HEARING TO REVIEW THE STATE OF THE CROP INSURANCE INDUSTRY

HEARING

BEFORE THE

SUBCOMMITTEE ON
GENERAL FARM COMMODITIES
AND RISK MANAGEMENT

OF THE

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HOUSE OF REPRESENTATIVES

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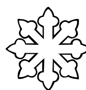

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HEARING TO REVIEW THE STATE OF THE CROP INSURANCE INDUSTRY

THURSDAY, JULY 22, 2010

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

The Subcommittee met, pursuant to call, at 9:30 a.m., in Room 1300, Longworth House Office Building, Hon. Leonard L. Boswell [Chairman of the Subcommittee] presiding.

Members present: Representatives Boswell, Walz, Schrader, Herseth Sandlin, Kissell, Pomeroy, Peterson (*ex officio*), Costa, Moran, Graves, Conaway, and Lucas (*ex officio*).

Staff present: Aleta Botts, Liz Friedlander, Craig Jagger, John Konya, Clark Ogilvie, James Ryder, April Slayton, Rebekah Solem, Tamara Hinton, Kevin Kramp, Nicole Scott, Pelham Straughn, Pete Thomson, Jamie Mitchell, and Sangina Wright.

OPENING STATEMENT OF HON. LEONARD L. BOSWELL, A REPRESENTATIVE IN CONGRESS FROM IOWA

The CHAIRMAN. I would like to call the meeting to order.

Welcome, everybody. I say in the beginning that my friend, Ranking Member, Jerry has had a death in the family and may show up late. I am not sure just yet.

I also have my next door neighbor, Mr. Sam Graves, here. A state line divides us, I guess, but we have known each other a long time. We both like to talk about airplanes. In fact, we have already done it this morning, haven't we Sam?

Mr. GRAVES. Yes, we have.

The CHAIRMAN. Anyway we will come to order, and I would like to thank you for being here as we review the state of the crop insurance industry.

I would like to thank the witnesses. Of course, when we have somebody from the home state here, we are always kind of pleased about that. We all look forward to these opportunities; and I want to give a welcome to the two Iowans who will be on the second panel, Mr. Rutledge and Mr. Dalton, for making the trip. Being from Iowa, the state with over 92,000 farms and over 30 million acres in production, we understand the challenges that farmers in that agriculture business face.

You probably heard this too many times, but it has been quite an impact on me, so I will keep telling it. When I returned to Iowa after spending a period of time in the Army—I was drafted and

thought I'd be gone a couple of years. I was gone a little over 20 years—I came back to do something I wanted to do very badly and that was to farm. My, my, how it had changed, big time.

I already knew—I always knew that, at least the size of the operation that I was involved in, and all sizes, actually, there are a couple of things you have to have. It is so capital intensive, you have to have a good banker you can work with; and, of course, you have to have the farmer store to buy and sell your product. You just have to have both.

Then we went through the farm crisis in the late 1970s, early 1980s. Down in our part of the country we had banks closing, and it was tough. It was a tough time, and a lot didn't survive it. A lot of the neighbors I had did not survive.

I had moved into the Iowa Legislature, and I had—Sam, I had five banks in my Senate district that went down. It was like a death in the family when that happens in a community. Throughout all that something else emerged, and that was the realization that you had to have a third element that had not been pursued too much and that was a good insurance program with a good insurance agent to help you manage your risk. So I and many others utilized that and didn't want to go back to what we just went through.

So I share that story because I understand the importance of the crop insurance industry, not just in our state but across the country. Last year alone, 265 million acres were enrolled in crop insurance. Sign-up and buy-up levels for crop insurance levels are at an all-time high, understandably so, proving that farmers appreciate having additional options to help them manage risk. However, certain regions and certain crops are under-represented. So, trying to look ahead, we need to see how we can make this program work for more producers.

Initially, I have to say cutting funding for the program makes the task a lot more difficult. Budgets are tight, but tight budgets do not mean we must jeopardize the risk management tools that we have today, or put in question what improvements we can make in the future.

We have been very concerned at the level of cuts proposed by RMA through the standard renegotiation agreement, the SRA process. While I believe the national deficit is one of the most pressing issues facing our nation, we must not pull the rug out from under our farmers and ranchers to address the issue.

Over $5 billion taken out of the crop insurance program in the 2008 Farm Bill and now an additional $6 billion removed through this SRA, I ask is there enough left to ensure farmers have access to affordable coverage, while trying to expand the program for crops for which it currently is not a viable option.

We must also acknowledge that the crop insurance industry is a business, and both the companies and agents need to make a profit in order to stay in the market and to stay in business. We can't begrudge them that. However, it is also the Committee's job to guarantee that every cent of taxpayer money spent in the program is spent wisely, and truly goes to provide a safety net for our producers.

We are making strides to help the American farmer, and I look forward to hearing more about the crop insurance program from our witnesses today. So I thank you again. Your testimony will be an essential means to us for the Committee to move toward the 2012 Farm Bill.

[The prepared statement of Mr. Boswell follows:]

PREPARED STATEMENT OF HON. LEONARD L. BOSWELL, A REPRESENTATIVE IN CONGRESS FROM IOWA

I would like to thank everyone for joining us here today as we review the state of the crop insurance industry. I would especially like to thank our witnesses. A very warm welcome to the two Iowans on the panel, Mr. Rutledge and Mr. Dalton, for making the trip to D.C. This Committee looks forward to hearing your valuable insight.

Being from Iowa—a state with over 92,000 farms and over 30 million acres in production—I understand the challenges that farmers and those in the agriculture business face today.

When I retired from the Army and returned home to Iowa and to farm, I quickly realized that farming had greatly changed during the 20 years I was away. Back then, I had always said that in order to farm, producers needed to have access to a bank and a place to sell their product. After surviving the farm crisis in the 1980's, I also realized the importance of a good crop insurance agent to help me to manage my risk. I worked with an agent in my area to ensure that I was never put in the position that I was in during the 1980's farm crisis again.

I shared that story because I understand the importance of the crop insurance industry not only in my State of Iowa but across the country. Last year alone 265 million acres were enrolled in crop insurance.

Sign-up and buy-up levels for crop insurance products are at an all-time high, proving that farmers appreciate having additional options to help them manage risk. However, certain regions and certain crops are under-represented. Looking ahead, we need to see how we can make this program work for more producers. Additionally, I have to say that cutting funding of the program makes that task much more difficult. Budgets are tight, but tight budgets do not mean we must jeopardize the risk management tools that we have today or put in question what improvements we can make in the future.

I have been very concerned with the level of cuts proposed by the RMA through the Standard Renegotiation Agreement (SRA) process. While I believe the national deficit is one of the most pressing issues facing our nation, we must not pull the rug out from under our farmers and ranchers to address that issue.

With over $5 billion taken out of the crop insurance program in the 2008 Farm Bill and now an additional $6 billion removed through the SRA, I ask—is there enough left to ensure farmers have access to affordable coverage while trying to expand the program to crops for which it is currently not a viable option?

We also must acknowledge that the crop insurance industry is a business, and both the companies and agents need to make a profit in order to stay in the market. We can't begrudge them that; however, it is also this Committee's job to guarantee that every cent of taxpayer money which is spent in the program is spent wisely and truly goes to provide a safety net for our producers.

We are making great strides to help the American farmer and I look forward to hearing more about the crop insurance program from our witnesses today. Thank you again, your testimony will be an essential means for us as we continue to move towards the 2012 Farm Bill.

I would now like to turn to my good friend, Sam Graves, for any opening statements he would like to make.

The CHAIRMAN. I would like to turn to my friend and neighbor, Sam Graves, for any opening statements he would like to make.

OPENING STATEMENT OF HON. SAM GRAVES, A REPRESENTATIVE IN CONGRESS FROM MISSOURI

Mr. GRAVES. Thank you, Mr. Chairman. I want to thank you for calling this hearing to review the state of the crop insurance industry.

Despite the creation of new commodities support and disaster assistance programs in the 2008 Farm Bill, agriculture producers in my district and in many other Congressional districts continue to rely on traditional farm programs and crop insurance to meet their risk management needs.

Agriculture producers need options to take into account the various and unique characteristics of their individual operations. The crop insurance industry has often been a source of innovation in developing products to meet these needs. Unfortunately, the recently enacted SRA reduces the farm safety net by some $6 billion. I think many on this Committee would agree that the run-up in A&O in 2008 was a problem that needed to be addressed, but there were other strategies available that would not have so deeply impacted the farm safety net baseline.

Mr. Chairman, I think you summed things up pretty well; and, with that, I, too, am looking forward to hearing the testimony today and look forward to hearing what the witnesses have to say.

The CHAIRMAN. Well, thank you very much.

I see we have been joined by Mr. Lucas from Oklahoma, the Ranking Member of the full Committee, and would recognize Frank for any statements you might want to make.

OPENING STATEMENT OF HON. FRANK D. LUCAS, A REPRESENTATIVE IN CONGRESS FROM OKLAHOMA

Mr. LUCAS. Thank you, Mr. Chairman. I appreciate that. And I want to thank Administrator Murphy and all the panelists for being here today.

I do wonder why we are having a hearing a week after companies basically have had a take-it-or-leave-it scenario thrust before them. The airing of some of these concerns would have been much more productive if they were not happening after the fact.

As the Department likes to point out, all 16 companies did sign the new SRA, but the signing of the agreement should not imply that the companies agree with the terms. If a company did not sign the document, the company would simply cease to exist, and thousands of people would be out of jobs.

A number of troubling items have arisen out of this Standard Renegotiation Agreement, and I think this Committee needs to take a serious look at the precedent that this renegotiation has set, and whether Congress needs to set stronger parameters of what changes can be made in future agreements.

As the Administrator will tell us, Congress gave the Department discretion to renegotiate this agreement, but I am not sure that these wholesale changes were envisioned when that discretion was given in the 2008 Farm Bill. As one of our witnesses points out today, this power of the purse is and should be reserved to Congress. This duty was usurped by the Department in this case.

In the field hearing the Chairman held this spring, the importance of the crop insurance program to producers was reiterated time and time again. I worry that these huge cuts might imperil the delivery system that our producers depend upon.

In the 2008 Farm Bill, Congress made cuts to the program totaling around $6 billion. I don't think anyone involved in those negotiations thought that less than 2 years later the Department would

again cut such a massive sum of money out of a program our producers depend on with such intensity.

I also worry that the Department, in response to a letter from one of our producer groups, said, "USDA remains open and willing to engage with the relevant Congressional committees to achieve crop insurance reform in a way that addresses the baseline concerns." Simply put, the Department failed in that regard as a vast majority, if not all, of the cuts in the program have vanished from the baseline. Yes, they are gone from the baseline.

In addition, I worry about some of the last-minute provisions to the agreement, including the hard cap on agent commissions, limiting the ability of companies to sue, and a change in the A&O formula that generally affects my great State of Oklahoma.

I do, though, commend Administrator Murphy, though, as he has consistently been up front and engaging in this process. I appreciate the open lines of communication that he and his office have shown to the Members of this Committee. I believe you were given an almost impossible job, sir, and you performed it admirably, considering everything.

With that, Mr. Chairman, I yield back.

The CHAIRMAN. Thank you, Mr. Lucas; and I appreciate what you just said.

Mr. Moran and I work very close together on trying to set these timetables, and your point is well taken about the timing. However, both Jerry and myself and probably you, since I know you pretty well, have been in contact with Mr. Murphy, so your point is well taken. I do remind us all that we do have some say in this before it is all said and done, so that is what we are trying to go through as we have this hearing today.

With that, I would ask that the rest of the Members present would follow standard procedure and request that they submit their opening statements for the record so we can begin the testimony and have ample time for questions.

[The prepared statements of Mr. Peterson and Mr. Moran follow:]

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

Thank you, Chairman Boswell, for holding this hearing today to take a look at where things stand in terms of the crop insurance industry.

This hearing is particularly timely as the U.S. Department of Agriculture has just finished the process of renegotiating the Standard Reinsurance Agreement (SRA) with the companies that provide crop insurance coverage to farmers and ranchers. Many people have a lot of opinions about how that process was carried out and what the outcome will be for farmers.

As a result of the SRA renegotiation, $4 billion will go to reducing the Federal deficit and $2 billion will go into improving risk management and conservation programs. As everyone knows, I am a strong supporter of reducing the Federal budget deficit because we are simply on an unsustainable path right now. And I want it to be noted that agriculture was first in line to contribute savings to the deficit, and the contribution of $4 billion was significant. If every other part of government followed this example and found a proportionate amount of savings in their programs, we could make some serious headway against the debt crisis we are facing in this country.

In the 2008 Farm Bill, we asked USDA to renegotiate the SRA, and that's what they have done. Many of us did not expect that as a result of those negotiations, there would be $6 billion in savings. I understand that there are concerns about how such a large change in the SRA could impact the delivery of crop insurance to farmers. We have some time between now and when we write the 2012 Farm

Bill, and if we see that the SRA is having an adverse effect on farmers, we could make some modifications at that time to address any problems that come up.

Again, thank you Chairman Boswell for holding this timely hearing today, and I look forward to the testimony.

PREPARED STATEMENT OF HON. JERRY MORAN, A REPRESENTATIVE IN CONGRESS FROM KANSAS

Thank you, Mr. Chairman, for holding this hearing. Given the recent events in the crop insurance industry, chiefly the signing of the 2011 Standard Reinsurance Agreement (SRA), it is important that we hold this hearing. While I am disappointed that we did not hold this hearing before the SRA was completed, which would have enabled Members of the Committee to publicly put their concerns and objections on record before RMA arrived at the final agreement terms, I am glad we have that opportunity now. Congress must exercise its oversight authority and doing so now will give us an idea about what parts of the SRA we must closely monitor as it is implemented.

Compared to the first draft of the SRA released by the Risk Management Agency (RMA) in December of 2009, I believe the final draft is much improved. However, I do not want this to be misconstrued as me giving the 2011 SRA my stamp of approval. In fact, I continue to have significant concerns about the substance of the agreement. I am worried not only how it could adversely impact service to the agricultural producer, but also how it will affect the vitality of the existing crop insurance industry.

While I plan to discuss my concerns further during the question period, I would like to highlight some initial issues. First, despite promises from Secretary of Agriculture Tom Vilsack that he would work with the Committee to protect the budget baseline for the next Farm Bill, it appears there was no real attempt made by the Department to fulfill this promise. While the Department reduced its program cuts from $8.4 billion to $6 billion, it appears none of that funding will remain available to the Committee to assist it in writing the 2012 Farm Bill. Furthermore, the Department has set a dangerous precedent of taking funds from a commodity program to support two mandatory conservation programs in the Conservation Reserve Program (CRP) and the Conservation Stewardship Program (CSP). When the last farm bill was written, the Congressional Budget Office (CBO) made assumptions about the cost of these programs, and in regard to CRP, assumed the program would be operated at near capacity for the life of the farm bill. This included the reenrollment of new and expiring CRP acres. It is perplexing why the Department now thinks it necessary to find additional offsets to run the program as Congress intended. If this example is followed, every time a CRP general signup is held, the Department is going to look for another way to reduce the producer safety net. Let me be clear, this is not what Congress intended.

Second, while Congress directed RMA to examine different methods of calculating the Administrative and Operating (A&O) subsidy, it did not direct RMA to restrict agent commissions. Agent commissions are an internal business decision of private companies. Often these agreements are made with independent agent contractors. RMA's decision to interfere with agent commissions is an unnecessary and unauthorized intrusion of government into a private business model. While crop insurance is a construct of the Federal Government, it was purposefully setup to operate through the use of a private delivery system. I worry that restrictions on agent commissions will eventually lead to a decrease in service to farmers and ranchers.

Third, I have significant concerns that subparagraph III(a)(2)(K) of the 2011 SRA is an unauthorized restriction of the legal rights of not only companies who are participants in the SRA, but also agents who are not party to the agreement. I suspect that most courts would find such a provision to constitute a contract of adhesion and the provisions stricken upon legal challenge. It is troublesome that an Administration that advertises its commitment to transparency and equity would unilaterally try to cut off the legal rights of insurance companies and agents. It is especially troublesome that this provision was added at the last minute with little open debate or negotiation. The addition of such a provision begs the question: "What is the Department trying to hide?"

Finally, I am concerned about the overall shifting of risk in this SRA from the private insurance and reinsurance industry to the government and ultimately the taxpayer. If RMA is concerned that profits in the crop insurance industry were getting excessive, why not move the program toward a more market oriented model. For example, rather than the government taking a greater share of the more profitable policies from the companies through realignment of the commercial funds, why

not simply transfer a greater share of the riskier policies to the companies, while allowing the companies to retain the more profitable polices. This would enable the companies greater upside potential, while also allowing the companies, through reinsurance, to spread risk across the industry.

I hope these topics will be addressed by RMA in its testimony and I look forward to further discussion throughout the hearing today.

The CHAIRMAN. I would like to welcome the first panel which, of course, is, as you see, Mr. Murphy, Administrator, Risk Management Agency, U.S. Department of Agriculture.

Mr. Murphy, welcome and please begin.

STATEMENT OF WILLIAM J. "BILL" MURPHY, ADMINISTRATOR, RISK MANAGEMENT AGENCY, U.S. DEPARTMENT OF AGRICULTURE, WASHINGTON, D.C.

Mr. MURPHY. Chairman Boswell, Congressman Graves, Members of the Subcommittee, as Administrator of the Risk Management Agency I am pleased to meet with you today to discuss progress, challenges, and successes of the Federal Crop Insurance Program, and in particular the recently negotiated Standard Reinsurance Agreement.

Secretary Vilsack asked me to administer the Federal Crop Insurance Program in a manner that provides effective risk management services necessary for American farmers and ranchers, and one that offers such services to producers in all geographical areas, regardless of the size of their operation.

Further, the Secretary and I are aware that in today's economy it is important that the program be cost effective and give a fair value for the taxpayers' dollar.

The crop insurance program has grown in coverage and in value to producers over the last decade. In 1999, just 73 percent of insured acres for the ten major commodities had buy-up coverage. Today, that has risen to 92 percent. Not only are coverage levels increasing, but the type of coverage farmers are purchasing is shifting to the more complex, comprehensive revenue coverages.

Many banks now require crop insurance coverage before making operating loans. Federal crop insurance has become an indispensable fact in the life of the American farmers.

Negotiations for the 2011 SRA began in 2009, and were completed on July 13th, 2010, when the USDA announced that all 16 of the approved crop insurance companies had signed the new SRA. During the negotiation, RMA held many meetings with the companies to hear their concerns, their suggestions and to exchange ideas. Elements of many of the provisions in the final agreement were based on recommendations from the companies toward these negotiations.

RMA and the companies negotiated in good faith and with respectful dialogue. The resulting agreement provides a reasonable rate of return to the companies for delivering the program, and will achieve $6 billion in savings over the next 10 years.

The new SRA will have no adverse impact on farmers' premium costs. In fact, certain farmers are likely to see a reduced insurance cost with the performance-based discount program resulting from the savings generated by this agreement.

The new SRA allows Administrative and Operating expense subsidies to fluctuate within a range, but removes the potential for the

type of excess windfalls experienced during the 2007 to 2009 price bubble.

The new SRA also for the first time provides the companies and their agents with financial protection from declines in the A&O subsidy should crop prices fall sharply.

RMA also took steps in the new agreement to limit compensation to crop insurance agents. Companies have been unable to contain a disturbing escalation in agent commissions. In 2009, companies reported to RMA that the average agent commission in the Corn Belt States—Iowa, Illinois, Indiana, Minnesota, and Nebraska—was 18.6 percent, a premium, whereas the A&O subsidy paid to the companies was only 17.1 percent.

Companies have been increasingly relying on expected underwriting gains which may or may not be realized to pay generous compensation arrangement to agents, while trying to meet their other program delivery costs. RMA is particularly sensitive to this issue because of the failure of American Growers due to similar circumstances in 2002, which cost taxpayers millions of dollars, disrupted program delivery, and still today is requiring government resources to close out this book of business.

To help ensure that does not reoccur, the new agreement limits company expenditures on base agent commissions to 80 percent of the A&O subsidy at the state level. This is the so-called "soft cap."

In addition, if companies are in an underwriting profit, they may share this profit with agents, but total compensation will be limited to 100 percent of the annual subsidy at the state level. This is known as the "hard cap."

RMA believes that the amount companies can pay for their agents under the new SRA is reasonable and adequate to maintain producer servicing levels we see today. I, along with members of the Federal Crop Insurance Corporation Board of Directors, all the RMA staff across the country, recognize that the program is dependant on a reliable delivery system. The approved insurance companies who deliver this program with their network of agents and RMA rely heavily on each other to operate the program efficiently and effectively to meet the needs of Americans producers. At the same time, we are aware of our responsibility to be good stewards of taxpayer money. RMA is pleased to have a new and solid SRA in place.

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

[The prepared statement of Mr. Murphy follows:]

PREPARED STATEMENT OF WILLIAM J. "BILL" MURPHY, ADMINISTRATOR, RISK MANAGEMENT AGENCY, U.S. DEPARTMENT OF AGRICULTURE, WASHINGTON, D.C.

Chairman Boswell, Ranking Member Moran, and Members of the Subcommittee, as Administrator of the Risk Management Agency (RMA), I am pleased to meet with you today to discuss the latest developments in RMA, the progress and challenges of the Federal Crop Insurance Program, and, in particular, to provide an update on the recently negotiated Standard Reinsurance Agreement (SRA) and its benefits to the agricultural community and the American taxpayer. My staff and I work daily to validate the utility of current insurance products—making certain we have the best protection possible for all of America's farmers and ranchers. We work 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. In our role

as regulators, we must also ensure the continued integrity and actuarial soundness of the Federal Crop Insurance Program.

Secretary Vilsack asked me to administer the Federal Crop Insurance Program in a manner that provides effective risk management services necessary for American farmers and ranchers; and that offers such services and opportunities to participate in the program to farmers and ranchers in all geographical areas regardless of the size of their operation. The Secretary and I are aware that in today's economy it is important that the program be cost effective and give a fair value for the taxpayers' dollar.

The crop insurance program has grown in coverage and in value to producers over the last decade. In 1999, just 73 percent of insured acres for the ten staple crops had buy up coverage, compared to 92 percent in 2009. Not only are coverage levels increasing, but the type of coverage farmers are purchasing is shifting to the more comprehensive revenue coverage. Many banks require crop insurance coverage in order to make operating loans to crop producers. Federal crop insurance has become a fact of life for many farmers—and one in which American farmers would find it difficult to continue providing America and the world with an abundant supply of food, fiber and fuel without the program.

This growth has been accomplished in an actuarially sound manner as required by Congress, and the program is working well. Over the last 2 decades, premiums (producer premiums added to premium subsidies) have been sufficient to cover the indemnities paid to producers plus a reasonable reserve, as directed by the Federal Crop Insurance Act.

The 2011 Standard Reinsurance Agreement

The Food, Conservation, and Energy Act of 2008 (2008 Farm Bill) allowed the renegotiation of the Standard Reinsurance Agreement (SRA), which is the agreement between USDA and the approved private insurance companies who deliver the program through a network of insurance agents. Negotiations began late in 2009, and on July 13, 2010, USDA announced that all of the approved crop insurance companies had signed the new SRA. At the beginning of the negotiations, Secretary Vilsack and I established six objectives for the new SRA that would build on the strengths of the program. The objectives were designed to align with RMA's primary mission to help producers manage the significant risks associated with agriculture. We maintained our focus on those objectives throughout the process and they have served us and America's farmers well. They are:

(1) Maintain producer access to critical risk management tools;

(2) Align the Administrative and Operating (A&O) subsidy paid to insurance companies closer to actual delivery costs;

(3) Provide a reasonable rate of return to insurance companies;

(4) Protect producers from higher costs while equalizing reinsurance performance across states to more effectively reach under-served producers, commodities, and areas;

(5) Simplify provisions to make the SRA more understandable and transparent; and

(6) Enhance program integrity.

During the negotiations RMA held many meetings with the companies to hear their concerns and suggestions. Elements of several provisions in the final agreement were suggested by the companies during the negotiation. RMA and the companies negotiated in good faith and with respectful dialogue resulting in an agreement that provides a reasonable rate of return to the companies for delivering the program, and will achieve $6 billion in savings over the next 10 years. Two-thirds of the savings from the new SRA, $4 billion, will go toward paying down the Federal deficit. The $4 billion in budget savings USDA achieved is one of the first and most significant steps that a Federal agency has achieved in reducing mandatory spending from the long term Federal deficit. The President has laid out an aggressive plan for reducing the deficit and we are pleased to take a leadership role in that effort.

The remaining ⅓ will support high priority risk management and conservation programs. This $2 billion invested in farm programs will be used, in part, to improve and expand several RMA risk management products. In fact, the Pasture, Rangeland, and Forage (PRF) program has already been expanded as a result of the savings obtained through the SRA. Under the Rainfall Index (RI)-PRF plan of insurance, RMA will expand coverage for the 2011 crop year to specific counties in Colorado, and all counties in the states of California, Florida, Georgia, New York, North Dakota, Oklahoma, Pennsylvania, South Carolina, and Texas, bringing the total

number of states where the program is available to 16. The Vegetation Index (VI)-PRF will be expanded to the balance of counties in Idaho, Oregon, and South Dakota, and all counties in the states of Arizona, New Mexico, and Utah for 2011, bringing the state total where VI–PRF is available to nine.

RMA has also received requests for further expansion of PRF in Nevada, Arkansas, Maryland, and Minnesota. RMA will take the expansion request for the 2012 crop year to the Federal Crop Insurance Corporation Board of Directors later this year for their consideration and potential approval.

As a result of these savings, RMA also plans to provide a performance based discount or refund, which will reduce the cost of crop insurance for certain producers. Additionally, USDA has used this opportunity to increase Conservation Reserve Program (CRP) acreage to the maximum authorized level; investing in new and amended Conservation Reserve Enhancement Program initiatives; and investing in CRP monitoring.

The new SRA will have no adverse impact on farmers' premium costs. In fact, some farmers may even see reduced insurance costs with a performance-based discount or refund that result from the savings generated by this agreement.

SRA Structure

The 2011 SRA was structured to reflect the realities of today's agriculture economy. Since government payments to crop insurance companies are tied to crop prices and price volatility, the unprecedented spike in commodity prices in recent years caused government payments to companies to more than double, from $1.8 billion in 2006 to $3.8 billion in 2009. The new SRA allows A&O payments to fluctuate within a range that removes the extremes. This will prevent windfall profits created by price spikes, like those we have seen in recent years, but will also ensure an adequate A&O subsidy is provided to companies. The new agreement provides a maximum A&O amount of $1.3 billion in 2011, and increases it yearly with inflation to $1.37 billion in 2015. This is almost 40 percent more than the $935 million the crop insurance companies received in A&O payments in 2006 (the last year before the price spikes) and 35 percent less than the $2 billion the industry received in 2008 (the height of the price spikes). Companies will be protected against extremely low crop prices by a minimum A&O reimbursement. This provision will ensure that the crop insurance companies receive at minimum about $1 billion in A&O payments, or slightly more than what it received in 2006 to deliver the program. This added protection will ensure that the companies have enough money to deliver the program, even if prices or price volatilities fall sharply.

Agents' Compensation

To ensure the viability and integrity of the crop insurance delivery program, RMA took steps in the new agreement to limit compensation to crop insurance agents. Even in the face of cuts in A&O imposed by Congress, companies were unable to contain the escalation in agent commissions. A recent analysis showed that about 20 percent of A&O is needed to pay expenses related to loss adjustment, information technology, employees, and other operations (excluding agent commissions), yet many companies were paying agents far above the entire A&O subsidy amount in certain parts of the country. In 2009, average agent commission rates in the Corn Belt States (Iowa, Illinois, Indiana, Minnesota and Nebraska) were 18.6 percent of premium and the A&O paid to the companies was 17.1 percent. Therefore, these companies were relying on underwriting gains (which may or may not be realized) to pay for costs other than agent commissions. Companies were also moving A&O payments and bidding up agent commissions in the Corn Belt, which generally includes the most profitable states.

The new SRA includes a cap on agent commissions to ensure that companies have sufficient funds to pay the other operating expenses in years in which there may not be an underwriting gain. As the regulator for the Federal Crop Insurance Program, RMA saw a clear need to ensure that companies have sufficient funds to pay operating expenses (including agent commissions) without resorting to the reliance on uncertain underwriting gains.

