTURE, WASHINGTON, D.C.

Mr. GOULD. Mr. Chairman, Congressman Peterson and Members of the Subcommittee, I am Eldon Gould, Administrator of the Risk Management Agency. I am a life-long farmer from northern Illinois, with a 1,500 acre corn, soybean and wheat farm and a 700 sow farrow-to-wean hog operation. I am here today to report on the progress and the challenges of the Federal Crop Insurance Program.

Under the auspices of the Federal Crop Insurance Corporation Board of Directors and its Chairman, Dr. Keith Collins, the Federal Crop Insurance Program has experienced extraordinary growth in the last quarter century. In 2006, RMA provided $49.9 billion of protection to farmers, covering nearly 80 percent of the major crops. This coverage was offered through 1.1 million policies, insuring about 242 million acres. For 2007, we estimate we will reach $65 billion in protection for American agriculture.

To continue to offer this important protection, we must modernize the tools we use to administer the program. For example, RMA must update its information technology systems. Our current outdated IT business systems are at the end of their expected lifecycle. We now use 120 databases to gather and store information. As a result, comparisons across multiple crop years that are useful in detecting unusual patterns of activity cannot be made without expensive and separate data manipulation that exceeds the technical and funding capacity of the agency. In a re-proposal of last year's request, we have asked for help from insurance providers for the development and maintenance of a new IT system. The companies would be assessed a fee based on ½¢ per dollar of premium.

We also propose to expand the use of mandatory ARPA research and development funding for data mining and data warehousing activities required by ARPA, and to continue the testing and development of a comprehensive information management system known as CIMS. CIMS allows RMA and the Farm Service Agency to standardize our common business elements, reporting requirements, producer identification and acreage reporting, as required by the 2002 Farm Bill. The first stage of CIMS is operating internally as a proof-of-concept project. When fully operational, it will provide RMA, FSA and reinsurance companies secure electronic access to information and identify discrepancies between RMA and FSA data.

RMA's program compliance function workload has increased substantially over the years since the implementation of ARPA and the subsequent expansion of the program. RMA is now emphasizing preemption through better quality control and assurance. Efforts such as data mining, remote sensing, geospatial information technologies and other computer-based resources are heavily reliant on information technology and they emphasize our urgent need to update our IT systems. We have preempted millions of dollars worth of expected payments through the expanded use of data mining, which allows us to search out unusual patterns and with the assistance of FSA offices, conduct growing season spot checks. We are constantly identifying ways to balance competing needs to make our products fraud proof, while seeking to provide responsive, useful risk protection to farmers. We still have work to do and improvements to make, but we are making good progress in our fight against program abuse.

In his 2007 Farm Bill proposals, Secretary Johanns offered several ideas to strengthen the Federal Crop Insurance Program. One proposal that has generated a great deal of interest is the idea of a supplemental deductible coverage. We are proposing literal gap coverage that a producer can buy to cover 100 percent of their deductible losses under the Crop Insurance Program. This approach would help to address the gap and safety net to cover crop losses that are less than the size of the deductible. The growth and effectiveness of the Crop Insurance Program is dependent upon a reliable delivery system, insurance products that meet the needs of producers, and an adequate IT investment strategy.

Again, I think you for the opportunity to participate in this important hearing and I look forward to responding to your questions.

[The prepared statement of Mr. Gould follows:]

Statement by Eldon Gould
Administrator
Risk Management Agency
United States Department of Agriculture
Before the House Agriculture Subcommittee on
General Farm Commodities and Risk Management
Tuesday, May 1, 2007

Mr. Chairman and members of the Subcommittee, I am Eldon Gould, Administrator of the Risk Management Agency (RMA). I am a life-long farmer in northern Illinois, with a 1,500 acre corn, soybeans and wheat farm and a 700 sow farrow-to-wean hog operation.

My role here today is to report on the progress and challenges of the Federal crop insurance program and, in particular, to provide an update on our successes and challenges in implementing the Agricultural Risk Protection Act of 2000 (ARPA). In fulfillment of the mandates of ARPA, and under the direction of the Federal Crop Insurance Corporation (FCIC) Board of Directors (Board), with its Chairman, Dr. Keith Collins, the Risk Management Agency continues to fulfill the mandates of ARPA by bringing new and innovative insurance products to the agricultural community. We work daily to validate the utility of current insurance products, to ensure outreach to small and limited resource farmers, to promote equity in risk sharing and to guard against fraud, waste and abuse within the program.

Secretary Johanns asked me to administer the crop insurance program in a timely and farmer-friendly manner. True cooperation between the Federal government and our approved insurance providers (AIP) is necessary to meet our common goals of providing effective insurance products, processing timely and accurate claims for producers when losses occur and identifying and eliminating fraud, waste and abuse in the program to the greatest extent possible.

Effective outreach to our stakeholders and customers is also necessary to identify attributes of the program that are working well and the aspects that need to be changed to improve efficiency and effectiveness. Administration of the crop insurance program requires all interested parties working together to identify viable insurance products and solutions that meet the needs of the agricultural community and follow legislative guidelines. Moreover, if the program is to continue to be successful, the checks and balances necessary to guard against the risks of fraud, waste and abuse need strengthening. Our dual roles of regulator and reinsurer make this cooperation the path to excellence.

The Standard Reinsurance Agreement (SRA) included key changes for the 2005 and subsequent reinsurance years. These entailed a lowering of the percentage rate of administrative and operating (A&O) expense reimbursement and a rebalancing of risk sharing between the government and AIP's. In addition, RMA enhanced the reporting and monitoring of AIP's and their affiliates with respect to financial solvency and program integrity. To complement that enhancement, RMA has strengthened formal ties with state insurance regulators and the National Association of Insurance Commissioners.

We now have 16 AIP's selling and servicing crop insurance. Most companies have requested authorization to increase the amount of premium they write and the number of states they intend to serve.

For the 2006 insurance year, A&O reimbursements are estimated at $958 million, up from $552 million in 2000. Despite the decline in the A&O reimbursement percentage, the total dollar reimbursement is up because of the increase in premium per policy, primarily due to higher average coverage levels, greater purchase of revenue insurance, and RMA rate adjustments. Underwriting gains for the companies are up as well, rising from $282 million in 2000 to $890 million estimated for 2006. The combined increases in A&O and underwriting gains have helped improve the financial performance of the companies and encouraged new entrants into the program.

The Federal crop insurance program has experienced extraordinary growth in the last quarter century. Through the private sector delivery system in crop year 2006, RMA provided $49.9 billion of protection to farmers on approximately 360 commodities, covering nearly 80 percent of major crops for which we can determine total eligible acres within the United States. This coverage was offered through 21 plans of insurance and approximately 1.1 million policies insuring about 242 million acres. In 2005, crop insurance provided approximately $2.4 billion in indemnity payments to farmers and ranchers. For 2006, indemnity payments totaled approximately $3.4 billion. We estimate that in 2007, we will reach $65 billion in protection for American agriculture.

Attached to my testimony are several charts that provide further background and highlight the growth of the Federal crop insurance program under ARPA.

Since the enactment of ARPA, RMA has aggressively expanded availability of existing crop insurance programs to producers. Sixty-two proposals have been submitted to the Board under Section 508(h) of the Federal Crop Insurance Act (Act) since mid 2000 when ARPA was enacted. Of that total, the Board has approved 34 and disapproved eight. The submitter withdrew thirteen, four were returned or deemed incomplete, and one was tabled pending further action. RMA has 24 active pilot programs in various stages of development.

Having reviewed priorities and schedules for product development RMA has determined that, barring any significant unforeseen hurdles, within the next five years a risk management product will be available to potentially cover approximately 98 percent of the commercial value of U.S. crops. That is not to say that the task of having effective and useful products will be complete. We continue to look for ways to make traditional APH products more effective and useful for producers, and this year we have added a livestock product, LRP Lamb, as well as Pasture, Rangeland, Forage insurance to address other needs identified by ARPA. We will manage these products to maturity and continue to search for new ways to improve the ability of farmers and ranchers to manage risk.

Now I would like to provide an update to the Subcommittee on the following key issues.

RMA Program Issues

- **Information Technology**
- **Program Integrity**
- **Conflict of Interest**
- **Pasture, Rangeland, Forage and Hay Initiatives**
- **Cooperative Discount Issue**
- **Premium Reduction Plans**
- **Combination Policy**
- **Growth of Corn Price due to Ethanol Production**

Information Technology (IT)
In order for RMA to successfully operate the multi-billion dollar Federal crop insurance program, while controlling fraud, waste, and abuse, it is prudent and necessary to have a current and reliable operating system to deliver the crop insurance program. The system's last major overhaul occurred about 12 years ago.

The current IT business systems are based on outdated system architectures and are at the end of their expected life cycle. This includes the use of data structures that do not provide the ability to readily obtain consistent information and analysis from the 120 databases in use at RMA. As a result, comparisons across multiple crop years that are useful in detecting unusual patterns of activity cannot be made without expensive and separate data manipulation that exceeds the technical and funding capacity of the Agency. In addition, the data warehouse which consolidates the information from all of these databases and is used to support the data mining efforts is at the end of its useful life and must be replaced.

The 2008 Budget includes two proposals that will facilitate funding of our IT needs.

The first is a reproposal of last year's request, which required insurance providers to share in the cost to develop and maintain a new IT system. Insurance providers would be assessed a fee based on one-half cent per dollar of premium sold. The fee is estimated to generate an amount not to exceed $15 million annually. After the new IT system has been developed, the assessment would be shifted to maintenance and would be expected to reduce the annual appropriation of the salaries and expenses account of RMA.

The second would expand the uses of mandatory ARPA research and development funding for datamining and data warehousing activities required by ARPA, and the testing and development of the Comprehensive Information Management System (CIMS).

ARPA provided RMA with mandatory funding to implement data mining and data warehousing to improve compliance and program integrity for years 2001-2005. At the close of FY 2005, these mandatory funds were depleted and Congress appropriated discretionary funding for this purpose for FY 2006. These activities allow RMA to effectively detect fraud, waste, and abuse in the crop insurance program.

Similarly CIMS was fully funded through 2007 by the 2002 Farm Bill. Specifically, CIMS is a requirement of section 10706 of the Farm Security and Rural Investment Act of 2002. The first stage of CIMS, a proof of concept project, is operating and provides a centralized source of RMA and Farm Service Agency (FSA) information. Developed applications provide RMA, FSA, and reinsured companies' electronic access to approved CIMS information. The CIMS project is completing recommendations to standardize RMA and FSA common business elements, reporting requirements and program dates to the extent practical for producer identification and acreage reporting. CIMS identifies potential discrepancies between RMA and FSA data. This early detection will reduce fraud, waste, and abuse within the various USDA programs. Under section 10706, all current information of RMA and FSA is to be combined, reconciled, redefined, and reformatted in such a manner so that the agencies can use the information management system. It was the sense of Congress that CIMS would lay valuable groundwork for further modernization of information technology systems of USDA agencies in the future. This will lead to the one stop reporting of common producer and acreage information, which will reduce the reporting burdens on farmers, ranchers, and producers, RMA, FSA, and approved insurance providers with the delivery of USDA programs.

Program Integrity

RMA's Compliance function workload increased substantially due to the expansion of the Federal crop insurance program and the implementation of ARPA. In order to address the increases, RMA is emphasizing preemption through better quality control and assurance, while still aggressively pursuing program abuse by assisting USDA's Office of Inspector General and the Department of Justice. Improvements in quality controls and investigations continue to be assisted by new and better technology, specifically the use of data mining, remote sensing, geospatial information technologies and other computer-based resources.

The most recent renegotiation of the SRA resulted in changes in the way RMA ensures program compliance. The SRA directs insurance providers to expend more resources on quality assurance and internal controls than ever before. The SRA also recognizes that insurance providers have improved internal control processes in response to new Federal financial reporting requirements. The SRA permits the insurance providers to document and receive credit for their efforts rather than complying with a separate set of assurance mandates.

In conjunction with the new insurance provider quality control requirements, RMA Compliance has revised its work plans to reflect a more balanced approach between quality assurance and investigating program abuses. In a time of declining resources and increased responsibilities, effective internal controls provide a significant cost-benefit compared to identifying and prosecuting program abuse alone. RMA is currently reviewing company operations and internal controls to determine if their efforts actually address crop insurance program vulnerability concerns.

RMA Compliance personnel completed the second year of structured random policy reviews in 2006, and will soon begin the third round in the three-year cycle of reviewing participating insurance providers. Compliance completes the random reviews, in conjunction with an assessment of each insurance provider's operational compliance, and uses the information to establish a program error rate under the Improper Payments Information Act of 2002.

RMA is making significant progress in preempting fraud, waste and abuse through the expanded use of data mining. We have preempted millions of dollars' worth of expected payments and RMA continues to identify ways to reduce program abuse. RMA continues to use data mining to identify anomalous producer, adjuster, and agent program results and, with the assistance of FSA offices, conducts growing season spot checks to ensure that new claims for losses are legitimate. These spot checks based on data mining have resulted in a significant reduction in anomalous claims for certain situations. Specifically, reduced indemnities on spot-checked policies were approximately $112 million in 2002, $82 million for 2003, $71 million in 2004, $138 million in 2005, and $35 million in 2006.

RMA is also using data mining to verify compliance with established rules and regulations. For example, data mining identified policies where a comparison of past claims and production data indicated that insurance providers may have failed to use claim production data to establish future approved yields, as required by regulation. RMA is providing this information to the insurance providers to assist them in correcting producer data for subsequent crop years. Insurance providers are only required to make changes when an error is found.

The Government Accountability Office (GAO) audited RMA compliance activities in 2005, and recommended areas for improving our compliance efforts. The GAO made several recommendations that RMA accepted and is working to implement.

Compliance managers continue to concentrate on the mission-critical tasks of evaluating and improving new processes to prevent and deter fraud, waste and abuse in the crop insurance program. We have dedicated significant resources to building and adapting a reporting and tracking system to complement and integrate the oversight mandates established by ARPA and other statutory requirements.

While RMA, FSA and the insurance providers have preempted tens of millions of dollars of improper payments through these and other measures, RMA is constantly identifying ways to balance competing needs to make our products fraud-proof while seeking to provide responsive, useful risk protection to farmers. We still have work to do and improvements to make, but we are making good progress in our fight against program abuse.

Conflict of Interest Supplementary Guidance

RMA is finalizing a Manager's Bulletin that contains further guidance to assist insurance providers in implementing changes to the SRA regarding conflict of interest disclosure. The Bulletin will establish standards for reporting conflicts of interests by insurance provider employees, agents, and loss adjusters. It will thereby promote program integrity and ensure adequate internal controls based on the identification of certain conflict of interest problems in past audits and investigations of fraud, waste and abuse in the program.

Pasture, Rangeland, Forage and Hay Initiatives

In August 2006, RMA announced the availability of the Pasture, Rangeland, Forage insurance products for pasture and rangeland, in response to ARPA requirements. There are over 400 million acres of rangeland, 120 million acres of pasture, and 62 million acres of hay in the United States, and we clearly saw a need. The new insurance products are area-based products that trigger indemnities based on indexes. One index is based on accumulated rainfall and the other is based on a temperature-adjusted measure of vegetation obtained from the National Oceanographic and Atmospheric Administration. Both products will use new technology to help solve the problem of the inability to directly measure forage production across the diverse range and pasture settings on U.S. farms and ranches. Each pilot program is offered in six states. As of April 9, 2007, the sales of the new Pasture, Rangeland and Forage Rainfall and Vegetation Index pilot programs have exceeded expectations. There have been a robust 8,023 Rainfall Index policies sold covering 24,535,220 acres with $328,234,326 in total liability. Each state in the pilot has a policy sold. The pilot area in Texas had the greatest number of polices sold with 5,928 policies and over 20.8 million acres covered. In the pilot, Texas has the largest area and South Carolina has the smallest number of potential acres. South Carolina had the lowest number of polices sold at 9 and just over 2,000 acres insured with $159,995 in liability. The total liability to date exceeds the estimated participation of ten percent and $205 million for the life of the pilot.

Vegetation Index pilot program sales are at 1,687 policies sold covering 3,962,930 acres and $61,786,236 in total liability. All states in the pilot sold policies with the exception of Pennsylvania. The South Dakota pilot area contained the largest potential acres and has the highest number of policies with 885 polices sold. These policies insure 3,029,871 acres and a liability of $41,982,206. The state with the lowest number of sales is South Carolina with two policies covering 318 acres and $20,289 in liability.

The participation in the pilot program areas are at approximately 16 percent, while the target goal was 10 percent at the end of the pilot.

Combination Policy

RMA is continuing to develop a "Combination" policy, which merges similar features from the existing Actual Production History, Crop Revenue Coverage, Income Protection, Indexed Income Protection and Revenue Assurance plans of insurance into one consolidated plan. We have been working on this for some time now, and the draft final rule is being completed. The final rule is targeted to be effective for the 2009 reinsurance year.

We believe this change will continue to give producers a broad array of insurance options, but in a more straightforward manner resulting in more streamlined and improved product delivery and operations.

The regulation proposes to reduce duplication and to simplify revenue and yield protection into: (1) One set of policy materials, special provisions, and actuarial documents; (2) One rating and pricing methodology; (3) One premium calculator; and, (4) One database. This combination of APH, CRC, RA, IP, and IIP provides simplification, fewer documents to read and process, and less chance of errors for producers, crop insurance companies, sales agents, and RMA.

Cooperative Discount and Rebating Issue

The SRA prohibits insurance providers from providing rebates to producers, except for two specific instances provided in the Act. One of these exceptions is the Premium Reduction Plan, which is provided in section 508(e)(3) of the Act, which I will address later in my testimony. The other rebating exception is provided in section 508(b)(5)(B) of the Act and involves the participation of farmer-owned cooperatives in providing crop insurance to their members. Section 508(b)(5)(B) of the Act is very clear that all payments from cooperative or trade associations to members must comply with and be subject to State law governing insurance rebating in the States in which payments are to be made. To qualify to pay a dividend or other such payment to its members under 508(b)(5)(B), an entity must be recognized by RMA as a cooperative or trade association and RMA must receive certification from the respective State department of insurance that the payment program complies with State rebating law.

Interest by insurance providers and their agents in providing premium discounts through cooperatives was intensified by the moratorium on the Premium Reduction Plan for the 2007 reinsurance year, enacted in 2006 appropriations legislation. RMA soon began receiving reports that individuals were exploring creative schemes to rebate insurance premiums, including the formation of cooperative-like entities that might qualify under section 508(b)(5)(B). Evidence also emerged that many State insurance departments were unaware that the rebating programs of cooperative and trade associations were clearly subject to State rebating law.

As a result of these developments, RMA became increasingly concerned that these recent developments might disrupt the marketplace for Federal crop insurance. And, it determined that its existing procedures for operating cooperative and trade association programs under section 508(b)(5)(B) were inadequate. Consequently, RMA has taken the following actions:

- RMA halted approval of cooperative dividend programs for the 2007 reinsurance year, until adequate procedures could be developed and established through a Managers Bulletin.

- RMA has enlisted the active support of the National Association of Insurance Commissioners (NAIC). NAIC is assisting RMA in raising awareness of the States anti-rebating responsibilities under this particular section of the Act. NAIC has circulated a draft "Model Letter" which will guide States in their evaluation of cooperative and trade association rebating proposals under State rebating law and respond effectively and decisively to RMA.

- RMA drafted a Managers Bulletin that incorporates procedures that approved insurance providers must follow to sponsor cooperative and trade associations. It includes the items the entity and the insurance provider must submit for RMA to be able to determine that an entity is a cooperative or trade association and its dividend program complies with State rebating law. RMA circulated the draft Managers Bulletin to the industry and, based on their input, is finalizing the Bulletin for publication.

Through these actions, RMA is confident that the intent of Congress will be preserved by encouraging participation by legitimate farmer-owned cooperatives under section 508(b)(5)(B). RMA is further confident that, as a result, the stability of the marketplace for crop insurance will not be threatened by schemes to establish cooperative-like entities for the sole purpose of crop insurance rebating.

Premium Reduction Plans (PRP)

The PRP is not available during the 2007 reinsurance year (RY) due to language in the 2006 FY (Fiscal Year) Appropriations Bill as extended by the current Continuing Resolution. However, RMA is evaluating requests from 2006 RY PRP-eligible AIPs after the 2006 RY annual settlement in February 2007. We are finalizing a Managers Bulletin that will provide clarification and guidance regarding PRP payment authorization requests for 2006. This will allow us to be prepared to offer PRP for the 2008 RY.

Premium Costs for Corn

The rise in projected demand for plant-based fuel has caused a projected increase in the price of corn and an increase in premiums for revenue based insurance products for corn. For example, in Page County, Iowa, the price election per bushel of corn is up 57% and the producer portion of the premium is up 62 percent. Additional acres in corn mean fewer acres in other crops and fewer bushels of soybeans, for example, means higher prices as well. The soybean price election in Iroquois County, Illinois, is up 31 percent and the producer portion of the premium is up 29 percent. We cannot tell this early in the crop year the extent to which the number of acres insured will be affected by the higher premiums.

Farm Bill Proposals

In putting the farm bill proposals together, USDA aimed to make farm policy more equitable, predictable and better able to withstand challenge. The Farm Security and Rural Investment Act of 2002 (FSRIA) was the right policy for the times. It was the first-ever farm bill with an energy title, and it increased conservation spending by about 80 percent. When it was developed, commodity prices were low, exports had declined for several years in a row, and the debt-to-asset ratio was at about 15 percent.

But times have changed and farm policy must reflect the new realities. Today, commodity prices are strong for most program crops, and we are seeing record and near-record production and yields. The debt-to-asset ratio has now fallen to 11.8 percent; the lowest number USDA has ever recorded. Exports, meanwhile, have increased every year since 2002 and last year hit a record $68.7 billion. They are expected to grow to $78 billion this year.

USDA put a great deal of time and energy into developing a comprehensive set of proposals for the 2007 Farm Bill that will help move the farm economy to a new level of prosperity and growth. Secretary Johanns began this process by holding 52 forums across the country to gather input directly from those most affected by farm policy – America's farmers and ranchers. In all, USDA received more than four thousand comments from producers and other stakeholders across the country. The collective common sense drawn from those comments has really formed the heart of the farm bill proposals.