History has shown us that this step is necessary. In 2002, the largest crop insurance company in the program, American Growers Insurance Company, failed in large part because of high commissions paid to retain and acquire agents. American Growers' expenses exceeded the amount of A&O received so they were forced to rely on underwriting gains to remain solvent. Since 2002 was a moderately bad crop year, many crop insurance companies did not receive underwriting gains. American Growers actually ended the year with a small underwriting gain. However, its failure to receive an underwriting gain large enough to cover its commitments caused the company to collapse. This major failure caused widespread confusion and uncer-

tainty in the crop insurance program, and the remnants of this failure still are being felt by the program today.

Eight years later, in 2010, companies are still relying on large underwriting gains to operate the program and have been fortunate to have seen an unprecedented run of profitable underwriting years. The real possibility of even a modest loss year, such as 2002, however, creates a situation where several companies could be at risk for failure and thus jeopardize the entire delivery system.

The new agreement limits companies' expenditures on base agent commissions to 80 percent (soft cap) of the A&O subsidy at a state level. Companies may still use profit sharing, but total agent compensation will be limited to 100 percent (hard cap) of the A&O subsidy at a state level to ensure fair and equitable competition among all companies in all states.

While the second draft proposal included only a "soft cap" on agent commissions equal to 80% of the A&O subsidy, the final agreement added a "hard cap" on total agent compensation at 100% of A&O subsidy on a state basis. This was done after considering concerns expressed by many companies and others that a soft cap alone would create equity issues between the states and provide an incentive for some companies to only write business in the most profitable states. Companies writing in these most profitable states would attract agents by claiming a potential for more consistent and higher rates of return and, consequently, greater availability of funding to provide for agent profit sharing. Providing a hard cap on profit sharing will limit the potential for companies to engage in such market-disrupting activities. Federal crop insurance is a nationwide program and the SRA should ensure that the companies and their agents have the incentives to provide service to all producers.

Even with the hard cap, the expected amount of compensation potentially available to agents will be about $1.3 billion annually, given the expected A&O subsidy and average expected underwriting gain amounts provided by the agreement. On average, for the 2011 to 2015 life of the SRA, agent commissions will be limited to about $1.1 billion annually, while profit sharing will be limited annually to about $270 million. On average, the 100 percent cap allows around ⅓ of total underwriting gains to be shared with agents, as determined by the companies.

RMA analysis shows that the cap will primarily affect the Corn Belt states where companies generally have been paying average agent commissions above the total A&O subsidy. All other states have seen average commissions paid below the total A&O subsidy and are not likely to be affected.

For this year—2010—under the current SRA, agent commissions are already expected to decrease due to lower commodity prices and price volatilities not due to the new SRA. For example, Iowa agent commissions are expected to fall from about $140 million in 2009 to about $110 million in 2010, under the current SRA. The new SRA hard cap will be placed at about $105 million in 2011. Therefore, the provisions of the new SRA will result in an average 5.7 percent decline from 2010 in dollar terms in Iowa.

However, this is 72% greater than the dollars Iowa agents received in 2006, even though the number of policies serviced is virtually unchanged. In effect, expected 2011 agent compensation reflects the equivalent of compounded annual income increases of 12% over this 5 year period, an impressive record that can be matched by very few others in the recent, sluggish economy. In an environment where the number of Iowa policies is stagnant, therefore, RMA believes compensation to agents through the new SRA is more than reasonable for 2011 and, with the built-in inflation adjustment factor, the compensation cap is guaranteed to increase with expected inflation.

Risk Sharing

The previous agreement's risk sharing terms were structured in such a way that some states in the Corn Belt experienced much greater profitability for companies and agents than in other states. Analysis by Milliman, Inc. also indicates that the industry as a whole has been making far above a reasonable rate of return. This analysis shows that over the last 21 years a reasonable rate of return for the companies averaged 12.7 percent, while the companies actually received an average rate of return of 17.0 percent. The new agreement provides an expected return to companies of about 14.5 percent, almost two percentage points above the reasonable rate of return.

The new SRA rebalances the risk sharing terms to better equalize expected returns throughout the different states, including terms that are more profitable for states outside the Corn Belt. The new SRA also maintains the Assigned Risk Fund, which provides companies with stop loss protection at a state level.

The new agreement sets the Net Book Quota Share at 6.5 percent, with 1.5 percentage points of underwriting gain to be distributed to those companies that sell and service policyholders in 17 underserved or less-served states (Group 3 states). This provides an additional financial incentive for companies to continue doing business in these underserved or less-served states.

Together, the changes we have made in the new SRA, through negotiations with the private companies, will create a more sustainable Federal Crop Insurance Program, and the expansion of key risk management and conservation programs will improve the safety net for America's farmers and ranchers. The new SRA represents a fair deal for farmers and the government, the companies, the agents, and the taxpayers.

Status of the Federal Crop Insurance Program

The Federal Crop Insurance Program is helping the men and women who produce America's agricultural products to manage risk in an inherently risky business. For crop year 2009 with 1.2 million policies on 265 million acres, the program provided coverage for $79.6 billion in crop value. Of the $8.9 billion in total premium, USDA subsidized $5.4 billion for farmers, and paid out over $5 billion in claims for lost or damaged crops. In addition, RMA awarded $8.6 million in Partnership Agreements to assist small and underserved producers across the country.

Producers generally have a choice of crop or livestock policies, with coverage they can tailor to best fit their risk management needs. In many cases, producers can buy insurance coverage for a yield loss, or revenue protection to provide coverage for a decline in yield or price. Today, most producers "buy up" to higher levels of coverage ranging up to 85 percent (smallest deductible), although a low level of catastrophic coverage (CAT) is still available for a nominal fee with the premium fully subsidized. Indemnity payments are usually made within 30 days after the producer signs the claim form.

The crop insurance program has seen sustained growth as demonstrated by the increasing proportion of acres insured at buy up levels over the last decade (see *Attachment 3*). In 2009, 92 percent of insured acres for the ten staple crops had buy-up coverage, compared to just 73 percent in 1999. Not only are buy up levels increasing, but the type of coverage being purchased is shifting to the more comprehensive revenue coverage (see *Attachment 4*). In 2009, revenue coverage accounted for 57 percent of the insured acres, compared to just 27 percent in 1999. In addition, the average coverage level (percent of the total crop covered) for buy up insurance has increased. In 2009, the average coverage level rose to a record-high of 73 percent. In 1999, the average was 67 percent.

Program Integrity

In conjunction with the improved quality control requirements in the new SRA, 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 the success of their efforts to address crop insurance program vulnerability concerns.

RMA continues to make significant progress in preempting fraud, waste and abuse through the expanded use of data mining. We have preempted millions of dollars' worth of projected payments, and RMA continues to use data mining to identify anomalous producer, adjuster, and agent program results. With the assistance of the Farm Service Agency (FSA) offices, RMA and companies conduct growing season spot checks to ensure that claims for losses are legitimate. These spot checks based on data mining have resulted in a significant reduction in anomalous claims for those situations.

We are improving the timing and quality of our sanctions requests as well. RMA continues to work with USDA's Office of General Counsel (OGC) to limit the number of cases declined due to insufficient evidence. This improvement is attributable to Compliance personnel becoming more proficient at identifying evidence and establishing cases that will pass legal sufficiency requirements. The Administrative Sanctions regulations that were identified by the Government Accountability Office (GAO) as requiring publication were published and were effective on January 20, 2009. Although RMA was using the statutory authority to impose sanctions before the regulations were published, RMA agreed with GAO that the publication should be prioritized to ensure that program participants and other interested parties were given appropriate constructive notice of the rules.

RMA is continually seeking new and more effective ways to work with the other regulatory bodies and government agencies as well as insurance companies, agents and producers to ensure the integrity of the Federal Crop Insurance Program. RMA compliance reviews continue to reveal that there are only a small number of producers who have been involved in fraud or illicit activity. While no level of criminal or abusive behavior is acceptable, RMA continues to believe the number of persons involved in criminal activity is relatively small.

While RMA, FSA and the insurance providers have preempted tens of millions of dollars of improper payments through quality controls, data mining, and other measures, RMA is constantly identifying ways to balance competing needs to make our products less susceptible to fraud 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 waste, fraud and abuse.

In the recent past, there have been some concerns expressed about unresolved Office of Inspector General (OIG) Audit recommendations. In particular, RMA was cited as having 70 OIG audit recommendations pending for a year or more after agencies agreed to implement them. However, according to RMA's records, there are only 14 audit recommendations that now meet this criterion. RMA believes that both OIG and GAO audits have resulted in program improvements over the years and continues to commit significant resources to resolving and implementing audit recommendations that can reasonably be expected to achieve greater efficiency or effectiveness for the program and the taxpayer.

Organics

In January 2010, RMA submitted a report to Congress entitled Organic Crops and the Federal Crop Insurance Program, as required by the 2008 Farm Bill. The report included information on the numbers and varieties of organic crops insured; the status of the development of new insurance approaches to organic crops and the progress of implementing organic initiatives required by the 2008 Farm Bill. The 2008 Farm Bill also required that RMA contract for research into whether or not sufficient data exists upon which RMA could determine a price election for organic crops; if such data does exist to pursue further development of a pricing methodology using that data; and that RMA contract for research into underwriting, risk and loss experience of organic crops as compared with the same crops produced in the same counties during the same crop years using nonorganic methods. Three studies that resulted from this research, *Organic Crops: Report on Research of Additional Price Elections; Organic Crops: Final Development of Additional Price Elections* and *Organic Crops: Revised Written Rating Report* are expected to be released shortly.

Review of Rating Methodology

RMA contracted with Sumaria Systems Inc. for a thorough actuarial review of the methodology and procedures used to determine the Actual Production History (yield) target rates and the rating process for the new Common Crop Insurance Policy Basic Provisions (often referred to as COMBO policy) under the Federal Crop Insurance Program. The draft report was received in November 2009 and was made available for public comment. A final version of the review is now available at *http://www.rma.usda.gov/pubs/2009/comprehensivereview.pdf* on the RMA website.

The review found that RMA's general premium rating methodology (based on historical losses) is appropriate and should continue to be used. However, the study identified several areas for potential improvement, the most significant of which is to determine if all historical losses should be given the same weight in determining premium rates. In addition, key aspects of today's crop insurance program along with crop production technology would also be considered and evaluated for potential effects on past experience. This would provide a basis for evaluating the degree to which past catastrophic events may affect the historical loss data used in establishing current premium rates, and as appropriate, allow for adjustments to those rates. This could potentially result in lower premium rates in several parts of the country, especially the Corn Belt. RMA is currently in the process of soliciting bids for this review of its historical loss data so that work can commence later this year. In the near term, premium rates for the most popular revenue products, Crop Revenue Coverage (CRC) and Revenue Assurance (RA), are expected to be generally lower for the 2010 crop year as a result of decreasing price volatilities.

New Common Crop Insurance Policy (COMBO Policy)

The new Common Crop Insurance Policy, frequently referred to as the COMBO policy, is an initiative by RMA to combine and simplify the crop insurance program. RMA has combined CRC, RA, Income Protection (IP), and Indexed Income Protection (IIP) into a single uniform policy. RMA kept and combined the principle fea-

tures of the five plans that producers bought most often and developed a single rating and pricing component so all insurance coverage is consistent in insurance protection and cost to producers. The new Basic Provisions are effective for the 2011 crop year for crops with a contract change date of April 30, 2010 or later (effective for most 2011 crops) and for the 2012 crop year for crops with a 2011 crop year contract change date prior to April 30, 2010.

Comprehensive Information Management System

The Comprehensive Information Management System, referred to as CIMS, is designed to provide approved users timely access to 2006 thru 2010 RMA and Farm Service Agency (FSA) producer information and data. The system has improved operations between RMA and FSA and has the potential to continue improving information transfer. At this time, FSA employees have access to CIMS, which has led to a 56% reduction in entity differences for producers participating in the programs of the two agencies, including support for the SURE program. Crop insurance companies have made over 18 million CIMS inquiries or requests for information, reducing resources and costs to obtain electronically data similar to the hard copy information that normally resides at the FSA County office. Companies are also incorporating the use of Common Land Unit reporting into their systems to enhance reconciliation efforts for acreage reporting and other applications for administering programs for prevented planting and cause of loss verification. RMA also is actively participating in the USDA Acreage/Crop Reporting Streamlining initiative to establish common USDA producer commodity reporting standards to facilitate greater use of CIMS and Agency sharing and reconciliation of data, along with potential incorporation of data obtained through the use of precision-ag technology.

Information Technology Modernization

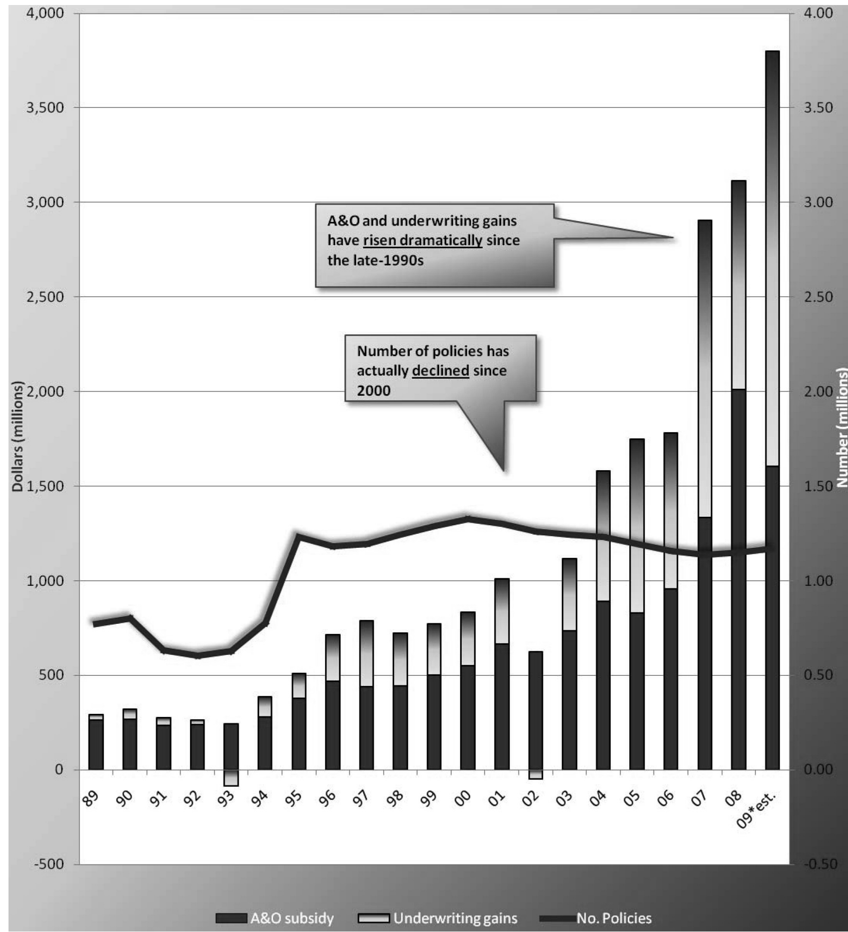
RMA's Information Technology Modernization (ITM) program is a multi-year, phased-implementation reengineering initiative to support COMBO and new insurance programs and products, increase actuarial capabilities, and provide efficient policy and financial processing for producers and insurance companies. The first phase, successfully operational in April 2010, focused on actuarial processes, policy processing, premium calculations, and other functions needed to administer various 2011 crop year insurance offers, and implement the new COMBO policy. The next phases of the ITM program, corporate business reporting and financial accounting, are in development with final completion scheduled for the end of 2011.

I, along with members of the Federal Crop Insurance Corporation Board of Directors, all the RMA staff across the country, recognize that the program is dependent on a reliable delivery system. The approved insurance companies, who deliver this program with their network of agents, and RMA, are mutually dependent on each other to operate the program efficiently and effectively to meet the needs of producers. We are very aware of our responsibility to be good stewards of taxpayer money. By creating a new standard reinsurance agreement that maintains excellent service to farmers and ranchers, provides incentives for companies to operate in underserved and less served areas, provides a reasonable return for the companies and removes windfall government payments that were an unintended consequence of the past SRA structure, RMA is pleased to have met the goals set at the beginning of this negotiation. Again, thank you for the opportunity to participate in this important hearing. I look forward to responding to your questions.

ATTACHMENTS

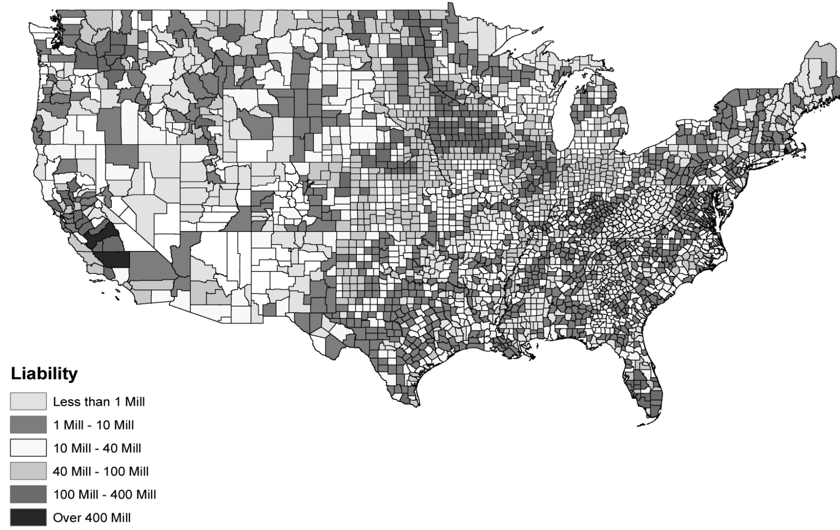
Attachment 1

AIP Revenue from FCIC



Attachment 2

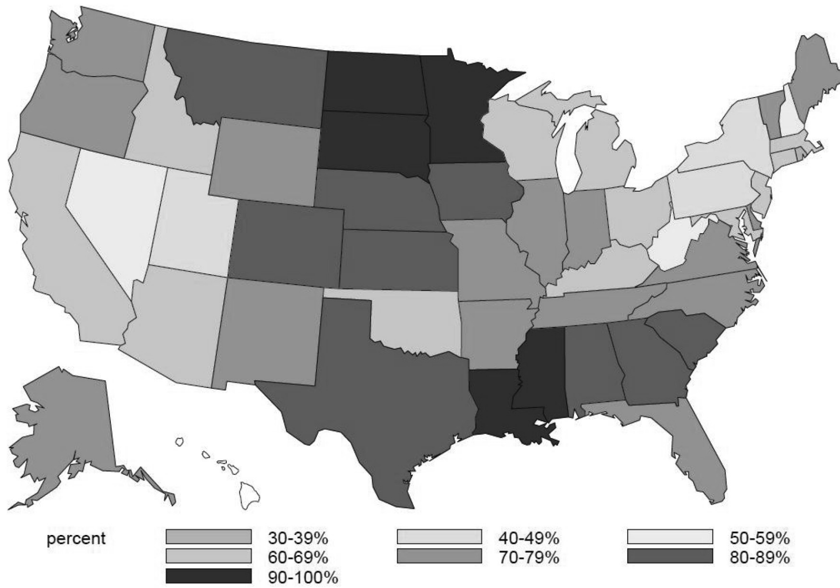
2009 Total Liability All Crops



Attachment 3

2009 Proportion of Planted Acres Insured

Crops Included: Barley. Grain Corn, Grain Sorghum, Peanuts, Pima Cotton, Potatoes, Rice, Soybeans, Tobacco, Upland Cotton and Wheat



NASS as of: 03/17/2010.
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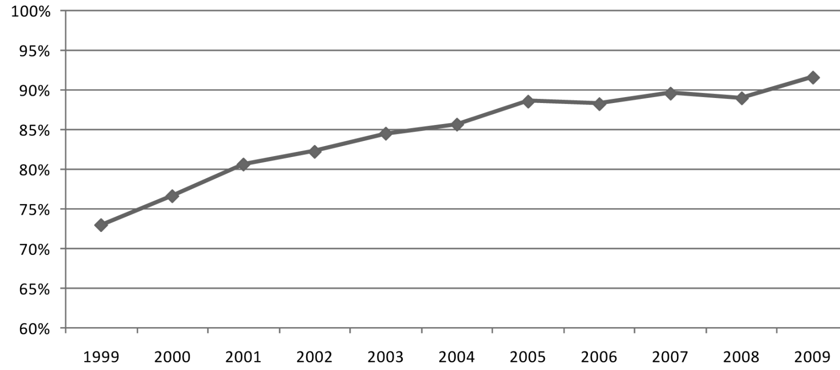
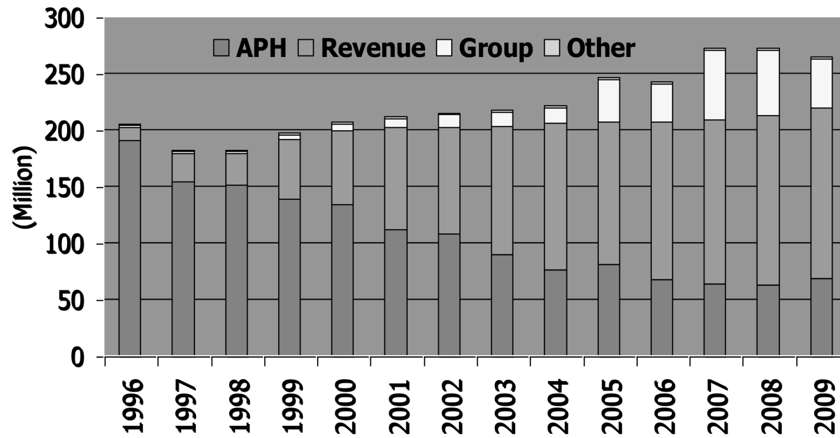
Attachment 4

Proportion of Insured Acres with Buy Up Coverage in the Federal Crop Insurance Program



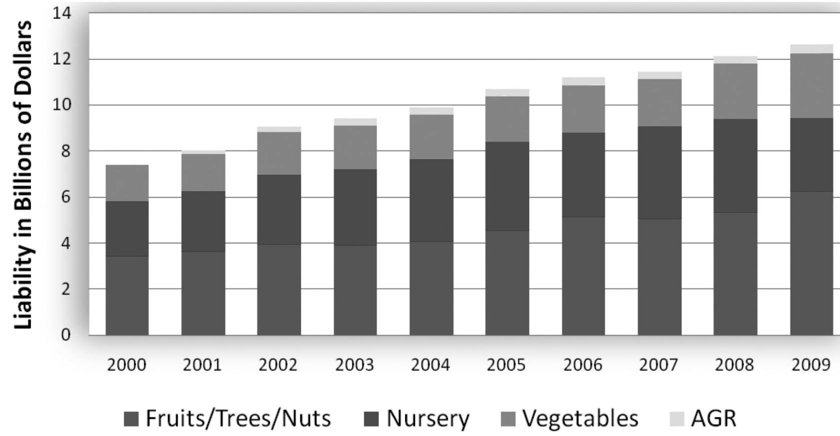
Attachment 5

Acres by Plan Category



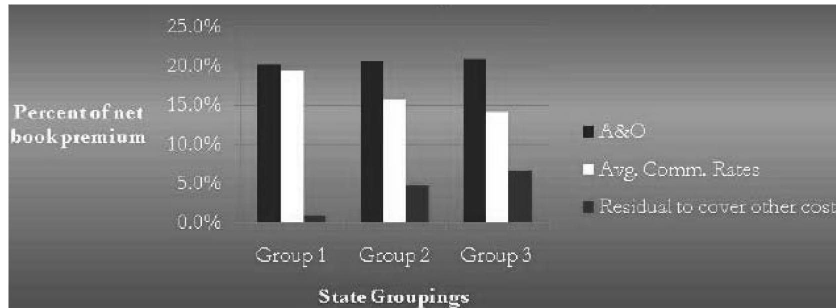
Attachment 6

FCIC Program Growth for Specialty Crops



Attachment 7

2008 Comparison of A&O to Agent Commissions by State Group



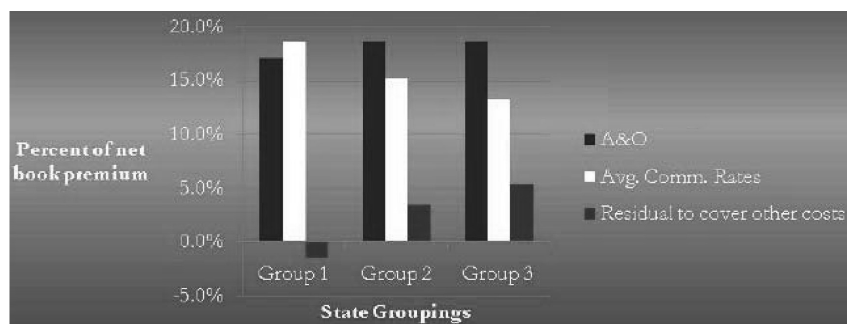
Attachment 8

2008 Comparison of A&O to Agent Commissions by State Group

2008	Group 1	Group 2	Group 3
A&O	20.2%	20.6%	20.8%
Avg. Comm. Rates	**19.3%**	**15.7%**	**14.1%**
Comm. % of A&O	95.5%	76.2%	67.8%
Residual to cover costs	0.9%	4.9%	6.7%

Attachment 9

2009 Comparison of A&O to Agent Commissions by State Group

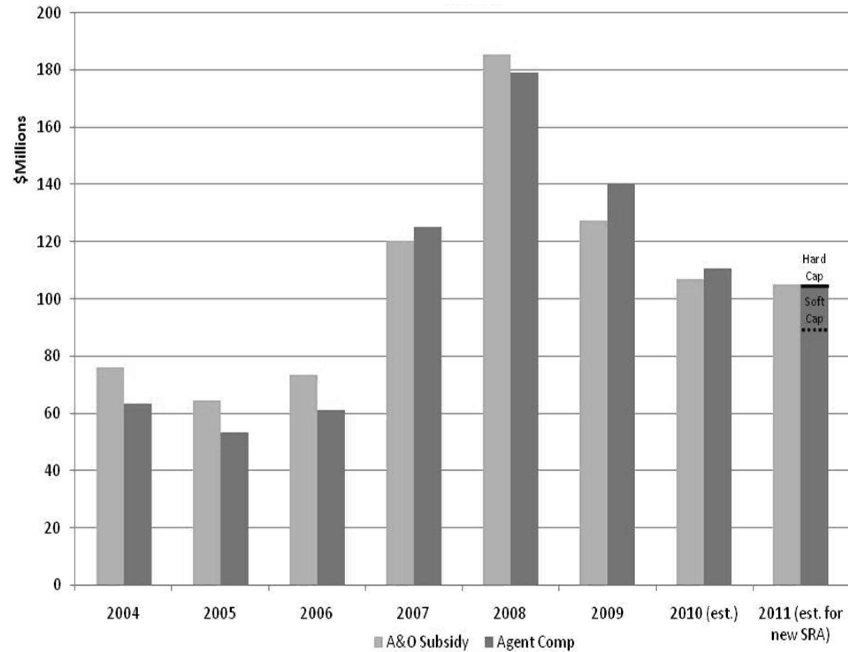


Attachment 10

2009	Group 1	Group 2	Group 3
A&O	17.1%	18.6%	18.6%
Avg. Comm. Rates	**18.6%**	**15.2%**	**13.2%**
Comm. % of A&O	108.8%	81.7%	71.0%
Residual to cover costs	−1.5%	3.4%	5.4%

Attachment 11

Iowa



Attachment 12

Iowa Agent Compensation Analysis

Year	No. of policies	Premium ($)	A&O (% of premium)	A&O and CAT LAE ($)	Agent Comp. (% of premium)	Agent Compensa-tion ($)
2004	130,286	354,511,745	21.5%	76,087,416	17.9%	63,457,602
2005	127,423	310,529,453	20.8%	64,719,502	17.2%	53,411,066
2006	125,543	366,833,451	20.0%	73,507,061	16.7%	61,261,186
2007	121,633	600,208,831	20.1%	120,463,261	20.9%	125,443,646
2008	123,948	914,548,177	20.3%	185,687,109	19.6%	179,251,443
2009	127,402	743,726,271	17.2%	127,663,700	18.9%	140,564,265
2010 (est.)	127,402	622,151,163	17.2%	107,010,000	17.8%	110,742,907
2011 (est. for new SRA)				105,122,000		105,122,000

The CHAIRMAN. Well, thank you very much.

I am going to ask you a couple of questions. We have several here, so I will be short, and we may have a second or third round.