The Department certainly heard a great deal of support for the structure of FSRIA, but also heard many suggestions on how to improve current policies and many of them were surprising. Secretary Johanns and the USDA team took all of what was heard into account as these proposals were crafted. And they sought to combine the best features of our farm policies of past years—including preserving a strong safety net for producers—with a more market-oriented approach to meeting the challenges and seizing the opportunities that we know future years will bring.

The Farm Bill proposals will put American agriculture on a strong competitive footing for years to come while also making responsible use of taxpayer dollars. With that, let me go into more detail on several of the crop insurance-related proposals.

The first proposal would allow farmers to purchase supplemental insurance that would cover all or part of their individual policy deductible in the event of a county or area wide loss. We are proposing literal "gap coverage" that a producer can buy to cover 100 percent of their deductible loss under the crop insurance program.

The threshold at which the supplemental insurance would be activated is a county-wide loss of 10 percent or more. When the loss under the group policy is sufficiently large, the grower's deductible would be completely covered, resulting in 100 percent of losses being covered. The supplemental policy would cover the 'hole' in crop insurance, as well as provide compensation for disaster situations.

Ultimately, this approach would help to address the gap in the safety net that exists due to the fact that current crop insurance products fail to cover crop losses that are less than the size of the deductible. This proposal would increase the Administration's commitment to crop insurance by $350 million over 10 years.

Secondly, we are proposing again that if you receive program payments you should have crop insurance. Crop insurance is already widely used by producers. Some states have 90 percent-participation or more, but we want to get that last 10 percent enrolled. If a producer gets subsidies, we feel strongly that crop insurance should be used to help manage their risk. Higher participation and higher coverage will help obviate the need for costly supplemental assistance that undermines the crop insurance program.

The conditions under which program linkage will take place under the Administration's Farm Bill proposal are substantially different from that which existed in 1994 when linkage was previously attempted. Voluntary participation in the crop insurance program for major U.S. commodities is already around 80 percent, and almost 90 percent of those participants are already buying higher levels of coverage that satisfy the minimum linkage requirement. In the mid-1990's, voluntary participation was significantly lower, particularly at buy-up levels of coverage, and so mandatory coverage affected a much larger percentage of producers.

A third Farm Bill proposal would provide the authority for RMA to renegotiate the financial terms of the Standard Reinsurance Agreement (SRA) once every 3 years.

RMA needs the opportunity to make changes in the SRA to address MPCI primary business changes. Revisions may be needed to strengthen program integrity efforts, or to bring the company underwriting gain potential back to a reasonable level. Without this opportunity, current terms and provisions would continue despite the fact they may be no longer in the best interest of the program.

As we all know, participation in the crop insurance program has grown significantly since the implementation of ARPA. Given this fact and the large number of changes taking place within agriculture today, it is in the best interest of all parties to have an SRA that is reflective of market conditions and dynamics.

Another key proposal would be to allocate up to $10 million in annual funding to strengthen crop insurance compliance efforts. This proposal would allow RMA's Compliance office to fill critical staffing needs in addition to providing funding for compliance related strategies including support for data mining, satellite imaging, and Geographic Information Systems.

RMA bases the need for enhancing the current Compliance staffing levels on the continuous program growth coupled with fewer on-board Compliance staff now than in the 1990's. Compliance has been seeking additional staff to address this critical shortage for the past few years.

Initially, RMA would look to use the money as indicated in past requests. We would spend approximately $1.5 million to support 15 staff years for Compliance. Twelve staff years would be distributed to the six Compliance field offices to fill Compliance reviewer positions. The three remaining positions would be allocated to Washington to provide for a Compliance Assistant Deputy, a Management Control Officer, and a dedicated OIG Hotline Complaint coordinator. This will enhance the oversight and support efforts to deter fraud, waste, and abuse in the program.

Another Administration proposal would be to increase the net book quota share (USDA FCIC's share of risk on premiums currently retained by the companies) from the current 5 percent to 22 percent and provide a ceding commission to the reinsured companies of 2 percent of premium.

The Net Book Quota Share (NBQS) is a means for RMA to participate in the crop insurance program at the same level as a commercial reinsurer. RMA assumes a percent of the companies retained premium, loss, and resulting underwriting gain or loss, similar to a commercial quota share reinsurer. The loss ratio and rate of return is the same for both the company and RMA, thus it does not impact the risk sharing of the other SRA reinsurance terms. A commercial quota share MPCI reinsurer will pay a ceding commission to the reinsured to aid in offsetting the costs of generating business. While the current NBQS provisions do not include a ceding commission, the proposal does include a 2 percent ceding commission. The impact to the companies retained business is limited by the significant increase in premium over the last several years. The total company retained premium for the 2006 reinsurance year is $3.68 billion. If this proposal had been in effect for the 2006 reinsurance year the company retained premium would be approximately $2.87 billion, which is greater than the 2003 retained premium amount of $2.61 billion.

The Administration has proposed reducing the administrative and operating expense reimbursement to the reinsured companies by 2 percentage points for all policies other than CAT policies.

Payments to companies for delivery of the crop insurance program have steadily increased, both in absolute terms and on a per-policy basis, over the past decade. In 1990, companies were paid about $280 million as compensation for program delivery, or about $350 per policy. By 2006, payments to companies were about $940 million, for a per policy payment of about $820. For 2007, payments to companies are expected to exceed $1.1 billion because of higher commodity prices, or over $950 per policy. With a two percentage point reduction in A&O, payments to companies would still be about $1 billion, more than has been paid in any other year. Further, higher commodity prices are expected to be sustained for at least the next few years, with the result that future A&O payments (inclusive of the two percentage point reduction) will still be far larger than those of recent years. Hence, this proposal will not create a disincentive to provide proper service to farmers.

Finally, the Administration proposes to allow private crop insurance companies to have direct access to data mining information currently held by RMA. Companies could use this information to reveal potential fraud and abuse. Companies would be allowed to query information related only to their respective clientele. To fund such activities, RMA would be required to charge a user fee for this service.

Conclusion

RMA continues to evaluate and provide new products and to promote the adoption of crop insurance as a risk management tool so that the government can further reduce the need for ad hoc disaster payments to the agriculture community.

The growth and effectiveness of the crop insurance program is dependent on a reliable delivery system; insurance products that meet the needs of producers; investment in information technology to ensure the delivery system is timely, accurate and dependable; and adequate funding to support compliance and program integrity, maintenance and administration, product evaluation and new product development, and a dependable and equitable delivery system.

USDA Farm Bill proposals will further strengthen the Federal crop insurance program and insure that this critical safety net continues to serve America's farmers and ranchers.

Again, thank you for the opportunity to participate in this important hearing. I look forward to responding to questions on these issues.

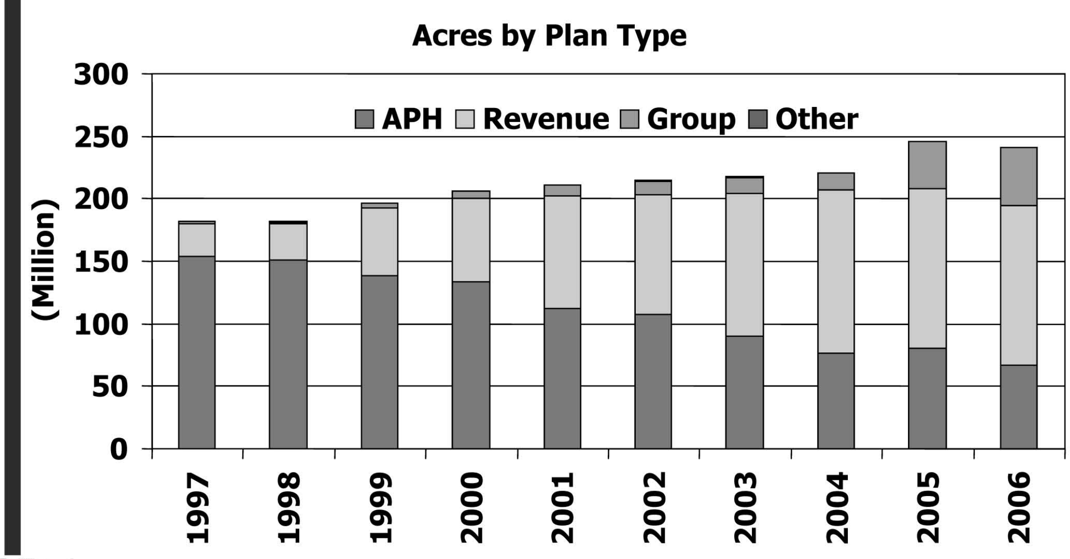
Program Status (2006 CY)

$49+ Billion Liability	242 Million Acres	360+ Commodities

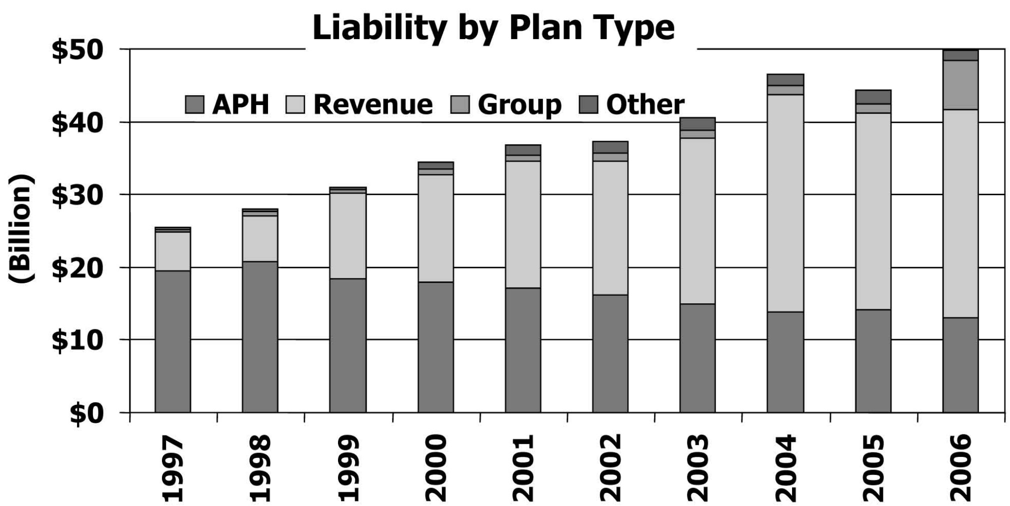
21 Existing Crop Insurance Plans

Actual Production History (APH)
Adjusted Gross Revenue (AGR)
Adjusted Gross Revenue Lite (AGR-Lite)
Aquaculture Dollar
Avocado Revenue Coverage
Crop Revenue Coverage (CRC)
Dollar Amount of Insurance
Fixed Dollar
Grower Yield Certification (GYC)
Grower Yield Certification Span (GYC Span)
Group Risk Plan (GRP) (Pasture, Range & Forage
Group Risk Protection Income Protection (GRIP)
Income Protection (IP)
Indexed Income Protection (IIP)
Livestock Gross Margin (LGM)
Livestock Risk Protection (LRP)
Pecan Revenue
Revenue Assurance (RA)
Tobacco - Guaranteed Production
Yield Based Dollar Amount of Insurance
Tree Based Dollar Amount of Insurance

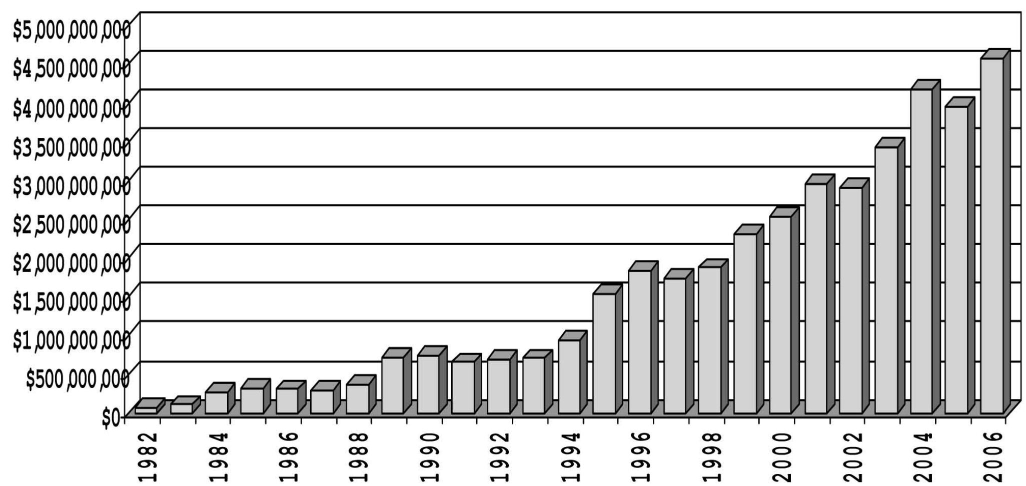
Program Growth: Participation by Insurance Plan and Acres



Program Growth: Participation by Insurance Plan and Liability



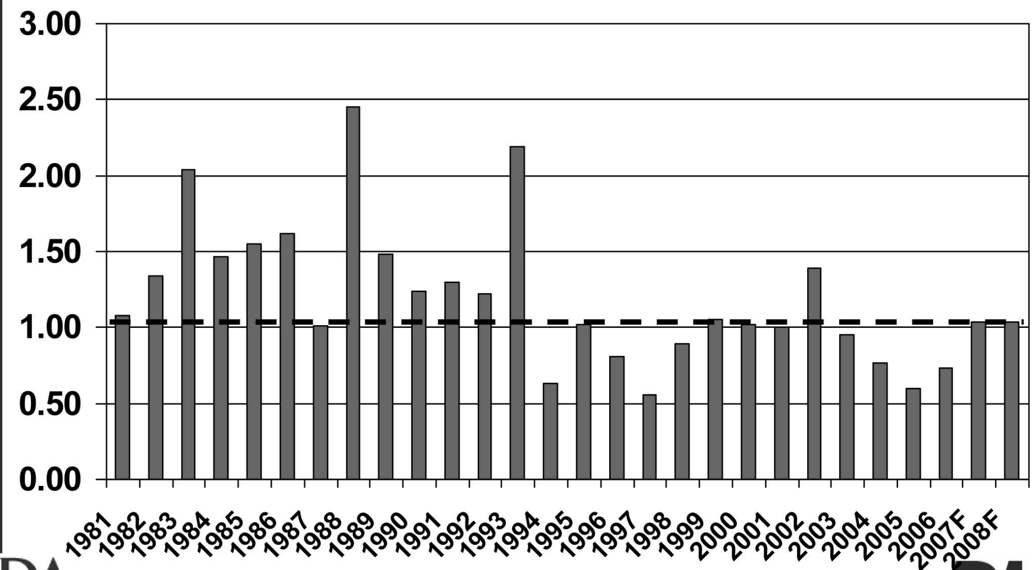
Historical Industry Premium Volume - MPCI 1982-2006



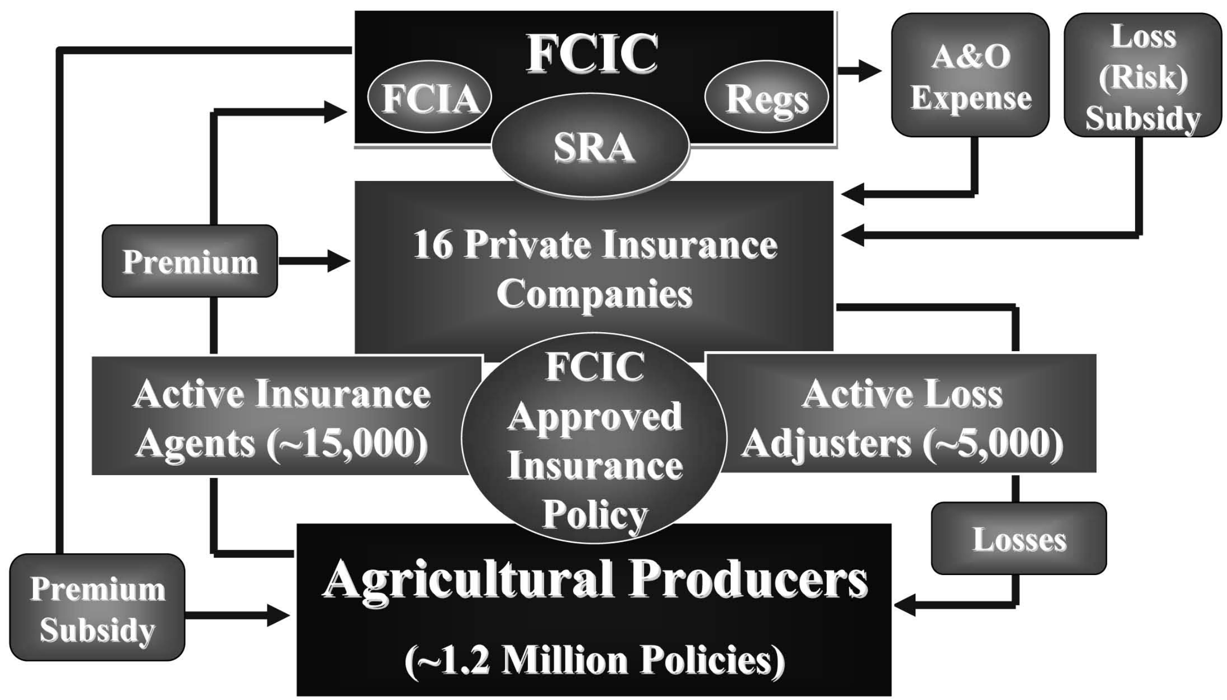
USDA

RMA

Crop Insurance Loss Ratio



Federal Crop Insurance
Delivery System



Mr. ETHERIDGE. Thank you, Mr. Gould. The chair would like to remind Members that they will be recognized for questions in order of seniority for Members who were present at the time the gavel fell when we started the hearing. After that, Members will be recognized in order of arrival and I appreciate the Members understanding of this. I now recognize myself for 5 minutes.

Dr. Collins, first, I have two questions regarding organic crops. Today, when it insures organic-grown crops, the FCIC charges a 5 percent premium surcharge. Many organic growers, however, feel that this surcharge is unfounded, because the risks of loss for organic crops are no different from conventional-grown crops in the same place, the same time, and that premiums really should be the same. Additionally, they would like to be able to purchase Federal crop insurance to cover their crops at a higher price. I understand that, over the past year, FCIC has been working with the Agricultural Marketing Service on a system to collect higher sales prices for organic crops, both retail and wholesale, at various points along the marketing chain. So my question to you is, as Chairman of the FCIC, what kind of data would you need to convince you to eliminate the 5 percent surcharge, and if presented with that information, could the FCIC take the initiative to eliminate the surcharge? And finally, will the data collected with AMS provide FCIC with the information it needs to insure organic crops at their actual market price?

Dr. COLLINS. Okay, Mr. Chairman, I will offer a couple of thoughts on this issue. We get a lot of questions about organic agriculture and of course, for all of our products that we have, organic producers can buy crop insurance. They do pay, as you indicated, a 5 percent premium load for the risks of organic production, that is, the variability of yields on organic production relative to conventional production. I would point out that the 5 percent load does not apply to GRP or GRIP policies. It only applies to individual yield policies. The question does come up frequently about whether that load is merited.

First of all, let me say that organic production is small relative to the size of our program and we don't have a long history of data. In 2006, we had 355,000 acres of organic crops insured, compared with 242 million acres in our program. So you are talking about $\frac{1}{10}$ or $\frac{2}{10}$ of a percent of our total book of business. It was not until 2004, when organic agriculture really began to take off in our program, that we started collecting data on organic production as a practice now have the acres that are identified in our data system as organic. The first 2 years we have that data are 2005 and 2006. We have looked at the loss ratio for organic production compared with conventional production for both of those years and the loss ratio was higher for organic production than it was for conventional production. So that tells us that we are probably justified, at this point, with the 5 percent load on the premium for organic agriculture. Our goal in the long term would be to have a unique price for organic products and a unique rating for organic products.

Mr. ETHERIDGE. So the answer is probably not now?

Dr. COLLINS. The answer is probably not now. We have just started collecting———

Mr. ETHERIDGE. All right. Can you keep us informed of that as it moves along, because I think that is of considerable interest.

Dr. COLLINS. Absolutely.

Mr. ETHERIDGE. All right. Next, let me talk about the recent GAO report on climate change and its potential impact regarding Federal crop insurance. The report recommended that the administration of RMA conduct an analysis of potential long-term implications of climate change on the FCIC and its mission use and the assessment from the Interagency Climate Change Science Program and the Intergovernmental Panel on Climate Change. In response to GAO's report sent by the Under Secretary, who is a Member of the FCIC Board, USDA agreed with the recommendations, generally, then proceeded to explain that RMA does assess the long-term implication future weather events can have on crop insurance, all without directly responding to the recommendations. Given the inherent difficulty of forecasting weather events, how does RMA evaluate future risk? What specific action items are RMA and FCIC taking to respond to the GAO recommendations, and will RMA be utilizing the findings of the Climate Change Science Programs and Intergovernmental Panel on Climate Change as it evaluates future weather conditions and the future crop insurance system, because that is certainly going to have an impact.

Mr. GOULD. Mr. Chairman, all of USDA is very much involved with looking at climate change. We, as the Risk Management Agency, are alert to opportunities to improve our rating data on an ongoing basis. Presently, the agency works, as we look back at producers' average production histories, so if there were changes in climate, it would reflect over time with a producer's average production history and it will affect our rating accordingly. But as we look forward, if there were new opportunities and somebody somehow can predict the weather, whether it is dramatic or less dramatic, I am sure we would be more than interested and willing to take a look at that information.

Mr. ETHERIDGE. I may want to come back to this, because I am not really sure we got an answer on that one and my time has expired and I will yield to Mr. Neugebauer for 5 minutes.

Mr. NEUGEBAUER. Thank you, Mr. Chairman. I had several people from the crop insurance industry in my offices last week and by the way, I had Administrator Gould in there as well, and I think many of them are concerned about some of the new proposals, particularly the reduction of the A&O by two percentage points, and the other, increasing the USDA's net book quota share of premiums retained by the companies. Some of them are concerned about what kind of implications that has long term in the industry. Can you alleviate some of their concerns about that?

Mr. GOULD. I can try. I would say that, as we look at the crop insurance in its entirety, not only from the Risk Management Agency's standpoint, but from the companies' standpoint as well, if we stand back and look and see how the marketplace is changing, the amount of dollars that we are spending for the delivery of the Crop Insurance Program and because of that, we are suggesting that, as the value of each individual premium has nearly doubled in recent years, that it seems like there would be a need for less compensation for the A&O expenses, so our proposal to reduce that by 2 percent is proposed for that reason. As far as the reinsurance, we have looked at that and simply have suggested that the government, through the FCIC, retain some of that reinsurance that is now going either to the companies—to reinsurance companies.

Mr. NEUGEBAUER. What happens if the loss ratios, though, move up, isn't that going to—what kind of impact, then, does that have on the agency?

Mr. GOULD. Well, that would impact everybody that is involved with the insurance business, whether it is the companies, the reinsurance companies or of course the agency. As we monitor the financial health of the companies, we expect them to be able to withstand a loss ratio of 5.0 for any 1 year, so we think that is a viable threshold for the companies. And if you look back over recent years, the loss ratio has been less than one, so it has been profitable, not only for the companies and reinsurance companies, but the taxpayer as well.

Mr. NEUGEBAUER. One of the things that the industry says is that underwriting gains are not necessarily profits, that in fact allows them to build up reserves for future years. In some years when the losses are lower, the underwriting gains are higher, but in those years where we have a pattern of heavy losses, that allows them to sustain that. They are concerned about the Federal Government dipping into their ability to be able to build up those reserves. Is that good policy?

Mr. GOULD. Well, I guess it depends. First of all, let me say that we agree with that concept. The question is, what period of years do we want to go back and look and see what the loss ratio is? Ultimately, the question comes down to what those profits should be, and I am not an owner/operator of an insurance company, so I am not going to go there. I guess the only thing I would add was that we have no new insurance companies coming into the program and we have none leaving, so that might be a long way of saying maybe it is about right.

Mr. NEUGEBAUER. It is about right the way it is now?

Mr. GOULD. Again, I would rather not go that far. I am just saying we have no new insurance companies coming into the program nor do we have any leaving for lack of profits.

Mr. NEUGEBAUER. But we don't know what might happen if we began to move in this direction?

Mr. GOULD. That is probably accurate.

Mr. NEUGEBAUER. I want to move quickly, and I hope we will have a chance for some other questions, because there is a particular bill that I have introduced that I want to discuss with you, but we talked a little bit last week and for the record, can you kind of tell me where we are on doing something about these declining yields? I know that two different proposals were submitted to you. I understand you didn't like either one of them. But where are we going to move in that direction?

Mr. GOULD. Well, as Dr. Collins said in his testimony, we are taking a look at that. The two proposals that came before the Board, they had problems with those. They didn't seem to fit real well, were not in the best interest of producers, had some statutory question marks attached to them, and so currently, hopefully we can take the best of both of those proposals and put those together and make something, probably an indexed yield approach that would be beneficial to producers.

Mr. NEUGEBAUER. Would that require any kind of a statutory change or do you think you can do that internally?

Mr. GOULD. With the proposal that we are currently looking at, it would not require a statutory change, but we are limited to a degree of what we can do under the current statute.

Mr. ETHERIDGE. The gentleman's time has expired and I recognize the Chairman of the Committee, Mr. Peterson.

Mr. PETERSON. Thank you, Mr. Chairman. Dr. Collins or Administrator Gould, we now have 16 insurance companies, right?

Dr. COLLINS. Yes, sir.

Mr. PETERSON. How many did we have before ARPA and how many new companies have joined since ARPA? I mean completely new, not mergers or acquired or so forth. Do you have those numbers?

Dr. COLLINS. I can't tell you exactly. I think, when I first became Chairman of this Board, which was right after ARPA was enacted, my recollection is that we had about 17 companies. We had American Growers become insolvent. We had another, The Hartford leave. We had another merge. So we got down as low as 14 and we are at 16 today. And this is rough. I am just giving you———

Mr. PETERSON. So are there any new companies?

Dr. COLLINS. Yes, we have had new companies over the last couple of years.

Mr. PETERSON. Completely new?

Dr. COLLINS. Completely new, yes.

Mr. PETERSON. Two new companies?

Dr. COLLINS. As many as five. That is my recollection. I can check that for you, but I think that is my recollection.

Mr. PETERSON. Apparently, you are proposing to lower the loss ratio. I guess that was the discussion we were having here. From 1.075 to 1.0, what impact is that going to have on the premiums that farmers pay, and would the impact be felt nationally or is it going to affect some states more than others?

Dr. COLLINS. Yes, that is a little bit of a difficult question. The statutory loss ratio that we have to shoot for is 1.075. In our President's budget baseline, we use 1.04, so we project indemnities based on a loss ratio of 1.04. Our historical experience over the last half dozen years or so has been .9, so we are well below that. We have done what analysts call backcasting. We have looked at our current rates and asked what the loss ratios would look like if we had the experience of the past and we get a loss ratio of about one. So we think that going to a 1.0 statutory rate implies very little change in premiums. Nevertheless, it gets a budget savings because our long-term baseline assumes 1.04.

Mr. PETERSON. How much are the savings?

Dr. COLLINS. We scored it at a little over a billion dollars over 10 years. The Congressional Budget Office, who also uses 1.04 as the long-term loss ratio, somehow came up with a much lower number. Theirs was $200 million to $300 million over 10 years.

Mr. PETERSON. That is normal, I think.

Dr. COLLINS. My experience as well.

Mr. PETERSON. Under, I guess, what we know of your supplemental deductible coverage, apparently the way you are going to do this you are going to dictate how much of a producer's deductible for crop insurance will be covered depending on how low a county's yield will fall below 90 percent of the county's average yield for the crop. Why wouldn't you allow the producer to decide for himself how much of the deductible acreage he wants to cover with the supplemental insurance? Why have you set it up like———

Dr. COLLINS. Yes. Well, in our book, the 183 page book that has the Administration's proposals in it, we had one example in there and in that example, if someone buys an individual policy with 75 percent coverage and the county yield goes below 75 percent of the average county yield, then the whole deductible would get covered 100 percent. So in that sense, we have fixed it and we haven't given the producer a choice. However, in the proposal, as we have further developed it, we believe that the producer should have a choice and we would propose that the producer does have a choice. We think that the producer could select the trigger level at which the producer would get 100 percent of the deductible covered. For the 75 percent example I just gave you, a producer might say okay, I am going to select the 75 percent as the trigger level. If the county yield falls below 75 percent of its average, then I am going to get 100 percent of my deductible covered. Or the producer could say I am going to select 50 percent as the trigger level. If the county yield falls below 50 percent of the average, then I will get 100 percent of my deductible covered. And of course the lower the producer selects that trigger level, the lower the producer's premium is going to be, because the less likely that the indemnity is going to trigger and cover the deductible. So as we envision it now, we would like to give the producers some flexibility to figure out just how fast that deductible would be covered and thereby have more flexibility over the premium rate that they would have to pay.

Mr. PETERSON. You can submit this to me, but you haven't got any actual numbers on what this would cost to buy a certain kind of coverage? Do you have that information?

Dr. COLLINS. We have done some examples. I don't know that we have made these public yet, but we certainly could.

Mr. PETERSON. Well, if you could get that to———

Dr. COLLINS. We certainly could.

Mr. PETERSON.—me as soon as———

Dr. COLLINS. Sure.

Mr. PETERSON.—you can. We need that.

Dr. COLLINS. I think, if we want to promote this idea, we ought to give you what you want.

Mr. PETERSON. Right.

Dr. COLLINS. So we will do that.

Mr. PETERSON. All right. Thank you. Thank you, Mr. Chairman.

Mr. ETHERIDGE. Thank you. And I would ask that you make that available to the Subcommittee as well. Thank you.

Dr. COLLINS. Yes, sir.

Mr. ETHERIDGE. Thank you, Mr. Chairman. I now would yield to the gentleman, Mr. Conaway, from Texas. Five minutes.

Mr. CONAWAY. Thank you, Mr. Chairman. I am familiar with work that is being done at Tarleton State on data mining and the opportunity to try to find folks who either, by accident or intent, are trying to game the system and Mr. Gould, you mentioned briefly something about that. If you wouldn't mind expanding on that and talking to us about the conflicts between RMA and FSA, in terms of sharing data and taking full advantage of the FSA's local committees, in terms of moving some of these cases forward. As well as expanding your general attitude toward auditors and prosecutors and other folks who would take the information that is gleaned through the data mining and push it to conclusion, as to folks who may or may not be gaming the system. Do you have enough assets? Do you have enough people to exploit the information that you are getting, as it relates to the work done at Tarleton and I think some other places as well?

Mr. GOULD. Well, it seems like you have a number of questions there.

Mr. CONAWAY. Well, I assumed you would filibuster the last 4 minutes.

Mr. GOULD. Thank you. First of all, let me talk a little bit about the relationship between RMA and FSA. The common thread there is a common information management system, the CIMS project that was actually mandated in the 2002 Farm Bill. We have gone to great lengths to get that off the ground, get it implemented and make it useful for both agencies. It probably comes as no surprise, as we move in that direction, we have encountered more hurdles and more obstacles than we thought could possibly be there, but nevertheless, we are moving forward. We have a good working relationship between the two agencies and I can assure you that both the Administrator of FSA and myself are committed to moving the project forward. So as that project does move forward, then we will be able to share information between the two agencies and also with the companies, as it relates to the Crop Insurance Program.

To talk more specifically about data mining, that is actually a very fascinating, interesting and rewarding effort that we do. As we look for anomalies in the program, not only amongst producers, but agents and claims adjusters, and as we look at those and go forth and pursue some of those and in the case of producers, if they are anomalous, for whatever reason, they show up on a county FSA spot checklist. Then the FSA personnel within the county, at the local level, then are charged with the responsibility of keeping an eye on those producers to provide a little ground truth. At the same time, the producers are provided a letter so they know that they are on the spot checklist and it is amazing how fast those producers respond to the fact that they are being watched and their behavior carries forth for many years.

And so to make a long story short, data mining has been very rewarding and we just wish that we had the dollars and the manpower to do more. It just seems to be a very worthwhile and an efficient way of providing integrity to the crop insurance business.

Mr. CONAWAY. Well, given the positive cash flow that results generally from it; you mentioned that you pursue some of the anomalies. It would be helpful to the Committee to understand exactly what the level of commitment that RMA has to this and if there are unfunded wish lists that you would say if we had X dollars to provide additional resources to the investigatory piece of this, it would be positive to the overall position of the system. I don't want you to look flatfooted on this, but it seems to me that if you think this does work, that we would want you to at least let us know what you think the proper level of commitment to this ought to be with respect to resources and funding.

Mr. GOULD. We are suggesting that if we had 15 more FTEs, provide two in each of the regional offices, plus three more people in Washington to oversee the program, and if we could more adequately fund our IT system to provide that portion of the effort, then we could go a long ways towards doing a better job there.

Mr. CONAWAY. Was that in your 2008 budget request?

Mr. GOULD. Yes, it is.

Mr. CONAWAY. Okay. Thank you, Mr. Chairman.

Mr. ETHERIDGE. The gentleman yields back. The gentle lady from Kansas, Mrs. Boyda, is now recognized for 5 minutes.

Mrs. BOYDA. Thank you, Chairman Etheridge. And thank you for your testimony here today. I come from Kansas, so certainly crop insurance is a topic of a great deal of discussion. FSA closures and the lack of technology or some of the technology problems that we are experiencing in Kansas as well. So you have my full support on making sure that we keep technology relevant and operable. Please move forward with that.

I would like to go back to the issue of climate change, if we could. One of you mentioned a littler earlier that there didn't seem to be systemic weather problems. Coming from Kansas, we are in either the seventh, eighth or ninth, depending on how you are going to count it, year of severe drought, especially in western Kansas. So my question to you is, when we are looking at climate change, how does the agency plan for that? Or maybe I should ask, is the agency planning for that or are we marching ahead as if weather or climate change really isn't an issue?

Mr. GOULD. Well, that is a difficult question. I guess the question ultimately comes down to if we have a weather pattern, if it is in Kansas or someplace else, that has been, in your case, dry now for a number of years, is that really climate change? And we might look at other parts of the country where we have had—it has been dry for a number of years and then the rainfall pattern changes and so then it doesn't look so much like climate change. I can assure you that up until the time I came to Washington, I planted 44 crops and over that period of time, you would go through years when it was either too wet or too dry and then there were some years in there it was just right, but being a typical producer, I don't ever remember those.

Mrs. BOYDA. Yes.

Mr. GOULD. So I think the real issue then is how do we define climate change and what do we do about it? I think that the bigger issue that we can respond to more near term is what we can do about our declining yields for the producers that are going through those periods of ongoing yield losses; and whether we want to attribute them to climate change or an anomaly in weather pattern.

Dr. COLLINS. Could I comment on this as well?

Mrs. BOYDA. Sure.

Dr. COLLINS. Well with respect to climate change and crop insurance, it is a very complicated issue, obviously, because most climate change projections are for the year 2100 and they are long-term, slowly evolving changes and as that change occurs, there are mitigations that occur. Ecosystems adjust. There are also counterbalancing effects like more carbon dioxide in the atmosphere. This creates the fertilization effect, which actually increases plant production, not reduce it. So you have offsetting effects and so it is very hard to know how this is going to play out over time. I think, for crop insurance purposes, what is most important is if climate change leads to abrupt short-term changes in climate. And then the question for us is, is our rating appropriate? Are we going to charge producers the right amount of money given the losses that they face? And probably the single most important variable for us in doing that is what we call our county reference yields. That is the yield that we use to determine the base rating for crop insurance. And so the important thing for us over time as the climate changes, is to make sure we have the best, the most timely, the most scientific methods in place to determine reference yields so we have the most appropriate rating. So I think there are things we can do to defend ourselves against climate change, not even knowing how it is going to come out in the longer term.

Mrs. BOYDA. Could you explain to me again, just for declining yields, in the three sentences that all go back home and say what we are planning to do with declining yields? Could one of you summarize that real distinctly?

Dr. COLLINS. I will try.

Mrs. BOYDA. Thank you.

Dr. COLLINS. At the moment, we are not proposing to do anything. We have just tabled two contracted products that would have dealt with declining yields, because they suffered from some, what we believe, some inequity and serious actuarial problems and they would have caused us to have to increase premium rates quite a bit. So what we want to do is focus on one of the methods we use right now. We have something called a 60 percent t-yield plug and that is used when a producer experiences a year when the producer's yield is below 60 percent of the county average. We allow the producer to take 60 percent of the county average and put that into their long-term average that determines their premium rate and their coverage level. What we have found is, for producers whose yields are poor, generally, relative to the county, like if they are typically 70 or 80 percent of the county, that 60 percent yield plug works very, very well. It boosts their actual production history. But for producers whose yields are at or above the county average and they have a bad year, it doesn't work very well at all. So what we are proposing to do is to go back and look at the current yield plug and index it, that is, take account of a producer's yield relative to the county to determine a new yield plug for those producers whose average yield is better than the county over time. So that is not a sentence or two. I apologize for that. But the idea is to take———

Mrs. BOYDA. Obviously, you have never run for office.

Dr. COLLINS. I can guarantee you that. The current yield is very simple. The current plug is very simple. It is just 60 percent of the county t-yield that applies to everybody. What we want to do is adjust the plug based on the producer's productivity relative to the county.

Mrs. BOYDA. Thank you.

Dr. COLLINS. That is one sentence.

Mrs. BOYDA. My time is up. Thank you.

Mr. ETHERIDGE. I thank the gentle lady. Mr. Scott from Georgia, for 5 minutes.

Mr. SCOTT. Thank you very much, Mr. Chairman. Two points that I would like to discuss and get your opinions on. One is your assessment of the seriousness of global warming. I mean, I have listened to your comments. There are two schools of thought. One is that we are in a natural time of global warming. But give me your honest opinion of the greenhouse effect, the greenhouse gas effect, the emissions or carbon dioxide in the air, the impact that this would have. Are we really, in your opinion, in a serious, serious time of global warming? We get mixed signals from this Administration and until recently, it has not been clear how serious this Administration is taking global warming. And as the Chief Economist of the Agriculture Department, it seems to me that you would probably be the best person that could give an adequate explanation of where this Administration is on its seriousness it is taking of global warming and again, as it impacts crop insurance.

Dr. COLLINS. In response to that question, it is my personal experience that the Administration takes global climate change very seriously. The Federal Government spends between $4 billion and $5 billion a year on its climate change programs. We have two primary programs, the Climate Change Science Program, CCSP, and the Climate Change Technology Program, CCTP. Both of these programs focus on measurement of climate and technology to adapt to climate change. Every year, the Administration puts out a report. The title of it is called *Our Changing Planet*. This year's version is about to come out soon. I would encourage that you look at it, because it lays out what the Administration thinks about the science of climate change, and it is my opinion that the Administration accepts the findings of the Intergovernmental Panel on Climate Change, which is more than 2,000 climate scientists who have concluded that the Earth is warming and that it is likely due to human activity.

I think the Administration does take it seriously and the question is, what are they doing about it? And that is where people are open to debate about what the proper prescription is, and the focus of the Administration has been on voluntary action and technology. I can't tell you, government-wide, all the programs that are underway, but I can speak to USDA's programs. We spend about $70 million a year on climate change. Our focus is on understanding how a changing climate affects ecosystems and how you can mitigate the effects of climate change.

I also think that we have taken a focused effort to try and adapt our programs at USDA to reduce greenhouse gas emissions. We have, in fact, looked at all our conservation programs and amended them to try and encourage greenhouse gas offsets where we can. One simple example is, in the Conservation Reserve Program, we give bonus points to someone who wants to enroll land in the Conservation Reserve Program for the amount of greenhouse gas reductions that their enrollment will result in, and we have done things like that across all of our programs. So, I guess the short answer to this is that I personally think that we are taking it seriously. You might not agree with the path of response, but I think we have one.

Mr. SCOTT. Let me ask you just the same way to my other point. Do you think that global warming has an impact on the declining yields? Particularly, in the past successive years, we have a pattern of declining yields, which results in the producers coverage declining, their premium rates rising, and given the fact that we are coming up with the 2007 Farm Bill, do you see us making or would you make any recommendations that we address that in the upcoming farm bill, the declining yields?

Dr. COLLINS. First of all, I would say that I know of no scientific evidence that suggests that declining yields patterns in certain areas of the country in recent years are due to climate change. I do not know of a climate scientist who has said that and those who I have asked have said it is uncertain at this point. Therefore, I would not make a recommendation for the farm bill to do something specifically to address this.

Mr. SCOTT. My time is past.

Mr. ETHERIDGE. Thank you. The gentleman's time has expired. The other gentleman from Georgia, Mr. Marshall, for 5 minutes.

Mr. MARSHALL. Thank you, Mr. Chairman. I have had a number of pecan farmers in Georgia tell me that they think our crop insurance programs don't really fit their crop very well and it has to do with yield-based policies and problems with poor years. And just a minute ago, Dr. Collins, in talking about this, you said that the way it is structured is there is a county plug of 60 percent available to somebody who has a year that drops below and that 60 percent plug is one that is being used in order to avoid having their overall base go down too far. You are thinking about adjusting that by some scaled approach, having in mind the different production levels that farmers within that county enjoy. Suppose you have got counties that have had, as typically happens where pecans are concerned and we are going to have a problem with pecans this year in Georgia because of the freeze, but suppose you have an entire county experience several years of lower yields. What my guys tell me is that is a problem for them as far as their yield-based insurance is concerned. Can you help describe what that problem is and what the possible solution might be?

Dr. COLLINS. Yes. The problem when yields go down is two-fold. You mentioned one of them and that is that the effective coverage goes down for the producer. If they are buying a 65 percent policy and their so-called actual production history is declining, then you multiple the 65———

Mr. MARSHALL. Right.

Dr. COLLINS.—times their yield history and that is declining.

Mr. MARSHALL. Right. They described this problem.

Dr. COLLINS. And second, we risk classify producers based on their yield relative to the county reference yield and therefore, as their yield goes down relative to the county yield, their premiums go up. So not only does their coverage go down, but they are paying more for less coverage.

Mr. MARSHALL. I would like you to assume that there is a countywide problem, though, so everybody is suffering from the same difficulty. Their base is going down and let us assume that goes on for several years. Is there any fix for the countywide problem?

Dr. COLLINS. Not that I can think of, other than the adjustments that we put in over time to deal with this kind of thing. The one adjustment is the yield plug that I already mentioned. We have a second adjustment. The yield plug is the most used adjustment. There are others. Another one is a floor.

Mr. MARSHALL. Well, the yield plug doesn't help as much if it is a countywide problem. It is a repeated countywide problem year to year.

Dr. COLLINS. Well, if the county t-yield is going down—now, the county yield is a 10 year average, so the yield plug is 60 percent of a 10 year average. So a couple of countywide yield declines are not going to pull that t-yield down very much. I am sorry. Go ahead.

Mr. MARSHALL. I have only got 5 minutes here, so if I could jump in. It is related. Another thing that they say is that pecans, particularly, and there would be other crops that fit this mold, pecans in particular have a problem with damage being done, say, by a tornado, by heavy winds. The damage to yield plays out over a number of years. Maybe the first year there is no crop, but then in the second year there is going to be pretty marginal crop and gradually the tree is going to recover. But how does crop insurance work? Let us assume that what I just described is correct and I know there are differences of opinions about that.

Dr. COLLINS. Right.

Mr. MARSHALL. But assuming it is correct and Georgia pecan growers believe that it is, how does crop insurance cover folks who have that kind of long-term problem associated with a current disaster? They are going to experience lower yields year after year after year.

Dr. COLLINS. You know, I am not sure. I am going to ask Mr. Gould. I am familiar with some of our tree policies where the entire tree is lost and we have provisions for what we call R&R, recovery and rehabilitation, where we actually cover the cost of replanting the tree and the foregone income until the tree is back into full production. Our Florida Fruit Tree Program works that way. I am not sure about pecans. I will ask Mr. Gould if he knows.

Mr. GOULD. Maybe. I am not sure I know anything much more except I would add that some of our tree policies are actually 2 year policies to compensate for some of those concerns that you raised. I cannot tell you today if the pecan policy is one of them and will have to get back to you on that.

Mr. MARSHALL. That would be great and I don't know, there may be other crops that are in a similar situation.

Dr. COLLINS. Right, right.

Mr. MARSHALL. Thank you.

Mr. ETHERIDGE. I thank the gentleman. The gentleman yields back. Excuse me. While you are doing that, if you would, please include two others on that because in North Carolina we got hit pretty hard this time, up in the mountains and other areas with our peach trees, with our vineyards and other stuff. If you will include us as a part of that and make sure I get a copy of that, I would appreciate it. Thank you, sir. Now I yield 5 minutes to the gentle lady from South Dakota, Ms. Herseth Sandlin.