I am aware of a letter that was sent to the Congress Members regarding the SRA. Secretary Vilsack, he argues that the commission caps are needed to protect crop insurance companies, and to ensure they remain solvent. So if that is a concern of the RMA, why would the not consider other protective measures for the companies? For example, include reserve requirements or solvency status of the companies? And I am curious why were agent caps not in the first or second draft of the SRA, if this was needed?

Mr. MURPHY. Okay. Yes, I understand the concerns with the caps. Like I said in my opening statement, we basically have two. There are other ways, and we certainly have employed new methods to ensure that the companies have financial standards since the failure of American Growers. But, still, whenever you are working with information supplied for taxes, or supplied to current insurance requirements at the state level, you are looking in the past. That does not prevent something from occurring in the current year, and that was our greatest concern.

The soft cap basically was developed—and that is 80 percent—the total compensation a company can pay is 80 percent of the projected A&O. That is all they can guarantee up front. We are seeing a disturbing trend in the increasing amount, and the only way the companies will be able to make this is relying on underwriting gains.

This is exactly what happened to American Growers. In fact, in 2002, American Growers was the only AIP that had a profit. Yet they were the only company that went out of business. The reason that that happened is that they over-committed on agent commissions. We thought this was probably the only way we can ensure that this will not occur in the future.

We have new companies coming on, there is going to be significant competition, and I just think the reliance on using agent commissions as a way to get market share is very problematic for the stability of those companies. I think it was very important to do the soft caps.

When we get into the hard cap, another issue that came up is that we have reduced the A&O significantly in this program. There was a lot of concern over equity in the program, equity from a company standpoint. We all imagine that in the future, under this new SRA, the most profitable states will be the Midwest. And so there was concern that the companies would get in, feel the need to move up into those areas, expand their businesses, maybe leave areas with less profit in order to guarantee an ever-increasing profit share with the companies. In order to avoid that from happening, we put the hard cap in.

I think there is also a question of equity to the agents. We are finding that agent commissions in Iowa are three times agent commissions in Texas.

The CHAIRMAN. Explain that.

Mr. MURPHY. Agent commissions—this is a study from the GAO. If you take a look at the GAO report, they went out and took a look

at agent commissions, and they found that there is a significant difference.

I have had agents come up and talk to me within the last year from Iowa who said they have been offered commission schedules of 30 percent. And I know of agents in Texas whose commission schedules are ten percent. Yet, it requires the same amount of work. I think there is an equity issue here, also, for the program.

Allowing these unabated agent commissions to continue also causes marketing problems. We have had a real problem over the last couple of years with rebating. This rebating has been occurring in Iowa and the other "I" States. I received many calls from insurance commissioners in those areas last year who were very concerned about the rebating; and they said, "I realize it is a Federal program, but if these agents think they can rebate on crop insurance they will start doing this in other lines of insurance, and we will have a real problem here." There was much concern about that.

Another big concern is entry of companies into the program. Having these high insurance commissions out there is a barrier for a company coming in and starting in the program, because they would have to immediately try to compete with these rates.

In my talking with your staffs, with the companies themselves, with the commodity groups, one of the big issues is competition in the program. The feeling is we still have to have strong competition with a number of companies. I thought this also was a way to help address that.

The CHAIRMAN. I appreciate that. We will come back to it, I think.

You know, Mr. Murphy, I want to ask when this panel is finished, if you have time, if you could stay and listen at least to the next panel. I am not going to call you back to the table without having given you forewarning, but I still have some concerns.

I have met a lot of agents out there, too, and I haven't heard that yet, so maybe you will need to share with me this 30 percent figure. I have heard some high figures, but I haven't heard that. And we have talked about this, so I will stop. It just seems like we are trying to tell them how to conduct business to the point it is just stepping too far. So we will explore that some more, as we go along, but at this point I want to yield to my Ranking Member, my friend, Sam.

Mr. GRAVES. Thank you, Mr. Chairman.

Mr. Murphy, as far as the Corn Belt or the big states, what is the percentage of farmers that are participating in crop insurance, corn growers.

Mr. MURPHY. Some of the highest participation, in my testimony I have a map in the back that lays out by state participation, but the "I" States certainly have some of the highest participation, 85, 90 percent.

Mr. GRAVES. Is it that high.

Mr. MURPHY. Oh, yes.

Mr. GRAVES. Last month, the corn growers testified. They, obviously, emphasized the importance of crop insurance as a risk management tool. But they were arguing the loss ratio experience across crops and regions, that it should converge over time. And we

have a pretty big gap right now in loss ratio for corn as compared to other programs. And I know there has been a study that endorsed the current rating systems, but I would like you to address that for just a little bit.

Because it seems to me like we are going have to see some fundamental changes in that. When farmers are out there deciding if they are going to do it or not, that has to be a factor.

Mr. MURPHY. I have talked to growers from the "I" States that have—both corn and soybean growers—have raised this concern about the rate. Especially if you look at the history over the last 10 years, there have been incredible yields, new technology in seed, just a number of things. And when they look at the premium they are paying, which is substantial, even with the subsidies, they have a growing concern whether the program is working for them.

But, it is dangerous only to look at the last 10 years. If we were having this conversation at the end of the 1980s, it would be totally different. The question would be, what is happening to corn production in this country? It is on the decline yield-wise. So in order to do insurance you cannot just look at the last 10 years. You have to look long term.

Our experience in Iowa, Indiana, Illinois, is that you really have high severity of loss, but it doesn't occur that often, which is low frequency. When you look at other states, perhaps Texas, they have high frequency of loss, but they have low severity when they have them. And these play into the whole rating method. Because if you look at Iowa you have to look over long term, and you will find from the mid-1970s that those rates are accurate, and that is what the study found.

Also, for Texas, if you look at it, they have frequent losses but low severity over time. Their loss ratios come up to the mandated $1 loss ratio that we are working on.

And so you have those sort of things that are playing into it.

We did have a study. We were very happy with the group that came in and did this. It involved some of the best ag economists in the country. We had an excellent actuary take a look at those. And, basically, they came back and said our rating method is sound and you can't look at just 10 years, you have to look long term.

So, I think, over all, they did identify some things we need to take a look at. For instance, the losses, the two losses in the 1980s and 1993, is that expected to repeat over time and how should we treat that in a rating? We have a study about to be started on that very issue.

I think we can take a look and expect some changes as a result of the rating. But we have to be careful and be sound as we look at regs, especially in the "I" States which contribute so much to the program.

Mr. GRAVES. As far as participation goes—this is just for my information—in your heavily irrigated areas, what is the participation, just roughly.

Mr. MURPHY. I am very familiar with California. Prior to coming into D.C. In 2005, I was the regional director for the Davis region, which was located in California.

Producers out there tend to take lower levels of coverage as a rule. They invest in their risk management through a number of

other things such as irrigation. Many of them participate with private weather companies so they can invest in that. My experience has been what they will normally do is keep low levels of coverage. If they have a loss, they will start buying up higher levels until their financial stability returns. Then they will drop.

I think that is also an issue with the rice growers in the South. What we have seen is that there has been heavy investment. They have the water systems and the way to get the water to the rice, and to them that is the major concern.

I think that does impact the level of coverage farmers buy, but I think that is to be expected. There are different ways to address risk. We encourage that a farmer look at all different ways.

Mr. GRAVES. Thanks, Mr. Chairman.

The CHAIRMAN. Well, thank you, Mr. Graves.

I now recognize the gentleman from Minnesota, Mr. Walz.

Mr. WALZ. Well, thank you, Mr. Chairman.

And, Mr. Murphy, thank you for the work you do. Thank you for being concerned about the safety net for our producers as well as you are in a very tough position watching out for taxpayer dollars. So I appreciate you tackling this. It is a very difficult one. I think all of us up here see it, too, from the need to make sure that those products are out there protecting them, and also watching out for those agents who are working hard and doing what they need to do.

I have just a couple of questions here. The one I wanted to get at, just slightly different here, on the current policy on the APHs and the transfer to new lands, an area of deep concern for me is new and beginning farmers and ranchers. And I am wondering if you could explain how the current policy of transfer impacts them.

A secondary one—and maybe my colleague from South Dakota will talk about this. She has been a champion and a leader for many years on both these and sod buster in new land. So if you could address that on APHs.

Mr. MURPHY. Sure, Congressman.

There have been concerns raised from both the aspect of a new farmer coming into our program, needing the risk management, and issues have developed, also some of the conservation groups have been wondering if crop insurance is somehow an incentive to break out new lands.

Both of these come under what we call added land provisions of the program. You know, with the way farming is going with bigger farms, this is constantly happening. New farm land is being brought into an existing operation, so we have to have rules to address it.

Now, land that has been farmed within the last 3 years, has different rules than the land that is being broken now, which I think makes sense when you give it some thought. If land has been farmed in the last 3 years and is coming to an existing operation, if it is less than 640 acres, the companies basically handle those requirements. Ensuring that it has similar potential as the current acreage. The management is shown on the existing acreage. You know that certain expectations can come from this, to look at the yields from the acreage that came on. And so they do that, and they make any adjustments.

Anything over 640 acres has to go to the regional office, and the regional office basically works with the company and the farmer to come up with anything that needs to be done, as far as rating or guarantees or that sort of thing.

We do not allow additions of greater than 2,000 acres to an existing unit. These are becoming more and more prevalent, as you can imagine, today. Where this becomes an issue with a farmer entering the program is that if he doesn't have any acreage he is basically using the county yield. He is competing with a farmer that has an APH, perhaps 6 to 10 years, a very good APH. And with that kind of protection, can that existing farmer outbid the beginning farmer? And, definitely, there is a potential for that occurring, so I think that is a potential issue.

Mr. WALZ. What is the solution, in your mind.

Mr. MURPHY. I would like sometime to discuss that sort of thing and maybe even bring in some other people who have been looking at these issues.

Beginning farmers definitely are facing a challenge. You know, you get a new guy who has only 3 years of record, and he gets a loss. I mean, that is a tremendous impact.

Mr. WALZ. Well, I would look forward to working with you on that one. It is one of the concerns I have, and it is an area we have taken up that I think it is a concern and a growing concern as we age out in farm country.

The last question I had, I wanted to come back to you and try and get this right. You pointed out American Growers failure in 2002. It is your assessment that high agent commissions were the sole failure in that company?

Mr. MURPHY. No, certainly not the sole, but it was a major contributor to it.

Basically, the company was relying on a 10 to 15 percent underwriting gain in order to make up all——

Mr. WALZ. And you said you brought actuarial folks in to take a look at that?

Mr. MURPHY. Oh, yes, we have studied that body.

Mr. WALZ. That is the canary in the coal mine, that you think that model could replicate down the line.

Mr. MURPHY. Yes, I am concerned, and there are some other things.

One of the things we did after the failure of that company is that we actually went ahead and paid all agent commissions that year. We were roundly criticized by the audit agencies and some Members of Congress for doing that, but we thought that was the best way to get the agent cooperation and get this business moved off to the companies, and they did a fantastic job of it.

I am afraid if this happened again I don't know if I would be able to make that commitment. I am wondering what impact that will have on ability of that business, of growers being stuck out there with no coverage?

Mr. WALZ. Very good.

I yield back. Thank you, Mr. Chairman.

The CHAIRMAN. Thank you, Mr. Walz.

I am having trouble keeping track of our panel here. I see Ms. Herseth Sandlin stepped out. I will now recognize the gentleman from Oregon.

Mr. SCHRADER. Just a few simple questions, I guess.

You have testified a little bit about the increased competition you hope to see in the marketplace. And with the renegotiated SRA, how many companies are in the—for my benefit, anyway, how many companies are in the mix right now, and how many more do you see coming in as a result of the renegotiation?

Mr. MURPHY. Currently, we have 16 companies. Our most recent entry was right in the middle of the negotiations. We had a new company come on. They actually got involved with spring sales for 2010. They will do the full year in 2011. It is very difficult to foresee how many companies are going to come in, in the future. We will have to see.

It is interesting the companies that have been coming in, sort of different companies than traditional insurance companies. We have John Deere involved in the program. AEM has some involvement in the program. So it is interesting, the mix that we are seeing in it. But I don't think I can say how many we will have.

Why companies leave, that is interesting as well. The last time we had a company leave was basically in the middle of the best year the industry ever had. Okay? And then we have a company come in when we are right in the middle of a negotiation of the SRA. So it is very difficult to see what draws companies in or draws companies out. It is a mix of factors, certainly not just the underwriting gain potential of the agreement.

Mr. SCHRADER. What is reasonable agent compensation? This is a pretty Byzantine system, from my standpoint, that, obviously, there is a goal, that you consider some reasonable rate of return for an individual agent or for a company, frankly, both those.

Mr. MURPHY. The company we did a study with, Milliman—take a look at that. It is on our website. It has been part of the negotiations and a source of a lot of discussion.

But why we are especially happy with this individual who did the study is he actually does this for the private insurance industry at the state level. He argues on behalf of the companies. He uses the same methodology for this study of what the companies could get.

Basically, what his study came back with is that they should over—historically, it should have been—about 12.7 percent would have been an adequate return. Historically, the companies have received about 17 percent. But although he was very careful to say, I am not saying that you should make it 12.7. I am just saying if you look at different methodologies that is where it comes up to. You have to take other things into consideration.

In the final agreement we ended up at 14.5 percent long term. Certainly there will be years when the companies make much more than that, and there will be years when they make much less. You are looking at an average over time.

In today's economy, I think a 14.5 percent return is pretty good. I wish I was getting a 14.5 percent return.

So, agents, it is trickier, definitely. We don't really have a lot of good data. Like I said, GAO did a study. You can look at it a num-

ber of different ways. I think it would be considered a mono-line in the normal insurance world. That sees ten percent, a little bit more than that, commission. Definitely, the agent has the more difficult role in our program.

You know, I often tell the story that I have property in Pennsylvania: I live here in D.C; I insure cars; have rental insurance; my property up in PA; I have never met my agent. Yet, a crop insurance agent, is visiting with the insured two to three times. So, I think additional compensation is certainly justified.

Why I am generally pleased with where we are today in the agreement is that, in 2010, under the current SRA, we are going to pay the companies about $1.3 billion in A&O. That basically is what will occur in 2007 without—or 2011 with the new SRA if there are not a lot of changes in price or volatility. So if the companies can operate today and the agents can operate today at the current amount, I don't see where there would be a major problem in the future.

Mr. SCHRADER. Thank you very much. I yield back.

The CHAIRMAN. Well, thank you.

Well, on that very subject you just finished on we are going to have to discuss it some more. You just said a very significant statement that I was getting ready to say to you. You said it, so I want to appreciate that.

A lot of agents for other things I insure for, I never see them. But my crop insurance agent, I not only see him, he would walk the fields. In some cases, I spend a lot of time with him.

So it is very critical that you do the best you can, and it is capital intensive for that producer out there. And you want what you need, but you don't want something you don't need. And so they spend a lot of time.

I am very sincere when I say the three elements that that producer has to have today is not only the capital intensive, the banker, he has to be able to work with, and they have a cash flow. They have to show they have this protection.

And then of course they have to have a place to buy and sell product. And I think it is right up there, same level, they have to have a good insurance agent. In every community we have insurance agents, and they are very much a part of the community. And Mr. Graves and I, all of us, travel back and forth. We have a lot of contact. And I want to you appreciate that, too, and I think you do.

I thought we were going to let you go, but I see Mr. Pomeroy has arrived, so better late than never. You were here for a while. Then you were called out. We are happy to recognize the gentleman.

Mr. POMEROY. Thank you, Mr. Chairman.

Crop insurance has been an issue I have long been deeply interested in, and it is such a critical risk management element of North Dakota ag production that I did want to participate in the hearing. I am trying to have two meetings at once, and that never works all that well, so thank you very much.

The CHAIRMAN. I am supposed to be in Armed Services right now, but, anyway, go ahead.

Mr. POMEROY. We have had some activity here with the crop insurance. This isn't your run of the mill, what is up with RMA.

They have absolutely worked through the most substantial and substantive process relative to the SRA renegotiation that we could have imagined.

I want to put a little history on the effort. Because if you just look at—let's take the crop insurance industry's perspective. If you look at the losses taken, are these changes made which will result in savings to the Federal Government; therefore, checks not written to private insurance companies and agents? There may be just enormous concern.

But, on the other hand, we had a very, very dangerous stretch during the last farm bill where others wanted to take apart this program. In fact, it was to our great surprise that the Government Oversight Committee, without notice to the Agriculture Committee, held a hearing on crop insurance. They had a GAO report written by a disgruntled GAO employee, in my view, that didn't know very much about crop insurance, but had long held a view that there was unjust payment to the private sector within crop insurance. They wrote a report that was precisely what every enemy of farm programs wanted.

We worked so long and hard to build a crop insurance program that was getting adequate coverage out to farmers, the 1993 reforms, the ARPA legislation. And we saw the market response in terms of national spread of risk, at buy up levels, a tool that really is beginning to function like it never has in terms of meeting risk protection needs of farmers.

And to have our city friends in another Committee without so much as giving us the dignity of acknowledging their investigation was a bit much. We had some very angry words with some of our city friends, including down on the House floor as the farm bill was being pushed forward. There was more than one occasion where we came within an eyelash of devastating, mindless cuts, imposed by those that don't know the first thing about risk management for farming.

The lesson I drew from that is we needed to take a look at this program, sensitive to the concerns of the program's critics, and make an evaluation. Were they right? Were they wrong? If changes needed to be made, we are the architects that needed to make them. And I believe that basically the farm bill gave us the opportunity with the SRA to have that take place.

I would contrast this SRA with the preceding SRA renegotiation in very important ways, most notably an element that you capture in your testimony, Mr. Murphy. RMA and the companies negotiated in good faith with respectful dialogue. You know, even that alone was missing in the last go-around.

The target was handed down by OMB. It was not reached in consultation with the crop insurance companies, I will tell you that. Some green-eyeshade guy put a number on a page, and RMA was given the assignment of jamming it into the program.

From the beginning, it wasn't as though I didn't have some substantial concern about the directions of RMA, but in meeting with you, Mr. Murphy, as well as Mr. Miller I felt that there was an earnest effort to proceed in a very rational, substantive way, using, among other things, the consulting assessment that we have done on the program.

I believe that the end result, the SRA, will reflect the most substantial entitlement savings generated by anybody relative to addressing Federal budget deficit. We will be able to hold our heads high when we next go into a farm bill with a crop insurance program structured basically as the SRA has provided.

I certainly don't want to minimize our private-sector partners looking at this kind of savings and feeling not all that great about it. That was a very substantial change. But I would tell them this was a case where change was going to be made, we were going to make it, others were going to make it, it was going to be made substantively, it was going to be made with a meat ax. I believe the process that came out represents a very serious and fair effort.

The fact that we have universal participation in the SRA by the 16 companies that are our private-sector partners reflects, in the end, an acceptance of the product. I commend the industry for coming to the table, for providing the counsel, in the end for taking the tough medicine.

You know, like a lot of things, this may not be everything people hope for, but it could have been a lot worse. I am quite confident that this will work, that our farmers at the end of the day, bottom line, will be able to continue to have quality risk-management products. So I thank you for leading this effort, Mr. Murphy. It is one I admire.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you.

Mr. Murphy, we are going to stop here. I do invite you to stay and listen, if you possibly can. I am not going to call you back to the table, but I might call you. And I do want to close this. You have been very open, and I appreciate that. We want to do the same with you, and continue this dialogue, and we want to do the best we can for the responsibility that we all have. So thank you very much and appreciate your witness today.

Mr. MURPHY. Thank you, Mr. Chairman and the Committee.

The CHAIRMAN. You bet.

I would like to call the second panel to the table.

Mr. Murphy, first change of the day, sit back down, please.

Second panel will just hold momentarily. Mr. Peterson has joined us, and we would like to recognize him before we dismiss you—before we finally dismiss you.

Mr. Chairman.

Mr. PETERSON. Thank you, Mr. Chairman. Thank you for your leadership.

I wanted to pursue this what they call administrative PAYGO, I guess, and exactly how this is working. So, as far as you know, they are definitely going to take $2 billion of this and put some of it into rangeland and some into CRP, is that the case?

Mr. MURPHY. That is my understanding, Mr. Chairman.

Mr. PETERSON. So we will be able to get those programs up to where—the question is—I still don't understand. That stuff was in the farm bill. We found the money to pay for it. So I don't understand why the money is not there. Do you know why it is not there?

Mr. MURPHY. Unfortunately, I am not aware of the specifics. I have heard you raise this concern before. I believe you were going

to have some conversations with folks, with OMB and the Administration. I think they would be better suited to address your concerns. I believe that is in the budgeting process, as you know, that I am not that strongly familiar with.

Mr. PETERSON. So nobody ever told you anything about this? Were there discussions about when you were finalizing——

Mr. MURPHY. No, no. Basically, my discussions were when they denoted some of the money for crop insurance work for expanding a PRF, asked us to take a look at what other expansions were on the books that could be done and how much money we would need for them. I took a look at that to develop a good performance discount, which hopefully we will be able to make public soon.

But I am not aware of the specifics on why so much money was put into one. I believe it has something to do with mandatory—you can only take crop insurance savings that you would take out of crop insurance. It could only be used for other programs. You can't do it across the board, only certain things. That is the extent. Because some ideas came up to do some other things with the savings, and the decision was you couldn't legally do certain things.

Mr. PETERSON. So they could do it to restore mandatory money but not discretionary money?

Mr. MURPHY. Apparently. There may be more in-depth budget rules that apply, but I would not be aware of them.

Mr. PETERSON. It is still a mystery to me why we paid for 32 million acres of CRP in the baseline and why there wasn't money to do that. And we haven't gotten any answers from anybody of what happened to that money. It disappeared someplace, I guess, but—so you didn't—you don't know anything about that.

Mr. MURPHY. No, no, no. Just basically what I told you before. So my understanding is that the decision was made a few years ago to do this. I think it evolved in anticipation of how much acreage would be enrolled in CRP.

Mr. PETERSON. Well, if they didn't have a sign-up, there wasn't going to be acres enrolled. It doesn't take a rocket scientist to figure that out.

Mr. MURPHY. I was very happy that some of the funding out of negotiation——

Mr. PETERSON. Well, we are glad they are getting these programs up to where they are supposed to be, but it is very troubling. We have the appropriators over—on our mandatory programs. Now we have OMB apparently doing something similar. And, we struggle to find the money to be able to do this stuff, and then somebody else diverts it.

Well, if you ever find out anything, we haven't gotten any information back from OMB yet.

Mr. MURPHY. I would be happy to bring the questions back and your concern and see if they can get something up to you.

Mr. PETERSON. All right, thank you.

Thank you very much, Mr. Chairman.

The CHAIRMAN. Thank you.

Mr. Murphy, we are going to excuse you again. Thank you again for your testimony and I hope you appreciate that a lot of us share the same concerns that you just heard from Chairman Peterson, and maybe you can shed some light on that.

We would like to welcome the second panel to the table. Just as a matter of short introduction, we have Mr. Rutledge, President of Farmers Mutual Hail Insurance of Iowa, on behalf of Crop Insurance Research Bureau; Mr. Robert Parkerson, President of National Crop Insurance Services of Overland Park, Kansas; Mr. Steven Frerichs, the Legislative Consultant at Rain and Hail, on behalf of the American Association of Crop Insurers.

I am going to skip over Mr. Deal and let Mr. Walz introduce him in just a moment.

Mr. John Dalton, President of Midwest Insurance Associates, President, Agri-Land Insurance Agency, on behalf of Independent Insurance Agents & Brokers of America; Ms. Kathy Fowler, President of National Association of Crop Insurance Agents, Memphis, Texas; and Mr. Jordan Roach, Vice Chairman, Crop Insurance Professional Association of Fresno, California.

Mr. Walz, would you like to introduce——

Mr. WALZ. Well, thank you, Mr. Chairman.

It is an honor for me to introduce another Minnesotan, but I think somebody here probably needs less than me. Jim Deal has been involved in this crop insurance business for the past 50 years, and was instrumental during the Carter Administration of moving this from a government-run program to the private sector. He has done everything from Manager of the Federal Crop Insurance Corporation, Executive Director of National Association of Crop Insurance Agents, CEO and Chairman of National Ag Underwriters, currently CEO and Chairman of NAU Country Insurance Company. But I think it is important to note, with all of us in this room, he was instrumental in providing the tools necessary to make rural America thrive, and is somebody who has been heavily engaged in resources from veterans' issues to others in building our strong communities.

So it is a real honor for me to introduce Jim Deal, lives with his wife Pam in Ramsey, Minnesota, and countless grandchildren that are always there.

So thank you.

The CHAIRMAN. Thank you, Mr. Walz. I appreciate that.

With that, we will begin with Mr. Rutledge who brings—hello again—vast experience from an agent up through the industry. We appreciate having you here. Would you start, and share your testimony?

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

Mr. RUTLEDGE. Chairman Boswell, Mr. Graves, Chairman Peterson, Members of the Committee, good morning.

My name is Steve Rutledge, and I am the President and CEO of Farmers Mutual Hail located in West Des Moines, Iowa. Farmers Mutual Hail has been in the business of offering risk management tools to agricultural producers for over 117 years. I believe we were the first company to successfully write crop insurance in the United States.

In addition, I am also the past Chairman of CIRB, Crop Insurance Research Bureau. CIRB is a national trade association composed of insurance companies, reinsurance companies and brokers and others involved in the crop insurance business. I appear before you today on behalf of CIRB and thank you for the opportunity.

As it turns out—and you just mentioned it, Mr. Chairman—when we had the opportunity to speak a couple of weeks ago back home in Iowa I had asked if there were any specific issues that you might like me to address, and you suggested that I just say what I think, and so I will.

At the time the 1980 Crop Insurance Act was passed, Farmers Mutual Hail was one of several who declined to participate and remained just a private crop hail insurance writer. That decision made 30 years ago seemed reasonable until the mid to late 1990s. During that time, private industry developed revenue insurance and government greatly increased subsidies to the producers. Those were excellent products, and we quickly realized that times had changed and we would no longer survive unless we chose to participate in the Federal Crop Insurance Program. So we joined the program in 1999.

Since then, there have been three SRA negotiations, two farm bills, and each one reduced the industry's potential profit margin, while further increasing the workload. Like many others in the business, I feel like I have spent virtually all of those 11 years either trying to figure out how to survive and compete after the most recent round of cuts, or working to minimize the pain of the inevitable next round. In fact, much has changed just since I last testified before this Committee in the 2007.

Given the cuts in the last farm bill and the new SRA, the industry has finally reached the point where many companies are considering leaving the business and are selling their ownerships to larger, more diversified and more well-capitalized companies. It seems the days of crop-only insurance companies are rapidly passing, and that fact should probably worry us all. Since the last SRA was negotiated in 2005, nearly ⅔ of the 16 companies which still remain in crop insurance have altered their original ownership and structure. Many agents are now also beginning to search for opportunities to sell or restructure their agencies, and many commercial reinsurers are questioning the viability of crop insurance in their business plans. It seems inevitable that more jobs will be lost and the face of the industry will change.

The result of the changes made during the past couple of years, particularly for the Midwest, will likely be fewer companies, fewer agents, fewer reinsurers, and fewer jobs, all likely leading to a decline in the quality of service to the producers. And I don't think the industry is crying wolf here, because this time the sheep are already running away.

Yes, we all signed the SRA, but, to paraphrase Secretary Clinton, how do you get tough with your regulator? Nonetheless, I imagine the industry and the program will survive, but we are diminished. We won't be as good as we could be.

And this program has been extremely successful. The private-sector involvement in the crop insurance program has given our nation's farmers and ranchers, on whom this country so depends, the

best possible tools to ensure their continued survival. Now it seems that we should turn our attention to the survival of the crop insurance industry.

As we begin discussions on the next farm bill, it is my sincere hope that we can all work together to improve the health of the industry, thereby securing the integrity of the program. The Federal Crop Insurance Program is the envy of the agricultural world and is the core of our own country's agricultural safety net. How can we not protect the program that has served the country so well?

Thank you for your time and attention.