Ms. HERSETH SANDLIN. Thank you, Mr. Chairman, and thanks to both of you for your testimony today. Dr. Collins, in the Administration's farm bill proposal, it proposes to reduce the Federal cost of the Crop Insurance Program by increasing the farmer-paid premiums. I am somewhat concerned that this may discourage participation in the program after years of increasing participation. Has the Department done any analysis on what the proposed premium increases might do to farmer participation in the program?

Dr. COLLINS. We have done some, Ms. Herseth Sandlin. I would say that our overall analysis is to take all of these proposals as a package, and it is true that the reduction in the premium subsidy, which is five percentage points for policies that are 70 percent coverage or less, two percentage points for policies that are 75 percent or higher, could discourage some purchases. We think the main effect might be that producers would drop down a notch on coverage, so it might reduce coverage level more so than participation. Offsetting that would be the proposal for linkage, that if you are going to get price and income support, then you would have to buy crop insurance and we think that could add 17, 18 million acres to participation. So we have sort of looked at these together.

Ms. HERSETH SANDLIN. Sorry. Could either of you update me on the status of the pilot programs or products coming out of RMA that have been approved, as it relates to producers, livestock producers and the coverage of their grass or pastureland, in terms of participation or those who are buying that new product? I think, for counties in South Dakota west of the Missouri River, they can participate in the pilot that deals with vegetation and the vegetative cover.

Dr. COLLINS. Do you want to do that?

Mr. GOULD. Yes. We refer to that as our pasture, rangeland and forage product that just came out last fall. It is an interesting concept, in that we are actually using new and updated technology. Actually, it is a two policy program, and national in scope. We measure the vegetative index and that is done within grids. And also, then, we have a rainfall policy that is also measured in grids. And then all of that information is indexed and the producer buys policies that are in a timeframe that is important to him and at a level that is important to him for either the vegetative index or the rainfall index. The rainfall index has been the most popular, so far. And while the vegetative index has a lot of interest, it has less interest than the rainfall policy. We anticipated, being a pilot program, that we might expect 10 percent of the eligible acres to be enrolled and in fact, we had 17 percent of the eligible acres enrolled. So the response, as a first-year pilot project, was overwhelming and we are encouraged by the sign up we have had. A year from now, we will all know how it all worked out, but we will continue the pilot. In fact, we have had producers in areas outside of the pilot area express interest and wondered how soon we are going to expand the pilot area.

Ms. HERSETH SANDLIN. Yes, I have heard the same inquiries and I think there was some disappointment among producers I represent, that they are not eligible for the rainfall pilot. I think that, like you said, there is some interest and I discussed with some of the producers in central South Dakota how the vegetative pilot would work. Are you in partnership with USGS and ARS's data center at all on this, in terms of Landsat 7 images and either for this pilot or have there been any discussions with the Department as it relates to the resources and assets of USGS as it relates to climate change, given the records that they have going back a number of decades and the ongoing analysis that could be done going forward?

Mr. GOULD. I honestly don't know the answer to that. I do know that, in developing a policy, we went back and looked at, I think I heard, some 30 years of data to develop the policy and index as to how the policy would work, but I don't know whose data we looked at or where it came from.

Ms. HERSETH SANDLIN. Thank you both. Thank you, Mr. Chairman. If perhaps we could get maybe more regular updates to the Subcommittee about how these pilots are working and the considerations that the Department is reviewing to expand eligibility for others to participate, I would appreciate it. Thank you.

Mr. ETHERIDGE. I thank the gentle lady. Her time has expired. And if you would keep us on a regular update on that, that would be great. I would appreciate that. Now I yield 5 minutes to Mr. Conaway to ask questions for the Ranking Member, Mr. Goodlatte.

Mr. CONAWAY. Thank you, Mr. Chairman. I appreciate your indulgence. Mr. Goodlatte has a constituent who grows Asian pears and he recently suffered a loss as a result of freezing. Apparently, there is no crop insurance available for this particular crop and the deadline for signing up for NAP, the Noninsured Assistance Program, coverage came during the middle of his pear harvest. Is there flexibility in setting the NAP sign-up deadline or what can be done to help in this particular situation?

Dr. COLLINS. Well, we don't run the NAP program. That is a Farm Service Agency program. I can't answer for sure on what they might say on that, but generally when we have a deadline for sign ups, it is for actuarial reasons; it is so that you commit to paying a fee or you commit to paying a premium before you know how much loss you have so that we are not buying a loss. That may be the basis for establishing the deadlines for that program. I don't know. We could check with the Farm Service Agency and see what flexibility is there, unless Mr. Gould has———

Mr. GOULD. No, I am not aware of their program, the details of it, so we will have to get the information from FSA and get back to you on that.

Mr. CONAWAY. Okay, this is Mr. Goodlatte's question. I have precious few pears grown in the desert of west Texas, but yes, if you wouldn't mind getting back to Mr. Goodlatte on this issue.

Mr. MARSHALL. Will the gentleman yield?

Mr. CONAWAY. Yes.

Mr. MARSHALL. Mr. Conaway? I don't know whether disaster benefits apply to a crop like this, but assuming that they do, as I understand it, the way the supplemental is written, the crops that are planted before the end of February would be eligible for disaster benefits.

Mr. CONAWAY. Yes, this doesn't relate to the supplemental kind of disaster. This was just a regular ongoing problem. From the tone of the question, apparently the deadline is generally, for sign up each year, is generally in the middle of the harvest time. But anyway, if you could get back to Mr. Goodlatte on that, I am sure he would appreciate it. I yield back.

Mr. ETHERIDGE. I thank the gentleman. Let me thank both of you for your testimony today and if you would, I would like to now invite the second panel to the table. Thank you for coming and if you will, please get back to us with the material you had committed to get to us in writing. I appreciate it.

Mr. GOULD. We will do that.

Dr. COLLINS. Thank you very much.

Mr. ETHERIDGE. And as the second panel comes, we are not going to really take a break. We are going to go straight into the second panel in an attempt to not lose any more time than we absolutely have to. Okay, let me thank you for being here and we will start with Mr. Robert Parkerson, President of the National Crop Insurance Services in Overland Park, Kansas. Next will be Mr. Steve Harms, Chairman of the American Association of Crop Insurers, from Johnston, Iowa; Ms. Kathy Fowler, President of the National Association of Crop Insurance Agents, Memphis, Texas; Mr. Steve Rutledge, President of the Farmers Mutual Hail Insurance Company, on behalf of the Crop Insurance Research Bureau in West Des Moines, Iowa. Let me ask you to summarize your statement in 5 minutes. Your full statement will be entered into the record. Mr. Parkerson, please begin when you are ready and if you will, each one of you follow accordingly and I won't interrupt you again. Mr. Parkerson.

STATEMENT OF ROBERT W. PARKERSON, PRESIDENT, NATIONAL CROP INSURANCE SERVICES, OVERLAND PARK, KS

Mr. PARKERSON. Thank you, Mr. Chairman. My name is Robert Parkerson. I serve as the President of the National Crop Insurance Services, NCIS, on whose behalf my testimony is presented today. I would like to thank the Subcommittee for the opportunity to present this testimony.

Today, I would like to emphasize three topics of concern of the private sector, the first, maintaining an economically sound program, second, enhancing program integrity, and third, funding RMA adequately. We will also touch upon a few topics proposed by the Administration for the 2007 Farm Bill.

First, maintaining an economically viable Crop Insurance Program requires two objectives. First, when weather conditions are favorable, resulting in lower-than-expected loss ratios, the private sector must be permitted to earn the profits that sustain its ability to make long-term commitments to the program, and there must be adequate and reasonably priced commercial reinsurance available in addition to the reinsurance provided through the SRA. Program profitability enables companies to build reserves to face the inevitable catastrophe losses that accompany agriculture. We need to remember, for example, the widespread droughts of 1988 and even 2002; flooding in 1993. The industry must have the resources to cope with these events. Although it is too early to predict what the losses may be in 2007, it is not starting out well; early freeze damage in California, the Mid-Atlantic and the parts of the Great Plains. If this adverse weather continues, all of us would be grateful for the reserves that were built.

I now want to turn the importance of commercial reinsurance of the Federal Crop Insurance Program. Depending on the resources of each individual company, the availability of commercial reinsurance at adequate levels is essential to all companies. For these companies to survive in this program, they must be able to transfer a portion of their risk to commercial reinsurers. Commercial reinsurers will not accept risk if profit margins are too thin. Quite simply, they have other alternatives to invest their capital. We should not and cannot drive the commercial reinsurers out of this program. Therefore, I must now offer some concerns that the Administration's proposed farm bill has brought up.

The proposal would drastically reduce reinsurer participation in the program. For example, there is now a 5 percent premium paid to FCIC under the SRA for quota share of reinsurance. The Administration proposes to increase this to 22 percent. That type of profit erosion is draconian and will result in driving commercial reinsurers out of the crop insurance market. The Administration also proposes a two percentage point reduction in administration and operating subsidy, the A&O subsidy that has been steadily declining over the last decade. Reducing the subsidy, while stimulating increased quota share costs by over 440 percent, which the 22 percent represents, invites serious and adverse consequences.

Program integrity: Let me talk about that a moment on behalf of the industry. We believe that the Federal Crop Insurance Program operates with a high degree of integrity. Yet, with taxpayer dollars and the private sector resources at risk, vigilance is a must. To this end, NCIS last year held a program integrity conference. This conference centered on the crop insurance industry's ability to reduce fraud, waste and abuse and how best to handle these issues in a growing and complex program. Once again, a program integrity conference will be held this year, May 21 and 22 in Overland Park, Kansas.

Our third concern, Congress needs to provide RMA with ample funding to participate as an equal partner in the risk management training and education programs that the private sector sponsors. NCIS annually sponsors various national conferences on program issues, and we also sponsor schools to train loss adjusters. Our national conferences are well attended by both company representatives and RMA personnel, who often make major presentations at these schools. Loss adjustment schools are well attended by the company employees and are taught by our industry's most experienced personnel. An adequate operating budget for RMA to send its experts to our conferences and schools is a necessity. When actively participating in industry-sponsored programs, RMA offers valuable contributions.

In closing, crop insurance is an effective risk management tool for growers to protect themselves. As an industry, we take seriously our responsibility to deliver the Federal Crop Insurance Program. Maintaining an economically sound program, enhancing program integrity and funding RMA adequately are paramount to making the Crop Insurance Program work for the farmers and ranchers who rely on it to protect their livelihood and to protect the country's food supply. Thank you, Mr. Chairman.

[The prepared statement of Mr. Parkerson follows:]

Testimony Before the U.S. House of Representatives Committee on Agriculture: Subcommittee on General Farm Commodities and Risk Management
May 1, 2007

Mr. Chairman, my name is Robert W. Parkerson. I serve as President of National Crop Insurance Services (NCIS), on whose behalf my testimony is presented today. I would like to thank the Subcommittee for the opportunity to present this testimony.

NATIONAL CROP INSURANCE SERVICES

NCIS is a not-for-profit trade association whose members include every crop insurance company that participates in the Federal crop insurance program. NCIS and its predecessor organizations have provided members support in their crop insurance businesses since 1915.

NCIS has worked actively with the Risk Management Agency (RMA) as an approved contractor and with the Board of the Federal Crop Insurance Corporation (FCIC) as an expert reviewer. We have received more than twenty risk management education grants or research awards over the last several years and have served as expert reviewers on fourteen projects.

NCIS is also a licensed advisory organization and statistical agent for private Crop-Hail insurance in forty-nine of the fifty states, and it assists the crop insurance industry in meeting the regulatory requirements of these states. This is accomplished by filing the appropriate policy forms and statistical information with state insurance departments. Further, NCIS serves as a liaison with individual state insurance departments through active participation with the National Association of Insurance Commissioners (NAIC).

In 2006, NCIS member companies wrote more than $4.7 billion in Federal multiple peril crop insurance and related revenue products premium and over $400 million in private Crop-Hail insurance products premium. The potential liability between both programs was approximately $65 billion. NCIS member companies service policies that encompass all farmers participating in the federal and private programs, including limited resource and socially disadvantaged farmers. In partnership with the Federal government, our participating member companies comprise the safety net that equitably provides risk management to America's farmers.

Today, I want to emphasize three topics of great concern to private sector participants in the Federal crop insurance program – maintaining an economically sound program, enhancing program integrity, and funding RMA adequately. Discussion of these topics also will provide some private sector perspectives on the Administration's proposed 2007 Farm Bill.

MAINTAINING A SOUND PROGRAM

The Federal crop insurance program has reached a mature stage of development. Since 1980, when the public-private partnership for delivery of MPCI coverage began, covered acreage has expanded dramatically, with twenty-one insurance plans now available covering approximately 80% of the acres for major program crops and equating to 70 – 85% of potential value of these crops.

Together, the private sector and FCIC have paid substantial indemnities to our agricultural producers when they have encountered bad years. In fact, the program's cumulative average loss ratio for 1980 – 95 was 1.5, well in excess of the expected levels established in the Federal Crop Insurance Act. Substantial improvements in annual loss ratios over the last decade have had significant and positive financial and program integrity consequences, as discussed below.

Maintaining an economically viable crop insurance program requires that two objectives be achieved. First, when weather conditions are favorable, resulting in a lower than expected loss ratio, the private sector must be permitted to earn the profits that sustain its ability to make long-term commitments to the program. Second, there must be adequate and reasonably priced commercial reinsurance available in addition to the reinsurance provided through the FCIC's Standard Reinsurance Agreement (SRA).

Now that the program has achieved greater and improved actuarial soundness, an inevitable consequence of this improvement must be placed on the table and recognized as a positive development. Quite simply, the truth is that when actuarial soundness improves, the financial health of insurance providers and their reinsurers also improves.

Years with low national average loss ratios will produce significant profits. That is a very positive development for several reasons. Congress, the Administration, and the insurance companies should not be embarrassed by this reality. Program profitability enables existing program participants to build reserves to face the inevitable catastrophic losses that come with agriculture. We need to remember, for example, the widespread droughts of 1988 and 2002 and flooding of 1993, and have the resources to cope with such events. Although it is too early to predict what the losses will be in 2007, this year, unfortunately, is not starting out well – with early season freeze damage in California, some Southern and Middle Atlantic areas, and parts of the Great Plains. If weather remains adverse, all of us will be grateful for reserves built in prior years.

Profitability also draws new entrants into the program. This, in turn, can benefit the program through different and broader perspectives and increasing the innovative drive of the recent past.

Profitability is also good for the government's fiscal interests. Profitability means that the burden on the taxpayer is reduced when America's farmers have fewer losses than expected. Improved actuarial soundness also is evidenced by the private sector's willingness to share greater risk under the SRAs negotiated in 1997 and 2004, and it also is manifested by their increased designation of policies to the Commercial Fund, where the private sector has a risk at least equal to, if not greater than, the government's risk.

I now want to turn to the importance of commercial reinsurance to the Federal crop insurance program. Although FCIC provides substantial support to the program through reinsurance available under the SRA, companies still remain exposed to substantial risks. Depending on the resources of individual companies, the availability of commercial reinsurance at adequate levels and reasonably priced rates is essential. Even our strongest members cannot individually sustain their multi-billion dollar portions of widespread losses. Thus, for them to survive, to remain profitable, and to be energetic participants in the Federal crop insurance program, they must be able to transfer a portion of their risks to commercial reinsurers. Commercial reinsurers will not accept these risks if profit margins are too thin. Quite simply, they have other alternatives for investing their capital. We should not, we cannot, drive commercial reinsurers from the program.

Having noted the importance of commercial reinsurance, I now must offer some concerns about the Administration's proposed Farm Bill. The proposal drastically would reduce the potential profitability of the program. For instance, there is now a 5% premium paid to FCIC under the SRA for quota share reinsurance. The Administration proposes increasing this to 22%. That type of profit erosion, quite frankly, is draconian and will result in driving commercial reinsurers from the crop insurance market. The Administration also proposes a two percentage point reduction in administrative and operating subsidy. As it is now, the A&O subsidy has been steadily declining over the last decade. Reducing the subsidy, while simultaneously increasing quota share costs by 440%, invites serious and adverse consequences.

ENHANCING PROGRAM INTEGRITY

When discussing improved actuarial soundness, I noted that there are resulting program integrity consequences. First, the profits associated with lower loss ratios provide resources which permit improving internal controls as part of promoting program integrity. Second, reduced loss ratios also are a positive sign that RMA has improved its program management. To illustrate, we have not witnessed since 2000 any broad-based criticism by USDA's Office of Inspector General of RMA's development of costly and inappropriate coverages.

Comments on loss ratios bring me to a beneficial proposal in the Administration's 2007 Farm Bill. It proposes reducing the expected loss ratio from 1.075 to 1.0. That may seem like a minor change, but it could have major significance for improving program integrity as well as actuarial soundness. Tightening down the expected loss ratio sends a significant signal that we do not want to invite losses through inadequately developed coverages.

We believe that the Federal crop insurance program operates with a high degree of integrity. Yet, with taxpayers' dollars and the private sector's resources at risk, vigilance is required. To this end, NCIS last year held its first annual Program Integrity Conference. That conference centered on the crop insurance industry's ability to reduce fraud, waste, and abuse and how best to handle these issues in a growing and complex program. Senator Pat Roberts, RMA Administrator Eldon Gould, and Bert Little of Tarleton State University were key speakers at this conference. Over 100 people from the crop insurance industry attended this day and a half event. Representatives from the RMA, NAIC, OIG, FBI, International Center for Ethics in Business, NCIS, and crop insurance companies spoke on various issues dealing with fraud, waste, and abuse.

Our second annual Program Integrity Conference will be held on May 21 – 22, 2007, in Overland Park, Kansas. Like last year's program, this conference will focus on reducing fraud, waste, and abuse. Many of the same organizations who contributed to last year's program will be participants this year. Key speakers will be Congressman Jerry Moran from this Committee, as well RMA Administrator Eldon Gould.

For those of us working in the crop insurance industry, our livelihoods depend on the integrity of this program. Without it farmers would not have the safety net they so richly deserve. Without it the crop insurance industry would be smaller and fewer in number. We have all worked too hard and achieved too much to allow the slightest erosion of integrity to cause the downfall of this program.

As part of improving program integrity, we want to urge Congress to adopt the Administration's proposal in its version of the 2007 Farm Bill giving companies direct access to the data mining efforts that have been underway since passage of the Agricultural Risk Protection Act of 2000. It is fine to gather data and to analyze it. That does not complete the process, however, as the results of data mining efforts need to be provided directly to each company participating in the program. Doing so will permit each company to work proactively on improving compliance by its agents and loss adjusters. In short, for data mining to have real utility in reducing losses, the private sector needs direct and faster access to data mining results. We are pleased that the proposed Farm Bill addresses this issue.

ENHANCING RMA RESOURCES

The private sector can only do so much through its own efforts to improve the integrity of the Federal crop insurance program. Please let me outline several steps which Congress can take to enhance RMA's resources beyond those proposed in the 2007 Farm Bill.

First, Congress should provide RMA with an adequate budget to match the data processing systems utilized by the private sector. RMA needs its own thoroughly modern data processing system that interfaces with the private sector's state of the art systems. This goes beyond data mining and relates to fundamental day-to-day business operations. We absolutely never should encounter a situation where farmers who have suffered legitimate losses covered by their MPCI policies cannot be paid promptly because of inadequacies in the data processing system of RMA. We have come to the brink on this issue in the past, but fortunately not encountered any disaster. RMA should have a state of the art data processing system to match the companies' systems so that policyholders' claims are processed and paid promptly.

Second, Congress needs to provide RMA with ample funding to participate as an equal partner in the risk management training and education programs that the private sector sponsors. For example, we at NCIS sponsor annually various national conferences on program issues, and we also sponsor schools to train loss adjusters. We average conducting twenty to twenty-five such schools and conferences annually. Our national conferences are well attended by both company representatives and RMA personnel, who often make major presentations. Loss adjustment schools are well attended by company personnel, and they are taught by our industry's most experienced adjusters. Over the past few years, we routinely have had insightful RMA participation. An adequate operating budget for RMA to send its experts in different crops to our conferences and schools is essential. When actively participating in our industry sponsored programs, RMA offers valuable contributions.

The private sector firmly believes that educational efforts can be key deterrents to fraud, waste, and abuse. The Federal crop insurance program is complex, and improving understanding of its terms and operation should help limit fraud, waste, and abuse. Everyone involved—our policyholders, agents, adjusters, RMA personnel, and company employees—all need to understand the program and recognize that their individual actions affect the integrity of the entire crop insurance program. On a whole, agents who sell crop insurance and loss adjusters who determine the amount of indemnitees payable are honest and dedicated professionals. As a result of their dedication, America's farmers can be assured that program options will be accurately explained to them at time of purchase, and that losses will be adjusted fairly and accurately in the event of damage. Moreover, through proper education, company employees, agents, and adjusters are becoming better equipped to recognize behavior outside the bounds of program compliance. Knowing this encourages policyholders to behave in an ethical manner. The benefits of effective training are that errors can be avoided, that uniformity in adjusting losses can be increased, thus leading to higher confidence in the program, and that there will be appropriate discipline in those rare instances of intentional wrongdoing. Achieving these benefits can be improved by greater RMA participation in our loss adjustment schools. It simply is "penny wise, but pound foolish" to deny RMA the economic resources to participate at a greater level than it now can.

CONCLUDING POINTS

NCIS is in regular contact with Mr. Gould and his staff and we have worked diligently together to resolve issues as they arise in the program. Some of these have dealt directly with program vulnerabilities that, if not corrected, could lead to program abuse. Even though this process has been successful, there are still some issues to be resolved. Certain review processes still take a random approach towards discovering program vulnerabilities. We want to sit down with RMA and follow up on discussions of processes and methods that would allow us all to all "work smarter."

Crop insurance is an effective risk management tool for growers to protect themselves. Growers must have confidence in the stability of the program and purchase adequate coverage. As an industry we take seriously our responsibility to deliver the federal crop insurance program with integrity and fairness, and we have a long history of being proactive in addressing issues of fraud, waste, and abuse. We shall continue to be proactive. We realize the 2007 Farm Bill is a work in process. We remain available to answer questions and to provide comments as your work continues.

STATEMENT OF STEVEN C. HARMS, CHAIRMAN, AMERICAN ASSOCIATION OF CROP INSURERS; PRESIDENT AND CHAIRMAN, BOARD OF DIRECTORS, RAIN AND HAIL, L.L.C., JOHNSTON, IA

Mr. HARMS. Good morning, Mr. Chairman, Ranking Member Moran, and Members of the Subcommittee. I am Steve Harms, President of Rain and Hail, L.L.C., headquartered in Johnston, Iowa, and market the Crop Insurance Program in all 50 of the United States. My testimony today is presented in my capacity as Chairman of the American Association of Crop Insurers. Thank you for allowing me to testify today and I request that my written statement be submitted for the record.

Before I summarize my testimony, I would like to point out that, historically, the Crop Insurance Program is not part of the farm bill. The last two significant reforms of the program took place in 1994 and 2000, not in the farm bill. The Federal Crop Insurance Act is a separate statute that need not be reauthorized in the bill. I respectfully request that the Committee not pursue changes to the Crop Insurance Program as it considers the 2007 Farm Bill.

My testimony will make the following three points about the Federal Crop Insurance Program: Number one, it is working; Number two, it can be improved; and Number three, the program can be harmed. The program is working and the modern Federal Crop Insurance Program is a huge success. Providing protection from risks that are beyond a farmer's control has been the basic and fundamental goal of the Federal Crop Insurance Program from its very inception. For the 2006 year, the program provided about $50 billion of protection, a record level of coverage at that time, which is up from only $11 billion in 1993. For the 2007 year, projections indicate that farm risk protection will likely exceed $60 billion. The modern Federal Crop Insurance Program is an indispensable risk management tool. The program has grown more complex, including more policy choices and more stringent regulations, on its way to becoming an efficient and effective risk management tool. Since we are in a new era of production agriculture, where every available acre will need to satisfy our food and energy demands, more farmers will need the Crop Insurance Program than ever before.

The modern Federal Crop Insurance Program is an indispensable financing tool. Without crop insurance, many farmers would be unable to obtain financing. Crop insurance makes the process of farmers obtaining annual operating loans much easier, simpler and efficient. In the case of farmers who have purchased crop insurance, banks usually require less collateral because they consider these farmers to be better protected. Many younger farmers with less collateral will be unable to obtain the financing without crop insurance. The modern Crop Insurance Program is an indispensable marketing tool. Crop insurance allows producers to market in advance of production, as well as disaster assistance when the crop county loss ratio exceeds a trigger level to farmers who have received an indemnity payment.

Another opportunity to improve the program is in updating the provisions of existing legislation which are no longer relevant given the economic realities. In this regard, AACI believes Section 508(e)(3), known as the Premium Reduction Plan, or PRP, should be deleted. The program can be harmed. Proposals that would take the Crop Insurance Program in the wrong direction should be rejected. In this regard, the following USDA proposals especially should be rejected, which are increasing net book quota share from the current 5 percent to 22 percent and providing only 2 percent of premium back to the companies; cuts to the farmer subsidy to deliver the program, such as reducing the administrative and operating expenses by two percentage points for all policies other than CAT policies; a mandatory purchase requirement for farmers who participate in commodity programs; and last but not least, cuts to the premium subsidies that reduce participation.

The press often makes the mistake of reporting underwriting gains as profits, thus conveying the false impression that the industry is making huge profits. Both A&O reimbursements and underwriting gains are gross revenue earned by approved crop insurance providers under the terms and conditions of the USDA developed and approved Standard Reinsurance Agreement that each company must agree to and sign in order to be eligible for the program. They are not profits.

In closing, I would like to thank you for this opportunity to present AACI's views about the Crop Insurance Program and I look forward to further discussion with the Members today.

[The prepared statement of Mr. Harms follows:]

TESTIMONY
Of
Steve Harms
American Association of Crop Insurers
To
House Agriculture Subcommittee
General Farm Commodities and Risk Management
1300 Longworth House Office Building
Tuesday, May 1, 2007

Introduction

Good morning Chairman Etheridge, Ranking Member Moran and members of the Subcommittee. I am Steve Harms, President, Rain and Hail, L.L.C., which is headquartered in Johnston, Iowa, and markets the crop insurance program in all fifty of the United States. My testimony today is presented in my capacity as Chairman of the American Association of Crop Insurers (AACI).

Thank you for scheduling this hearing in your oversight of the federal crop insurance system as well as in your preparation for writing the 2007 Farm Bill. AACI, with members representing all segments of the private sector element of the crop insurance system, appreciates being invited to provide testimony and respond to questions from Members of the Subcommittee.

My testimony will make the following three points about the federal crop insurance program:

1. The program is working – and is more essential than ever as our farmers struggle to meet the nation's energy and food needs.
2. The program can be improved – continue with ARPA-type changes.
3. The program can be harmed – avoid wayward recommendations.

The Program Is Working

The modern federal crop insurance program is such a huge success that it is the envy of the world. Other nations, such as Brazil, France and Japan, are working toward the development of their own crop insurance programs. Providing protection from risks that are beyond a farmer's control through a more affordable and stable insurance system has been the basic and fundamental goal of the federal crop insurance program from its very inception almost three-quarters of a century ago. In recent years, especially since passage of ARPA in 2000, USDA has routinely testified before Congress that the federal crop insurance program is highly successful, especially in increasing the number of acres insured and the level of protection or coverage per acre. Total net acres insured have increased from about 83 million in 1993 to about 242 million in 2006. For the 2006 crop insurance year, the program provided about 50 billion dollars of protection—a record level of coverage at that time, which was up from only about 11 billion in 1993. For the 2007 crop insurance year, projections indicate that farm risk protection will likely exceed 60 billion dollars.

<u>The modern federal crop insurance program is an indispensable risk management tool.</u> The program has grown more complex, including more policy choices and more stringent regulations, on its way to becoming an efficient and effective risk management tool. An important factor in the growth of crop insurance is the growth in the number of policy options available to farmers. These additional options provide farmers with the capacity and the flexibility to insure a wider array of agriculture enterprises. They also permit the customization of risk management strategies to individual farm and farmer needs and requirements. And it is acutely important to know and understand that the expansion in policy options was a direct result of farmer requests and demands for more coverage options in more specific enterprise situations. The result has been vast improvements in the matching of farmer risk management needs to actual coverage.

Along with more complexity there are more regulations. And while regulations are certainly burdensome, they do generally serve to help enhance program integrity, which is a fundamental requirement for continuing a high level of congressional and public support for the crop insurance program.

<u>The modern federal crop insurance program is an indispensable financing tool.</u> <u>Without crop insurance, many farmers would be unable to obtain financing.</u> Crop insurance makes the process of farmers obtaining annual operating loans much easier, simpler and efficient. In the case of farmers who have purchased crop insurance, banks usually require less collateral because they consider these farmers to be better protected. <u>Many younger farmers with less collateral would be unable to obtain financing without crop insurance.</u>

Farmers understand more and more that crop insurance is another cost of doing business. However, the purchasing cost of crop insurance provides certain benefits for the farming operation, including greater ability to finance land purchases, enter into land rental contracts and arrange production input purchases. Protection provided by the program gives lenders much more confidence in extending credit.

<u>The national commitment to greater energy self-sufficiency makes crop insurance much more important than ever.</u> Farmers will have to plant on every available acre in order to supply our energy as well as food and fiber needs. Furthermore, as the national alternative energy initiative focuses on renewable feedstock beyond corn for generating ethanol, farmers and their lenders will need a level of confidence in order to allocate sufficient land and other resources necessary to produce desired supplies of cellulosic feedstock. Thus, the federal crop insurance program must be an integral part of the government's effort to build a more self-sufficient domestic energy supply.

As the current demand for ethanol feedstock drives up the price of corn and all other commodities that compete for the same and input resources, farm subsidy payments are projected to decline. Farmers will receive more of their income from the market and less from the government. However, this relationship works best for farmers who make a crop. As we know, crops fail many times. For example, we have already witnessed a series of crop disasters in 2007, from the citrus and avocado freeze on the West Coast in January to a series of hard freezes that badly damaged wheat in the Midwest, especially the south central part of Kansas, to the Easter freeze of a few weeks ago that has destroyed many farmers' apple and peach crops in the Southeast.

Thus, the role of federal crop insurance program is greater than at any time in its history. Without a strong program, farmers cannot be expected to grow the new as well as existing crops that are necessary to meet our energy needs and feed the nation. Certainly, a weaker federal crop insurance program would undermine America's drive to greater energy self-sufficiency while maintaining food security.

The modern crop insurance program is an indispensable marketing tool. Crop insurance allows producers to market in advance of production as well as harvest with an assurance that if the crop fails, they can buy replacement bushels to fulfill their contract. Today, it is more common place than ever, and the practice continues growing rapidly, for farm advisors to explore with producers how crop insurance offers the opportunity to more aggressively market, especially in times of high prices, extracting profits from markets, while they are available, in order to better control their financial destiny. With the confidence of this crop insurance backstop, producers can extract profits from the market place at no cost to the Government. The importance of crop insurance in marketing farm commodities today cannot be over emphasized, and if the program continues to grow, marketing assistance will become an even greater benefit in the future. Without crop insurance, farmers would be less likely to implement marketing strategies that allows farmers to take advantage of price increases that occur during the growing season.

One of the reasons farmers have not taken advantage of high market prices that have been available in past is the fear of not being able to satisfy the terms and conditions of any associated contract. Crop insurance, as we know it today, provides replacement-cost coverage that allows farmers to act on marketing opportunities. Increased numbers of farmers using marketing tools is a strong indication that, as a group, they are gaining confidence in making money from the market by forward marketing.

Crop insurance works well because it is a unique public-private partnership. History has demonstrated that without Government subsidies and reinsurance, farmers could not afford to pay the premiums that are necessary for a national crop insurance program. History has also demonstrated that without the private sector delivery system, the federal government could never sell and service the program efficiently.

From 1938 until 1981, the USDA was solely responsible for delivering the federal crop insurance program. However, in those years, crop insurance was not an extensive program and certainly not the national program that it is today. In fact, it was more or less only a token program – one that was available only for a few commodities in a few counties in a few states. In this time period, the private insurance industry marketed only crop hail policies.
Beginning in 1981 and continuing until the late 1980s, Congress authorized a transition period for the federal crop insurance program, during which it was delivered both by USDA, through a structure known as "master marketers," as well as private sector companies, through a structure known as the "standard reinsurance agreement" (SRA). During this period, the program was not considered successful and it never insured more than a third of the eligible acreage in the country. Not until it was completely delivered by the private sector and after receiving increased funding in the 1994 crop insurance legislation did the program begin to approach its current level of success.

Congressional funding for the program has also played a significant role in helping achieve the program's current level of success. Increases in premium subsidies have resulted in increased participation levels and increased coverage levels. Increases in coverage and participation have been shown to be directly linked to the amount of program funding. It can be assumed that any reduction in funding for the program will have negative impacts on farmers' participation and coverage under the program, resulting in a reduced safety net and an increased demand and need for other less efficient and more costly forms of Federal assistance.

The Program Can Be Improved

With the program having successfully grown through a series of incremental developments, especially over the last 25 years, opportunities to continue expanding coverage and improving the value of the crop insurance program to farmers should be considered and evaluated with input from the private sector insurance delivery partners.

The "Gap Coverage," identified by USDA in its Farm Bill Proposals for Crop Insurance (now referred to as "Supplemental Deductible Coverage," (SDC) by RMA) identifies one option for providing additional disaster assistance. Although sufficient details are not available at this time to fully evaluate, AACI is concerned about the possibility the concept includes incentives for farmers to buy less individual coverage.

Private sector partners certainly want to work with Congress and the administration to identify positive changes and continue improving the crop insurance program for the benefit of the nation's farmers, including the development of an additional, workable disaster assistance option. Properly structured, we believe an insurance-based program would successfully provide additional or bonus disaster assistance in county-wide natural disaster instances. Crop insurance companies and agencies are interested and ready to work with all parties to accomplish this goal.

In that regard, AACI recommends establishing, as an additional disaster assistance provision for farmers, the County Crop Disaster Plan (CCDP), with the following objectives and benefits:

- Provide a crop insurance solution to demands for additional disaster assistance payments.
- Encourage crop insurance participation.
- Encourage producers to move to and maintain a significant level of crop insurance coverage on an MPCI or revenue coverage plan.
- Use the private sector crop insurance system to deliver the additional disaster assistance payments.
- Provide additional disaster assistance payments when the crop county loss ratio exceeds a trigger level to farmers who have received indemnity payments.
- Benefits of this option include a built-in qualification test and no increase in moral hazard.

Another opportunity to improve the program is in updating provisions of existing legislation that are no longer relevant given the economic realities. In this regard, AACI believes Section 508(e)(3), known as the Premium Reduction Plan (PRP) that was added by P.L. 103-354 in 1994, is a provision of the Federal Crop Insurance Program that should be eliminated, as the current farmer participation levels and A&O subsidy amounts are vastly different than when the provision was incorporated into law, and the provision is no longer necessary or relevant.

The Program Can Be Harmed

The crop insurance program operates, for the most part, under legislation that is separate from the Farm Bill. A case can be made that the program successes noted earlier have been enabled by the legislative authority being separate from farm bill provisions. Successful insurance programs rely on stability, and crop insurance legislation that is separate and insulated from the recurring farm bill process has helped ensure the stability of the crop insurance program. We suggest that changes to the crop insurance provisions should only occur in legislation apart from the farm bill process as was the case in 1994 and 2000.

Some Farm Bill proposals for crop insurance regurgitates policy changes that have either been tried in the past and found wanting or have been proposed in the past and have been rejected because they would take the program in the wrong direction. Some newer proposals are simply wayward in nature and should be avoided. Proposals that would take the crop insurance program in the wrong direction should be rejected. **In this regard, the following USDA proposals especially should be rejected:**

a. Increase the net book quota share from the current 5 percent to 22 percent and provide ceding commission to the reinsured companies of 2 percent of premium.

b. Cuts to the farmer subsidy to deliver the program such as reducing the administrative and operating expense reimbursement by 2 percentage points for all policies other than CAT policies.
c. A mandatory purchase requirement for farmers who participate in commodity programs.
d. Cuts to premium subsidies that reduce participation.

Crop insurance is a federal government program developed to satisfy certain public policy objectives regarding aspects of risk management inherent to production agriculture enterprises. Companies are required to sell and service a predetermined and pre-approved program to all farmers, ranchers and growers. They are not free to turn away higher –risk farmers or smaller farmers whose premiums are not large enough to cover the cost of sales and service. They are required to sell to all farmers and for all insurable commodities in a state where they do business.

A study released in September, 1989, by Arthur Andersen & Company concluded that USDA experienced delivery costs twice the amount of the private sector participants, on average. Specifically, the study reported that for 1987 total delivery cost by private sector companies equaled 43.17 percent of premium while for master marketers the total was 85.30 percent. This finding and other factors supported a move by Congress to transition to sole delivery of the federal crop insurance program by private sector insurance companies and agents.

Some reports raise questions about certain aspects of the cost of the modern federal crop insurance program. Federal cost of the program includes funds to pay a portion of the farmers' premium amount for each policy and funds to pay approved insurance providers' (AIPs) total expenses for selling and servicing policies. Therefore, in general, increased federal cost of the program reflects implementation of congressional intent to expand and enhance coverage of farmers across the nation.

The congressional objective has been to have a federal crop insurance program that is an efficient and effective production agriculture risk management tool equally and universally available to all farmers across the nation. Therefore, premium support cost will always be consistent with the level of farmer participation in the program. To the degree that the congressional objective is more fully satisfied, meaning more farmers participating and purchasing more protection, premium support cost increases.

Federal reimbursements for delivering the crop insurance program do not cover the costs of the private sector. Normally, insurance premiums are expense loaded, which means the administrative costs of selling, servicing and delivering the coverage are loaded into and are a part of the premium. This is not the case with crop insurance. Rather, the government pays these costs on behalf of policyholders. This policyholder subsidy, known as administrative and operating (A&O) reimbursement, is paid to private sector companies that deliver the program to offset the costs of selling and servicing of policies. However, the A&O amounts paid fall short of covering companies' expenses for delivering the program. Currently, the average percentage A&O reimbursement rate is approximately 20 percent of premium, which is down from an average high of more than 32 percent in the early 1990s. Companies indicate that the current A&O reimbursement rate does not cover all policy selling and servicing expenses.

Company statements regarding their total selling and servicing cost are consistent with the conclusion of an April 1997 GAO Report to Congressional Committees in which the analysis indicated that the reimbursement rate would need to be 26.5 percent of premium to "adequately reimburse companies for their reasonable expenses of selling and servicing crop insurance."

Administrative and operating (A&O) reimbursements and underwriting gain opportunities are the elements for attracting and keeping private companies, agencies and capital in the business. To the extent that A&O reimbursements are insufficient for the sale and servicing of crop insurance, these expenses must be met through underwriting gains.

The press often makes the mistake of reporting underwriting gains as profits, thus conveying the false impression that the industry is making huge profits. Both A&O reimbursements and underwriting gains are **gross revenue** earned by approved crop insurance providers (crop insurance companies) under the terms and conditions of the USDA developed and approved SRA that each company must agree to and sign in order to be an eligible program participant. **They are not profits. All businesses, including approved crop insurance companies and affiliated agencies, must subtract all expenses from their gross revenue in order to determine their profits.** These expenses include unreimbursed delivery expenses, reinsurance premiums, the building of reserves for loss years, taxes on earnings and other expenses.

Reimbursement of delivery expenses and the potential for underwriting gains do not over compensate for the risk taken by crop insurance companies. Crop insurance is a risky business, especially when compared to other lines of insurance and taking into consideration the nature of the risk associated with production agriculture enterprises relative to the risk in other insured ventures. Multiple studies have shown that crop insurance profitability is lower and more volatile than other lines of property and casualty insurance (Deloitte and Touché 2004, Price Waterhouse Coopers 1999 and 1997, Milliman and Roberts 2002). Indeed any analysis of Best's Aggregates and Averages will demonstrate this fact. The Deloitte and Touché study reported a 10 year profitability measure of 7.9 percent for the crop insurance program with a standard deviation of 12.9 percent while other lines of property and casualty insurance ran a 12.7 percent return with an 8.9 percent standard deviation (1992 – 2002).

The increased cost of operating a successful, nationwide crop insurance program should not be viewed as a large "piggy bank" from which to take money to fund other programs. Crop insurance cost is driven largely by the level of success of the program in meeting Congress' public policy objectives for the program to be an efficient and effective risk management tool that is fairly and equitably available to all farmers regardless of size, location or enterprise. However, in addition to participation rates, commodity price changes have a significant impact on program cost, resulting from the impact on total amount of liability protection provided to farmers that companies have to properly manage. A historical characteristic of commodity prices is that they do change – increasing as well as, unfortunately, decreasing. Regardless of whether prices are increasing or decreasing and regardless of whether resulting A&O reimbursements fully cover costs, companies must effectively manage program liability to be viable in the long-term to have the capacity to provide stable and dependable service and protection to farmers.

Keith Collins, Chief Economist at USDA, testified in March, 2006, before a House Agriculture Subcommittee that program liability or coverage is up about one-third and program acres is up about one-fifth since the passage of ARPA in 2000. In that testimony, Collins also stated, "Recent increases in the administrative and operating expense reimbursement and underwriting gains have strengthened the financial performance of the companies and encouraged new entrants and we believe that will help increase service to producers."

Any raids on the crop insurance funds will result in higher premium costs and less service for farmers. They would signal a retreat from all the gains in building the best crop insurance program in the world. It would be a retreat from ARPA and all the efforts made in previous legislation and program changes to provide essential risk management for America's farmers, ranchers and growers that would also be readily accepted by lending institutions and commodity markets.

Closing

Thank you for this opportunity to present AACI's views about the federal crop insurance program. I look forward to further discussion with Members of the Subcommittee today.

STATEMENT OF KATHY FOWLER, PRESIDENT, NATIONAL ASSOCIATION OF CROP INSURANCE AGENTS, MEMPHIS, TX

Ms. FOWLER. Chairman Etheridge, good morning. Good morning, Ranking Member Moran. I am Kathy Fowler. I am here on behalf of NACIA, National Association of Crop Insurance Agents. I would like to take this opportunity to thank you and consider it a real privilege to be here.

Actually, I am an agent, myself, located in a small community in the lower Texas panhandle, population 2,500. I come here today with a whole different perspective from the other members on the panel. I represent an organization that is solely supported and represents the interests of crop insurance agents across the Nation. Actually, we are small business folks operating in the ag community where the crops are grown. We have a lot of involvement with community projects, little league games, support FFA projects/4–H projects. We become very involved in support with the local kids by purchasing these projects, like stock shows. So therefore we have a lot of communication and a lot of interaction with producers. We start with the children at a very young age, along various avenues for the communication.

Agents are very dedicated in their work. Actually, at my agency, we put about 75,000 miles a year on vehicles. My husband seems to think that I have a love affair with a laptop, watching the Weather Channel or the radar screen. Agents are on the frontline. We are out there, we are the first phone call, so it is imperative that we respond and unfortunately, mother nature does not always react to business hours Monday through Friday or 8 a.m. to 5 p.m. So when that producer calls, and I live in west Texas and we have a sandstorm, that has wiped out your entire crop, the phone rings the first thing the next morning. “Hey, what are my options in order to stay within the policy guidelines? I think I have lost my crop. Can I replant? Do I have to replant? Is there a late plant provision? Is there a replant payment? Just exactly where am I at?” And lo and behold, I have several real life experiences, but one of them is the pastor calls and says, “Hey when can we stop the sand from blowing? You know, it is filling up the church?” So we have to be really reactive and really responsive.

And this program is huge. It is very complex. There are a lot of different things out there. We have come a long ways to really pattern this program for the individual needs of the producer. It is exceptionally difficult to deliver and very different from traditional insurance. If you go out and you purchase a homeowners policy or an auto policy, you set the parameters of the policy, pay the premium and you are good to go. You come around for an annual renewal. Unless you have made a trade on an auto or purchased a new home, a lot of times there is very, very little interaction or communication with your agent. You pay the bill and you continue your insurance policy. What we are looking at today with farmers, it is imperative that you review that process every year. There are program changes; there are policy changes. We recalculate a farmer’s yield every year. We were looking at virtually very little dryland production in my area last year, so those yields have gone down. Price selections change. If you see the price selections on the grain crops, they have gone up substantially. So therefore, if your yield has gone down, price selection is up, you may be okay. If you are planting a different crop, you may need to take a look at some different coverage, move up a level. And we spend a lot of time educating the lender, that way the lender, as he understands what the program is there to provide and we meet his expectations.