[The prepared statement of Mr. Rutledge follows:]

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

Chairman Boswell, Ranking Member Moran, Members of the Committee, good morning. 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 the agricultural producers of the Midwest for over 117 years, and today writes both private hail insurance and federally reinsured Multiple Peril coverage in 15 states. Additionally, I am the past Chairman of the Crop Insurance Research Bureau ("CIRB"), headquartered in Washington, D.C., and currently serve on the Executive Committee of that organization. CIRB is a national trade association composed of insurance companies that write Federal crop insurance as well as private crop-hail insurance, commercial 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-sized crop insurance companies. Our members write in nearly every state and provide billions of dollars in federally reinsured multiple peril crop insurance protection, or "MPCI." These insurance company members bring to the Federal partnership a wealth of knowledge about the MPCI program and are committed to providing risk management support to the farmers and ranchers of this nation. Our membership also includes some of the most significant members of the private commercial reinsurance community in terms of their involvement in the crop insurance program. These members are vital to both crop hail and Federal crop insurance, and we are proud to be a leading voice within the industry for the reinsurance community.

In my testimony I will attempt to illustrate the importance of the public-private partnership in the delivery of the Federal Crop Insurance Program, the necessity of continued support by private reinsurance companies in managing the program risk of Approved Insurance Providers or "AIPs," and finally the expected impact of recent changes to the Federal Crop Insurance Program on those segments of the industry, as well as to the agents who comprise a significant part of the delivery system.

Perspective

Much has changed since we last appeared before this Committee in 2007. The spike in commodity prices that occurred during the 2008 reinsurance year put the crop insurance program on tenuous grounds, with regulators becoming concerned that companies and agents were too profitable. Although both initially benefited from the increase in prices, the landscape has since changed. Crop prices have declined significantly, as have the rates charged to producers. The largest reductions in rates took effect in the 2010 reinsurance year, with additional cuts expected for the 2011 reinsurance year. This combination of price and rate decline will cause the Federal Crop Insurance Program premium to shrink from over $9.8 billion in 2008 to an estimated $7.0 to $7.5 billion in 2011. The savings in A&O paid to AIPs due to this decline has contributed greatly to the savings achieved by RMA.

In this context, the industry took a substantial financial hit in the 2008 Farm Bill, with cuts totaling $6 billion over 10 years. While some of these cuts came in the form of timing shifts, their impact cannot be underestimated. Furthermore, as the industry worked to absorb and adjust to these reductions, the U.S. Department

of Agriculture embarked on a renegotiation of the Standard Reinsurance Agreement, or "SRA." While I will go into more detail on that in a moment, the end result of the renegotiation was another $6 billion cut to the program that in part sought to address "yesterday's" problem.

The reduction in funding does not mean that the crop insurance program has become less complex. Just the opposite is true. Regulatory compliance requirements of the program, especially with the advent of the 2011 SRA, have intensified thereby compelling AIPs to spend more of the fewer dollars available to assure conformity with the program. The financial cuts and added compliance costs come at a time when the industry is struggling to manage many large and complicated system changes, while at the same time managing an ever increasing number of pilot programs, plans, coverage levels, and additional training requirements. The additive nature of these stresses combine to put the industry at risk.

It is important to emphasize that the Federal Crop Insurance Program as it exists today is the cornerstone of our agricultural safety net and the envy of the rest of the world as other nations attempt to replicate our success. The clearest illustration of the value of the program is that roughly 80% of our nation's farmers recognize the importance of the program by investing premium dollars in MPCI products. Subtract so called "hobby farms" and it is not inaccurate to say that virtually every farmer in this country buys MPCI. Crop insurance has played a vital role in maintaining the availability of credit for farmers who need ever larger loans to cover rapidly escalating input costs. Ag lenders have made it clear to their borrowers that without this income security, credit will not be forthcoming. This was true before the credit crunch; it is even more focused since the onset of the current crisis.

The Federal Crop Insurance Program currently provides a level of security and flexibility for American agriculture that likely exceeds the expectations when the public-private partnership was first legislated into existence 30 years ago. The program, which initially offered only yield protection for mostly row crops, has expanded into a national insurance system that allows farmers and ranchers to manage both weather and price risks. Our success has been rooted in significant government investment and a robust private sector delivery and risk-sharing system. The products offered by crop insurance have proliferated so that companies and agents can tailor coverage to the individual farmer's needs. Additionally, crop insurance providers have introduced greater efficiency into the program, relying on greater volumes to repay costs and ultimately dipping into profits to preserve a viable system.

Today, in addition to providing protection for yield losses, crop insurance companies also offer price protection with the revenue plans of coverage that comprise about 80% of the total insurance sold. The majority of these revenue products were initially developed by the private sector. This type of insurance coverage not only provides considerable protection for producers, but also provides yet another level of security for lenders, thus increasing 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 proactive 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.

We also believe that access to commercial reinsurance is a critical component of this public-private partnership. From the perspective of our members, private reinsurance provides an invaluable benefit to the program by enhancing the capacity of AIPs. Without this benefit, less well-capitalized companies could be forced to sharply reduce their volumes of business in order to maintain adequate levels of capitalization relative to premium. The availability of commercial reinsurance also enhances competition, reducing the risk to the government that could arise if only a few insurers were able and willing to deliver the program. Not only does commercial reinsurance make it possible for new companies to enter the market, but also it allows for AIPs to gain experience in new markets without risking significant portions of their own capital. Against this backdrop, it is counterintuitive that USDA has chosen, once again, to transfer more risk to the taxpayers and away from AIPs and their reinsurers in the new SRA.

We believe that a strong, viable crop insurance program is critical to the future of American agriculture. I doubt that our younger farmers who have struggled to acquire the resources necessary to begin a successful operation could even contemplate a career in farming without the Federal Crop Insurance Program, and I believe we all agree that we need more youth in agriculture. Simply put, the value

of the Federal Crop Insurance Program to American agriculture cannot be overstated.

2011 Standard Reinsurance Agreement

The 2008 Farm Bill authorized USDA, through the Risk Management Agency, to renegotiate the Standard Reinsurance Agreement for the 2011 reinsurance year, which began on July 1. We have just completed that task, and all 16 Approved Insurance Providers have signed the 2011 SRA. While we appreciate the willingness of RMA to consider the views of the industry throughout the months-long process, we remain concerned about the implications of the final product for the future of crop insurance.

Generally, we believe that the roughly $6 billion in cuts to the program will jeopardize the viability of several AIPs and agents in their ability to provide critical risk management support to producers. In addition, we were also troubled during the process by the introduction of various changes in the three different drafts of the agreement that did not appear to result from the negotiations. But, to paraphrase Secretary of State Hillary Clinton, "how do you get tough with your regulator?"

For example, we question the provision that was included for the first time in the third draft of the SRA that penalized AIPs who sued the Department of Agriculture, even if the suit was not filed directly by the AIP. While the provision was converted into a covenant not to sue through negotiation, we question the late addition of the issue and the insistence that agents be included in the covenant, especially given that agents are not a party to the SRA contract.

We also note that the issue of capping compensation to agents was not introduced until the second draft and even more worrisome, the introduction of an even more stringent "hard cap" on commissions was not included until the third draft, which was presented to the industry as "final" thus affording industry no opportunity to discuss this issue. We believe that had there been genuine concern regarding company insolvency, which seems to relate to the 2002 year, this should have been addressed in the 2005 SRA or in an earlier draft of the 2011 rewrite.

We are also disappointed that RMA chose not to phase in the changes to the gain/loss formula in the Group 1 states. Doing so would have provided AIPs with the financial flexibility and additional time needed to geographically expand their operations, a strategy which RMA seems to provide incentive for in the new SRA. Further, since the rationale for reducing potential underwriting gains in Group 1 states was predicated partly on the premise that these states were more prone to infrequent but very catastrophic events, the decision to greatly increase risk to AIPs in these states compared to all others seems a bit contradictory and also disappointing. RMA's approach instead hinders the opportunity for AIPs to adjust their business plans to account for the changes in the new SRA, in particular the likelihood that their commercial reinsurance costs will increase for business written in Group 1 states due to the reduced profit margins and increased risk.

Along those lines and given our substantial reinsurance membership, we also emphasize that this SRA could have significant ramifications for the private reinsurance market as it shifts risk away from the market and to the government. For instance, under the new SRA, quota share reinsurers may see reduced profit-sharing opportunities and will therefore have less of an incentive to participate in the market. The reinsurance community is well prepared to manage risk within crop insurance but with this SRA, as previously mentioned, RMA is effectively removing risk from a market that has worked successfully for years and instead placing a burden on the American taxpayer.

Moving Forward

The 2008 Farm Bill and the 2011 SRA have exacted their toll on crop insurance. The industry is now holding its breath as Congress begins to consider the 2012 Farm Bill. As we start that process, we must emphasize that crop insurance has already borne the brunt of the fiscal pressures facing Washington multiple times. We have found ourselves under the scalpel, and we fear that further mandated reductions that may be considered in the 2012 legislation will place the program in an even more precarious position.

We remain confident that a viable farm safety net starts and ends with a successful crop insurance program. We understand that a number of proposals that affect crop insurance have been floated for the farm bill rewrite. We will review each of them carefully. From the recent hearings held here in Washington and across the country, however, one key area of agreement is obvious: the Federal Crop Insurance Program is an essential tool for American farmers.

The crop insurance industry has continued to perform reasonably well over the past several years. To that extent, the industry may well be a victim of its own suc-

cess. In reality, though, it has been the unprecedented run of profitable years, occasioned by generally favorable weather patterns, that has allowed the industry to survive without a major upheaval of the marketplace. Nonetheless, many AIPs were forced to make operational changes during this period, including selling to larger, more well-capitalized companies in order to secure their survival. Since the last SRA went into effect in 2005, less than ⅓ of the AIPs have maintained their original ownership and organizational structure.

With the changes that I have discussed, however, USDA has gone too far. Virtually every AIP has had discussions regarding new sales, mergers, or acquisitions. In addition, many agents have already expressed the desire to move some of their work back to the AIPs or are attempting to negotiate the outright sale of their agencies. The new reality is that AIPs and agents seriously question the future in the crop insurance business and many are choosing to search for a way out. Jobs will be lost, service to producers will suffer, and the face of the industry will change. Those who remain simply hope that their faith in the eventual recognition of the value of the private sector in crop insurance has not been misplaced.

We look forward to working with you in the coming months and years as you continue to fashion our farm policy. We thank you for the opportunity to testify, and we stand ready to answer any questions you may have.

EXHIBIT A

CIRB Full Members

- ADM Crop Risk Services
- American Agricultural Insurance Company
  - Arkansas Farm Bureau
  - Idaho Farm Bureau Insurance
  - Indiana Farm Bureau Insurance
  - North Carolina Farm Bureau Insurance
  - Oklahoma Farm Bureau Insurance Company
  - Virginia Farm Bureau Mutual Insurance Company
- ARMtech Insurance Services
- BMS Intermediaries, Inc.
- COUNTRY Insurance & Financial Services
- Farmers Mutual Hail Insurance Company of Iowa
- Guy Carpenter & Company, LLC
- James River Insurance Company
- Partner Re Insurance Company of the U.S.
- Totsch Enterprises
- Western Agricultural Insurance Company

CIRB Associate Members

- Aon Re
- Endurance Reinsurance Corporation of America
- MAPFRE Re Insurance Corporation
- Max Re Europe Limited
- Munich Reinsurance Company
- National Association of Mutual Insurance Companies
- State Farm Fire & Casualty Insurance Company
- Sirius International
- Swiss Reinsurance

The CHAIRMAN. Thank you for your testimony.

We will move on and hear from all of the panelists, and then we will go back for questions.

At this time, I recognize Mr. Parkerson, President of National Crop Insurance Services, Overland Park, Kansas. Welcome.

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

Mr. PARKERSON. Thank you, Mr. Chairman.

Mr. Chairman, Mr. Moran, and Members of the Committee, thank you for inviting the National Crop Insurance Services to today's hearing.

NCIS is a nonprofit trade association consisting of all 16 SRA holders. In 2009, the insured Federal crop and hail liability of our members totaled $150 billion. Starting over a year ago, NCIS coordinated the industry's participation in the SRA negotiation. The companies carried out their activity transparently and in good faith. We sought a new agreement that would be ensuring effective service to the producers, safeguarding taxpayers' interest, and providing the companies an opportunity to earn a reasonable return. Unfortunately, this final agreement may have put some of those objectives at risk.

The first SRA draft released in December set an ominous tone to the negotiations. With $8.4 billion in cuts, the Administration staked out an extreme position well beyond, we believe, their targeted cuts. They knew from the outset that the companies would have no choice but to accept the final outcome.

This outcome remains fraught with problems. For example, the overall cap on A&O reduced the effect on price spikes on A&O payments, as we all required and hoped for. But the reality is A&O is cutting in on top of the farm bill. These cuts are large. The agents' compensation is capped.

Those changes were made without adequate study of delivery costs at a request by GAO. The hard cap on agent income was first revealed in the final SRA without any opportunity to comment. The A&O provisions will cause competitive issues and operational problems, as noted in my written statement.

Had the new SRA been in effect in 2009, A&O and underwriting gains would have been 25 percent lower in the Group 1 states and six percent lower in other states. We fail to see how such cuts could stabilize the industry and raise incentives to improve service, as the Administration has claimed.

Looking ahead, we find little security in the development of the past 2 years and the prospects that lay before us. Regulatory burdens continue to rise, including IT, data reporting, quality control, and training.

One of the stacks of paper before me is the procedures for 2005, the smaller one. The higher stack is the new SRA and its requirements. Clearly, the workload is not declining.

In short, Mr. Chairman, the companies must do more. They will be under a strain to do it, as they are going to get paid less and get paid less often.

The SRA raises issues also for Congress. We ask this Committee to help us ensure that the SRA receives recognition for this deficit reduction, hopefully preventing any further reduction in production agriculture.

Congress also should be considering the SRA process. Companies have very little leverage to negotiate any equal partnership with RMA. The final SRA introduced a new process, non-negotiable con-

cepts without industry comment, including the agent's hard cap and the requirement to forego legal recourse. We are concerned that a multi-billion dollar change in the legislative program can be made through unilateral discretion.

The crop insurance companies are committed to the public-private partnership. Together, we have built a program that now provides $80 billion in protection, up $31 billion from a decade ago. Insurance is now available for over 100 crops and most livestock types. It is unthinkable today that the farmer could plan, secure credit, invest in forward market, as they do, without individual crop insurance coverage tailored to each producer's unique need.

With your help, we will strive to keep this enormously successful program as the producer's best defense against future risks that are inherent in farming.

Thank you, Mr. Chairman. That completes my oral statement.

[The prepared statement of Mr. Parkerson follows:]

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

Mr. Chairman, Mr. Ranking Member and other Members of the Subcommittee, thank you for inviting the National Crop Insurance Services to appear at today's hearing to discuss the Standard Reinsurance Agreement (SRA) and its implications for the future of the crop insurance industry. I will briefly describe the role of NCIS and the approved insurance providers (the companies) in the negotiations of the 2011 SRA, identify some key issues of agreement and controversy, and conclude with an assessment of why the new SRA, combined with other factors, raise serious concerns for the crop insurance industry as it moves ahead, striving to provide the best in risk management service to America's agricultural producers.

The Function of NCIS in the Crop Insurance Industry

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.

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 2009, NCIS member companies wrote nearly $9 billion in Federal multiple peril crop insurance and related revenue products premium and $620 million in private Crop-Hail insurance products premium. The potential liability between both programs was approximately $105 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 the preeminent risk management program to America's farmers.

Role of NCIS and the Companies in the SRA Negotiations

NCIS began preparations for the new SRA early in 2008 by engaging company leaders on the future of the industry. By early 2009, after being advised by the Administration that the 2005 SRA was unlikely to be renewed for the 2011 reinsurance year, NCIS and all 16 companies that deliver the Federal Crop Insurance Program to America's farmers met and initiated a specific plan for negotiating the new SRA. NCIS organized five working groups, chaired by and consisting of representatives from all 16 crop insurance companies. The working groups addressed five subject areas: financial provisions, the Plan of Operations, information technology and data, quality standards and controls and education and training. The working

groups met beginning last spring, reviewing the performance of the 2005 SRA and developing recommendations for the 2011 SRA.

In September 2009, RMA notified Congress that the 2005 SRA would not be renewed. In October 2009, in response to RMA's request for SRA proposals from the industry, NCIS submitted formal recommendations for the 2011 SRA on behalf of its member companies and reflecting the efforts of the working groups. Since December 2009 when RMA released the first SRA draft until mid-July 2010, when the 2011 SRA went into effect, NCIS and the companies held frequent meetings with RMA and provided substantial written comments to RMA on the first and second drafts. NCIS also organized a technical, legal review of the final SRA conducted by NCIS and company attorneys. Throughout the process, NCIS was very aware of antitrust issues and worked closely with USDA's Office of General Counsel, RMA leadership, industry leadership and third party legal counsel to ensure the negotiations were conducted properly. On behalf of the industry, we thank Members of Congress for including language in the 2008 Farm Bill that ensured the companies could confer with one another and with RMA in developing the new SRA.

NCIS and its member companies organized and carried out their activities with the primary objective of negotiating transparently and in good faith. Among our objectives was a new agreement that ensures effective service to producers, safeguards taxpayers' interests, and provides an opportunity for the insurance companies to earn a reasonable return relative to other lines of insurance, accounting for their relative risks. Unfortunately, the final agreement may put all these objectives at risk.

The Negotiations: Substantive Issues but a Predetermined Outcome

The first draft of the SRA released in December 2009 set an ominous tone for the negotiations. The first draft was a significant overreach by the Administration. The Administration proposed an unprecedented and potentially very damaging reduction of $8.4 billion over 10 years in program funding. They proposed an inflexible formula for calculating administrative and operating (A&O) expense payments to the companies that would have used a proxy measure of premiums based on fixed "reference prices." These reference prices were sharply below policy prices and would never change. The first draft replaced the Assigned Risk Fund with a "Residual Fund" that would have enabled companies writing bad business to shift their risks to other companies. The first draft's reinsurance terms created separate gain and loss provisions for four different groups of states; groupings that had little apparent rationalization. The reinsurance terms sharply reduced potential gains while also reducing potential losses, in effect shifting risk to taxpayers and crowding out private reinsurance. Moreover, the Administration proposed increasing the net book quota share—its tax on underwriting gains—from 5% to 10%. Crop insurance companies are in the business of taking on and managing risks, but the Administration wanted to take over risks and the potential for gains as well, moving away from the Federal Crop Insurance Act's reliance on private industry and exposing the taxpayer to greater losses in bad years.

I will not belabor the industry's position at the beginning of the process, beyond saying that the Administration's first-draft overreach was so great that subsequent concessions by them would still leave the companies at a serious disadvantage. Clearly, the 2011 SRA was a budget-driven process that took full advantage of the companies' short-term inability to exit the program. Congress authorized a negotiation in the 2008 Farm Bill presumably with the idea that it be open and balanced. But, the Administration had a budget cutting target and simply staked out an extreme position to the right of it, knowing full well that, in the end, the companies had no choice but to accept the final outcome.

In the second and third drafts of the 2011 SRA, the gap between the Administration's proposals and the companies' proposals narrowed. The reference price concept was thrown out, the Residual Fund concept was dropped, the number of state groups for reinsurance terms was reduced from four to two (the first group includes the Corn Belt states of Iowa, Illinois, Indiana, Minnesota, and Nebraska and the second comprises all other states), and the reinsurance terms were improved for the companies. There were a number of concepts that companies and the Administration could agree upon. Both sides wanted to address the concern that A&O payments could unnecessarily shoot up when there are market price spikes, such as occurred in 2008. Both sides agreed that reinsurance gain and loss provisions should be made more profitable for the lowest return states and reduced for the highest return states. This "rebalancing" of returns would help companies cover costs and hopefully earn a small underwriting profit in the low return states.

Unfortunately, the final 2011 SRA fails to achieve a fair balance among these shared concepts. The final draft has been signed by the 16 companies, but that

hardly means the companies think things are satisfactory. Here are a few of the glaring issues with the 2011 SRA:

- The size of the overall funding cut remains unsupported and represents a decided risk to the companies. The Administration premised its budget-cutting objective on two RMA-funded studies (contracted to Milliman, Inc.) on the companies' rate of return on equity. The flaws in this approach are legion. First, the Administration never provided an explanation of how the Milliman results were utilized to determine the final gain and loss provisions for reinsurance. Second, the Milliman studies are rebuttable on numerous grounds. Milliman estimated the equity of crop insurance firms using a model that did not take account actual firm equity and crop insurance regulatory requirements for equity, thus producing unverifiable estimates of industry equity; they failed to consider reinsurance and actual A&O costs; and they did not include a long enough period of time to adequately account for the potential for catastrophic loss. The Administration repeatedly defended its proposals in public based on the returns to companies since 2006, a period that included an unusually rare spike in crop prices and the two lowest loss ratio years in the history of the program dating to 1981. Arguing for steep budget cuts based on unusual circumstances clearly is not a sound actuarial basis for determining expected future returns and establishing sound policy. The Administration appears to be betting that the program's good performance in recent years will continue. The insurance companies have to go along for the ride, but they may have no seat belt on.
- The A&O cap used by the Administration in the final SRA is preferable to the use of fixed reference prices; however, RMA's change in approach does not mask the reality that the A&O cuts remain large coming on top of the A&O funding reductions of the 2008 Farm Bill. RMA's own assessment shows A&O cuts of $220 million per year during 2011–2015. These A&O cuts are being imposed oblivious to the payment delays that will occur in 2012. As a result of a 2008 Farm Bill budget mechanism, companies will have to wait up to 9 months to receive payments from RMA to fund their businesses. Operating costs must be paid and companies will have to borrow in difficult credit markets to meet payrolls. Moreover the new A&O reductions were determined before RMA has completed its study of agent costs of delivery. RMA agreed with recent GAO findings that a study of agent business costs was necessary to fully understand total delivery expenses and to judge the appropriate level of delivery payments to companies and agents. In this case, there were insufficient facts to influence a predetermined budget cut.
- The 2011 SRA implements soft and hard caps on the companies' compensation of agents. These caps were not proposed by NCIS in its initial recommendations to RMA last October and were not proposed in any comments submitted to RMA on the SRA drafts. The soft cap, which restricts agent compensation to 80% of the A&O a company receives in a state, first appeared in the second draft SRA. However, the hard cap, which restricts agent compensation plus profit sharing to 100% of the A&O a company receives in a state, was presented in the final SRA—without the opportunity to comment by the companies. These A&O provisions are fraught with competitive issues and administrative problems.
    - A major problem is that RMA will not know the overall limit on A&O payments until the year is over. Companies must pay their agents for their work before the year is over. How will companies know what 80% of their A&O payments are when they won't know what their total payments will be until the year is over?
    - Another critical issue is the definition of compensation. NCIS has agreed to work with RMA to define agent compensation in a clear way so that companies will be able to implement the caps without being out of compliance. It is obvious at this point that the caps on agent compensation could easily be violated quite unintentionally by companies that are assiduously trying to stay within the caps. Penalties for noncompliance may be severe. We recommend that Congress keep abreast of this issue and help ensure that RMA shows forbearance for unintentional violations.
    - Finally, many of our member companies have raised concerns over the impact of the caps on agents. They fear that agents may shift from one company to another to chase the prospect of better profit sharing. They fear that the compensation caps could lead to consolidation and reduced service, especially for smaller farm operations that have lower premium volume. We recommend that Congress monitor closely the structural changes that may take place

among agents and companies as a result of the change in A&O payments and agent commission caps.

- The final gain/loss provisions and A&O reductions combined are expected to reduce returns well below historical levels in the Corn Belt states. In addition, the changes in prospective net returns in other states do not reflect their loss experiences. The Administration rejected the industry's recommendation that higher return states that were not put into Group 1 (Corn Belt) be given less favorable reinsurance terms than the underserved states. Preliminary NCIS analysis indicates that had the 2011 SRA been in effect for 2009, the Group 1 states would have had a combined reduction in A&O payments and underwriting gains of nearly 25%. The remaining states, while seeing an increase in underwriting gains, would still have faced a collective decline of around 6% in A&O payments and underwriting gains combined. It is unclear how such a decline in returns is going to increase incentives for companies to operate and improve service in low return states, as the Administration claims.

In addition to the problems just identified with the key financial terms of the 2011 SRA, the SRA imposes a range of administrative requirements on the companies. Many people do not realize that the SRA encompasses hundreds of pages of IT, data reporting (such as common land units and FSA data reconciliation), training and quality control requirements (such as large claim reviews). These regulatory burdens continue to escalate. For example, the Crop Insurance Handbook for the 2011 SRA, which specifies the requirements to write crop insurance, is now 834 pages long, compared with 525 for the 2005 SRA. Appendix III of the 2011 SRA, which specifies information and reporting requirements, is 826 pages, compared with 205 pages for the 2005 SRA. In addition to these SRA requirements, FCIC continues to approve new products and revise and expand existing products, all of which demand increased servicing by the companies. For example, between 2000 and 2009, there have been 37 introductions of new crop or insurance plans.

The 2011 SRA: A Yellow Flag That Augurs for Policy Caution Over the Next Several Years

As the industry looks ahead, we can find little security in the developments of the past 2 years and the economic prospects before us. Congress and others need to know that the combination of the $6.4 billion in 2008 Farm Bill reductions, the $6 billion in SRA reductions, the delay in payments to companies in 2012 and the increase in workload and investments needed to adequately deliver this program and meet its regulatory requirements are going to strain this industry, even with normal weather over the next several years. The companies must do more and are going to get paid less, and get paid less frequently, to do it.

The 2011 SRA outcome raises several issues relevant to future actions by Congress. First, the Federal Crop Insurance Program, the safety net for American farmers and ranchers, has now contributed greatly towards deficit reduction. We believe we have done so for this industry as well as for production agriculture in general. We ask that this Committee work to ensure that these funding cuts receive appropriate recognition and prevent further cuts for production agriculture, such as in the 2012 Farm Bill.

Second, while the industry would hope to be able to move forward with no further financial shocks, we emphasize that, unlike private property casualty companies, crop insurance companies do not set premium rates and cannot compete using rate changes. Nor are the companies able to adjust rates to recoup losses in previous years. Premium rate changes can have major impacts on industry profitability, and the companies are handicapped by not knowing what will happen with respect to premium rates. Historically, the companies have not been part of the rate setting process.

Third, Congress should assess the concept of a periodically negotiated SRA. The companies have little leverage to conduct such a negotiation as an equal partner with RMA. RMA conducted the negotiations in a mutually respectful fashion but with far less than full transparency. Requests for key data and analyses were not satisfied. Even today, as we testify, we do not have the details of the baseline USDA used to score the 2011 SRA. In the final SRA draft, which was not negotiable, RMA introduced major new concepts that had not received public or industry comment. These concepts included the hard cap on agent commissions and the requirement that companies forgo legal recourse in the event that the Administration has acted illegally with its A&O provisions. Finally, should multi-billion dollar changes in legislated programs be made through unilateral discretionary actions?

The crop insurance companies are committed to the public-private partnership. We are committed to the efficient functioning of competition and markets. We be-

lieve the private sector, not the government, is the best way to provide the individual risk management information and tools that are indispensable for farmers today. We believe that is the way farmers want the program to operate. We believe this program can be expanded and improved to provide even better protection for farmers and ranchers. We ask that Congress pay careful attention to the impacts of the 2008 Farm Bill and the 2011 SRA and work with the crop insurance industry to strengthen this valued program.

Thank you Mr. Chairman, that completes my statement.

The CHAIRMAN. Thank you.

We will move on to Mr. Stephen Frerichs, Legislative Consultant, Rain and Hail, on behalf of the American Association of Crop Insurers from Alexandria, Virginia. Please proceed.

STATEMENT OF STEPHEN FRERICHS, PRESIDENT, AGVANTAGE, LLC; LEGISLATIVE CONSULTANT, RAIN AND HAIL, L.L.C., ALEXANDRIA, VA; ON BEHALF OF AMERICAN ASSOCIATION OF CROP INSURERS

Mr. FRERICHS. Thank you, Chairman Boswell.

Chairman Boswell, Ranking Member Moran, and Members of the Committee, thank you for holding this hearing today. I believe this is the first opportunity that the crop insurance industry has had to comment before Congress on the process and content of the SRA.

I am Stephen Frerichs, a member of Rain and Hail's crop insurance team, and I am speaking today on behalf of the American Association of Crop Insurers. Rain and Hail is a member of AACI.

I am going to make five points today. My written testimony makes additional points.

My first point, signing the SRA does not imply a consensus agreement, nor success for the industry, a point that Ranking Member Lucas made.

USDA says on its website a successful conclusion of the SRA negotiation has occurred, in part because all companies signed. However, we want you to know that companies did not have a choice. There is absolutely no latitude in this partnership: Sign and you are in business, at least for the short term; don't sign, and you are out of business immediately. To suggest that the 2011 agreement is a success because crop insurance companies signed is misleading.

Never before has any Administration made this level of reductions in an SRA. We believe the reduction greatly exceeds the intent of Congress. The power of the purse is and should be reserved to Congress. Therefore, we recommend the renegotiation authority be reviewed. Perhaps it should be repealed or, at a minimum, modified to include safeguards, especially for maintaining the integrity of the agriculture budget baseline.

My second point, $12 billion in cuts is significant and will impact the industry.

Mr. Chairman, I am not hear today to cry the sky is falling, but I will make a prediction similar to Mr. Rutledge. You can't cut over $12 billion out of a program and not expect to see changes. The industry will consolidate, both at the company and at the agency level. Clearly, no one will survive without making significant changes to their business operations. These changes may impact farmer service and availability.

My third point, the financial impact from the cuts is not uniform across the states. States in so-called Group 1 will be by far hit the hardest. Group 1 states include Iowa, Illinois, Indiana, Minnesota, and Nebraska.

Appendix tables 1 and *2* in my written testimony illustrate the enormous disparities of the cuts under the agreement. Over 80 percent of the expected 2011 cut is taken by these five states. These states represented about 34 percent of the program premium.

Additionally, the combined impact of the A&O cap and the commission cap will be felt hardest in State Group 1. Our initial estimate for 2011 is that the A&O proration will be 83 percent. That means the maximum agency payment rate for revenue policies on average will be in the 11.8 to 12.6 percent range. As you know, over 80 percent of the business is now in revenue policy. For State Group 1, this compares to average compensation in the 23 percent range in 2009 for those states. Can you imagine taking a 50 percent cut in pay?

Mr. Chairman, the bottom line is that five states take the brunt of these cuts, disproportionately so.

My fourth point, last minute changes. RMA released three drafts for comment over a 7 month period. Each draft contained new and befuddling provisions. The third and final draft was no different. We object to compensation caps that result in no savings and do little to protect a company's financial stability.

We object strongly to Section III(a)(2)(K) appearing for the first time in the final agreement. It is one thing to ask companies who are party to the agreement to waive legal rights; it is quite another concept to force companies to ask agents who are not part of the agreement to waive their rights.

We entered this process in good faith. We were up front about our doubts regarding USDA's legal authority. Rather than responding to our doubts, USDA decided to strip our rights.

My fifth and final point, is the need for stability and contract sanctity. Crop insurance companies, as is the case for any company in today's economy, need an extended period of stability. In short, the companies need contract sanctity. In the authorization language, Congress limited the Administration to one renegotiation of the SRA every 5 years. We urge Congress to abide by that same time interval.

As Chairman Peterson has said, with these cuts, agriculture is the first sector to do its part towards deficit reduction. With the 2008 Farm Bill and the 2011 SRA cuts, the crop insurance program has been reduced by over $12 billion. These cuts to the program are deep and significant. Collectively, they will have an impact on rural businesses and jobs. Therefore, we urge Congress to fully recognize these reductions and leave the crop insurance program out of any initiatives to cut Federal spending for 5 years.

On a personal note, Mr. Moran, I would like to offer my condolences to you on the loss of your mother. My mother passed away over 10 years ago, and I think I have some understanding of what you are going through.

[The prepared statement of Mr. Frerichs follows:]

PREPARED STATEMENT OF STEPHEN FRERICHS, PRESIDENT, AGVANTAGE, LLC; LEGISLATIVE CONSULTANT, RAIN AND HAIL, L.L.C., ALEXANDRIA, VA; ON BEHALF OF AMERICAN ASSOCIATION OF CROP INSURERS

Good morning, Mr. Chairman, and Members of the House Agriculture Subcommittee on General Farm Commodities and Risk Management. My name is Stephen Frerichs and I am a member of the Rain and Hail L.L.C. national crop insurance team. Rain and Hail is an employee owned company and one of the U.S. Department of Agriculture (USDA) Risk Management Agency's (RMA) largest Approved Insurance Providers (AIP), writing nearly $2 billion of policies in 49 states. Furthermore, Rain and Hail has marketed and serviced Federal crop insurance policies throughout the history of the public-private partnership, which was authorized by the Federal Crop Insurance Act of 1980.

Today, I am testifying as a representative of the American Association of Crop Insurers (AACI), a trade association with membership from all areas of the Federal crop insurance private sector delivery industry. On behalf of the Board of Directors and members of AACI, I want to thank you for scheduling this hearing. With development of the 2011 Standard Reinsurance Agreement (SRA), as authorized by Congress and managed by RMA, now complete, AACI appreciates the opportunity to comment on both the development process as well as the final product.

Signing the SRA Does Not Imply a Consensus Agreement

As USDA commented on several occasions, all of the AIPs signed the 2011 SRA. However, we want Members of this Subcommittee and Congress generally to fully recognize companies did not have a choice. Why? Because the companies are crop insurance companies built for the purpose of delivering the program to the nation's farmers. Not signing the SRA means the companies are immediately out of the crop insurance business, eliminating all income and jobs related to crop insurance line of business and reducing the value of those assets significantly. Therefore, the idea promoted by USDA that by signing the agreement companies willingly agreed to the SRA changes is not accurate. There is absolutely no latitude in this partnership. Sign and you're in business, at least for the short term. Don't sign and you're out of business immediately.

Mr. Chairman and Members of the Subcommittee, millions and millions of dollars and years and years of time have been devoted to organizing and building crop insurance companies in order to be an effective and efficient partner with USDA in the public-private partnership. This partnership has been so successful in offering to the nation's farmers a top quality risk management program that it is the envy of the world, which other nations are seeking to copy. It is a misrepresentation of the simple facts of the partnership for anyone to suggest that the 2011 SRA, which unilaterally makes $6 billion of cuts in the program after Congress already made over $6 billion in cuts in the 2008 Farm Bill, is acceptable because the crop insurance companies have signed.

It will take time to document the consequences of the necessary crop insurance company adjustments and changes made necessary by the terms and conditions, both financial and regulatory, incorporated in the 2011 SRA by RMA. In the process of implementing the 2011 SRA, we want this Subcommittee and Congress generally to know the paramount goal of the crop insurance companies will be to continue service to the nation's farmers, to the maximum extent possible. It will take some time to know whether all companies who sign the agreement can withstand the dual challenges of a lower income and more regulations instituted by the 2011 SRA.

Financial Terms Take Another $6 Billion Cut

Despite repeated pleas for caution from across the agriculture sector as well as Members of Congress, including some who serve on this Subcommittee, RMA was unyielding in its quest to cut an additional $6 billion from the crop insurance program over the next 10 years. As a result, many farmers who depend on crop insurance to help manage the risks associated with their farming enterprises could suffer changes in service as companies and agencies contract or consolidate as they respond naturally to a reduction in income.

The additional $6 billion in cuts are being imposed by the Administration before the full implementation of the more than $6 billion in cuts imposed by the 2008 Farm Bill. Furthermore, this second $6 billion cut will be imposed during a period of time when RMA is implementing major administrative changes to the management of the program. The RMA should have completed these administrative changes and fully implemented the cuts mandated by the 2008 Farm Bill before placing additional financial and regulatory pressure on the delivery system. Instead, the Administration is abandoning caution and moving ahead with a second round of huge

reductions in financial support and implementation of concepts not provided for review in the months and months of negotiations on the 2011 SRA.

Another alarming aspect of these cuts is that they are based on a remarkable string of good weather and consistently high yields over the past several years. A long term view of weather trends would indicate that we are past due for a weather disaster that would cause large losses by the crop insurers. All of the RMA examples used to justify their cuts do not include the last year of a major drought in the Corn Belt, 1988. Most of their examples show a trend of program cost going almost straight up, a trend that cannot be sustained. However, curiously, these trend lines stop at 2008, a year of record high commodity prices and before the $6 billion of farm bill cuts have been implemented. They do not reflect the sharp downturn in prices since 2008. By cutting the funding of the private sector delivery system so severely based on the best yield and price data ever, the RMA may seriously undermine the ability of the companies to sustain one or more significant loss years.

Never before in SRA negotiations has any Administration made anything that even approached this level of reductions in the financial terms of the agreement. We believe the reduction greatly exceeds the intent of Congress in granting the renegotiation authority. The "power of the purse" is and should be reserved to the Congress. In our view, the Administration exceeded its legislative mandate. Therefore, we recommend the renegotiation authority be carefully reviewed by Congress as to whether it should be repealed altogether or whether it can be modified to include appropriate safeguards, especially for maintaining the integrity of the agriculture budget baseline.

Financial Impact Not Uniform Across States

The distribution of the financial impact of the 2011 SRA is by no means uniform. States in the so-called "Group 1" will be by far the hardest hit. Group 1 states include Iowa, Illinois, Indiana, Minnesota and Nebraska. *Appendix Tables 1* and *2* illustrate the enormous disparity of the cuts under this agreement. As you can see from *Appendix Table 1,* over 80 percent of the expected 2011 cut is taken by the five states in State Group 1. These states represented only 34 percent of the program premium in 2009. Both the Underwriting Gain and A&O Cap fall heaviest on these five states. State Group 3 actually ends up a net "winner" as the Quota Share incentive payment is expected to overcome the A&O Cap impact in these 17 states.

Additionally, the combined impact of the A&O Cap and the commission cap will be felt hardest in State Group 1. *Appendix Table 2* details the impact of the A&O Cap on expected A&O payment rates. The A&O cap kicks in when A&O payments on buy-up policies exceed $1.221 billion. A&O on buy-up policies is then pro-rated so that it cannot exceed $1.221 billion. If A&O is pro-rated, the A&O payment rate is factored down by the pro-rated amount. Further, a new 80 percent compensation cap (80 percent of A&O payment rate) now applies to agency agreements on a state average basis. If a company has an underwriting gain (net of reinsurance costs) then the company can pay up to 100 percent of the A&O payment rate. However, initial compensation levels will have to be at the 80 percent compensation cap because a company will not know if it will incur an underwriting gain until the year is over.

Our initial estimate for 2011 is that the A&O pro-ration will be 83 percent. That means the maximum agency payment rate, on average, for Actual Production History policies will be in the area of 14 to 14.9 percent under the 80 percent compensation cap and for Revenue policies, on average, it will be in the 11.8 to 12.6 percent range. For State Group 1, this compares to average compensation (commission plus profit share) in the 23 percent range (all policies combined) in 2009. Obviously, this is a significant cut by any stretch of the imagination. On the other hand, State Group 3, where average compensation in 2009 is in the 14 percent range, may see only a marginal impact if the *pro-rata* estimate for 2011 bears out.

Mr. Chairman, the bottom-line is that five states take the brunt of these cuts—Iowa, Illinois, Indiana, Minnesota and Nebraska. We submit that is unfair and a mistake that will unduly burden these five states.

Last Minute Changes With No Industry Input

The companies are alarmed about the number of new changes that were unilaterally inserted into the final draft of the SRA without prior consultation with the industry and no chance to comment. While RMA conducted a number of meetings with companies and their trade associations throughout the negotiating period of time, they appear to have been orchestrated primarily to facilitate the objective of imposing a predetermined level of cuts and certain policy changes on the program at the industry's expense.

For example, RMA repeatedly cited its goal of improving service for producers and the Secretary of Agriculture has focused on programs to help smaller farmers, but the final draft of the SRA goes in a completely opposite direction. Many of our companies expressed concerns about putting undue limitations on agent commissions, and then the final draft abruptly changed from an individual policy **commission** limit to a **compensation** limit per state. Instead of rejecting a bad idea, they made it more perverse. Now it is possible for some agents to be reimbursed more than others in a state, but with a state-wide cap it becomes a zero-sum game. Companies will be able to pay some agents more than the percentage limit if overall in the state they stay within the limit. Agents will be incentivized to drop their smaller clients and produce a portfolio of larger policies with which they can negotiate a larger commission. This provision could leave smaller agents to face greatly reduced commissions and smaller producers hoping that someone will be interested in servicing their policies. AACI objects to this perverse method of dealing with agents' commissions that jeopardizes service to small and medium-sized producers.

More generally, this agreement includes precedent setting requirements that have not been even contemplated in previous SRAs and, equally important, are unheard of in normal, private insurance agreements. RMA's argument that these particular provisions are necessary to protect the financial soundness of the companies is puzzling. The annual Plan of Operation (PO) requirement provides RMA considerable latitude in its company financial oversight responsibility. A company's capital adequacy provisions can be adjusted annually by RMA in the required PO submissions, which must be approved by RMA prior to the company engaging in activities for the new reinsurance year.

Stripping Companies of Fundamental Legal Rights in Order To Protect the RMA's Own Weak Legal Position

On another front, we object to the last minute insertion of Section III(a)(2)(K) in the final agreement, even in its revised form of a covenant to not sue. Obviously, this Section is an attempt to protect the FCIC from litigation that they fear because the industry earlier brought to FCIC's attention that they did not have the authority to make some of the cuts they were proposing in the SRA. Rather than provide an adequate response to the third-party legal opinion submitted to them, RMA imposed a provision to strip the companies and the agents of their legal rights. Companies and agencies should not be forced to agree to this gross overreaching and unprecedented regulation that takes away private rights.

The Current Trend of Huge Cuts Will Destroy Many Rural Enterprises, Cost Thousands of Jobs and Undermine our Stable and Abundant Food Supply

The current pattern of using the crop insurance program as a bank to fund other priorities, as demonstrated by the 2008 Farm Bill cuts of $6 billion and the SRA cuts of an additional $6 billion, cannot continue. Continuing to cut Federal support for the crop insurance program will mean destruction of the primary risk protection program for commercial American farmers. This outcome would be a terrible development for the nation's farmers, rural economies and the national economy, specifically including the consumer-taxpayer, since all taxpayers are consumers.

In fact, farmers from around the nation testifying at the recently completed House Agriculture Committee's 2012 Farm Bill hearings indicated they want to, at a minimum, continue the current level of crop insurance program benefits and would like to have the benefits improved for all crops around the nation. It would be ironic, indeed, if our government were to destroy a successful crop insurance program at the very moment U.S. farmers want to expand it and other nations all over the world are trying to replicate it and make it a part of their farm safety net.

Without an effective risk management program like the current Federal Crop Insurance Program, many farmers would not be able to withstand the weather-related risks of producing crops, and they would not be able to secure adequate financing, especially in the tighter credit environment of today, to properly finance the capital intensive production of crops that agriculture has become today. These farmers would not be farming. When farmers don't farm, the nation's economy not only loses farm jobs, it also loses jobs in sectors directly related to the production of crops, including a wide array of production input products and services. Moreover, subsequently lost revenue and commercial activities from production agriculture input sales and services as well as related services, together with the related lost tax revenue, adversely impact jobs in indirect sectors, including auto and home building industries.

Moreover, when farmers don't farm, it destabilizes America's stable supply of low cost food for all of the nation's consumers. Reduced supplies of agricultural commod-

ities raise food costs, which today represent, on average, only about 9–10 percent of disposable income in the U.S. Higher food prices increase the cost of food to all consumer-taxpayers as well as for the government's food assistance programs, meaning more funding would be needed for the Supplemental Nutrition Assistance Program (SNAP) and all other related programs.

Time for Intellectually Honest Program Accounting and Analysis

RMA constantly invokes the Milliman studies it commissioned on "reasonable" and "historical" rates of return as the analytical basis for its decision to make additional cuts in crop insurance company income. From our understanding of fair and balanced research methodology, we conclude these studies are flawed because of key assumptions imposed by RMA.

The "reasonable" rate of return study produced a result that is biased to the high side because it does not accurately account for the true level of risk associated with production agriculture. This bias was introduced to the analysis through the RMA requirement that the study not include the disaster experience of 1988 and other disasters in the earlier 1980s. Milliman, to its credit, makes note of that fact. In all economic settings, higher levels of risk demand and earn higher rates of return. We wonder if the risk factor in the study was intentionally biased downward by excluding a high loss year to show a lower rate of "reasonable" return.

The "historical" rate of return study also produced a result that is biased to the high side because it does not accurately account for the true costs associated with delivering the modern Federal Crop Insurance Program, especially given the required capital amounts, compliance rules and massive set of regulations. This bias was introduced to the analysis through the RMA requirement that the study make the assumption that total cost of delivery exactly equals the A&O payment amount, a totally arbitrary assumption, with the result of biasing cost of delivery to the low side. Several industry studies over the last 10 to 15 years have all shown total cost of delivery to exceed A&O payments by four to six percent of premium. RMA has not commissioned a study to analyze the true and total cost of delivering the modern crop insurance program. Although, RMA recently indicated it would conduct the study in the next year or so.

Collectively, these RMA assumptions have created a biased public view of the rate of return to crop insurance companies over time. If RMA is truly interested in the financial health of the companies, as it has publicly stated and given as justification for key new 2011 SRA regulations, specifically including the agent payment cap, it is time to produce an intellectually honest analysis of the profitability of delivering the program. We urge this Subcommittee to make such a study the highest priority.

Need for Stability, Clear Vision and Confidence

It has taken not only years, but decades to have the Federal Crop Insurance Program attain the current levels of participation and benefit for our nation's farmers. Only in America could this public-private partnership have been so successful. While certainly there is opportunity to continue improving the program, today it stands second to none as a world-class agriculture risk protection and management tool.

A lot of people have contributed to the development and evolution of the modern crop insurance program, however, no effort has been greater than that made by Congress and Members of this Subcommittee. On behalf of the AACI membership and the farmers we serve, I want to take this opportunity to thank you for your support of a quality risk protection and management program. Given the natural and global market elements they work and live with every day that are beyond their control, our farmers deserve the certainty and predictability of the risk management program you have provided.

But an important and critical point must be made here and that is private sector ingenuity, creativity and capital have contributed significantly to the building of the crop insurance program in operation today, especially the farmer service component. We believe private sector participation is an irreplaceable factor in assuring maximum farmer satisfaction with the program.

However, crop insurance companies, as is the case for companies in other sectors of the nation's economy today, need an extended period of stability, both financial and regulatory, to develop greater confidence in the partnership with the government as regulator. The companies need a clearer vision of the financial future, a coherent and consistent plan for understanding and managing the massive set of new regulations and an effective plan to deal with a lower income. It is important to make these points because we are concerned that the potential for unintended consequences inherent with some of the changes included in the 2011 SRA is not recognized nor understood by the regulator.

In the authorization language, Congress limited the Administration to one renegotiation of the SRA every 5 years. We urge Congress to abide by the same time interval and set the crop insurance program aside for 5 years regarding further budget cuts. As Chairman Peterson has said, with these cuts in the crop insurance program, agriculture is the first sector in government to do its part in deficit reduction. With the 2008 Farm Bill cuts and the 2011 SRA cuts, support for the crop insurance program has been reduced by over $12 billion. These cuts to the program are deep and significant and, regardless of comments to the contrary, collectively they will have an impact on rural businesses and jobs. Therefore, we urge Congress to fully recognize these reductions and leave the crop insurance program out of any initiatives to cut Federal spending for 5 years, including budget reconciliation bills and farm bills.

APPENDIX

Table 1. Estimated Distribution of 2011 Cut by State Groups

	Percent of Cut
State Group 1	83.8%
State Group 2	22.0%
State Group 3	−5.8%

Group 1 States: Illinois, Indiana, Iowa, Minnesota, and Nebraska.

Group 2 States: Alabama, Arizona, Arkansas, California, Colorado, Florida, Georgia, Idaho, Kansas, Kentucky, Louisiana, Michigan, Missouri, Mississippi, Montana, North Carolina, North Dakota, New Mexico, Ohio, Oklahoma, Oregon, South Carolina, South Dakota, Tennessee, Texas, Virginia, Washington, and Wisconsin.

Group 3 States: Alaska, Connecticut, Delaware, Hawaii, Maine, Massachusetts, Maryland, Nevada, New Hampshire, New Jersey, New York, Pennsylvania, Rhode Island, Utah, Vermont, West Virginia, and Wyoming.

Table 2. Impact of Compensation Cap under Varying A&O Cap Scenarios

	A&O Payment Rate	A&O Cap Impact at Selected *Pro-Rata* Levels on A&O Pay Rate					
		No Cap	90%	85%	80%	70%	65%
Actual Production History	21.9%	21.9%	19.7%	18.5%	17.5%	15.3%	14.2%
Revenue	18.5%	18.5%	16.7%	15.7%	14.8%	13.0%	12%
		Maximum Agency Pay Rates @ 80% Compensation Cap @ Selected *Pro-Rata* Levels					
Actual Production History		17.5%	15.8%	14.9%	14%	12.3%	11.4%
Revenue		14.8%	13.3%	12.6%	11.8%	10.4%	9.6%
2008 A&O *Pro-rata* would have been				64%			
2009 A&O *Pro-rata* would have been				72%			
2011 A&O *Pro-rata* expected				83%			
State Group 1 Average Compensation 2009				23%			
State Group 2 Average Compensation 2009				16%			
State Group 3 Average Compensation 2009				14%			

Mr. MORAN. Thank you.

The CHAIRMAN. Thank you for your testimony.

I would like to move to Mr. Deal, Chairman of the Board, NAU Country Insurance Company in Andover, Minnesota.

STATEMENT OF JAMES D. DEAL, CHAIRMAN OF THE BOARD, NAU COUNTRY INSURANCE COMPANY, ANDOVER, MN

Mr. DEAL. Thank you, Mr. Chairman and the Members of the Committee on General Farm Commodities and Risk Management.

I am Jim Deal; and I come to you as a retired Federal employee, a former manager of a corporation, a former CEO and owner of National Ag and NAU Country. However, as of July 1, I am retired and no longer have any vested interest in any MPCI, so I come to you as an individual. This program started back in 1938, I started in 1956, so maybe my biggest contribution is as a historian more than anything else.

The high point in my life, obviously, was when President Jimmy Carter selected me as manager of FCIC; and he definitely had ideas. Through the numerous conversations I had with him, he did not like the *ad hoc* free disaster programs. They had to be eliminated.

Along with Secretary Bob Bergland, we worked hard to shore up the credit side for the farmers because of the tight credit even then. So we worked on that. So our thrust was to develop a program, and we selected crop insurance as the vehicle that we felt could best address it.

The other thing that the Administration, and particularly the President wanted, he said he wanted the farmers to pay part of the premium. He wanted the government to control and put the program out, but he felt that we needed the private sector for the delivery to get the participation we wanted. That was the grounds we worked on.

We got the Crop Insurance Act passed in 1980, and it was designed to make it more affordable and accessible to all farmers in all areas, and that marked the birth of the present crop insurance program. With the passage of the Act and its many amendments, and I talk about the history in my written testimony. I make a few comments on the SRA in the program.

I first would like to compliment Bill Murphy and his willingness to work with the private sector, and get what I consider a good reinsurance agreement out. I am sure both sides are going to tell you they are not 100 percent happy with the results, and I have said many times that sometimes good deals come out when both parties feel they have lost something. We will see. Certainly this is the case with the SRA. There were many things on both sides that had to give and take.

In my testimony, I talk about the risk, the underwriting gains, and in my estimation I believe the companies will walk away with a 15 percent reduction in gains. As in the previous testimony, those hardest hit in the Group 1 group, which you are aware of.

However, I also talk in my testimony about how I support the principles applied to the A&O side. Because, back in the beginning, one of the issues we were to address was to get a subsidy that established way back in the conception of the program that would cover the cost. One of the major roles in that is the role the agent plays in educating and assisting farmers and making their management decisions, and they are many more fold now than they were when we passed the legislation.

As they previously said, probably the most controversial issue is the hard and soft caps that are put in there. However, I believe these do give discipline to the program. Some will question what I say when I say that. I am not questioning as far as the amount. As I understand, there is a study that has been, or is going to be,

conducted relative to the cost of administering this program. I think you have to realize in the crop insurance program, both the agents and the companies, it is much more intense and there is a lot more service work that is required in this in relationship to a private policy. So, sometimes this has not been addressed enough to really do that.

I think this study, if they get it done and truly look at what is the cost of service, it is one of the issues we had when we passed the original legislation where we dealt strictly with commission to agents. I think that will help in this matter. I think the crop insurance program is the envy of the world.

If I might make a couple statements, I think the CAT program is wrong. This is a program covering nurseries and big corporations. The imputed premium on that that the taxpayer is paying is $308 million. I think they ought to be paying the same as the rest of the producers. You are offering them about $8 billion in protection at the taxpayers' expense. I think it is something that needs to be looked at and corrected.

The COMBO policy is a good move. I commend the RMA on combining this and simplifying the program.

Another one that I have a dislike for is the seed company discount reductions. I think this simply is hurting the integrity and increasing complexity of producers. This program, in my judgment, should be eliminated.

Revenue pricing: the base period when they used the 5 days out of the base period to pick the price can shoot a policy over or under dramatically. I think there should be a longer period of time to look at that.

And APH, as was mentioned earlier, I think with the technology and things we have now, the period of that ought to be shortened to improve the administration of the program.

And probably one of my most important points is the administrative changes that go on. Crop insurance has gone through a lot of turmoil in the last few years. I believe we need stability in the requirements to operate under the program, and stability in the financial terms of the agreement, to settle it down and stay with what we have.

The future: The effect of the crop insurance program as it relates to the producers is an absolutely needed requirement. It really helps financially, especially in tight credit times that we are having now. This is so essential for the banking and lending institutions to have to shore up the loans so the farmer can produce it.

The passing of the amendment and the major Act change in 1980, and the future changes that have been made since then, the success of this program is nothing short of amazing. This program is the foundation of ag credit out there right now for the farmers so they will be able to come back the next years and produce.

Last, I hope you really consider what has happened with the farm bill, with crop insurance, and the new SRA. As previously said, the farm bill took $6.5 billion out, which was moved towards nutrition programs, as I understand it. Now the new SRA takes $6 billion, of which $2 billion is going to conservation programs which we talked about. This represents, the two of them, about a 40 percent cut in the revenues for the companies.

My last point, if $4 billion is going for debt reduction—and it is Minnesota math so I don't know how close I am—but if you apply that to all of the Federal budget, that reduction should equate to somewhere between $2 to $2.4 trillion in debt reduction. So I hope you consider that crop insurance, we have done our part. I hope we get consideration on that.

And so, with that, I would like to thank you for the opportunity to testify. I am happy to answer any questions. Or later on, like I said, I am retired, so if staff needs me, I am available. Thank you.

[The prepared statement of Mr. Deal follows:]

PREPARED STATEMENT OF JAMES D. DEAL, CHAIRMAN OF THE BOARD, NAU COUNTRY INSURANCE COMPANY, ANDOVER, MN

Introduction

Good morning, Mr. Chairman, and Members of the House Agriculture Subcommittee on General Farm Commodities and Risk Management. My name is James Deal and I am testifying as a retired government employee and former Manager of the Federal Crop Insurance Corporation ("FCIC"). In my later years I was CEO and owner of National Ag Underwriters and NAU Country Insurance Company but have since retired and I currently have no vested interest in any MPCI crop insurance company. I welcome this opportunity to address the Committee on crop insurance as you prepare your work on the next farm bill.

I will submit my full statement for the record; however, I would like to highlight some of the high points.

My major role throughout my career with the government was when President Carter appointed me as Manager of the Federal Crop Insurance Corporation. I had two conversations with President Carter when he was running for President and also working closely with the Secretary of Agriculture, Bob Bergland whom I have known most of my adult life. Bob Bergland was the Chairman of the House Committee of Conservation and Credit before he became Secretary of Agriculture. Both the President and the Secretary had very definite opinions on what they wanted. President Carter had said he did not like the free disaster programs and wanted a more meaningful insurance program that was a three way partnership between the farmer, the government and the private sector. In the process of developing legislation, I received two personal notes from the President regarding what he wanted for the farmers. After Bob Bergland became Secretary of Agriculture, I worked closely with Congressman Ed Jones of Tennessee, who took over as Chairman and continued the development of the legislation. As Mr. Bergland has often said in reference to the disaster programs "they are too little, delivered too late and of no meaningful value."

It seems like old times testifying here. Back in the 1970's I spent a great deal of time testifying before the Committees on the revitalization of the crop insurance program. In fact, I spent lots of time with staff back in Chambers and various meeting rooms shaping and developing the new legislation to make crop insurance a major program for farmers to help stabilize their credit needs.