In my testimony, I stated that there are 21 different plans of insurance. Throughout an individual crop year, there are 23 sales closing dates or deadlines, so that means if that producer wants to take out coverage, he has to be within that deadline period. As proposals move forward, the permanent disaster, the supplemental coverage, I truly encourage you to utilize the expertise of the crop insurance agent. The infrastructure is already set. We have quite an investment in the technology. We have a proven track record to deliver this product in a timely manner to meet the requirements of the producer and the lender. And many agents started in this business when it went private in 1980. That is 26 years of expertise and knowledge. To the producer, this is a people business. We are here to have communication with that producer so that we can help him make a decision on what risk management products meet his needs the best, and that starts all the way from my staff to the equipment dealer, the fertilizer salesman, the lender, and actually the producer, your constituent.

I am very proud to be a part of this delivery system that offers a safety net for farmers and I truly believe in what I do. I want to thank you for your continued support.

[The prepared statement of Ms. Fowler follows:]

Testimony of Ms. Kathy Fowler
President
National Association of Crop Insurance Agents
before the
Subcommittee on General Farm Commodities and Risk Management
Committee on Agriculture
U.S. House of Representatives

May 1, 2007

Good morning Chairman Etheridge, Ranking Member Moran, and Members of the Committee. As previously mentioned, my name is Kathy Fowler, and I am president of the National Association of Crop Insurance Agents (NACIA). I thank you for the opportunity to testify before this Committee, and would like to start by giving you some background on who we are and what we do, and then discuss the upcoming Farm Bill reauthorization as it relates to the crop insurance program.

Agent Background

NACIA is the only organization that represents the sole interest of crop insurance agents, those who are on the ground, in the fields every day, talking to farmers and delivering the program to the producers. Our membership is comprised exclusively of agents and extends nationwide. We are community members and small business people offering meaningful employment in rural America. Agents are involved in community projects, school events, little league games, and lending support to FFA/4-H projects, while working with farmers on a day-to-day basis.

As agents, we are the individuals that provide a conduit between the approved insurance providers (companies) and the insurance recipients (farmers), and work to fully implement the program, ensuring that the most appropriate product is properly utilized to maximize the benefit and usefulness of the program. We serve as the primary line of communication between farmers and RMA, acting as a source of up-to-date information and providing education. We strive to stay current on changes in agriculture at the grassroots level across the nation. On a continual basis, we have thorough conversations with growers regarding every aspect of agricultural production.

A wide variety of products are offered through the federal crop insurance program, including 21 different plans of insurance covering well over 100 crops, with the 2007 crop year extending from November 2005, through July 2007, with 23 sales closing dates during that time period. RMA states that there are nearly 30 new insurance products under various stages of evaluation or development. It is our job as agents to know the fine point details and differences in coverage, in order to determine the product that proves to be the best fit for each farmer's individual operation. We review every provision of the product with the farmer, discuss various features of the policy, and mutually determine which coverage best serves the needs of the farmer by crop and by county. Renewals are performed each year, using the same process. Reviews are necessary due to changes in policy procedures, crop prices, and yields, which impact the insured's coverage and cost. As producers change to viable alternate crops to meet the demand of the marketplace, crop insurance must become pro-active in helping growers achieve a solid risk management plan acceptable to lenders.

In addition to introducing new products, RMA issues numerous changes to guidelines and regulations on a crop year basis to further clarify and enhance policy options. These notices require considerable review to ensure they are implemented in the proper manner and in accordance with regulation. We receive training, seek clarification and then provide updated communications by mail, farm meetings, agency websites, email, and personal calls to translate the regulations to farmers, playing a vital role in the proper administration of the program. Through this endeavor, we expose farmers to new insurance products that could be more beneficial to their operation. We also work to ensure that current insurance products are used in the most efficient, cost-effective manner. In addition, it is part of our job to fight waste, fraud, and abuse in the program and to make certain that small farmers and those with limited resources have adequate access to participation in the program.

Crop insurance, by its very nature, is extremely different from, and more complex, than your more mainstream insurance policies. An agent's job is unique, requiring both in-depth knowledge of the crop insurance program and the very details of crop production, as well as each farmer's individual operation. Farm visits are necessary to assist the producer in accurate reporting and policy regulation compliance. This job is not something that could be accomplished directly from Washington, or even through regional government offices. It is not something that could be administered totally online through a computer program. An agent's job requires personal relationships, personal knowledge, and personal expertise. Agents offer open lines of communication and availability of personnel in order to respond quickly when catastrophic events occur.

Farm Bill Reauthorization

As this Committee considers Farm Bill reauthorization, it is important to note several things. In this time of fiscal limitations, many have looked at the baselines of the various Farm Bill programs to see where the money is being spent. The baseline of the crop insurance program is one of the few that have risen since the 2002 Farm Bill. There are a multitude of programs, both new and existing, that are searching for funds. Many will point to the crop insurance program as a source for financing, stating that it is a program that could be reformed to produce savings. We would, however, assert that this view is extremely erroneous. The reason the expenditures have risen from the projected levels in 2002 is that the program is successfully doing what it was created to do. While not currently a perfect program, crop insurance is providing coverage to farmers and serves as their safety net during major crop losses.

Crop Insurance has become a powerful tool for farmers in many ways, including for the use of record keeping for data and management purposes, allowing integration with GPS systems, and forward contracting their cash crop. Lenders value projections when determining cash flow analysis for loans and many require coverage as collateral. Lenders base long term land financing on the stability of crop insurance so we must act responsibly and continue to improve our existing program.

According to RMA, in 2006, the crop insurance program distributed about 1.1 million policies, covering approximately 242 million acres with nearly 51 billion dollars in protection. Many levels of crop insurance reach 70 to 85 percent of potential crop value, and approximately 80 percent of major program crop acreage is insured. Crippling a program that is serving its intended purpose would not be wise, and would be extremely detrimental to our nation's agricultural producers. The crop insurance program needs to remain intact, as a consistent and stable program available to producers who already face considerable unpredictability in their occupation.

Some groups have questioned gains by those administering the program over the last year as evidence that the crop insurance program is in need of reform. We believe that it is extremely shortsighted to judge the merits of a program on a short-term basis. What the future holds for crop production is outside the realm of knowledge. Changes in climate have had drastic consequences. In 2007, we have already had serious freeze losses in California and the Carolinas. Just in the past three weeks, New England states have experienced flooding, along with drought induced wildfires in Georgia. We have forecasts of another round of hurricanes hitting US coastlines in the approaching 2007 summer.

Were there as many comments regarding the crop insurance program as compared to complaints about FEMA and the flood response in the southern coastline? The fact remains that a strong crop insurance program delivered by local agents allows for grower participation, with protection for a wide variety of crops. Now is not the time to damage the system that has worked well. The crop insurance program should remain strong and ready to assist producers presently and in the future.

Traditionally, the crop insurance program has not been a part of the overall Farm Bill reauthorization process, excluding minor tweaks to the program. It has been considered as separate legislation and funded separately from the Farm Bill. It has not been subject to threats to its funding, and has not been viewed in the context of one of many agricultural programs. We would encourage the consideration of this when contemplating changes to the program. Do not view crop insurance as simply a minor piece in the Farm Bill puzzle, as that is not its legislative history or precedent. We need to ensure that any decisions or changes improve our present crop insurance program and serve our farmers' risk management needs, as opposed to simply making changes because funding is needed for new initiatives or to benefit other non-related entities.

The crop insurance program is an extremely intricate and detailed program, with many inter-related aspects. We would urge extreme caution and the consultation of those well versed in the program's operations before making any adjustments. The unintended consequences of changes to the program, even if viewed as minor, could have drastic implications to the program as a whole and lead to unforeseen negative impacts on farmers. It may be helpful to view the program as a house of cards, which would benefit from strengthening and additional support, but could crumble if the wrong alteration were made in the wrong place.

Proposals

There have been several proposals introduced and discussed in the context of the 2007 Farm Bill reauthorization relating to or affecting the crop insurance program in various ways. Despite the ever-increasing involvement in the crop insurance program, calls for ad-hoc disaster relief are heard every year. Many people believe that permanent disaster relief of some kind will be included in the 2007 Farm Bill. If this is to be the case, we would strongly urge that it be designed in a way that includes crop insurance to be delivered through the currently established infrastructure. Crop insurance agents are the only individuals with the on the ground knowledge, experience, and expertise for the efficient provision of a nationwide, permanent program.

Another idea that has been proposed is revenue insurance. We believe that revenue insurance would be costly and inefficient, and would not be a method that would adequately address what is intended – protection for farmers from significant crop loss. By definition, insurance protects a quantitative item, not a variable by-product of transactions. There are too many influencing factors outside the realm of management for revenue insurance to be a plausible solution to provide a sufficient safety net for those who provide our nation's, and much of the world's, food supply.

While not a new idea, Premium Reduction Plan (PRP) also has potential to damage the crop insurance program. As I previously mentioned, the crop insurance program by nature requires an in-depth personal knowledge of both the available products and the unique situations of each individual who wishes to participate. Certainly we are not against a reduction in premium if offered equally to all farmers irrespective of carriers. Premium reductions could be offered based on better yields thereby encouraging good farming practices and rewarding a producer who accomplishes these goals.

We want to encourage RMA to expand and enhance the newly released Pasture, Rangeland and Forage Pilot program. This program reaches not only farmers but for the first time ranchers and affords them a dependable risk management program. PRF has opened up new opportunities for farmers and ranchers who have been overlooked in the past. This product has resulted in numerous first time participants in a crop insurance program, and we encourage additional education in this sector. Reports confirm that interest in the product has exceeded original expectations.

Closing

Since 1993, the federal crop insurance program has gone through major legislative overhaul and internal reform and upgrading. Despite some problems inherent in any program, the crop insurance program has become an extremely flexible, user-friendly, affordable, and effective program, successfully fulfilling its intended purpose. It is the premier federal safety net for agricultural producers against the hazards of weather and natural disaster. For the 2006 crop year, the federal crop insurance program was able to rescue farmers suffering losses with more than $3.2 billion in indemnities. This was done just as Congress intended, automatically by function of the program, without any effort or special action by Congress. In addition, the program has consistently proven its actuarial soundness, achieving a loss ratio of less than 1.00 in 8 of the past 14 years and less than 1.06 in 13 out of the last 14 years – an average well below the statutory target of 1.075. The federal crop insurance program is viewed as a tremendous success, both domestically and abroad. Other nations, including Brazil, France, and Japan, have observed our crop insurance program and are attempting to develop one of their own.

While the crop insurance program's successes are due to Congress, RMA, insurance companies, crop insurance agents, and the farmers themselves, we would like to remind you of the unique role agents play in the provision of this program. Agents are proud to be a supportive part of

America's agricultural safety net for farmers who provide low cost food and fiber to our nation's consumers.

Thank you again for the opportunity to testify, and we appreciate your continued support of this program.

STATEMENT OF STEVEN C. RUTLEDGE, CHAIRMAN, CROP INSURANCE RESEARCH BUREAU, INC.,; PRESIDENT AND CEO, FARMERS MUTUAL HAIL INSURANCE COMPANY OF IOWA, WEST DES MOINES, IA

Mr. RUTLEDGE. Mr. Chairman and Members of the Committee, my name is Steve Rutledge. I am President and CEO of Farmers Mutual Hail Insurance Company of Iowa. I also currently serve as Chairman of the Crop Insurance Research Bureau, or CIRB. CIRB is a national trade association composed of insurance companies, reinsurance companies and brokers involved in the crop insurance business. I appear before you today on behalf of CIRB and thank you for the opportunity. Since I am the last witness, there may be a little bit of repetition, so I would ask you to bear with me in that regard.

The Crop Insurance Program that exists today is the centerpiece of our agricultural safety net. Approximately 80 percent of our Nation's farmers recognize the value of the program and invest premium dollars to participate. The benefits to the producers are created by shifting the risk to the government and in no small part, to private insurers and reinsurers. As we enter the 2007 crop season, the possibility of paying a very large price for assuming that risk has never been greater. Many crop prices are near historic highs and these increases track through to the Crop Insurance Program. The liability assumed by the public-private partnership in 2007 will be immense. Although the past 3 years have been a profitable period for SRA holders, all of these profits, and then some, could be erased in the blink of an eye, given the level of risk that exists for this year.

Two weeks ago, CIRB members visited Capitol Hill and the most common theme expressed during those meetings was that—excuse me—although some needs have yet to be met, overall, the program is providing great value to our Nation's farmers. There was, however, a desire to better understand the impact of specific proposals and a concern about the perception that SRA holders are making excessive profits. Any discussion of profits must begin with the understanding that what RMA and others commonly refer to as underwriting gains, it does not translate directly to profit for SRA holders. Underwriting gains are based on the assumption that a company's expenses to deliver the program are equal to the expense reimbursement provided by the SRA. Currently, the expense reimbursement averages about 20½ percent. Most companies' actual expenses are considerably higher and the gap between the two must be filled from underwriting gains before any true profit can be produced. Possibly because of the perception I just described, USDA has proposed that RMA assume 22 percent of the industry's underwriting gain or loss.

The reinsurance provisions of the SRA provide a very good first line of defense against a catastrophic loss, but it is just the beginning of an adequate reinsurance program. Virtually all SRA holders buy a significant amount of commercial reinsurance to protect our financial stability. The proposed quota share would make crop insurance less attractive to reinsurers and some would redeploy their capital. The result is that an absolutely essential piece of the risk management process would be damaged. In addition to the havoc less reinsurance capacity would create for the SRA holders, we too would suffer financially. RMA would assume 22 percent of the company's net premium and losses, but little will be done to make up the gap between the expense reimbursement and the actual expenses that I described previously. And since the opportunity to make up that difference from underwriting gains has been eliminated, companies are guaranteed a loss on every dollar taken by that quota share.

Another proposal calls for a further reduction in the expense reimbursement paid to SRA holders. As you know, the SRA was renegotiated in 2005 and cuts to the expense reimbursement were implemented that year, with additional cuts implemented last year. At some point, efficiency must give way to poorer service to producers. I think we are at that point and any further cuts will only increase the potential that one or more, probably of the smaller SRA holders, will choose to exit the program.

Few, if any, insurance products are as complex as the Crop Insurance Program. Crop Insurance Program cost is driven partly by this complexity, but to a larger degree by the level of success of the program. Certainly the cost of the program has grown over the years, but so has the amount of crop value that is being protected. Suggestions that money from the Crop Insurance Program should be diverted to help fund other projects is possibly shortsighted. The Crop Insurance Program needs stability above all else. By assuring adequate funding of the program, its future and that of American agriculture will be secured. Thank you for your time and attention.

[The prepared statement of Mr. Rutledge follows:]

Testimony *of*

STEVE RUTLEDGE, President
Farmers Mutual Hail Insurance Company of Iowa

Chairman
Crop Insurance Research Bureau, Inc.
(CIRB)

Mr. Chairman, Members of the Committee, my name is Steve Rutledge. I am President and CEO of Farmers Mutual Hail Insurance Company of Iowa located in West Des Moines, IA. Farmers Mutual Hail has been in the business of offering risk management tools to agricultural producers of the Mid-West for over 114 years, and today writes both private hail insurance and federally reinsured Multiple Peril coverage in 15 states. I also currently serve as Chairman of the Crop Insurance Research Bureau (CIRB) of Overland Park, KS. CIRB is a national trade association composed of insurance companies that write federal crop insurance as well as private crop-hail insurance, reinsurance companies, reinsurance brokers and other organizations with an interest in the crop insurance program. A list of CIRB members is attached to my testimony. I appear before you today on behalf of CIRB, and thank you for the opportunity to offer testimony to the Committee on its behalf.

By way of background, CIRB members are, for the most part, small to medium size crop insurance companies. These insurance company members bring to the partnership a wealth of knowledge about the federal crop insurance program and are committed to providing risk management support to the farmers and ranchers of this nation. Our membership also includes members of the reinsurance community – an industry that is vital to both the crop hail and federal crop insurance programs. Our reinsurance members are some of the most significant in the world in terms of their involvement in the crop insurance program.

In my testimony I will attempt to illustrate the importance of the public – private relationship in the delivery of the federal crop insurance program, the necessity of continued support by private reinsurance companies in managing risk related to the program, and finally the potential impact of proposed changes to the federal crop insurance program on both segments of the industry. In addition, I will examine the potential impact to producers of some of the various changes currently proposed and also provide a few simple comments on the current status of the crop insurance industry.

HISTORICAL PERSPECTIVE

The crop insurance program that exists today is the centerpiece of our agricultural safety net and is the envy of the rest of the world. There may be no better illustration of the need and value of the program than the simple fact that approximately 80% of our nation's farmers recognize the value of the program and invest premium dollars to participate in the program.

The federal crop insurance program currently provides a level of security and flexibility for American agriculture which likely exceeds the expectations existing when the public/private partnership was first legislated into being more than 25 years ago. Today, in addition to providing protection for yield loss, price protection is also available with the revenue plans of coverage that comprise about 80% of the total insurance sold. As you are probably aware, the majority of revenue products were initially developed by the private sector. This type of insurance coverage not only provides considerable protection for producers, but also provides another level of security for lenders and increases the ability of farmers to access the operating loans necessary to get crops in the ground. Today's farmers are excellent business managers and everyday more and more recognize the value of pro active marketing. Revenue insurance plans have also greatly increased the motivation and flexibility of producers to develop professional plans to market their crops by reducing the risk involved in this process to a much more manageable level. Clearly, the contribution to the growth and improvement of today's crop insurance program by the private companies who cooperate with government to deliver the coverage has been substantial.

As we look to the future of agriculture in this country, we believe that a viable crop insurance program is critical. I doubt the younger farmers of this nation who struggle to acquire the resources necessary to begin a successful farming operation could even contemplate a career in farming without the federal crop insurance program. And, clearly, we need more youth in agriculture. Simply put, although there are still some issues yet to be resolved, the value of the federal crop insurance program to American agriculture cannot be overstated.

CURRENT PERSPECTIVE

But here's the worry. The benefits to producers are created by shifting risk to the government, and, in no small part, to private insurers and reinsurers. As we enter the 2007 crop season, the possibility of paying the price for assuming that risk and the potential magnitude of the indemnities paid has never been greater. Many crop prices are near historic highs. These increases track through to the crop insurance program. The base price for corn, for example, has increased more than 60% compared to the 2006 base price. For soybeans the increase is about 30%. Many other crops have also realized significant prices increases. The liability assumed by the public – private partnership in 2007 will be immense.

The past three years have been a profitable period for SRA holders. Traditional insurance principles tell us that companies need good years to build capital to weather the storms of the bad. Please see Exhibit D. Clearly the profits of the past three years - and then some - could be erased in the blink of an eye. Given the level of risk which exists for the 2007 season, it could well be this year. As an example, our best estimate is that a 30% price decline in corn and bean prices, even assuming there is no loss of yield, would cause the companies to have underwriting losses for the year. Respectfully, I would suggest that now is not the time to cut funding to any part of the crop insurance program.

IMPACT OF PROPOSED CHANGES

In the past few weeks other members of CIRB and I have had the opportunity to visit with a number of House and Senate Ag Committee members and staff. We have had the opportunity to review with them many of the proposals currently under consideration and also to discuss the perspective of various stakeholders in the crop insurance program. I found these meetings enlightening, and believe that, for the most part, we share a similar view of the program.

Perhaps the most common theme expressed during our meetings was that although some needs have yet to be met, particularly declining yield guarantees caused by multi-year losses, overall the program is providing great value to our nation's farmers. We found few, if any, stakeholders who have a desire to reduce that value by making dramatic changes to the SRA.

There was, however, some desire to better understand the impact of specific proposals and a concern about the perception that the SRA holders are making excessive profits. I would like to address the latter concern first and then comment on some of the proposed changes to the SRA.

UNDERWRITING GAINS

Any discussion of profits must begin with the understanding that what RMA and others refer to as underwriting gains does not translate directly to profits for SRA holders. The translation of the phrase "underwriting gains" to the phrase "company profits" is based on the assumption that a company's expenses to deliver the program are equal to the expense reimbursement, or A&O Premium Subsidy as it is known, provided by the SRA. Currently, the government reimbursement for A & O averages 20-21% of the premium for most SRA holders. From this the companies must pay expenses - for example, the money spent on regulatory compliance, technology, sales, loss adjusting, payroll and the like – related to delivering the coverage. The amount of actual expense will vary by company, of course, and I do not have access to those numbers, though they are reported annually by the companies to RMA and I assume they are available to you.

I do note, however, that a GAO report to Congress several years ago indicated that a reimbursement rate of at least 26.5% was necessary to adequately reimburse companies for reasonable expenses. Since the date of that report, ARPA was passed in 2000 and a great deal of additional expense was added for SRA holders due to the cost of compliance with some of its provisions. So in spite of increased efficiency, this percentage is likely a reasonable estimate of the amount spent by many SRA holders today.

If we assume an average A & O reimbursement of 20.5% and actual expense of 26.5%, the result is a 6% invasion of underwriting gains before any actual profit is produced for the companies. Put more simply, FCIC's private company partner has to realize at least a 6% gain on underwriting performance or it loses money. To categorize the underwriting gains of 2006 as pure profit is simply erroneous. Please refer to Exhibit C.

A & O reimbursement is typically reported separately and taken in context could give the impression that this money is additional income to the companies. As is evident from the example I just described, expense reimbursement has already been included in the calculation of profit. And I can assure you, we do not receive this money twice.

PROPOSED CHANGES TO THE SRA

Quota Share

Possibly because of the perception I just described, one of the proposals by USDA requires that RMA assume 22% of the industry's underwriting gain or loss. However, since this change is considered to be a reduction to the budget, the possibility of loss is essentially ignored. Given the amount of risk I described earlier in my testimony, to simply brush aside the potential for significant additional cost to the government from losses on this quota share proposal is fiscally dangerous.

So why would the industry oppose this change, other than the obvious concern of increased government cost due to losses from the quota share? To answer that question, we must look at the role of commercial reinsurance companies within the crop insurance program. These firms also have a huge stake in the continued success of the program, and they too have many concerns about some of the proposed changes. We must share their concerns since the program could not function without their support.