Historical

From the historical side, developing an all risk insurance program by the private sector has been tried well over the past 100 years, all of which failed. The reason for this failure was the risk of drought. Usually drought is wide spread and devastating and the government decided in 1937 to develop an insurance program to cover the risk the private section had failed at. The history of Federal Crop Insurance Program dates back to 1938 and I started working for Federal Crop Insurance program in 1956 so I guess I am mainly a historian now days! The program has gone through many changes from the beginning through today and the basic risk of drought was the challenge for the government to develop an actuarially sound program. Some highlights of the development of the program are as follows:

> Few sectors of the economy are as susceptible to the influence of nature as is agriculture. While science and technical knowledge have enabled the farmer to avoid or eliminate some dangers which menace harvest, the farmer remains powerless to avert damaging or total loss from weather hazards, insects and other forms of natural disaster.

Crop insurance is the most important part for the American farmers' safety net. Input costs have risen substantially and farmers must borrow money to complete planting. Weather risks are greater than ever and price volatility has made ag production riskier than ever. Banks and lending partners require farmers to have a way to repay loans if crops don't come through. Both large and small producers need a reasonable way to guarantee production and revenue to stay in business. The health of rural America is dependent on the farmer and crop insurance.

Original legislation was introduced in 1937 and passed in February 1938. The original legislation was for wheat insurance only and coverage began with the 1939 wheat crop. The coverage was a "premium in kind" which meant a farmer's premium was to deliver a bushel of wheat to the Evernormal Granary and if he had a loss on his crop he was permitted to pickup his guarantee from the same granary. However, this plan was never implemented but was administered by monetary exchange rate.

In 1938 Congress formed the Federal Crop Insurance Corporation (FCIC) with three objective in mind, (a) to protect the income of farmers against crop failure or price collapse; (b) to protect consumers against shortage of food supplies and extreme of prices; and (c) to assist business and employment by providing an even flow of farm supplies and establish stable farm buying power.

Crop insurance was suspended at the end of 1943 with no insurance offered for the 1944 crop year because of actuarial and loss adjustment control were not following sound insurance principles.

An amendment to the Federal Crop Insurance Act in December 1944 reinstated the insurance program effective for the spring planted crops in 1945. The 1945 program provided for insurance on cotton, flax, and wheat on a national basis and corn and tobacco on an experimental basis not to exceed 20 counties.

An amendment to the Federal Crop Insurance Act, August 1, 1947 effective for the 1948 crop year provided for reorganization on a sound actuarial basis. The amendment limited insurance to not more than seven crops (including wheat, cotton, flax, corn and tobacco) 200 wheat counties, 56 cotton counties, 50 counties each for corn and flax and 35 tobacco counties. The amendment also continued the provision for the addition of not more than three additional crops and 20 additional counties each year thereafter.

The Act was further amended on August 25, 1949 (63 Stat. 663) to expand the program to additional counties following the favorable experience in 1947 with premiums exceeding losses paid by nearly $8,500,000 and again in 1948 with premiums exceeding indemnities by over $5,900,000. This amendment authorized a maximum expansion each year from 1950 through 1953 equal to half the number of counties in which the Corporation was authorized to offer crop insurance in 1948 on each commodity. In addition, the Multiple Crop Insurance plan under which the investment in several crops is insured under one policy could be expanded to 75 counties in 1950 and to 25 additional counties in each of the next 3 years.

Effective beginning in 1954 the maximum number of new counties was increased from 20 counties per year to 100 counties per year in addition to the number of counties in which insurance was offered the preceding year. On September 12, 1964, the Act was amended to raise the limit from 100 to 150 counties that could be added each year.

The Act was further amended on August 3, 1956 (70 Stat. 1031) to authorize the charging of the direct cost of loss adjustments and a portion of the administrative expenses against premium income. These costs are not taken into consideration when premium rates are computed.

On July 23, 1957, the Act was further amended (71 Stat. 309) to authorize the corporation to provided reinsurance on any crop or plantation insurance provided in Puerto Rico by a duly-authorized agency of the Commonwealth provided such reinsurance is not available from a recognized private sources at a reasonable cost.

On August 4, 1959, the Act was further amended (73 Stat. 278) to eliminate the minimum participation requirement. This provision made it necessary to have the smaller of the 200 farms or 1–3 of the farms producing insured crop in a county covered by insurance in order for the program to operate in a county.

On September 12, 1964, the Act was further amended (78 Stat. *931 or 934*) to raise the yearly addition of new counties to the program from 100 to 150.

Federal Crop Insurance, the only widespread all-risk crop investment protection available to farmers, is a voluntary program offered on an individual basis on basic and specialty crops (including wheat, corn, cotton, tobacco and citrus) in 39 states. Insuring crops against natural hazards over which farmers have not control. Federal Crop Insurance is intended to help maintain a stable rural economy by spreading the impact of crop loss and damage over a period of many years.

Indemnities paid to farmers are paid from premiums collected each year from participating farmers. Some administrative costs are paid by Congressional appropriation.

In the 1971 crop year, 3,536 individual crop programs were operated in 1,452(?) counties. Over $800 million of production and nearly 400,000 individual crops were insured in 1971.

The limited expansion to new crops and new counties on a sound actuarial basis has brought Federal Crop Insurance to its present status. For 1977 Federal Crop Insurance offered insurance protection for 26 crops with 4,063 individual crop programs operating in 1,526 counties. Federal Crop Insurance has now assumed more than $2 billion ($2,101,673,535.00) liability for crop production investments and has a premium income in excess of $100 million ($102,206,227.00).

In 1980, Congress passed legislation that was designed to increase participation in the Federal Crop Insurance Program and make it more affordable and accessible. This modern era of crop insurance was marked by the introduction of a public-private partnership between the U.S. Government and private insurance companies bringing the efficiencies of a private sector delivery system together with the regulatory and financial support of the Federal Government.

The passage of the Federal Crop Insurance Act of 1980 marked the birth of the present Federal Crop Insurance Program and the start of the public-private partnership that has been the foundation for its success. With the passage of this Act, Congress for the first time embraced the goal of establishing a program that could provide protection for all farmers in all regions, with the intent that it replaces *ad hoc* disaster payments. I was Manager of FCIC and was the major architect for the Administration on this legislation.

The Federal Crop Insurance Reform Act of 1994 dramatically restructured the program. And in 1996, the Risk Management Agency (RMA) was created in the U.S. Department of Agriculture to administer the Federal Crop Insurance Program. Through subsidies built into the new program guidelines, participation increased dramatically. By 1998, more than 180 million acres of farmland were insured under the program, representing a three-fold increase over 1988. In 2008, more than 272 million acres are insured through the program protecting a record-setting $90 billion of crop value.

Although the implementation of the 1994 Act represented a major challenge, private industry rose to the occasion. The new program offering catastrophic insurance coverage was implemented successfully. In the year following passage of the 1994 Act participation, participation rates rose to 88 percent. Since that time private industry has assumed exclusive responsibility for the delivery of catastrophic insurance coverage in fourteen states and is expected to assume similar responsibility in other states soon. Although participation rates have fallen somewhat since the repeal of the 1994 Act provisions that made crop insurance a prerequisite for receipt of agricultural program benefits, they have remained well above the 50 percent goal set by Congress in 1980.

The widespread availability and high participation rates that have recently been achieved with the help of the private sector have finally permitted Congress to attain its long-sought goal of turning the crop insurance program into a replacement for *ad hoc* agricultural disaster assistance.

In the 1994 Act, Congress sought to eliminate *ad hoc* disaster assistance, and enlisting the private sector to increase the participation in the program was an integral part of its strategy. Congress has so far not wavered in its resolve to rely on the crop insurance program as its sole vehicle for delivering assistance to farmers stricken by natural calamities.

In May of 2000, Congress approved another important piece of legislation: the Agricultural Risk Protection Act (ARPA). The provisions of ARPA made it easier for farmers to access different types of insurance products including revenue insurance and protection based on historical yields. ARPA also increased premium

subsidy levels to farmers to encourage greater participation and included provisions designed to reduce fraud, waste and abuse.

In 2000, Congress enacted legislation that expanded the role of the private sector allowing entities to participate in conducting research and development of new insurance products and features. With the expansion of the contracting and partnering authority, RMA can enter into contracts or create partnerships for research and development of new and innovative insurance products. Private entities may also submit unsolicited proposals for insurance products to the Board for approval. If approved by the Board, these unsolicited insurance products could receive reimbursement for research, development and operating costs, in addition to any approved premium subsidies and reinsurance.

Even this brief examination of the history of the program's expansion and evolution indicates clearly that both Congress and the nation's farmers have a strong and continuing interest in encouraging widespread participation in the Multiple Peril Crop Insurance Program. Congress has clearly recognized the critical role played by private insurance companies and has taken steps, in all key pieces of legislation it has passed since 1980, to ensure their continuing involvement.

The crop insurance industry has changed significantly since its early days. Policies, procedures, and techniques have been modified over the years. The industry is constantly evaluating its insurance products in an ongoing effort to make sure that they are relevant and affordable for the farmer. As a result, the American farmer has more and better options to manage risks than at any time in history.

The Program

See Exhibit 1

I would first like to compliment Bill Murphy, head of Risk Management Association ("RMA"), in his willingness to work with the private sector in getting a good Standard Reinsurance Agreement (SRA) out. Both sides will tell you that they are not 100% happy with the result. I can tell you most good deals will end with both parties feeling like they had to give something up. This certainly was the case with the most recent draft of the Standard Reinsurance Agreement ("SRA"). I believe the new SRA brings a better balance of the risk which in turn will bring better balance of distribution. I have analyzed the profit and loss numbers and I believe the SRA is on an even keel with other private sector programs.

Underwriting Gains—With respect to underwriting gains, the companies will walk away with an overall reduction of about 15% of total underwriting gains. This money has traditionally been used to build surplus and to create that "rainy day" fund for the time when we have a loss year and need to provide the appropriate payments to our producers. Keep in mind that the reduction is much higher in the five Group 1 states (IA, IL, IN, MN and NE) which will see reductions nearly double the average while the other states will see reductions less than the average. Companies will need to tighten up operating costs and bear the burden of these reductions as RMA strongly fees this was necessary to address criticism with the program.

I also support the principals applied to A&O. Even larger cuts were mandated to the Administrative and Operating subsidies ("A&O" subsidy) paid by the government for policy acquisition, underwriting, claims and general operating costs of the program. This subsidy was established at the program's inception so the American farmer didn't have to shoulder the administrative costs of the program. The role of the agent educating and assisting our farmers in making risk management and purchasing decisions is a critical part of the program.

Most of the data being used to criticize RMA and the companies regarding A&O and agent commissions were exacerbated by the unusually high commodity prices in 2008. By 2010 the prices and volatility factors used for premium calculations had returned to normal levels. This concept was supported industry-wide and RMA worked on a formula that essentially caps the dollar amount of A&O even if prices were to escalate. This assists them in their budgeting process and answers the critics who have argued that the volatility in A&O payments is a burden the government should not have to shoulder.

Probably the most controversial of these changes relates to the government's hard and soft caps on total agent commissions. The most effected agents are those in the Group 1 states who RMA has been criticized heavily by the GAO and other oversight bodies in the last 5 years. Many of these agents received substantially more than all of the A&O leaving the company with nothing left to provide underwriting and claims service to the farmer . . . a major intent of the subsidy. Many other Group 2 and 3 agents may actually see commissions rise as a result of the new SRA

as they were used to receiving a 10–14% rate of commission. However, I believe this will give good discipline to the expenditure side and will add to the service of the American farmer. Some would question when I say that but I truly believe this will stop companies from trying to outbid each other on commissions. If the companies all start out with the same base line it will enhance the one element which is competition on service. Service is the name of the game with 89% of the farmers in the program. A company's major thrust would no longer be marketing but service to maintain their customer base. As to whether the A&O number is correct in relation to the services rendered, my understanding is that a study is or has been scheduled to be conducted. I do believe there is more service required on the part of the agents and the company with crop insurance over other lines of insurance. The study should result in determining the proper compensation.

The Crop Insurance Contract—A crop insurance contract is a commitment between insured farmers and their insurance providers. Either party has the right to cancel or terminate the contract at the end of each crop year. Unless the contract is canceled, it is normally automatically renewed the next year.

Under the contract, the insured farmer agrees to insure all the eligible acreage of a crop planted in a particular county. This choice is made county by county and crop by crop. All eligible acreage must be insured to reduce the potential for adverse selection against the insurance provider. Adverse selection generally exists whenever the insured person has better knowledge of the relative riskiness of a particular situation than the insurance provider does.

The insurance provider agrees to indemnify (that is, to protect) the insured farmer against losses that occur during the crop year. In most cases, the insurance covers loss of yield exceeding a deductible amount. Losses must be due to unavoidable perils beyond the farmer's control.

Over the last few years, products that combine yield and price coverage have been introduced. These products cover loss in value due to a change in market price during the insurance period, in addition to the perils covered by the standard loss of yield coverage.

Crop insurance policies also typically indemnify the insured person for other adverse events, such as the inability to plant or excessive loss of quality due to adverse weather. The nature and scope of this "helper" coverage vary depending on the crop. This is because of the differences in crops individual natures.

Government and Private Sector Roles—FCIC's mission is to encourage the sale of crop insurance—through licensed private agents and brokers—to the maximum extent possible. FCIC also provides reinsurance (subsidy) to approved commercial insurers which insure agricultural commodities using FCIC-approved acceptable plans. The private insurance companies reinsured by FCIC have sold and serviced all Multiple Peril Crop Insurance authorized under the Federal Crop Insurance Act.

Since there is both public and private sector involvement in the crop insurance program, these relationships result:

A contract of insurance exists between insured farmers and their commercial insurance providers.

Premium rates and insurance terms and conditions are established by FCIC for the products it develops, or established with FCIC approval for products developed by insurance providers.

Reinsurance agreements (cooperative financial assistance arrangements) exist between FCIC and the commercial insurance providers.

The Federal Crop Insurance Program is the Envy of the World—It has taken not only years, but decades to have the Federal Crop Insurance Program attain the current levels of participation and benefit for American farmers. And, while certainly there is room and opportunity to continue improving the program, today it stands second to none as a world-class agriculture risk protection and management tool. In fact, other countries such as France have begun to research the program and are even starting their own crop insurance program.

A lot of people have contributed to the development and evolution of the modern crop insurance program, however, no effort has been greater than that made by Congress and Members of this Committee. I want to take this opportunity to thank you for your support of a quality risk protection and management program. Given the natural and global market elements they work and live with every day that are beyond their control, America's farmers, ranchers and growers deserve the certainty and predictability of the risk management program you have provided.

Changing Demographics—Growing global populations, demographic changes, and economic growth will substantially increase the demand for agricultural products and create new markets for American products while increased agricultural efficiency in other countries will force U.S. agriculture to be more competitive.

Changing Structure of Agriculture—The structure of the food and fiber system—from farm to market—changed dramatically in the last decades of the twentieth century. Continued change is likely. An increasing share of U.S. food and fiber is being produced on fewer, larger, and more specialized farms. Similar change can be seen across the food and agriculture sector. Firms are larger, and production methods are more specialized. Production and marketing are more vertically and horizontally integrated. Concentration—characterized by sharp declines in the number of buyers or sellers of a product—is greater. Consumer preferences, new technology, and global markets drive continuing change, affecting farmers, processors, marketers, and consumers. Developing commercially feasible renewable resources and manufacturing products creates new demand for agricultural products and helps reduce U.S. dependence on foreign sources of nonrenewable resources.

Congressional Funding—The ability of RMA to respond to the needs of its beneficiaries, customers, and producers is determined largely by the level of funding provided by Congress. Due to the widespread concern about managing the Federal deficit, maintaining the long-term viability of the Social Security Trust Funds, and other mandatory programs, future discretionary budgets are expected to remain relatively tight.

Global Climate Change—Growing concern about the impact of emissions of greenhouse gases on the Earth's surface and atmosphere has prompted policy discussions and international negotiations. Specific concerns have been raised about the effects of global climate change on agriculture and the effects of agriculture on global climate change.

Globalization—The globalization of all aspects of the food and fiber system is having a major impact on American agriculture. From competitive markets around the world, to diseases without national boundaries, to population growth and evolving diets, we are seeing profound changes worldwide. These changes have led to a dramatically new trade environment, threats of exotic diseases and pests to domestic production, and international controversies over the use of biotechnology. To remain competitive, the food and agriculture sector needs to take these developments into consideration.

Needed Program Improvements

CAT Coverage—(*See Exhibit 2*)—Many forms of CAT coverage offer large corporate producers millions of dollars of liability coverage for a flat fee of $300 per policy. "Imputed" premium is 100% subsidized by the taxpayer. The "imputed" premium should be charged and that would put every producer on the same level. In 2009, "imputed" premium was $308 million annually with significant portions covering nurseries and other large commercial interest. The liability totaled more than $7.9 billion.

COMBO Policy—COMBO policies has simplified programs that combine different types of revenue and production plans into a "COMBO" policy for 2011 and is a long awaited move that will help simplify the program for producers and for the companies. We commend RMA for this. Keep in mind that companies had to bear the burdens of this substantial rewrite with less money under the program. Congress needs to encourage RMA to continue to move forward with simplification.

Information—The government needs to continue working with the industry to develop a Comprehensive Information Management System ("CIMS"). This is a positive enhancement for producers reporting information to companies and improves loss adjustment integrity and accuracy.

Seed Company Discounts—The government has allowed producers a premium discount if the producers use their seed. This is accomplished through 508(h) filings. Once this opened up, other seed companies are filing for similar discounts. The issues are as follows:

- The new programs place the burden of additional verification, underwriting, mandated spot checks and loss adjustment procedures on companies while actually paying them less (discounted premiums mean less A&O). The software programming alone is a major expenditure for these programs.
- The additional production capabilities of the hybrids will naturally increase coverages by improving producers APH over time. Once these take effect, the discount is no longer appropriate yet there is no plan to ever end the discounts. This will throw off policy ratings in the future. This is flawed.
- These programs are hurting program integrity and increasing complexity to the producers and this program should be eliminated.

Revenue Pricing—Price and volatility discovery periods for revenue plans are too short and have an artificial impact on policy pricing. For example, volatility factors are determined based on statistics from only 5 trading days at the end of price

discovery period. With substantial volatility in the markets, this can lead to some odd results causing producers to get policies that are substantially under/overpriced. The companies and taxpayers are hurt by this in the end. This base premium period should be extended to a longer period of time.

APH—With the rapid technological changes in production agriculture, the government needs to change its method of calculation producers' APH. By reducing the APH reporting periods, the program will better capture production yield data increasing coverages and better rating premiums. This will greatly improve the program while reducing record keeping burdens on the producer.

Administration Changes—This is probably one of the most important points I can make. Crop insurance has been through a very turbulent time. The 2008 Farm Bill and now the new SRA has caused a lot of uncertainty for companies, our agents and reinsurance partners. New operating standards and program initiatives keep adding to the costs of delivering the program yet reimbursements are continually in jeopardy or going down. We need stability in the requirements to operate under the program and stability in the financial terms of the agreement. Further change will place stress on these long term plans and chase capital away from the program. The American farmer cannot afford this.

Future

I would like to conclude with a few general comments relating to the future of the crop insurance program:

(1) Without an effective risk management program like the current Federal Crop Insurance Program, many farmers would not be able to withstand the weather-related risk of producing crops and they would not be able to secure adequate financing, especially in the tighter credit environment of today, to properly finance the capital intensive production of crops that agriculture has become today. These farmers would not be farming, When farmers don't farm, the nation's economy not only loses farm jobs, it also loses jobs in sectors directly related to the production of crops, including a wide array of production input products and services.

(2) Since passing the Crop Insurance Act of 1980 and the major amendments done since the passing of the Act, the success of the Program is nothing short of amazing. The crop insurance programs is now the foundation for Ag Credit and renders the farmers a comeback after a bad crop year and continue his farming operation in the future.

(3) Last, I hope you take into consideration the reduction this program has taken not only in the farm bill but also in the latest SRA. The 2008 Farm Bill provided a $6.5 billion in savings from crop insurance to fund nutrition and other programs over a 10 year period. The 2011 SRA has taken another $6 billion out of crop insurance with $2 million for Conservation Programs and $4 million for debt reduction. These changes cumulatively represent a $12.5 billion reduction to crop insurance over a 10 year period. This represents a 40% reduction in the amounts companies receive to administer and take risk under the program. If this percentage of debt reduction ($4 million) was applied to the Federal budget it would result in $2.3–$2.4 trillion of debt reduction. I hope you remember that we have done our part already; however, it goes without saying—no program is perfect and we need to continue to refine the program and hopefully are able to adapt to the ever-changing agriculture.

Thank you once again for this opportunity and I want you to know that I am available to you and staff if anyone has any questions either now or in the future.

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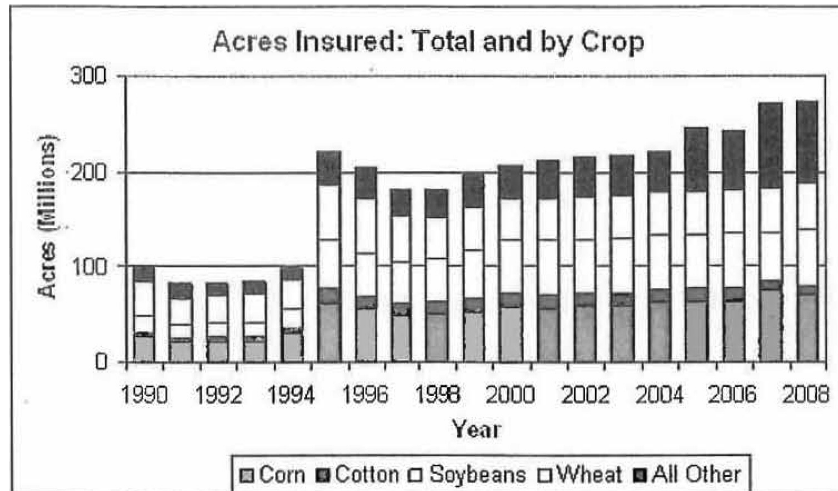
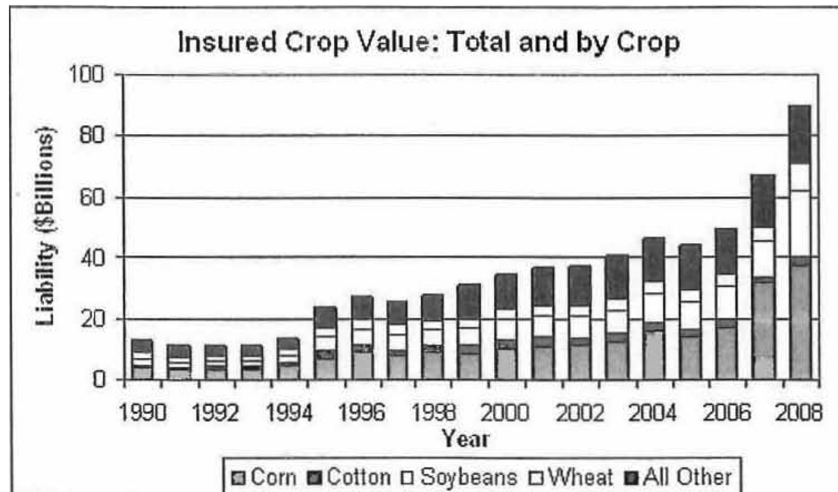
Exhibit 1



- There are 16 private sector insurance companies that currently sell and service policies through the Federal Crop Insurance Program. Altogether, these companies issued more than 1.1 million policies in 2008.



- According to Dr. Bert Little, Tarleton State University, the rate of fraud in the Federal Crop Insurance Program is estimated to be less than ½ of 1 percent. By insurance industry standards, this is an extremely low rate of fraud.
- More than 80 percent of insurable farmland in the United States is now protected through the Federal Crop Insurance Program. In 1985, that number stood at less than 18 percent.

Exhibit 2

Industry-Wide CAT Premium and Losses by State
2000-2009
as of June 11, 2010

	10 Year Avg	2000			2001		
State	Loss Ratio	Premium	Losses	Loss Ratio	Premium	Losses	Loss Ratio
AL	25.0%	1,561,455	1,022,230	65.5%	1,368,143	35,557	2.6%
AK	70.2%	12,460	31,084	249.5%	19,713	-	0.0%
AZ	17.1%	1,659,173	185,922	11.2%	1,456,997	793,255	54.4%
AR	15.0%	19,565,519	5,965,795	30.5%	16,713,899	978,443	5.9%
CA	13.9%	50,297,661	3,739,581	7.4%	50,083,070	7,814,650	15.6%
CO	44.6%	2,146,892	1,189,255	55.4%	1,548,413	346,844	22.4%
CT	3.0%	481,517	87,299	18.1%	487,987	7,747	1.6%
DE	18.2%	342,484	28,010	8.2%	323,382	12,405	3.8%
FL	55.3%	28,764,304	2,743,810	9.5%	31,348,974	4,130,327	13.2%
GA	12.6%	7,655,141	1,166,595	15.2%	6,227,399	204,610	3.3%
HI	25.4%	244,027	-	0.0%	236,573	413,363	174.7%
ID	6.1%	3,986,365	135,683	3.4%	2,879,577	367,652	12.8%
IL	19.0%	9,681,666	1,041,830	10.8%	9,176,152	416,157	4.5%
IN	13.1%	2,494,272	65,318	2.6%	2,263,950	19,715	0.9%
IA	17.5%	3,949,098	116,432	2.9%	3,588,923	474,837	13.2%
KS	67.4%	5,050,367	3,524,882	69.8%	3,162,285	1,487,321	47.0%
KY	24.2%	2,967,371	256,142	8.6%	2,562,741	51,666	2.0%
LA	25.5%	8,815,284	2,917,488	33.1%	7,965,953	1,559,733	19.6%
ME	6.1%	1,133,046	197,730	17.5%	1,220,524	17,745	1.5%
MD	16.6%	1,211,612	13,441	1.1%	1,017,366	33,477	3.3%
MA	51.9%	503,549	217,878	43.3%	326,202	375,421	115.1%
MI	24.9%	8,430,343	1,704,069	20.2%	8,524,212	4,736,944	55.6%
MN	22.4%	6,416,454	533,760	8.3%	5,765,563	1,953,753	33.9%
MS	12.4%	7,797,153	2,359,935	30.3%	5,814,353	276,952	4.8%
MO	20.1%	13,600,956	1,471,827	10.8%	12,439,638	1,984,022	15.9%
MT	128.1%	2,651,110	12,797,424	482.7%	2,122,198	5,185,930	244.4%
NE	27.0%	2,503,665	942,997	37.7%	1,844,945	232,855	12.6%
NV	19.6%	24,854	499	2.0%	74,721	-	0.0%
NH	14.2%	38,721	12,717	32.8%	70,588	16,083	22.8%
NJ	17.9%	1,624,069	597,614	36.8%	1,786,610	131,188	7.3%
NM	24.9%	1,362,366	469,537	34.5%	1,053,327	74,620	7.1%
NY	31.6%	3,295,540	2,529,679	76.8%	3,337,967	467,734	14.0%
NC	19.5%	6,847,582	666,524	9.7%	6,708,732	690,632	10.3%
ND	50.9%	3,864,710	899,614	23.3%	2,696,419	879,106	32.6%
OH	16.2%	2,279,469	354,510	15.6%	2,253,648	134,154	6.0%
OK	53.4%	2,655,787	1,847,291	69.6%	1,984,982	1,170,381	59.0%
OR	2.6%	3,499,030	99,531	2.8%	3,539,156	392,527	11.1%
PA	26.2%	1,935,307	340,534	17.6%	2,031,465	540,363	26.6%
RI	24.0%	37,238	2,619	7.0%	30,608	2,640	8.6%
SC	33.9%	4,077,661	1,779,847	43.6%	3,488,815	671,595	19.2%
SD	79.3%	2,360,333	618,132	26.2%	1,935,917	1,124,750	58.1%
TN	36.7%	7,975,214	983,521	12.3%	7,569,790	1,482,285	19.6%
TX	38.3%	13,811,905	8,777,975	63.6%	12,547,979	4,914,724	39.2%
UT	31.7%	149,208	237,348	159.1%	134,316	95,665	71.2%
VT	60.8%	149,313	138,789	93.0%	120,336	26,964	22.4%
VA	10.2%	1,477,348	73,294	5.0%	1,386,695	40,303	2.9%
WA	8.8%	7,566,334	260,215	3.4%	7,492,935	511,629	6.8%
WV	16.7%	116,936	28,826	24.7%	136,035	12,052	8.9%
WI	29.3%	5,463,576	531,410	9.7%	4,903,992	2,555,735	52.1%
WY	120.5%	303,983	135,214	44.5%	264,001	306,757	116.2%
Total	25.9%	264,839,428	65,841,657	24.9%	246,038,166	50,153,268	20.4%

	2002			2003			2004		
State	Premium	Losses	Loss Ratio	Premium	Losses	Loss Ratio	Premium	Losses	Loss Ratio
AL	1,214,314	339,313	27.9%	1,154,706	312,875	27.1%	1,330,697	122,395	9.2%
AK	23,593	272	1.2%	23,979	132,602	553.0%	28,385	-	0.0%
AZ	1,352,253	72,707	5.4%	1,326,684	626,310	47.2%	1,306,385	238,920	18.3%
AR	14,913,562	2,989,641	20.0%	14,308,875	2,092,610	14.6%	15,800,234	783,609	5.0%
CA	47,322,949	3,168,968	6.7%	49,029,637	4,841,214	9.9%	51,823,123	5,374,645	10.4%
CO	1,404,539	2,144,100	152.7%	1,006,054	439,447	43.7%	939,356	449,484	47.9%
CT	516,634	25,843	5.0%	432,728	9,908	2.3%	539,497	1,145	0.2%
DE	276,826	273,113	98.7%	211,515	43,174	20.4%	176,678	770	0.4%
FL	30,307,175	1,447,763	4.8%	28,928,359	1,985,224	6.9%	32,505,656	22,581,691	69.5%
GA	5,674,039	1,371,098	24.2%	5,608,335	929,719	16.6%	5,998,495	464,861	7.7%
HI	210,924	-	0.0%	179,833	-	0.0%	204,626	94,320	46.1%
ID	3,383,382	293,172	8.7%	3,825,304	559,117	14.6%	3,442,784	130,080	3.8%
IL	8,239,179	1,867,732	22.7%	8,008,190	774,544	9.7%	7,880,337	405,199	5.1%
IN	1,965,311	817,806	41.6%	1,790,106	385,463	21.5%	1,656,855	102,859	6.2%
IA	3,212,023	178,151	5.5%	3,173,670	779,293	24.6%	2,787,936	169,911	6.1%
KS	2,724,657	5,102,784	187.3%	1,934,622	1,269,259	65.6%	1,945,236	785,454	40.4%
KY	2,234,490	523,206	23.4%	2,097,487	323,060	15.4%	2,324,769	494,537	21.3%
LA	6,769,518	2,678,596	39.6%	6,896,998	1,672,787	24.3%	7,455,252	1,375,238	18.4%
ME	1,243,827	34,890	2.8%	1,170,227	-	0.0%	1,175,475	234,012	19.9%
MD	1,007,746	720,079	71.5%	972,784	622,651	64.0%	1,049,253	132,534	12.6%
MA	390,159	324,337	83.1%	375,157	188,034	50.1%	425,485	115,179	27.1%
MI	7,835,847	3,991,923	50.9%	7,485,996	899,166	12.0%	7,827,663	1,323,788	16.9%
MN	5,224,312	797,573	15.3%	5,078,296	1,577,854	31.1%	4,958,933	1,592,017	32.1%
MS	6,504,350	1,542,915	23.7%	6,951,900	910,134	13.1%	8,086,636	282,733	3.5%
MO	10,837,999	1,967,191	18.2%	10,769,806	1,989,524	18.5%	12,368,397	471,119	3.8%
MT	2,068,497	4,556,108	220.3%	1,810,063	1,006,292	55.6%	1,795,037	4,121,657	229.6%
NE	1,344,850	1,390,361	103.4%	998,253	141,871	14.2%	1,259,934	109,214	8.7%
NV	74,107	20,315	27.4%	60,949	81,768	134.2%	49,149	30,789	62.6%
NH	81,444	39,694	48.7%	83,516	-	0.0%	73,939	-	0.0%
NJ	1,831,298	906,719	49.5%	1,713,475	277,065	16.2%	1,717,468	326,384	19.0%
NM	1,218,966	304,117	24.9%	1,126,411	484,858	43.0%	1,166,859	126,252	10.8%
NY	3,377,333	3,482,677	103.1%	2,727,296	1,076,682	39.5%	3,271,440	1,014,127	31.0%
NC	6,109,683	4,216,673	69.0%	5,225,738	831,911	15.9%	5,385,941	1,248,541	23.2%
ND	2,482,514	4,046,986	163.0%	1,797,951	635,225	35.3%	1,623,959	1,536,785	94.6%
OH	2,022,083	1,376,813	68.1%	1,629,434	289,280	17.8%	1,647,516	233,232	14.2%
OK	1,947,239	1,717,647	88.2%	1,859,688	187,161	10.1%	2,002,676	229,393	11.5%
OR	4,074,996	141,856	3.5%	4,546,326	201,190	4.4%	5,524,044	40,010	0.7%
PA	1,768,595	2,828,798	159.9%	1,686,553	481,243	28.5%	1,791,467	206,976	11.6%
RI	26,757	9,475	35.4%	17,369	-	0.0%	23,619	-	0.0%
SC	3,070,785	4,056,570	132.1%	2,345,319	652,859	27.8%	2,599,818	151,396	5.8%
SD	1,594,701	6,047,273	379.2%	961,152	680,251	70.8%	861,998	748,697	86.9%
TN	6,784,461	2,106,651	31.1%	7,047,306	6,262,659	88.9%	7,519,004	525,750	7.0%
TX	12,703,117	4,728,260	37.2%	13,815,728	4,803,850	34.8%	15,847,796	1,733,134	10.9%
UT	101,364	87,223	86.0%	104,866	97,398	92.9%	93,060	6,250	6.7%
VT	144,619	235,662	163.0%	108,536	7,230	6.7%	125,057	-	0.0%
VA	1,508,247	470,709	31.2%	1,403,344	196,339	14.0%	1,446,616	20,780	1.4%
WA	7,325,036	824,778	11.3%	7,729,987	927,467	12.0%	7,869,614	926,342	11.8%
WV	170,250	36,241	21.3%	153,440	90,954	59.3%	169,000	37,348	22.1%
WI	4,338,767	759,169	17.5%	3,956,484	1,715,171	43.4%	3,731,476	2,787,110	74.7%
WY	335,833	1,300,686	387.3%	234,300	92,219	39.4%	247,285	602,031	243.5%
Total	231,295,150	78,364,634	33.9%	225,884,732	44,584,912	19.7%	241,881,915	54,488,698	22.5%

	2005			2006			2007		
State	Premium	Losses	Loss Ratio	Premium	Losses	Loss Ratio	Premium	Losses	Loss Ratio
AL	1,214,927	69,702	5.7%	1,032,240	431,445	41.8%	1,523,603	1,095,702	71.9%
AK	35,699	-	0.0%	32,167	1,547	4.8%	31,248	-	0.0%
AZ	1,605,659	78,453	4.9%	1,670,326	144,018	8.6%	1,524,498	70,632	4.6%
AR	15,790,464	3,855,780	24.4%	16,885,124	447,148	2.6%	23,814,827	2,109,320	8.9%
CA	53,963,207	3,532,340	6.5%	56,522,227	4,016,707	7.1%	57,321,416	13,433,480	23.4%
CO	991,480	395,775	39.9%	878,467	547,109	62.3%	1,260,261	120,345	9.5%
CT	466,449	19,881	4.3%	452,168	6,129	1.4%	744,098	2,391	0.3%
DE	154,400	2,398	1.6%	125,374	1,059	0.8%	164,898	37,121	22.5%
FL	32,213,701	77,142,081	239.5%	18,811,103	36,571,433	194.4%	26,756,694	637,899	2.4%
GA	5,103,959	308,024	6.0%	4,682,639	484,904	10.4%	5,788,910	1,650,054	28.5%
HI	194,116	24,109	12.4%	144,400	-	0.0%	193,351	-	0.0%
ID	3,638,606	353,101	9.7%	3,741,481	117,309	3.1%	4,930,880	424,247	8.6%
IL	6,138,163	622,752	10.1%	4,155,958	79,125	1.9%	7,061,582	559,456	7.9%
IN	1,250,226	58,506	4.7%	1,047,313	23,721	2.3%	1,550,318	133,529	8.6%
IA	2,062,340	77,778	3.8%	1,360,442	30,223	2.2%	1,977,234	62,086	3.1%
KS	2,112,409	521,457	24.7%	1,906,109	780,581	41.0%	2,795,723	4,557,384	163.0%
KY	1,681,298	526,889	31.3%	1,496,984	38,262	2.6%	1,990,192	2,478,100	124.5%
LA	7,130,564	910,731	12.8%	6,990,803	758,890	10.9%	9,421,820	395,045	4.2%
ME	791,305	39,653	5.0%	958,913	12,067	1.3%	1,142,882	12,288	1.1%
MD	979,031	2,146	0.2%	677,839	2,810	0.4%	1,255,151	226,358	18.0%
MA	438,931	237,856	54.2%	397,888	81,333	20.4%	479,928	109,972	22.9%
MI	7,108,511	597,582	8.4%	6,636,183	958,541	14.4%	8,662,967	1,518,090	17.5%
MN	4,583,205	630,915	13.8%	3,850,931	900,673	23.4%	4,851,108	2,497,287	51.5%
MS	7,772,102	390,779	5.0%	8,589,290	693,124	8.1%	11,239,720	262,048	2.3%
MO	11,606,337	1,314,984	11.3%	11,342,588	353,546	3.1%	16,053,343	5,685,645	35.4%
MT	1,850,407	206,901	11.2%	1,985,434	1,459,640	73.5%	2,391,269	478,101	20.0%
NE	1,044,975	83,157	8.0%	980,262	103,248	10.5%	1,504,150	82,075	5.5%
NV	134,025	5,791	4.3%	163,904	-	0.0%	183,898	-	0.0%
NH	71,064	-	0.0%	39,257	231	0.6%	55,595	-	0.0%
NJ	1,784,422	66,716	3.7%	1,407,818	121,783	8.7%	1,787,244	76,553	4.3%
NM	1,341,484	57,748	4.3%	1,289,598	291,863	22.6%	1,651,159	82,173	5.0%
NY	3,049,613	273,653	9.0%	2,926,983	818,990	28.0%	3,613,423	322,404	8.9%
NC	4,814,861	161,533	3.4%	4,047,041	73,648	1.8%	6,290,727	2,374,097	37.7%
ND	1,448,208	245,278	16.9%	1,306,360	1,255,517	96.1%	2,257,095	292,564	13.0%
OH	1,674,133	27,999	1.7%	1,079,950	34,793	3.2%	1,823,694	309,661	17.0%
OK	2,141,291	315,122	14.7%	1,949,226	2,103,799	107.9%	2,339,129	2,276,761	97.3%
OR	5,166,831	109,913	2.1%	5,403,807	138,974	2.6%	6,330,780	143,703	2.3%
PA	1,603,156	140,172	8.7%	1,335,146	120,171	9.0%	2,383,577	202,514	8.5%
RI	19,850	-	0.0%	24,166	46,774	193.6%	25,653	-	0.0%
SC	2,199,914	287,472	13.1%	2,224,117	64,667	2.9%	4,039,590	1,882,930	46.6%
SD	853,548	208,680	24.4%	841,064	1,803,147	214.4%	1,011,572	227,085	22.4%
TN	7,506,061	3,334,453	44.4%	6,086,751	2,136,148	35.1%	7,790,216	8,402,676	107.9%
TX	16,806,817	1,567,977	9.3%	13,002,734	8,520,562	65.5%	19,547,826	1,773,488	9.1%
UT	167,030	13,907	8.3%	258,910	34,976	13.5%	344,280	106,493	30.9%
VT	157,301	3,161	2.0%	145,497	311,461	214.1%	196,965	33,084	16.8%
VA	1,484,608	145,179	9.8%	1,042,323	29,663	2.8%	1,482,611	260,516	17.6%
WA	8,844,258	826,568	9.3%	9,236,054	758,927	8.2%	9,821,577	1,116,294	11.4%
WV	168,270	6,510	3.9%	148,081	35,345	23.9%	138,771	11,795	8.5%
WI	3,196,452	945,414	29.6%	2,803,401	382,111	13.6%	3,740,523	896,131	24.0%
WY	240,848	61,072	25.4%	291,261	703,759	241.6%	277,409	156,410	56.4%
Total	236,796,516	100,808,048	42.6%	214,408,102	68,831,901	32.1%	273,565,385	59,585,987	21.8%

	2008			2009			10 Year Avg
State	Premium	Losses	Loss Ratio	Premium	Losses	Loss Ratio	Loss Ratio
AL	2,229,921	89,297	4.0%	2,291,366	215,984	9.4%	25.0%
AK	37,102	29,717	80.1%	33,921	-	0.0%	70.2%
AZ	1,969,793	542,667	27.5%	2,258,669	4,315	0.2%	17.1%
AR	35,735,162	1,901,677	5.3%	31,227,808	9,547,295	30.6%	15.0%
CA	60,825,124	17,125,179	28.2%	59,119,500	11,724,182	19.8%	13.9%
CO	1,507,187	314,278	20.9%	1,839,173	81,173	4.4%	44.6%
CT	692,325	-	0.0%	677,004	3,500	0.5%	3.0%
DE	286,950	8,606	3.0%	263,892	17,294	6.6%	18.2%
FL	22,033,238	81,317	0.4%	24,365,513	5,385,039	22.1%	55.3%
GA	7,930,655	541,786	6.8%	6,974,923	621,060	8.9%	12.6%
HI	304,497	5,407	1.8%	219,281	3,957	1.8%	25.4%
ID	5,698,129	136,348	2.4%	6,875,459	59,759	0.9%	6.1%
IL	9,641,494	6,963,275	72.2%	7,062,564	1,943,614	27.5%	19.0%
IN	2,250,283	536,844	23.9%	1,763,782	219,976	12.5%	13.1%
IA	2,491,838	2,284,771	91.7%	1,312,059	359,440	27.4%	17.5%
KS	3,843,807	824,019	21.4%	3,221,948	484,778	15.0%	67.4%
KY	2,846,429	242,936	8.5%	2,214,827	480,971	21.7%	24.2%
LA	14,493,362	7,872,013	54.3%	10,255,955	1,838,082	17.9%	25.5%
ME	1,477,561	91,790	6.2%	1,929,839	104,434	5.4%	6.1%
MD	1,760,831	88,467	5.0%	1,533,585	56,725	3.7%	16.6%
MA	508,240	48,609	9.6%	460,409	535,826	116.4%	51.9%
MI	10,812,947	3,499,447	32.4%	10,631,440	1,690,236	15.9%	24.9%
MN	5,797,872	620,823	10.7%	4,695,847	368,077	7.8%	22.4%
MS	16,219,150	1,355,174	8.4%	10,627,310	3,011,324	28.3%	12.4%
MO	24,295,210	9,562,589	39.4%	16,997,051	3,394,113	20.0%	20.1%
MT	3,804,160	1,050,057	27.6%	3,923,096	402,364	10.3%	128.1%
NE	1,935,579	829,989	42.9%	1,577,234	128,997	8.2%	27.0%
NV	199,611	-	0.0%	273,782	103,553	37.8%	19.6%
NH	52,158	3,261	6.3%	43,703	14,732	33.7%	14.2%
NJ	2,025,269	623,491	30.8%	1,990,263	29,539	1.5%	17.9%
NM	1,913,784	620,276	32.4%	2,376,811	1,092,949	46.0%	24.9%
NY	4,466,487	228,701	5.1%	4,307,135	647,080	15.0%	31.6%
NC	8,751,500	1,116,602	12.8%	6,558,100	456,086	7.0%	19.5%
ND	2,788,596	1,309,606	47.0%	2,223,408	347,844	15.6%	50.9%
OH	2,074,046	115,456	5.6%	1,481,185	26,554	1.8%	16.2%
OK	3,477,061	675,477	19.4%	4,492,595	2,747,541	61.2%	53.4%
OR	6,966,081	30,368	0.4%	6,146,898	21,623	0.4%	2.6%
PA	3,566,362	411,923	11.6%	2,877,064	220,640	7.7%	26.2%
RI	34,861	2,310	6.6%	26,075	-	0.0%	24.0%
SC	5,650,351	1,384,636	24.5%	4,067,518	527,258	13.0%	33.9%
SD	1,595,759	125,186	7.8%	3,156,317	443,337	14.0%	79.3%
TN	8,954,547	719,893	8.0%	7,274,017	1,355,784	18.6%	36.7%
TX	23,263,679	9,201,673	39.6%	26,120,890	18,199,183	69.7%	38.3%
UT	433,181	49,617	11.5%	577,703	19,312	3.3%	31.7%
VT	203,774	24,215	11.9%	211,883	170,534	80.5%	60.8%
VA	1,781,484	109,247	6.1%	1,495,797	136,656	9.1%	10.2%
WA	10,994,355	957,069	8.7%	13,219,007	858,608	6.5%	8.8%
WV	168,585	1,248	0.7%	186,167	22	0.0%	16.7%
WI	4,901,780	950,121	19.4%	4,356,283	604,597	13.9%	29.3%
WY	297,073	28,168	9.5%	351,483	40,686	11.6%	120.5%
Total	335,989,230	75,335,626	22.4%	308,167,539	70,746,633	23.0%	25.9%

The CHAIRMAN. Thank you. That was a walk through history, and we appreciate your testimony.

We would like now to move on to Mr. Dalton, President, Midwest Insurance Associates, Agri-Land Insurance Agency, on behalf of the Independent Insurance Agents & Brokers of America.

STATEMENT OF JOHN F. DALTON, PRESIDENT, MIDWEST INSURANCE ASSOCIATES LLC AND AGRI-LAND INSURANCE AGENCY, COUNCIL BLUFFS, IA; ON BEHALF OF INDEPENDENT INSURANCE AGENTS & BROKERS OF AMERICA

Mr. DALTON. Good morning, Chairman Boswell, Ranking Member Moran, and the rest of the Subcommittee.

My name is John Dalton, and I am pleased to be here today on behalf of the Independent Insurance Agents & Brokers of America. I am the President of Midwest Insurance Associates, LLC, and Agri-Land Insurance Agency located in Council Bluffs, Iowa, and I am a member of the Big "I" Crop Insurance Task Force.

As you know, for the 2008 crop year, the Federal Crop Insurance Program provided coverage on more than 272 million acres across all 50 states. This is more than 80 percent of the insurable acreage, with liability protection totaling almost $90 billion.

Crop insurance agents are proud to be part of the successful expansion of this invaluable program to farmers, and I would like to thank you for the opportunity to provide our association's perspective on the state of the crop insurance industry.

I would like to begin today by expressing our concern as independent agents regarding components of the 2011 SRA. The Big "I" strongly opposes the new SRA's commission cap provisions. The current SRA represents the first time that RMA or any government agency has attempted to regulate crop insurance commissions rather than allow the marketplace to determine the appropriate commission rate. This also represents the first time that the Federal Government has intervened in the agent-company relationship.

For more than 20 years, insurance agents have worked side by side with the crop insurance companies, and the Federal Government, to increase the use of crop insurance across America. Crop insurance is a proven risk management tool that protects farmers against unforeseen calamities, and protects the Federal Government from even more disaster aid than it already hands out.

The Big "I" is deeply disappointed that the RMA has chosen to reward the success of insurance agents by thrusting itself into the agent-company relationship and instituting a cap on agent earnings. RMA has set out to determine agents' earning ability, earnings that agents use to raise their families, stimulate rural economies, and hire and pay workers in an agreement which the agents have no voice or legal ability to represent themselves.

In a time of great economic strain where rural economies are struggling and our best and brightest are migrating to more urban centers looking for better job opportunities, this proposal seeks to protect the interest of big business and impose caps on the Main Street workers. It is difficult for agents to understand how an Administration that has built its platform on supporting small busi-

nesses and regenerating rural economies has chosen now to turn their backs on Main Street America.

The proposed 80 percent commission cap does not save the government any money, not one red cent; and it only serves to further compromise the crop insurance program and its intended beneficiaries, farmers and ranchers. The $6 billion cut to the program, on top of the cuts already made to the 2008 Farm Bill, coupled with the controlling commission cap proposal, greatly undermine crop insurance agents.

The proposed changes to the delivery cost system concern us because these changes have a disproportionate effect on the Corn Belt States. Our large agricultural economy employs thousands of workers and creates thousands of sustainable jobs. In Iowa alone, there are over 7,000 workers who are tied to the crop insurance program. As a result, jeopardizing the solid structure of the Federal Crop Insurance Program may have far-reaching and unintended consequences for a state like Iowa, because its economy depends so heavily on agriculture.

The RMA's stated reason for instituting this commission cap is to protect companies from themselves, and they specifically cite the 2002 failure of the American Growers Insurance Company as a justification for the agent commission cap. However, common sense would suggest that there may be additional factors associated with the failure of this company.

It is widely known that American Growers was overly reliant on risky insurance products, specifically, the Crop Revenue Coverage Plus policy when they became insolvent. CRC PLUS, developed by American Growers, allowed farmers to buy up the spring price for their crops. In most cases, the farmer could buy more revenue coverage at the 75 percent level, and at a lesser premium, than buying an increased level of coverage at the lower spring price. For this reason, farmers in the Midwest lined up to buy corn and soybeans at the increased price, and farmers in the South bought up the CRC PLUS policies for cotton and rice.

American Growers soon lost track of the added liability generated by the additional price option that had been purchased on the commodities. When all of the paperwork for all of the new policies was finally received by the company, it was too late to purchase reinsurance for the additional coverage, and American Growers had no choice but to accept the additional liability. The poor crop year, combined with the failure of the new CRC PLUS policy, caused the company to collapse. American Growers received no more or no less A&O than any other crop companies at that time, yet they were the only company to fail.

Furthermore, even if RMA is truly concerned about the long-term viability of the crop insurance companies, there are less intrusive methods. RMA could have easily raised capital reserve requirements and solvency standards to ensure that companies had enough reserves to handle bad insurance years. Instead of taking this logical step, the RMA chose a far more controversial and more damaging path. Quite simply, instead of protecting companies by forcing them to be responsible and ready to protect themselves, RMA chose to protect the crop insurance companies by directly harming the agents. This is why the Big "I" firmly believes that

RMA has clearly chosen the interest of the insurance companies over that of small business.

I would also like to voice the strong opposition of the Big "I" to the "covenant not to sue" provision in the new SRA. This new provision, which is meant to apply both to insurance companies and to agents, would prohibit agents and companies from filing a lawsuit against the RMA over the A&O cuts to the program. Insurance agents are not parties to the SRA and should not be forced by such an agreement to waive their legal rights. The practical effect of this covenant not to sue is that agents cannot negotiate with RMA on the A&O cuts during the drafting of the SRA, and the agents are now going to be denied their legal right to challenge these cuts in court.

RMA is essentially saying that agents are not allowed to have any voice whatsoever on an issue that directly affects their livelihood, and are unable to seek legal redress if unfairly harmed.

Finally, we believe that the RMA may have overstepped its legal authority by instituting both the agent commission cap and the covenant not to sue. Insurance agents by law are not allowed to be parties to the SRA negotiations, and are, therefore, unable to formally negotiate these provisions even though they apply directly to insurance agents.

Additionally, we have found no explicit authority which gives RMA the authority to regulate commissions.

The Big "I" thanks the Committee for allowing us to present this testimony at today's hearing, and we would like to work with Congress on a legislative fix of the damaging provisions in this new agreement. Thank you.

[The prepared statement of Mr. Dalton follows:]

PREPARED STATEMENT OF JOHN F. DALTON, PRESIDENT, MIDWEST INSURANCE ASSOCIATES LLC AND AGRI-LAND INSURANCE AGENCY, COUNCIL BLUFFS, IA; ON BEHALF OF INDEPENDENT INSURANCE AGENTS & BROKERS OF AMERICA

Good morning, Chairman Boswell, Ranking Member Moran, and Members of the Subcommittee. My name is John Dalton and I am pleased to be here today on behalf of the Independent Insurance Agents & Brokers of America (IIABA). Thank you for the opportunity to provide our association's perspective on the state of the crop insurance industry. I am the President of Midwest Insurance Associates LLC and the Agri-Land Insurance Agency in Council Bluffs, Iowa and a member of the Big "I" Crop Insurance Task Force.

The Big "I" is the nation's oldest and largest national trade association of independent insurance agents and represents a network of more than 300,000 agents and agency employees nationwide. Independent agents offer all lines of insurance—property, casualty, life, health, employee benefit plans, retirement products, and crop insurance. Our agents serve the needs of their communities not only by offering important insurance products to their neighbors, but also by serving as key community leaders—we have agents who serve as volunteer firefighters, youth leaders, school board and city council members.

The typical agency employs licensed support-staff, who help in servicing the products as well as the writing agent. They have considerable overhead—computers with high-speed Internet connections, office space leases, advertising costs, auto expenses, payroll, their own insurance (liability, workers' compensation, health) taxes, and other expenses that are drawn directly from the agent's commissions collected from selling insurance products.

Today an agent does more work per crop policy than ever before. Agents do all the data entry, and they keep the yield records per unit—not per policy. The reality is that agents require an extraordinary amount of expertise in servicing this insurance product per acre. Crop insurance agents are proud to be partners in the successful expansion of this invaluable program for farmers, and we appreciate the op-

portunity to provide our perspective today on the important role independent agent's play in the sale and delivery of the Federal Crop Insurance Program (FCIP).

Standard Reinsurance Agreement

I would like to begin by thanking you for your leadership during this difficult economic time, and I would like to take this opportunity to express our concerns, as independent agents, regarding components of the 2011 SRA renegotiation as outlined in the third draft released on June 30, 2010. According to the new SRA, there will be a hard cap of $1.35 billion (or 18%) for Administrative and Operating (A&O) reimbursements to crop insurance companies. Companies will be further forced to cap agent commissions at 80% of the total A&O, per state. A total of 100% of the A&O will be available to agents if the company chooses to offer profit sharing.

The Big "I" strongly opposes the new SRA's commission cap provisions. The current SRA represents the first time that RMA, or any Federal agency, has attempted to regulate crop insurance commissions rather than allow the marketplace to determine the appropriate commission rate. This also represents the first time that the Federal Government has intervened in the agent-company relationship. For more than 20 years, insurance agents have worked side by side with crop insurance companies and the Federal Government to increase the use of crop insurance across America. Crop insurance is a proven risk management tool that protects farmers against unforeseen calamities—and protects the Federal Government from even more disaster aid than it already hands out. Because of the work of insurance agents, the crop insurance program has grown from relative obscurity to the widely used and successful program we are discussing today.

Statistics for the 2008 crop year, as reported by the Risk Management Agency (RMA), show how widely the program is accepted and utilized by farmers and how effectively and efficiently it serves their risk management and cash flow needs. For the 2008 crop year, the program provided coverage on more than 272 million acres across all 50 states, which is more than 80% of the insurable acreage, with liability protection totaling almost $90 billion. The Big "I" is deeply disappointed that the RMA has chosen to reward the success of insurance agents by thrusting itself into the agent-company relationship and instituting an unreasonable cap on agents' earnings.

RMA has set out to determine agents' earning ability—earnings that agents use to raise their families, stimulate rural economies, and hire and pay workers—in an agreement in which the agents have no voice or legal ability to represent themselves. In a time of great economic strain, where rural economies are struggling and our best and brightest are migrating to more urban centers looking for better job opportunities, this proposal seeks to protect the interests of big businesses and impose caps on main street workers. It is difficult for agents to understand how an Administration, that has repeatedly professed support to small businesses and the regeneration rural economies, has chosen to now turn their backs on main street America.

The proposed 80% commission cap does not save the government any money and only serves to further compromise the crop insurance program and its intended beneficiaries—farmers and ranchers. The $6 billion cut to the program—on top of the cuts already made to the 2008 Farm Bill—coupled with the controlling commission cap proposal greatly undermine crop insurance agents. These agents are the very people who have worked so hard to build the success of this program, revitalize rural communities, and build strong foundations for new and existing farmers.

In addition, we all know that commodity prices are cyclical, and commodities have a long and uninterrupted history of moving both up and down. The A&O subsidy for 2010 in Iowa will be significantly down compared to 2009 because of lower commodity prices and lower commodity volatilities. The proposed changes to the delivery cost system concern us because these changes have a disproportionate effect on the Corn Belt states. Our large agriculture economy employs thousands of workers and creates thousands of sustainable jobs. The number of agents and companies writing in the Midwest make this program highly competitive.