The reinsurance provisions of the SRA provide a very good first line of defense against catastrophic loss, but it is just the beginning of an adequate reinsurance program. Most, if not all, SRA holders buy a significant amount of commercial reinsurance to protect the risk that we retained. This commercial reinsurance is critical to protect the ability of companies to withstand significant losses and still maintain the financial stability to operate in future years.

Reinsurance companies - not only in the crop insurance market but also the property and casualty market - rely on the long term operational stability of the companies they reinsure since it typically takes many years to make up the losses from a single catastrophe. The proposed quota share could take several hundred million dollars of premium from the private sector, and the reinsurance community would lose the biggest share of premium. This would cause the expenses of the reinsurer to go up and the spread of exposure to loss to shrink, thereby increasing their risk. Crop insurance as a class would then be less competitive with other types of insurance causing some reinsurers to redeploy their capital. As one reinsurer put it to me, "Increase quota share = less premium = fewer reinsurers = less reinsurance capacity = fewer SRA holders = LESS SERVICE TO THE FARMER". The bottom line is that an absolutely essential piece of the risk management process necessary for a strong and viable crop insurance program would be damaged.

Aside from the complications this would create for the SRA holders, they too would suffer financially. The provisions of the quota share require RMA to assume 22% of the companies' net premiums and losses, however, little will be done to make up the 6% gap between A & O reimbursement and actual expenses I described previously. And with no opportunity to make up that difference with underwriting gains, companies are guaranteed they will lose money on every dollar taken by the quota share. I hope it is evident to all that this proposal is among the most damaging to the program. Again, please refer to Exhibit C.

REDUCTION IN A & O REIMBURSEMENT

Another proposal calls for a further reduction in the expense reimbursement paid to SRA holders. As you know, the SRA was revised in 2005 and cuts to the expense reimbursement were implemented that year with additional cuts taking place in 2006. Currently, the industry's four largest companies write about 73% of the business. The concentration of the business in the hands of fewer and fewer writers has been a steady trend since the program first started. Not that long ago, more than 50 companies participated in the federal crop program. Today there are 16. Although there are a variety of reasons for this decrease, it is safe to assume that the most compelling has been the need to continue to cut overhead due to the sharp reductions in the A&O reimbursement paid to companies. Please see Exhibit B.

At some point even the economies of scale enjoyed by the larger companies will not be enough to prevent efficiency from giving way to poorer service to producers. We are at that point and any further cuts will hurt all companies although the smaller ones would suffer the most. In some areas of the country only a handful of companies still operate. Again, as one reinsurer expressed it, "Reduced A & O = less income to SRA holders = higher demands on reinsurance terms = lower ROE to reinsurers = fewer reinsurers = less reinsurance capacity = fewer SRA holders = LESS SERVICE TO FARMERS". Maintaining a healthy balance between larger and smaller insurance providers is a benefit to the overall program and I suggest to you that balance needs to be protected.

RENEGOTIATION OF THE SRA PERIODICALLY

Another farm bill proposal involves the suggested periodic renegotiation of the Standard Reinsurance Agreement. As you probably know, the SRA runs on a reinsurance year cycle that begins on July 1 of the year preceding and ends on June 30 of the year current. So, for example, the 2007 reinsurance year began on July 1, 2006 and will end on June 30, 2007. The contract calls for a 180 day notice of cancellation period, so if the SRA is to be cancelled, notice must be given on or before December 31 of the year prior to the start of the reinsurance year. Under ARPA, RMA had the option of renegotiating the SRA once between 2001 and 2005. The 1998 SRA, which was in effect for the 1998 through 2004 reinsurance years, was cancelled for the 2005 reinsurance year and renegotiated with the companies. As of today the industry is approaching the end of its second reinsurance year under the 2005 SRA.

The uncertainty created by a constantly changing SRA is not helpful to the long term viability of the crop insurance program. To further compound the uncertainty with changes imposed by legislation is even more troubling. CIRB respectfully suggests that if changes are deemed necessary to the financial relationship with the reinsured companies, such changes are more appropriately addressed through the contract negotiation process. Our reinsurance partners are also affected by this. Again, as one reinsurer put it to me, "Inequitable negotiation practice = unfavorable terms = limited potential profit = loss of allocated reinsurance capital = fewer reinsurers = less reinsurance capacity = fewer SRA holders = LESS SERVICE TO FARMERS."

If, for example, Congress mandated a renegotiation of the SRA every five years, if necessary, companies would be able to develop a reasonable business plan without fear of midterm changes in the plan that would be detrimental to the uninterrupted delivery of federal crop insurance.

PERMANENT DISASTER PROGRAM

There was a great deal of discussion during CIRB's recent visit with Washington stakeholders about the concept and feasibility of a permanent disaster program. There are proposals which eliminate the catastrophic protection plans of crop insurance and substitute a standing disaster program, and RMA has proposed a supplemental deductible crop insurance product. This product is designed to help mitigate the problem of multi-year losses and also to address some other issues, it could also form the basis, potentially, for some type of disaster program.

Although the cost of a permanent disaster program was frequently mentioned as a limiting factor, possibly prohibitive due to its magnitude, should some version of a permanent disaster program actually come to fruition, I might suggest that the best vehicle for delivery is through the federal crop insurance program. The private partners have surely proven their ability to service the farming community in the most efficient and accurate manner possible.

Although the course of these proposals is uncertain, maintaining the stability of the crop insurance program must take priority.

CROP INSURANCE IS AN EXPENSIVE AND COMPLICATED PROGRAM TO DELIVER

Few if any insurance products are as complex as the federal crop insurance program. The investment in computer systems, software, etc. is immense and due to constantly changing regulations, simply keeping a system up-to-date takes thousands of man hours a year. And as you are aware, RMA is planning a major rewrite of their computer systems during the next 18 months. The cost to SRA holders to rewrite their systems to be compatible with RMA will be significant. As daunting a job as keeping systems current is, this process makes the delivery of insurance to the producer much more efficient and timely.

Cuts to the program could have serious negative effects on program delivery in other ways. Some companies would be forced to reduce support staff from top to bottom making the job of the agent even more complex than it is now. The ability of companies to have in place an effective system of checks and balances to assure compliance with the thousands of program rules and regulations could be jeopardized. The ability to help agents sell and service policies would have to be re-evaluated. Those agents who sell smaller numbers of policies and who need more assistance could be affected. Companies have assumed more and more risk with every change of the standard reinsurance agreement. Again, traditional insurance principles suggest that as companies take on more of the risk, the opportunity for gain should also increase.

MAINTAINING A SUCCESSFUL CROP INSURANCE PROGRAM

Crop insurance cost is driven largely by the level of success of the program in meeting Congress' public policy objectives for the program to be an efficient and effective risk management tool fairly and equitably available to all farmers regardless of size, location or enterprise. Keith Collins, Chief Economist at USDA, testified in March, 2006, before a House Agriculture Subcommittee, that program liability - or coverage - is up about one-third and program acres are up about one-fifth since the passage of ARPA in 2000. In that testimony, Collins also stated, "Recent increases in the administrative and operating expense reimbursement (*note added: While this is true on a simple dollar basis, A & O has decreased significantly on a percentage basis*) and underwriting gains have strengthened the financial performance of the companies and encouraged new entrants and we believe that will help increase service to producers."

Suggestions that money from the crop insurance program should be diverted to help fund other projects is, simply put, shortsighted. The crop insurance program needs stability above all else. By assuring adequate funding of the program, its future, and that of American agriculture, will be secured. Thank you for your time and attention.

EXHIBIT A

CIRB MEMBER COMPANIES

- * ASI-Agriserve, Inc.
- * American Agricultural Insurance Company
  - ++ Arkansas Farm Bureau
  - ++ Idaho Farm Bureau
  - ~~++ Indiana Farm Bureau~~
  - ++ North Carolina Farm Bureau
  - ++ Nodak Mutual Insurance Company
  - ++ Oklahoma Farm Bureau Mutual Insurance Company
  - ++ Virginia Farm Bureau Mutual Insurance Company
- * ARMtech Insurance Services
- ⊙ Collins
- ⊙ Cooper Gay Intermediaries
- * Country Insurance & Financial Services
- * Farm Bureau Mutual Insurance Company
- * Farmers Mutual Hail Insurance Company of Iowa
- ⊙ Guy Carpenter & Company, LLC

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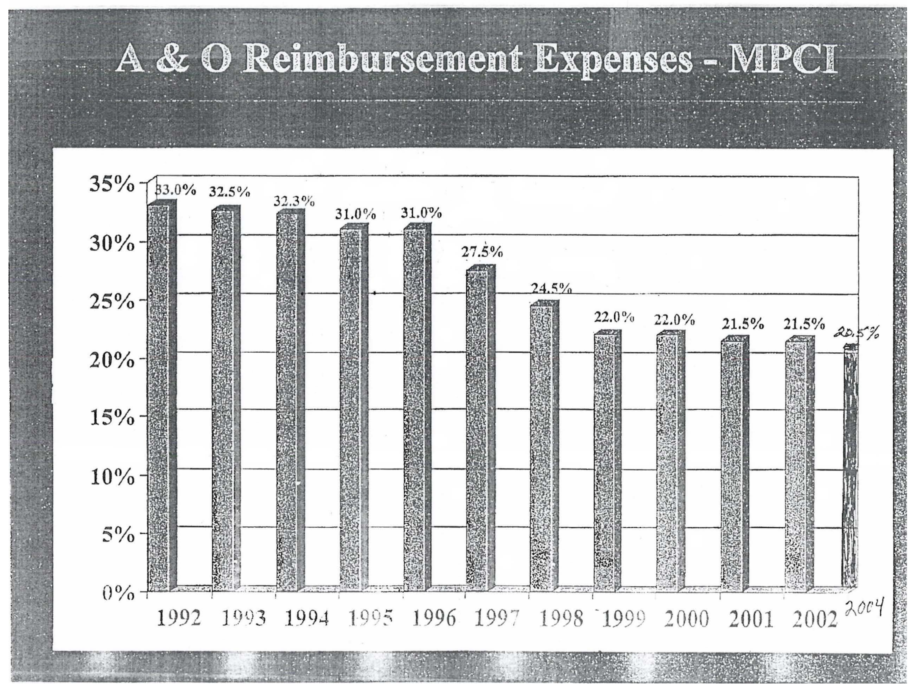
* SRA Holder
++ Members under AAIC's SRA
⊙ Reinsurance company or broker

Associate Members

AON Re
Baldwin Mutual Insurance Insurance Company
Endurance Reinsurance Corporation of America
Mapfre Reinsurance Corporation
National Association of Mutual Insurance Companies
Partner Reinsurance Company of the U.S.
State Farm Fire and Casualty Insurance Company
Totsch Enterprises

EXHIBIT B


A & O Reimbursement Expenses - MPCI
35%
30%
25%
20%
15%
10%
5%
0%
33.0%
32.5%
32.3%
31.0%
31.0%
27.5%
24.5%
22.0%
22.0%
21.5%
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20.5%
1992
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1996
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1998
1999
2000
2001
2002
2004

Exhibit C

Financial Impact of Proposed Quota Share and A&O Reduction

Example of how Administration proposals could affect company with net underwriting gains of 9% on $100 million in premium).

	Current	Proposed
Premium	$100,000,000	$100,000,000
Losses*	87,000,000	87,000,000
FCIC Reinsurance	4,000,000	4,000,000
Additional Quota Share	0	1,500,000
Underwriting Gains	9,000,000	9,000,000
Current A&O	21,000,000	
Proposed A&O		19,000,000
Actual Expenses	27,000,000	27,000,000
Operational Loss	(6,000,000)	(8,000,000)
Net Profit	**3,000,000**	**(5,000,000)**

* *Current FCIC Target Loss Ratio 107.5*
2008 Proposed FCIC Target Loss Ratio 100

Exhibit D

Total Premiums, Liability & Indemnities
1994-2007 (in millions $)

Year	Premium	Liability	Indemnities	Loss Ratio
1988	372	6,000	904	2.43
1989	814	13,536	1,212	1.49
1993	756	11,351	1,655	2.19
1994	949	13,608	601	.63
1995	1,543	23,728	1,568	1.02
1996	1,839	26,877	1,497	.81
1997	1,775	25,459	994	.56
1998	1,876	27,921	1,678	.89
1999	2,310	30,939	2,435	1.05
2000	2,540	34,444	2,595	1.02
2001	2,962	36,729	2,960	1.00
2002	2,916	37,299	4,067	1.39
2003	3,431	40,621	3,261	.95
2004	4,186	46,604	3,208	.77
2005	3,949	44,260	2,364	.60
2006	4,577	49,911	3,391	.74
TOTAL ('94-'06)	**34,863**	**438,400**	**30,619**	**.88**

Note: 1988, 1989 & 1993 demonstrate the risk that looms and the losses that can be sustained. 1988 wiped out all previous gains garnered by companies up to that time.

Exhibit E

2006 Crop Insurance Providers

Rank	Name of Ins. Provider	Premium	% of total
1	Rural Community Ins. Svcs.	$1,254,355,878	26.6
2	Rain & Hail LLC	1,085,711,146	23.1
3	Great American Ins. Co.	548,971,721	11.7
4	NAU Country Ins. Co.	542,701,068	11.5
5	ARMtech Insurance Svcs.	287,272,687	6.1
6	Heartland Crop Insurance	172,057,595	3.7
7	Producers Ag Ins. Co.	148,007,029	3.1
8	Farmers Mutual Hail Ins. Co	138,595,452	3.0
9	Crop 1 Insurance Direct	128,477,440	2.7
10	John Deere Risk Protection	120,150.403	2.5
11	Agro National LLC	116,995,127	2.5
12	Country Mutual Ins. Co.	63,568,863	1.4
13	American Farm Bureau Ins. Svc.	54,082,478	1.1
14	Agriserve	38,060,960	.8
15	Crop USA Ins. Agency	6,575,425	.1
	TOTAL PREMIUM	$4,706,869,897	100

Mr. ETHERIDGE. Thank you. The chair will now recognize the Members for 5 minutes and recognize myself first for 5 minutes.

The GAO recently issued a report and in that report they talked about climate change and its potential impact with regard to Federal insurance programs and it highlights its findings that many of the major private insurers are incorporating some elements of climate change in their risk management practices. Is this occurring in the crop insurance industry, and are companies trying to anticipate problems resulting from climate change? And I would ask each one of you to comment on that as it relates to your segment, as you know it.

Mr. PARKERSON. Mr. Chairman, I think we have a little experience in that report because we had been called by them a couple of times to participate in some of the programs, and we would basically mirror what Dr. Collins has told you and that is that this is based on a 10 year experience. They also have a catastrophe portion in the rating that they make and at this point in time, we think that, in the discussions we have had, part of this is being mixed with the property casualty business. There is a lot of damage, as you well know, in areas with the hurricanes. This has all been brought out and it is extremely true. When you build around the Gulf or on the beaches of Florida or California and those houses get blown down, they cost———

Mr. ETHERIDGE. So you are saying hurricanes and things like that don't affect crops?

Mr. PARKERSON. No, what I am saying is that I think that what we are doing now is being able to adequately adjust to it at this point.

Mr. ETHERIDGE. So you are saying the answer is no?

Mr. PARKERSON. That is right.

Mr. HARMS. I would agree with Mr. Parkerson, that currently we are not. There is nothing that we can really do to anticipate looking ahead, for what may happen. The information I have read, it does not bode well for agriculture in many areas.

Mr. ETHERIDGE. Okay.

Mr. HARMS. Which puts even more necessity to our quota share, to hold as much of that premium as we can and bill the bank for those years that we know are going to be coming, that losses, considerable losses———

Mr. ETHERIDGE. So your answer is no, too?

Mr. HARMS. Correct.

Ms. FOWLER. Yes.

Mr. ETHERIDGE. Is the same true all the way down, no?

Mr. RUTLEDGE. Pretty much. The reinsurance industry employs a lot of modeling agencies to try to model these types of effects, but the duration of the time that we have had to look at them hasn't been adequate to reach any conclusions.

Mr. ETHERIDGE. Okay. Mr. Parkerson supports the Administration's proposal to lower the loss ratio, according to his testimony, to 1.0. But the others of you, what are your thoughts on that?

Mr. HARMS. We would agree with that and we think the program has been operating less than that for the past number of years and we think that is a move in the right direction.

Mr. ETHERIDGE. Okay.

Ms. FOWLER. Go ahead.

Mr. RUTLEDGE. Yes, I would agree.

Mr. ETHERIDGE. Okay. To Mr. Harms and Ms. Fowler, you all mentioned premium reduction plans as a problem. Can you elaborate on how these plans impact the industry and particularly your segment of it? Could you expand on that, please?

Mr. HARMS. Yes. The premium reduction plan is one that we have got a lot of concerns about. Number one, it is based on potential efficiency from the companies' accounting report that is sent in to RMA from 2005 to 2006. A lot of variables occur within that, such as loss adjustment expense, what kind of agents' commissions the companies have to pay to see if, in fact, there is any efficiency between those 2 years. Our feeling is, with the Federal program, that it should not matter to the insured which company they write with as far as any type of a reduction in their premium. Out of the 16 companies, I think there were nine of us that did apply to be eligible for a PRP in 2007.

Mr. ETHERIDGE. Okay.

Ms. FOWLER. From the agent's standpoint, delivery standpoint, not against a premium reduction for producers, but it should be an equal opportunity for all producers within that crop. We don't want to see reduced service to the smaller farmers and currently, the way it is set up it would encourage cherry picking. The other thing too, is that it needs to be irrespective of carriers.

Mr. ETHERIDGE. Okay. If the panel will indulge me on one more final piece here. I would like to just have your comment on this. Let us imagine a farmer had bought a policy for 65 percent of coverage, multi-peril, and he had 500 acres of corn and the price of it was $3. And this year the same farmer buys the same policy, has no change in his APH, but has a price selection of $4, because we are now looking that this might happen. He is going to pay a higher premium for his policy and consequently the crop insurance company that sells him the policy would get a higher administrative and operating cost on that policy, and that would be a reimbursement, of course. It would be a higher reimbursement piece for the government. What additional costs would that company bear in administering the second higher cost policy?

Mr. HARMS. That is correct. I think if somebody could guarantee farmers that they will continue to have $4 corn and $8 soybeans, I think the industry would be very willing to work with the Subcommittee and RMA in looking at ways that we could reduce the cost of the program. But when you look back when we had corn that was $2.50 and soybeans at $5, the actual A&O was probably less than what the companies had as far as expenses.

Mr. ETHERIDGE. But wouldn't you say that farmer is paying the high premium and not getting anything out of it. That is my question.

Ms. FOWLER. Actually, that producer has a higher level of coverage at this point, because he is looking at his acres times the yield times the price selection. So therefore, even though his yield did not change, his coverage has initially gone up. In case he was to have a loss, then he would be paid at the higher price. And agents typically are on an annual renewal basis and by that those premiums and those compensations move up and down with that price selection, so we have to plan for the long term.

Mr. RUTLEDGE. In your example, $4 corn, higher premium, higher A&O reimbursement, a lot of that reimbursement goes right out our door on a percentage basis. The extra dollars, we don't see. The farmer has increased coverage, as Kathy was saying. Actually, our biggest fear is that we could have significant underwriting losses simply from a price decline rather than yield loss: $4 corn in February you don't see very often. That would be the worry.

Mr. ETHERIDGE. We may need to follow that one up. My time has expired and I will recognize the Ranking Member for 5 minutes.

Mr. MORAN. Mr. Chairman, thank you very much. Just a follow-up to Mr. Etheridge's question about increasing commodity prices means increasing premiums. That has been, until recently, one of the more common complaints that farmers are letting their Congressmen know, is my premiums are much more expensive this year. Is there anyone in the crop insurance industry that is receiving an advantage from higher prices, or is that increased premium all required because of the increased risk, the higher indemnity payments that would be paid if there is a loss? Does the increased premium accurately reflect the increased risk due to higher commodity prices?

Mr. HARMS. Well, as you know, the rates are not set by the companies. They are set by RMA. So we have to assume that those rates hopefully will be adequate to cover that additional risk that comes with $4 corn and $8 soybeans. There is more volatility there. The farmers are paying additional premiums. They can reduce their coverage to bring back the premiums to their 2006 level. That is an option that they can pursue and they could have pursued if they felt their 2007 premium was more than they wanted to pay.

Mr. MORAN. Is that a one-time election, the farmer makes that choice?

Mr. HARMS. Correct. It has to be done by that sales closing date for spring crops; that was March 15.

Ms. FOWLER. That is the very point that I made, that you should go back and renew that farmer's coverage every year and make sure he understands in case he needs to make changes.

Mr. RUTLEDGE. Assuming it is revenue coverage, the biggest advantage for the producer would be that he could go ahead and sell his grain at that high price, knowing that he is protected at the end of the year if he does lose his crop, so it is a significant value to the producer. Even though he pays a little bit more, he has got a much higher price he can sell his crop at.

Mr. MORAN. Well, I assume every banker is going to require that to be the case as well.

Mr. RUTLEDGE. Right.

Mr. MORAN. Mr. Rutledge, you indicated a phrase, level of risk this year. It caught my attention. Is there something unique about this point in time, or is the risk of 2007 no different than the risk of 2001 or 2012?

Mr. RUTLEDGE. No, it is different. In fact, we are even looking for different mechanisms to try and protect some of the risk. I don't think, in the history of the program, the base price set in the spring for corn and beans, for example, has ever been $4 or above.

This year it is. For soybeans it is over $8. Typically, if you look at a seasonal chart of grain prices, February, when we determine the spring base price, and October, when we determine the harvest price, are the low points of the year. Now we have got February as a very high price and $2.80 corn is probably average over a period of years. If we end up $2.80 corn this year, with no yield loss, the companies will have an underwriting loss just from that price decrease.

Mr. MORAN. And let me make sure I understand, because I assume a central point of the industry would be that you can't take away our retained earnings, the risks are great, and what you are reminding me is that those increased risks due to higher commodity prices are not covered solely by increased premiums. You have got to carry forward retained earnings in order to cover those losses should they occur.

Mr. RUTLEDGE. Correct. If we would have another 1988 or 1993, when 1988 was the drought and 1993 was the flood, and some other years, I don't know what the losses would be, because we didn't have revenue products in those years and now we do and they are going to greatly increase the extent of the losses when we have another year like that. And with these types of prices, it is a dangerous year.

Mr. MORAN. Have the number of companies, crop insurance companies, increased or decreased in the market?

Mr. RUTLEDGE. When I first got in the business, there were probably between 50 and 60 companies involved in the Federal Crop Insurance Program. Now there are 16—is the number that has been quoted.

Mr. MORAN. We had a couple of entrants, new entrants into the market last year or the year before. Is there a trend there, one way or the other?

Mr. RUTLEDGE. We had a couple of mergers and acquisitions at the same time. You know, one may come out, one may go. It has been steady for the last 3 or 4 years, I would say. Is that correct?

Mr. PARKERSON. That is correct, yes.

Mr. MORAN. My time has almost expired. I have 12 seconds to tell you that I spent my time yesterday in five Kansas counties, eight different wheat fields, and there are significant losses already evidenced by 3 days, as a consequence of 3 days in April of temperatures in the teens and lots of crop insurance issues about what do we do now? It is easy to see the damage. I had the agronomists with me. I had the regional RMA personnel with me. All of us were asked the question by the farmer, what now? And there are some crop insurance issues, but there is some real issues about what a farmer should now plant, plow up, and I would just echo the concerns that if the freeze damage I saw yesterday is any indication of what is to come, there are significant risks in your business this year. Thank you very much, Mr. Chairman.

Mr. ETHERIDGE. I thank the gentleman. I yield 5 minutes to the gentle lady from Kansas, Mrs. Boyda.

Mrs. BOYDA. I will yield.

Mr. ETHERIDGE. The gentleman from Virginia, the Ranking Member of the Committee.

Mr. GOODLATTE. Well, thank you, Mr. Chairman, and I thank you for holding this hearing. I have an opening statement that I will just submit for the record and would like to thank all of these witnesses as they help us find our way through a very important tool for farmers, but also one that is exceedingly complex. When we try to find solutions to make it work better for farmers and work for more farmers, it gets even more complex.

Let me ask you about something that the gentleman from Kansas started asking you about and didn't follow up. We will start with Mr. Harms but I will ask the others to join in. How comfortable are your companies with the premiums established by RMA? Do they sufficiently cover the risk you are taking?

Mr. HARMS. Yes, we are very comfortable with them. I think the results speak for themselves. The last number of years, we have been able to generate a loss ratio that has been considerably below the target loss ratio. So at this stage of the game, we are comfortable that they are probably as good as rates as we can be using.

Mr. GOODLATTE. Do you analyze the premiums of these policies yourself?

Mr. HARMS. Absolutely. Yes.

Mr. GOODLATTE. Mr. Parkerson?

Mr. PARKERSON. Yes, yes, we do. On behalf of the industry, we take a look at them.

Mr. GOODLATTE. And what is your attitude about the rates that they set?

Mr. PARKERSON. Our belief is that RMA is working hard and as indicated, they have taken on in the last couple of years a strong knowledge and have got their data pretty well together and I think those rating systems that they have seem to be working well.

Mr. GOODLATTE. Ms. Fowler?

Ms. FOWLER. Yes, we tend to look at the ratio between the coverage and the premium and actually, the coverage has increased and the premium has gone down according to the ratio procedure there.

Mr. GOODLATTE. So you analyze the policies yourself?

Ms. FOWLER. Yes.

Mr. GOODLATTE. Okay. And do you tell the USDA when you believe the premiums do not accurately reflect the risk?

Ms. FOWLER. Sure.

Mr. PARKERSON. Yes, we do.

Mr. GOODLATTE. What kind of response to do you get?

Mr. PARKERSON. Do you want me? We have definitely had meetings and on behalf of the industry, we have an actuarial department at NCIS and we take a good, hard look at the data and information. We go over and have meetings with them. On behalf of the industry, we meet with our Board of Directors and we have an actuarial statistical committee that reviews these policies and the forms that are there, and we don't hesitate. If we feel that there is something wrong, we go there.

Mr. GOODLATTE. But do you get a good response back?

Mr. PARKERSON. We do in overall purposes. I will be very candid. I think their hands are somewhat tied. Sometimes when we pointed out a shortfall in a policy or a rate, it takes them some time to turn, if you will, the train around because of the regulatory issues that are involved. But yes, they do take it to heart and yes, they do talk.

Mr. GOODLATTE. Well, let me ask you about that. When it takes them time to turn the train around———

Mr. PARKERSON. Yes?

Mr. GOODLATTE.—does it get turned around in that growing season, in that cycle?

Mr. PARKERSON. No, it cannot.

Mr. GOODLATTE. So you are stuck.

Mr. PARKERSON. We are basically stuck if we find a problem or an issue, somewhat stuck with that shortfall through the year, but then work on trying to get it corrected and changed.

Mr. GOODLATTE. Mr. Rutledge, does your organization review these issues?

Mr. RUTLEDGE. To the same extent most every other company does and in general the rates are as adequate as RMA knows how to make them. There may be some options. There are coverage options that are available, but there is just not enough data to know for sure. But yes, in general they are as good as they can make them, I think.

Mr. GOODLATTE. Ms. Fowler, let me ask you. In your testimony, you say that if a permanent disaster program is created, it should be designed in a way that includes crop insurance to be delivered through the currently established infrastructure. I wonder if you have any specific comments on how a crop insurance disaster program would work.

Ms. FOWLER. I guess what my reference really was to the fact that we have the infrastructure to deliver that. We have the data. We have the yields compiled, which are true, actual yields of that producer. And what I was referring to is our ability for the infrastructure, our technology, our computer systems, the interface that we have with GPS and all of those different types of things. We have the ability to turn it around and get it delivered on whatever regulations or compliance issues that you give us.

Mr. GOODLATTE. But you don't have any vision on how to implement something, like what has been proposed, that we would have a permanent disaster program that would require crop insurance and how those two things would work together or if they would indeed work together?

Ms. FOWLER. I guess, very well, they could work together. I have not seen any real details of either one, a permanent disaster. I think you could tweak this along with the program that we already have, since we do have a proven track record that it does work.

Mr. GOODLATTE. Great. Thank you. Thank you, Mr. Chairman.

Mr. ETHERIDGE. Thank you. The gentleman yields back. The gentleman from Georgia, Mr. Scott, for 5 minutes.

Mr. SCOTT. Thank you very much, Mr. Chairman. First, Ms. Fowler, I found your testimony to be very enlightening and intriguing. I would like to ask you to respond to some of the things you said in your testimony, in your stated testimony, that kind of concerned me and I found intriguing. You expressed great concern about the Crop Insurance Program *vis-à-vis* the farm bill. You made statements like crippling a program that is serving its intended purpose would not be wise and would be extremely detrimental to our Nation's agricultural producers. You went on to say now is not the time to damage the system that has worked so well and that the Crop Insurance Program has not been a part of the overall farm bill reauthorization process, and then do not view crop insurance as simply a minor piece of the farm bill puzzle. That seems to me that you are registering some anxieties here about the future of the Crop Insurance Program *vis-à-vis* the farm bill. I wonder if you might expound on that a bit, to make your position clear. Do you feel some threats out there as we tinker with the farm bill, for the Crop Insurance Program?

Ms. FOWLER. Yes, very much so. The crop insurance piece has always been a separate piece from the farm bill, other than tweaking in different areas. If you are talking about reducing premium subsidies, farmers are going to roll back. I mean, they are going to reduce their coverage. Then that is going to offset as far as we are looking at supplemental coverage or permanent disaster or something of that nature. I think we need to offer farmers the stability that we currently have. They have made long-term projections, whether it be in land purchases or equipment purchases. So I think we need to make sure that any time you start making a tweak, that it is awfully hard to get your arms around this huge, complex program, and it may sound good on paper, but all of a sudden, when you apply its reality, it makes quite a significant difference for the producer himself.

Mr. SCOTT. So you don't want to see anything done on the 2007 Farm Bill and the Crop Insurance Program, as it is? No changes, no nothing.

Ms. FOWLER. There is always room to better this program and to make changes, but typically, we are not a part of the farm bill process.

Mr. SCOTT. Yes. Okay. Now, Mr. Parkerson, your concern about adequate funding for RMA and I think you mentioned that there were two areas. Could you explain to us why and how the current data processing system is inadequate? And I think the other area you mentioned where we need additional funding would be in the training area. Could you elaborate on that?

Mr. PARKERSON. Certainly.

Mr. SCOTT. And there is a level of funding that we are currently doing. You are asking for something beyond that?

Mr. PARKERSON. What we are asking for in our testimony, what we meant and are trying to get across here is that, for example, I mentioned that we sponsor training programs and we have meetings across the country if we run into problems and we have asked RMA to participate in. According to my staff and myself, I have been asking them to participate in a particular training phase or understanding a loss procedure and ask for these people to meet us at meetings in the locales and have been told that they don't have the wherewithal to join us in those meetings. And if that is the case, then we are asking that you take a look at that, because their input is key to what we all do. If we don't understand a regulation or we don't understand a handbook and the procedure on how to address a particular crop, then we need that help and that does come up, because we are reading this thing maybe one way and somebody else reading it in a different manner.

Mr. SCOTT. And the data processing?

Mr. PARKERSON. The data processing, I will tell you this, that they are going through some major changes in the computer business and we are very interested and want to know what is going on. It is key. These companies spend millions of dollars on their computers to be able to report and talk to each other back and forth every day. If we don't understand what they are doing and how they are doing it or if they fall short, then that makes us fall short, which could in turn reflect on whether a farmer is going to get paid his indemnity.

Mr. SCOTT. How much money are we talking about? When you say adequate funding, how much?

Mr. PARKERSON. I can't give you that figure at this point. We have talked about it at different times and I would be happy to give you an idea, if you would like for me to.

Mr. SCOTT. That would be helpful.

Mr. PARKERSON. Okay.

Mr. ETHERIDGE. The gentleman's time has expired. The gentleman from Texas, Mr. Neugebauer, for 5 minutes.

Mr. NEUGEBAUER. Thank you, Mr. Chairman. I think you heard Chairman Peterson talk a little bit about something he and I have been having some discussions about and that is the fact that we need to somehow get crop insurance to the level that it is necessary that we don't have to be going through this political process that we are going through right now for ad hoc disaster programs. While I wasn't here when the 2002 Farm Bill was put in place, many folks thought that some of the changes that had been made over the years to the Crop Insurance Program was going to eliminate that and obviously that proved not to be true.

And I heard you say, Mr. Harms, that you don't think that we ought to be talking about crop insurance at the same time we talk about the farm bill. While I am not supporting taking any money out of the farm program, I do think it is an appropriate time to be having some discussion about improving crop insurance and with that, as many of you know and I think I have had some discussions with you, I have introduced a bill that gives the flexibility to basically do somewhat what the current disaster programs do. When the actual yield is below the county yield, that triggers a GRP or GRIP policy that the producer is able to put on top of their multiperil policy, thereby giving the producers one additional coverage. And I think, in some ways, that kind of helps address some of the problems with declining yields, because we are able to provide an opportunity to put additional coverage on top. I think that also provides our producers some flexibility on how to manage their risks and I think that is something desperately needed in the marketplace today, because as we all know, agriculture is big business now and the clients that you insure now aren't those small farmers, they are large operations.

With that, I would just like to hear from the panel. Is this a viable product and is this something that is needed in the marketplace today?

Mr. HARMS. Yes, we think if a disaster component is going to make it into the farm bill, then crop insurance wants to be involved in the process. The American Association of Crop Insurers has put together a task force. We are actively working to put together a proposal to begin sharing with the Subcommittee here very shortly. So we think there is a place for whatever you want to call it, a gap type of coverage to take care of that deductible on there and we think crop insurance can make a real difference in supplying that type of coverage. So we are working on it and we look forward to getting it to the Subcommittee very soon.

Mr. NEUGEBAUER. Ms. Fowler?

Ms. FOWLER. As agents, we are very eager and very interested to deliver this type of a product, the policy or policies, to that producer and be the one stop shop, which would be much less inconvenient for that producer.

Mr. NEUGEBAUER. Mr. Rutledge?

Mr. RUTLEDGE. RMA's supplemental deductible program is pretty similar to your bill. That may be able to be maneuvered into a type of disaster program and I don't know enough of the details about it, but I think if there is a permanent disaster program, we would like to be involved.

Mr. NEUGEBAUER. Mr. Parkerson?

Mr. PARKERSON. I would echo the same thing. We would like to be involved. I do think that it is going to take a lot of hard work and some real thought to putting this type of program together. But if it is available, I think the companies and these organizations are very capable of helping you deliver that type of product, but it is going to take some real work.

Mr. NEUGEBAUER. Well when you look back and we are having my bill re-scored as we speak, but even when we had it scored when we introduced it last year, it cost a lot less money for crop insurance than it has on what we spend on disaster programs over the last few years, and we can get it to the producer in a timely manner. The problem we have today is we have producers out there that have actually had consecutive losses and they are still waiting to see how the political process is going to unfold here and whether if and when we are going to have that.

And so I think it is good public policy and I think American taxpayers understand insurance. I think what makes disaster difficult is a lot of people don't quite understand the disaster philosophy and why we do disaster for some weather instances and why we don't do it for others, and so I would encourage you. I think, as we move into the environment we are in, in agriculture right now, I think if we do not improve the Crop Insurance Program, it won't do us any good to have a safety net necessarily for commodities, because if you don't have any commodities, it is very difficult to participate—for the commodity programs to provide you that safety net.

And so I really believe that we really need to be looking at these simultaneously. I do not want to take any money out of farm programs, but I think it makes good economic sense and fiscal sense to look at improving this with the addition of this. These are two products that you already sell, so we don't have to have a test demonstration period. This is something that we could get on the ground, really, in the next crop year if we will hurry. So with that, I yield back.

Mr. ETHERIDGE. I thank the gentleman. His time has expired. The Ranking Member now for closing questions and comments.

Mr. MORAN. Mr. Chairman, thank you. I will forego a closing statement, but I have a couple of questions I would like to ask. First, I would like to recognize Mr. Neugebauer and indicate that I believe his persistence will be rewarded on this topic, that it will happen at some point, as the Chairman said. And I am sorry I was not here for the testimony of Dr. Keith Collins and the Administrator. I continue to, for really the last 5 and 6 years, push RMA to develop a crop insurance product that would meet the needs of farmers in declining yield circumstances, multi-year disasters, and my impression is that once again FCIC, although they reviewed a couple of proposals, have taken no action, tabled the effort and I intend to pursue that further, Mr. Chairman, with the appropriate folks.

I simply wanted to ask a follow-up question to the issue of, really, a permanent disaster program. Mr. Harms, you in particular indicated, please don't deal with crop insurance in the farm bill. My guess is we are headed in that direction, in part because of the interest in a permanent disaster program. The proposals by the corn growers and the Administration all lend themselves to a discussion. My kind of initial question is, why not in the farm bill? What do you see as the disadvantage to dealing with these issues and in particular, any advice any of you have as we look at the issue of permanent disaster?

Mr. HARMS. I think, prior to the disaster component being expressed and worked on out here, we think having crop insurance outside the farm bill probably makes sense. That is how it has been in the past. But if there is going to be a supplemental coverage on top of the MPCI Program, then, yes, we need to be involved in the farm bill and we need to be involved in working with that, working with the program, that crop insurance can be an integral part of that type of coverage. So with the additional disaster, yes, crop insurance should be added.

Mr. MORAN. Anyone have any final thoughts in directing me in regard to permanent disaster? Good, we will do it our way, then.

Mr. HARMS. Again, that is what scares me, I think. The American Association of Crop Insurers———

Mr. ETHERIDGE. Speak now or forever hold your peace.

Mr. MORAN. And Mr. Parkerson, you are more politically astute than to say that. I appreciate your comments and appreciate your time today and I am glad to join you. Incidentally, in various locations yesterday in Kansas, farmers, if given the opportunity for disaster, ad hoc disaster assistance payments and the choice between 2005, 2006 and 2007, some of my farmers in some locations will be choosing 2007, which is a real surprise to me, after year after year of drought, that the freeze damage is greater than the losses due to lack of moisture.

Thank you, Mr. Chairman, for holding this hearing and I appreciate the chance to participate today.

Mr. ETHERIDGE. I thank the gentleman and let me just add to what he has just said. I think, when we find out how expensive the damage is going to be, really, across the country, especially in those areas along the Southern Belt, the Southeast and others that had not anticipated the really bad weather we have had this year, we normally think of droughts and floods and all of a sudden, the late season freezes may do more damage than any of us had ever anticipated at this point.

Let me thank each of you for coming, for your testimony, for your time. We appreciate that. And under the rules of the Committee, the record of today's hearing will remain open for 10 days to receive additional material and supplementary written responses from witnesses to any questions posed by a Member of the panel.

This hearing on the Subcommittee on General Farm Commodities and Risk Management is adjourned.

[Whereupon, at 12:06 p.m., the Subcommittee was adjourned.]

[Material submitted for inclusion in the record follows:]

STEVE HARMS,
Chairman,
American Association of Crop Insurers,
Johnston, IA.

Questions Submitted By Hon. Bob Etheridge, a Representative in Congress From North Carolina

Question 1. The Administration, the National Corn Growers and the American Farm Bureau Federation have all proposed changing the current price-based counter cyclical program with a revenue-based counter cyclical program. As offerors of very similar crop revenue insurance, what are your thoughts about the concept of moving to a revenue counter-cyclical program?

Answer. Revenue-based versus price-based is more complex, as it adds the required element of current year yield. Crop insurance is designed to address this, as it offers individual farm based revenue coverage. The revenue coverage proposals offered by the Administration, corn growers and AFBF are proposed on a national, state or regional approach, all of which will involve basis risk. Thus, they will only work to the extent that an individual farmer's revenue correlates with national, state or regional revenue. Corn growers in Iowa, Illinois and Indiana would likely correlate well with national revenue, but corn growers in Kansas, South Dakota or Texas likely would not.

Question 2. How interested are your companies in obtaining access to the data mining efforts? Willing enough to help with the cost?

Answer. We are very supportive and interested in the RMA data mining effort. We'd prefer to get the data sooner in the crop insurance cycle so that we have the benefit of the information while conducting our quality control processes and reviews and so we can adequately and more timely respond with appropriate action. We believe this is a Federal effort and should be funded by RMA via its normal appropriations.

Questions Submitted By Hon. Bob Goodlatte, a Representative in Congress From Virginia

Question 1. Why do you reject the notion of a "mandatory purchase requirement for farmers who participate in commodity programs"?

Answer. We do not support mandatory purchase requirements because the stated purpose is to alleviate the need for ad hoc disaster payments. We strongly disagree that a mandatory purchase requirement will alleviate the need for ad hoc disaster payments. Moreover, the mandatory purchase requirement put in place by the 1994 crop insurance reform legislation remained for only 1 year before Congress removed it in the 1996 Farm Bill. The mandatory purchase requirement would require additional cross compliance between RMA and FSA. We don't think their systems can adequately handle this. Finally, we believe most of the acres not participating are small land owners who would prefer to self insure.

Question 2. How comfortable are your companies with the premiums established by RMA? Do they sufficiently cover the risk you are taking? Do you analyze the premiums of these policies yourself? Do you tell USDA when you believe the premiums do not accurately reflect the risk of the policy? In circumstances where you have voiced concern about premiums, what has been RMA's response?

Answer. We review the premiums annually set by RMA. By and large they are adequate. When we find problems, we inform RMA. Sometimes, they respond with changes, other times they do not. For example, as RMA rolled out GRIP, we found problems with the yields they set in some counties and felt they yields would lead to adverse selection. We informed RMA of these concerns and some of the yields were corrected the following year.

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Questions Submitted By Hon. Bob Etheridge, a Representative in Congress From North Carolina

Question 1. The Administration, the National Corn Growers and the American Farm Bureau Federation have all proposed changing the current price-based counter cyclical program with a revenue-based counter cyclical program. As offerors of very similar crop revenue insurance, what are your thoughts about the concept of moving to a revenue counter-cyclical program?

Answer. I have read these proposals and although I do not have all the specifics, they do not seem to be that attractive nor do they seem to have much support. I can't tell how they would fit within the crop insurance program and may end up being a duplication of some parts of the crop insurance program.

I'm afraid I just do not have adequate knowledge of the specifics of these proposals to give a very good answer on this one.

Question 2. How interested are your companies in obtaining access to the data mining efforts? Willing enough to help with the cost?

Answer. My company, and I believe the majority of the other companies, are very interested in obtaining the data mining information. RMA has proposed the SRA holders pay a fee of ½ of 1 percent of premium to help them update and maintain their systems. If this fee will help keep data mining available and the industry is not subject to various other cuts, then I don't think there would be an objection to this item. Data mining can be a very valuable tool if we are allowed access to all appropriate data.

Questions Submitted By Hon. Bob Goodlatte, a Representative in Congress From Virginia

Question 1. In your testimony, you note correctly that crop insurance liabilities will be large this year—in excess of $65 billion. Much of this increase liability is due to the fact that the price election on corn was in excess of $4 per bushel. Even though liability is up, so are premiums. In your view, does the increase in premium sufficiently cover the risk at these price levels?

Answer. The premium increase due to price increases should be proportional to the increase in liability and if the premium rates set by RMA are correct then theoretically, the companies should be receiving adequate premium for the risk. The problem is that we have never had such high base prices before.

Typically, prices are low during Feb. when the base price is calculated, rise during the middle of the growing season due to various weather concerns that spook the markets and then fall and are on the low side again when the harvest price is calculated during October.

This year that pattern has been broken with the base prices for corn and soybeans the highest in the history of the program. This anomaly adds a new risk component not previously contemplated simply due to the magnitude of potential price movement. I don't believe this uncertainty is included in the rating of the revenue products.

Question 2. If a price decline of 30% occurs in corn and there is no loss of yield, do sufficient reserves exist in the industry to cover these underwriting losses? Is there any risk in your view that there are not sufficient reserves to cover large losses given the high price election for corn?

Answer. A price decline, assuming no yield losses, of 30% in the corn and bean prices would cause most SRA holders to suffer underwriting losses but adequate reserves exist to cover these losses since they would not be of great magnitude. The worst case scenario would be poor yields causing prices to rise above the base price. In that instance SRA holders would pay losses of great magnitude. Reserves probably exist (including payments we would receive from our reinsurers to help cover the losses) to cover the losses. However, I believe in this type of scenario, there would be one or more companies which would suffer financial losses of such degree that they might not be able to continue or would at least have to reduce their writings going forward. It could easily be the largest loss ever suffered by the program.

I do think there would be sufficient strength among the remaining companies to maintain adequate capacity to handle the needs of the program. However, we would all have to pay higher reinsurance costs and our margins would be reduced for some period of time.

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