According to the National Crop Insurance Services (NCIS), "agent commissions were cut more substantially in the Corn Belt areas, specifically the Midwest, than in other areas." Furthermore, NCIS noted that "they are rebalancing the program by making is less profitable in the Corn Belt, and more profitable in other areas." As a result, jeopardizing the solid structure of the FCIP may have far reaching and unintended consequences for a state like Iowa because its economy depends so heavily on agriculture. This rebalancing will most likely have little effect on economies that do not rely as heavily on the crop insurance business. Agents have acted in a responsible and prudent manner by working to enhance and deliver the crop pro-

gram to farmers and ranchers all across the country, especially in places where demand is the highest.

The RMA's stated reason for instituting this commission cap is to protect companies from themselves, and they specifically cite the 2002 failure of the American Growers Insurance Company (American Growers) as a justification for the agent commission cap. However, common sense would suggest that there may be additional factors associated with the failure of this company. It is widely known that American Growers was overly reliant on risky insurance products, specifically the Crop Revenue Coverage Plus policy (CRC PLUS) when they became insolvent. CRC PLUS, developed by American Growers, allowed farmers to "buy up" the spring price for their crops. In most cases, the farmer could buy more revenue coverage at the 75% level and at a lesser premium than buying an increased level of coverage at the lower spring price. For this reason, farmers in the Midwest lined up to buy corn and soybeans at the increased price, and farmers in the South bought up CRC PLUS policies for cotton and rice. American Growers soon lost track of the added liability generated by the additional price option that had been purchased on the commodities. When all of the paperwork for all of the new polices was finally received by the company, it was too late to purchase reinsurance for the additional coverage and American Growers had no choice but to accept the additional liability. The poor crop year, combined with the failure of the new CRC PLUS policy program caused the company to collapse. American Growers received no more or no less A&O than the other crop companies at this time, yet they were the only company to fail.

Furthermore, even if the RMA truly is concerned about the long term viability of crop insurance companies, there are other less intrusive methods that RMA could have taken short of these unprecedented commission caps that are very damaging to small businesses in an extremely difficult economy. For example, the RMA could have easily raised capital reserve requirements and solvency standards to ensure that companies had enough available reserves to handle bad insurance years. Instead of taking this logical step, the RMA instead chose a far more controversial and more damaging path. Quite simply, instead of protecting companies by forcing them to be responsible and ready to protect themselves, RMA chose to protect insurance companies by directly harming agents. This is why the Big "I" firmly believes that RMA has clearly chosen the interests of large insurance companies over those of small business owners.

I would also like to voice the Big "I's" strong objection to the "covenant not to sue" provision in the new SRA. This new provision, which is meant to apply to both insurance companies and agents, would prohibit agents and companies from filing a lawsuit against the RMA over the A&O cuts to the program. Insurance agents are not parties to the SRA and should not be forced by such an agreement to waive their legal rights. The practical effect of this covenant not to sue is that agents cannot negotiate with RMA on the A&O cuts during the drafting of the SRA, and agents are now going to be denied their legal right to challenge these cuts in court. RMA is essentially saying that agents are not allowed to have any voice whatsoever on an issue that directly affects their livelihood, and are unable to seek legal redress if unfairly harmed.

Finally, we believe that the RMA may have overstepped its legal authority by instituting both the agent commission cap and the "covenant not to sue." Insurance agents, by law, are not allowed to be parties to the SRA negotiations and are therefore unable to formally negotiate these provisions, even though they apply directly to insurance agents. Additionally, we have found no explicit authority which gives RMA the ability to regulate commissions. The Big "I" is strongly opposed to the RMA's overreaching and will pursue any and all avenues to fighting these provisions.

Agent Workload and Program Complexity

Unlike other lines of insurance sales, a crop agent's responsibilities require a much more hands-on approach, which invariably increases the threshold for errors and omissions (E&O) exposure (Professional Liability). On average, with advance meeting preparation, travel, and meeting time, an agent spends approximately 7 hours on a policy during the sales window alone. A transaction typically begins with the agent quoting the wide variety of different plans of insurance available, then explaining production reporting and supporting record requirements to the farmer. The agent explains different date requirements by crop and coverage for application, the actual production history (APH), the acreage report, and the farmer's options and claims. He completes APH-related forms for the farmer, calculates preliminary yields, reviews production early to determine if there is a revenue loss, reviews the APH form for completeness and accuracy, and forwards the signed form and any applicable worksheets to the company. The agent must also review approved APH

from the company to ensure accuracy, explain approved APH yields to the farmer, and provide him with a copy.

Additionally, the agent is responsible for implementing procedures for Preventive Planting, Yield Adjustment, Unit Division changes, Power of Attorney requirements, or any of the other technical policy provisions. All of preceding goes into writing the policy—and does not even factor in the consequences of a potential loss, which occurs more often than any other line of insurance. Compared to the sale of life, farmowners, homeowner's, or auto insurance, the sale of crop insurance is indeed extremely complex and challenging.

Crop Insurance—an Indispensable Financing Tool

The 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 and more 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 would be unable to obtain financing without crop insurance.

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 a lender much more confidence in extending credit.

Conclusion

The Big "I" thanks the Committee for allowing us to present this written testimony at today's hearing, and we would be happy to work with this Committee at any time to further explain the vital role that crop insurance agents play in the FCIP. The Big "I" strongly opposes the new SRA and would like to work with Congress on a legislative fix to the damaging provisions in this new agreement.

The CHAIRMAN. Thank you, Mr. Dalton.

I would now like to recognize Ms. Kathy Fowler, President, National Association of Crop Insurance Agents, Memphis, Texas.

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

Ms. FOWLER. Good morning, Chairman Boswell, Ranking Member Moran, and Members of the Committee.

As previously mentioned, I am Kathy Fowler from Memphis, Texas, and I am President of the National Association of Crop Insurance Agents, NACIA. I thank you for this opportunity to testify before this Committee.

As you may know, while crop insurance agents are an integral part of this crop insurance program, we are not one of the parties privy to the standard reinsurance agreement negotiations. So, we truly appreciate this opportunity to contribute to the discussions surrounding the crop insurance program.

As we take a look at the impact of the new SRA, it is yet to be seen what will come out of this agreement. That will be decided with agents and companies on the ground. As small business owners, we have to determine how to move forward on continuing to provide products to our farmers, and continuing our support of rural America. As agents, we have a unique position of interacting with farmers on a daily basis. We get to know their families, their farming operations, and their risk-management needs.

What we have found is that crop insurance is the preferred safety net. It is not only understood by farmers, but it is the most dependable form of risk management available. Of all of the programs, crop insurance is the only program that has proven itself. With crop insurance, a farmer knows exactly what will happen

when misfortune hits. And, more than that, a farmer knows his crop insurance agent is going to be there to answer any questions. Agents provide extended business hours, schedule meetings at night and weekends to accommodate the farmers when a natural disaster strikes. Farmers prefer crop insurance to other safety net programs, and have developed a real trust for this program. With other programs, assistance is too uncertain for farmers and lenders to waste time and money.

We do believe there are a good number of pilot and expansion programs that provide risk management. We would like to thank RMA for using the savings from the SRA for the needed expansion of the Pasture, Rangeland, and Forage Rainfall Index Program, especially in Texas. This program was approved 2 years ago, but funding was not provided until now. We are eager for good pilot programs to work, but if they are not funded, farmers are unable to benefit.

We would like to point out that the vegetative part of this program, PRF, has no traction. Producers do not fully understand or trust the vegetative program. Participation lags well behind the rainfall program.

Because crop insurance works, it is critical to maintain and support this program. The 2008 Farm Bill shifted the premium billing date of October 1 to August 15, with a payment due date of September 15. This is the most difficult financial time for producers. If premium payments are due on September 15, starting in crop year 2012, farmers with spring crops will struggle to make timely payment. Those who have to delay payment will face a 15 percent simple interest penalty payment at the time with the least amount of cash flow. We urge this Committee to postpone this date change to prevent putting unnecessary pressure on producers.

While we understand that the SRA has been signed and agreed to, certain provisions bring concern to agents. We question the legality of the SRA provisions, such as imposing a limit on the ability of agents to negotiate the amount of their compensation with crop insurance companies even though we are not a party to the SRA negotiations.

It is our role to live and work with the agreement made by the companies and the government. We may find that the new agreement works smoothly and it is business as usual; or we may find that we need to make adjustments, cuts, and diversify our business. While we understand that the $6 billion cut will affect the 2012 Farm Bill baseline and could affect program funding, we would like to recommend to this Committee that any additional cuts in the 2012 Farm Bill will jeopardize the service delivered to producers that they have come to rely on.

Producers do not solely rely on our knowledge of the program and their farming operation, but on the fact that we are a conduit between the insurance companies and the insurance recipients, the farmers. Unlike typical casualty insurance, we have a lot more customer interaction. It doesn't stop with the purchase of the product or filing the claim. We may interact with a producer anywhere from 15 to 20 times per farming operation, and this job is something that cannot be accomplished from Washington or regional offices or online. An agent's job requires personal relationships,

knowledge, expertise of not only the crop insurance program and lending procedures, but actual knowledge of the growing crop. We truly set the liability structure for their policy that allows them the collateral for their livelihood.

As Congressman Walz mentioned earlier, the added land provisions I do agree need some updating. As we move forward, we need to ensure any decision or changes improve our present crop insurance program and serve our farmers' risk management needs, as opposed to simply making cuts because funding is needed for new initiatives or will benefit other non-related programs.

I thank you again for this opportunity to testify, and I will be glad to answer any of your questions.

[The prepared statement of Ms. Fowler follows:]

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

Good morning, Chairman Boswell, 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. As you may know, while crop insurance agents are an integral part of the crop insurance program, we are not one of the parties privy to the Standard Reinsurance Agreement (SRA) negotiations. We appreciate the opportunity to contribute to the discussion surrounding the crop insurance program. For my part, I would like to explain the productivity of the program under new or upcoming regulations and legislation from the agent's view.

We are here today to discuss the potential impact of a decision made between companies and the government during the last SRA negotiations. It has yet to be seen what will come out of this agreement, as that will be decided with the agents and the companies on the ground. As small business owners, we have to determine how to move forward while continuing to provide products to our farmers and continuing our support of rural America.

As agents, we have the unique position of interacting with farmers on a daily basis. We get to know their families, their farming operations, and their risk management needs. What we have found is that crop insurance is their preferred safety net. It is not only understood by farmers, but it is the most dependable form of risk management available. Of all the programs, crop insurance is the only program that has proven itself. Since 1938, farmers have relied on crop insurance to provide the best policy to fit each distinctive farming operation.

With crop insurance a farmer knows exactly what will happen when misfortune hits, and more than that, a farmer knows his agent will be there to answer any questions. Agents provide extended business hours, nights, and weekends to accommodate the farmers when a natural disaster strikes. Farmers prefer crop insurance to other safety net programs and have developed a trust for those programs. With other programs, assistance is too uncertain for farmers or lenders to waste their time and money.

We do believe there are a number of good pilot and expansion programs that provide risk mitigation. And we would like to thank the RMA for using some of the savings from the SRA for the needed expansion of the Pasture, Rangeland, and Forage Rainfall Index Program (PRF–RI), especially in Texas. This program was approved 2 years ago, but funding has not been provided until now. We are eager for good pilot programs to work, but if they are not funded, farmers are unable to benefit. We would also like to point out that the vegetative part of the Pasture, Rangeland, and Forage policy has no traction. Producers do not fully understand or trust the vegetative program, and participation lags well behind the rainfall program.

Because the crop insurance program works, it is crucial to maintain and support the program. However, various provisions in the 2008 Farm Bill and the SRA have or will significantly impact the crop insurance industry. The 2008 Farm Bill shifted the premium billing date to August 15, with a payment due date of September 15, the most difficult financial time for producers. If premium payments are due on September 15 starting in 2012, farmers with spring crops will struggle to make timely payment. Those who have to delay payment, will face a 15 percent simple interest penalty payment at a time when the least amount of cash flow is available. We urge

the Committee to postpone this date change to prevent putting unnecessary pressure on producers.

While we understand that the SRA has been signed and agreed to, there are certain provisions that bring concern to agents. We question the legality of the SRA provisions, such as imposing a limit on the ability of agents to negotiate the amount of their compensation with crop insurance companies even though we are not parties to the SRA and had no direct role in its negotiation. These provisions have the potential to reduce the productivity of rural communities, from the agents to the farmers.

It is our role to live and work with the agreement made by the companies and the government. We may find that the new agreement works smoothly, and business can continue as usual; or we may find that we have to make adjustments, such as diversifying our business. While we understand that a $6 billion cut will affect the 2012 Farm Bill baseline, and subsequently affect program funding, we would like to remind this Committee that any additional cuts in the 2012 Farm Bill will jeopardize crop insurance services producers have come to rely on. This could also affect thousands of small businesses in rural America and would be devastating.

Producers do not rely solely on our knowledge of the program or our knowledge of their farming operation, but on the unique position we hold as a conduit between insurance companies and the insurance recipients—the farmers. By combining our knowledge of the insurance industry and our understanding of the distinctive attributes and needs of each farming operation, we are exclusively positioned to provide producers with the crop insurance that best fits each operation. Unlike typical casualty insurance, our interaction with the customer does not stop with the purchase of the product or the filing of a claim. We may interact with the farmer 15–25 times for every farming operation. This job is not something that can be accomplished directly from Washington, regional government offices, or online. An agent's job requires personal relationships, personal knowledge, and personal expertise of not only crop insurance and lending procedures, but also knowledge of the growing crops. We set the liability structure for their policy that allows them collateral to maintain their livelihoods.

As members of farming communities, we are intricately linked with the economical development of rural America. Many crop insurance agent companies are small businesses with ten or fewer employees. During an era where rural communities are shrinking and urban cities are growing, increasing jobs in small towns is crucial to keeping the heart of rural America pumping. The values embedded in small towns are a significant part of the American lifestyle. Maintaining and even increasing crop insurance agent jobs will contribute to the development of rural communities by reinvesting money and manpower in local businesses, school systems, and local governments. My agency is just one example of the entrepreneurial and hard-working spirit that pulses through rural communities. Crop insurance agents not only provide a direct service to producers, but provide services to the community at large.

According to RMA, in 2009, the crop insurance program distributed approximately 1.17 million policies, covering nearly 264 million acres with $79.2 billion in protection. Many levels of crop insurance reach 70 to 85 percent of potential crop value and 80 percent of major program crop acreage are insured. This program has proven to be the fundamental safety net for farmers year in and year out. It is relied upon by producers to ensure them access to credit that allows them cash flow to fund their businesses.

Going forward, 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.

In conclusion, I would like say how proud we are 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. We look forward to continuing our support of farmers, with the help of Congress, the RMA, and crop insurance agencies.

Thank you again for the opportunity to testify, and we appreciate your continued support of this program. I would be happy to answer any questions you may have.

The CHAIRMAN. Thank you.

I call to Members' attention that Mr. Costa, the gentleman from California, has joined us. He is not a Member of the Subcommittee, but he is a Member of the full Committee. I have conferred with my Ranking Member, and we would like to welcome you to join us and, in fact, invite you to introduce our next witness.

Mr. COSTA. Thank you very much, Mr. Chairman, Ranking Member Moran, and the Members of the Committee, for the good work that you do on these very important issues.

I am very pleased and honored to have a constituent, Mr. Jordan Roach, who is our last witness to testify on the second panel. I urge Members to pay close attention, as you have with the other witnesses, to his testimony, the *Tale of Two Cities,* as he refers to it. It reminds us once again that American agriculture is diverse throughout our nation, and one size does not fit all, and crop insurance, as it is applied to the different regions of America, have very important aspects when farmers, ranchers, and dairymen are balancing risk assessment *versus* the risk management, and the limited tools they have available to them to balance that risk assessment with that risk management.

Mr. Roach, we welcome you here, as all the witnesses, for the good work you are doing on behalf of American agriculture.

The CHAIRMAN. Thank you, Mr. Costa.

With that, Mr. Roach, you may begin.

STATEMENT OF JORDAN A. ROACH, VICE CHAIRMAN, CROP INSURANCE PROFESSIONALS ASSOCIATION LLC, FRESNO, CA

Mr. ROACH. Thank you very much.

Mr. Chairman, Congressman Moran, and Members of the Subcommittee, thank you for this opportunity. My name is Jordan Roach. I am from Fresno, California, and I am Vice President of Mary Roach Insurance Agency, which has provided farmers with professional and trustworthy crop insurance for 18 years.

Like many of the producers that we serve, our company is a family business. My mom started it, and I grew up around it in the vineyards and orchards of the farmers that we serve. And I must add that I hope one day my newborn daughter, Madeleine, will have the chance to follow in her grandmother's footsteps.

I am honored to appear before you as Vice Chairman of the Crop Insurance Professionals Association, or CIPA, an organization that is comprised of veteran agents dedicated to making crop insurance the best it can be for all farmers. For CIPA agents, crop insurance is not just a business, it is a way to serve farmers and ranchers who are also our friends and neighbors, and whose success is important to our communities.

Before going into substance, I would ask for three letters from CIPA to the USDA concerning the SRA might be included in the record.

The CHAIRMAN. Without objection, so ordered.

[The documents referred to are located on p. 78.]

Mr. ROACH. The letters articulate our best hopes and deepest concerns over the SRA, and I believe they will have lasting relevance as you enter the farm bill debate.

The theme of the letters, of my testimony, and of CIPA as an organization is this: Crop insurance is a model for public-private partnership that has accomplished much. It can accomplish more; and, given the challenges facing U.S. producers and fiscal constraints facing the government, it should be built upon.

In my written testimony, I do use the *Tale of Two Cities* metaphor to describe the state of crop insurance. These times are at once very exciting and troubling.

First the good news: Crop insurance is better and more vital to producers today than ever before. Crop insurance provides farmers with relevant and bankable protection, a contrast to ACRE and SURE, and especially critical to beginning farmers. Crop insurance is a safety net available to almost all producers where alternatives leave out specialty crop producers.

Farmers also appreciate the business-oriented contractual nature of insurance, paying for the coverage that they need, knowing it will be there timely and in full if disaster strikes, and that their privacy will be protected.

Finally, a private, competitive, and accountable agent force, along with the companies, have continually worked to improve products and services to producers. We would not have the successful program we have without private delivery.

For these reasons and other considerations relevant to lawmakers, including cost effectiveness, public acceptance, and WTO legality, one would hope that Washington would be celebrating the achievements of crop insurance.

But now the bad news. The SRA confirms that no good deed goes unpunished. USDA's PR spin machine worked overtime to justify deep cuts to private-sector delivery, rather than finding ways to better the program for the farmers it serves. CIPA's position on the SRA was simple: Rather than taking money from the industry and from the important baseline for agriculture, savings should be reinvested to address producer needs. If the goal of the Administration was to reduce overhead and delivery, this goal could be achieved by simply lowering the premium rates for all producers and, thus, A&O and premium for the government.

CIPA also encouraged the USDA to improve the APH to better reflect what farmers expect to produce, and to improve and expand policy options for underserved regions, crops, and practices. Sadly, with the exception of the PRF expansion, this did not happen. The SRA was therefore a missed opportunity to help farmers and was a blow to the agriculture budget, but it also means real pain and uncertainty for the industry.

Agents are impacted by the cuts to A&O, which at 15 to 20 percent on top of the 12 percent sustained in 2008, are severe. This cut is especially noxious because it contradicts a certainty that was written into the last farm bill, and comes at the same time that the COMBO policy and other new regulations and requirements are being foisted upon the industry. Total A&O will now be capped at roughly $1.3 billion, 15 percent less than the 2010 estimate and 25 percent below the 3 year average, even while the workload is increasing. This will cause a real problem.

But the commission caps in the SRA are the *coup de grâce*, an unprecedented intrusion by the government into private contracts between companies and agents. The caps are unnecessary to ensuring the financial health of companies, and save absolutely no taxpayer dollars. But we fear that they will undermine competition, service to underserved producers, and rural jobs. Hardest hit will be agents in states like Iowa and California. In the "I" States,

where the market has pushed standard commission rates higher, the cut could be anywhere from 30 to 50 percent for 2011.

In my State of California, where CAT coverage is the only economical option for many producers, commissions will be reduced to 4.8 percent. Combined with rate reductions which are on the horizon in the next couple of years, we expect a 50 percent reduction in commissions for CAT. This cap will impose serious hardships on the delivery of CAT, particularly to smaller farmers who are more likely to use it.

So where do we go from here? Fortunately, our industry is dynamic. While there will be economic and job ramifications, when we get through it, we will continue to provide a quality service to growers. As we head into the farm bill, I would ask you to consider what has and has not worked for the American farmer. We believe that crop insurance must be protected. No other program can deliver the same tailored risk management protection to all growers for such a low cost to the taxpayer.

We would also ask that the Subcommittee consider ways to spur USDA to use its existing authorities to expand quality coverage to all areas, and improve the existing policies, so that all producers have access to 85 percent revenue coverage. This goal was set by Chairman Lincoln at the Senate Agriculture Committee's first farm bill hearing, and we think that it represents wise and forward thinking, and it would certainly hedge the political and budgetary risks that are certain to come in the next farm bill.

Thank you once again for the opportunity to testify.

[The prepared statement of Mr. Roach follows:]

PREPARED STATEMENT OF JORDAN A. ROACH, VICE CHAIRMAN, CROP INSURANCE PROFESSIONALS ASSOCIATION LLC, FRESNO, CA

Mr. Chairman, Congressman Moran, Members of the Subcommittee, thank you for providing me with this opportunity to testify before the Subcommittee.

My name is Jordan Roach. I am a crop insurance agent from Fresno, California and I serve as Vice Chairman of the Crop Insurance Professionals Association, or CIPA.

CIPA is an agent organization comprised of veteran agents from across the country, from South Carolina to California, from Texas to Minnesota.

For CIPA agents, selling and servicing crop insurance is not just a business. It is a way to serve farmers and ranchers who also happen to be our friends and our neighbors and whose success is important to our whole community.

The purpose of this hearing is to review the state of the crop insurance industry. Mr. Chairman, this review is a "Tale of Two Cities."

In the first place, on the ground, Federal crop insurance is better and more vital today than ever before.

Everybody from lawmakers in Washington to local lenders are increasingly emphasizing that as budgets for farm bills get slimmer and slimmer, farmers and ranchers must increasingly manage their own price and production risks through tools such as crop insurance.

Producers who have traditionally benefited directly under farm bills will today point to (1) the near irrelevance of the Marketing Assistance Loan and Loan Deficiency Payments and Countercyclical Payments; (2) the great uncertainty of the new SURE program; and (3) the inability to take ACRE to the bank in order to obtain operating loans; and these producers conclude, more often than not, that the only safety net that they really have that is tailored to the risks unique to their individual operations is Federal crop insurance. And, in the case of most of my growers in California—who do not receive any direct benefit under the farm bill—this is absolutely the case.

Giving further witness to the centrality of Federal crop insurance to the American farmer and rancher is the $80 billion in liability covered just last year, which is up from $47 billion 5 years earlier and just $31 billion 10 years ago. All told, producers

received about $9 billion in indemnities in 2008 and another $5.2 billion in 2009. And, in stark contrast to *ad hoc* disaster assistance and SURE, crop insurance indemnities were paid to farmers and ranchers in the same timely manner in which one might reasonably expect to receive an indemnity on their car or home or other property and casualty line of insurance.

There are also other signs pointing to the emergence of Federal crop insurance as a core component of the farm safety net. As the Federal Government grapples with how to address budget deficits and debt, some taxpayers may not understand the importance of a farm bill but they do appreciate the need for insurance.

As the Doha Round continues to falter and we see increased potential for trade litigation, Federal crop insurance provides an unassailable source of protection.

As forces unfamiliar with the realities of farming and ranching today attempt to ratchet down allowable levels of support to producers and attempt to publicly embarrass producers for any support they do receive, Federal crop insurance works to address the real risk management needs of the farm while protecting producer privacy.

And, as farmers and ranchers seek some sense of certainty as they make long-term plans and investments, Federal crop insurance, which is enshrined in permanent law, offers at least some safe harbor from the rocky financial waters all around.

For these reasons and a host of others, one would think that Washington would be working to build upon the incredible success of Federal crop insurance since passage of the Agricultural Risk Protection Act of 2000. After all, as the Chairman of the Senate Agriculture, Nutrition, and Forestry Committee noted in that Committee's first farm bill hearing, there is existing authority under the Federal Crop Insurance Act to aggressively meet the risk management needs of all producers from all regions and of all crops. All that is required is a will to use that authority to help all producers obtain 85% revenue protection. We wholeheartedly agree with Chairman Lincoln: this is the right thing to do.

Unfortunately, in recent years, Washington has not only failed to move quickly down the road of expanding the quality and affordability of crop insurance coverage to the American farmer and rancher, but it seems to have actually hit the brakes and thrown us in reverse. While producers on the ground are clamoring for risk protection that is tailor-made to their operations, some in Washington appear headed in an opposite direction. This is the second part of the *Tale*.

Recent Presidential budget submissions; the slow pace of new policy development and approval; failure to address some systemic program issues, such as Actual Production History; the imprudent push for group risk and whole farm revenue approaches; as well as the recent renegotiation of the Standard Reinsurance Agreement are all very troubling omens for producers, especially beginning farmers, who depend on narrowly tailored risk management tools to weather Mother Nature and volatile markets and to obtain credit. I will touch on each.

First, I would like to thank this Committee for rejecting the Administration's agriculture budgets—which have included suggestions like eliminating CAT policies—year in and year out. I know this Committee appreciates that the farm safety net accounts for less than ¼ of 1 percent of the total Federal budget and only about 16% of the USDA budget and that even if we were to eliminate the farm safety net entirely, it would take 100 years of savings to eliminate just a single year of the U.S. deficit.

Second, regarding the renegotiation of the Standard Reinsurance Agreement, allow me to first direct your attention to the testimony of CIPA Chairman Ronnie Holt who appeared before the full Committee in Lubbock, Texas on May 17 and to three letters of correspondence from CIPA to Secretary Vilsack, dated February 12, April 22, and June 16, in which we outlined our grave concerns. I would respectfully request that these letters be made a part of the record so that I might avoid repeating the points in the context of this testimony.

CIPA's position on the SRA renegotiation was pretty simple. We argued that, if the goal of the Administration was to reduce overhead in the delivery of crop insurance, the goal could be better achieved by lowering premium rates for all producers. Lower premium rates for producers would not only help farmers but it would also lower administrative and operating expense payments, underwriting gains for companies, and the premium costs paid by the Federal Government.

Alternatively, CIPA encouraged the Administration to avoid deep cuts to Federal crop insurance that would undermine the all-important budget baseline for agriculture as Congress heads into the 2012 Farm Bill; service to farmers and ranchers; and good jobs in states like Iowa, Kansas, and my home State of California. We argued that the savings should not go deeper than the level of cuts resoundingly rejected by both the House and the Senate during consideration of the 2008 Farm Bill

and that any savings, whatever the level, ought to be reinvested back into Federal crop insurance to help producers obtain higher coverage at more affordable prices.

Among other things, we also argued for improvements to Actual Production History to eliminate the "double deductible" that many farmers must now pay; for improvements to the rating of certain crops and practices in order to lower producer-paid premiums commensurate with the lower risks; for improvements to policies for underserved crops and regions of the country to get all producers to 85% revenue protection, as Chairman Lincoln has called for; and for an aggressive expansion of policy options for producers to choose from to best protect their operations. We, as agents, were prepared to take cuts to our own commissions to pay for these important priorities that would greatly help our customer farmers and ranchers because we believe Federal crop insurance is about the producer. Yet, sadly, this problem has also been ignored.

Instead, the Administration elected to cut the companies and agents who deliver Federal crop insurance to the tune of $6 billion, on top of the $6 billion in cuts already sustained in the farm bill, many of the effects of which are still to be felt, such as the delay in payments to companies and the requirement of early payment of premiums by producers. Of the $6 billion, $4 billion in budget baseline was forever lost, thanks to the SRA. Moreover, even a good portion of the $2 billion in budget baseline said to have been "saved" under the SRA has, in fact, been lost from the farm safety net, having been dedicated to other mission areas within the Department of Agriculture.

While we appreciate the need to address our nation's staggering debt, and earnestly hope that this contribution toward deficit reduction will somehow shield the whole farm safety net from future cuts, we fear that, if past is prologue, this Committee will be invited to the next budget reconciliation event, nevertheless. Thus, with the farm safety net provided under the farm bill and Federal crop insurance already threadbare, we fear that future cuts are going to cause even more serious economic pain in the countryside, especially if there is an unexpected downturn in crop prices.

To the credit of this Committee and to the Congress, this was surely not what was intended in the farm bill. In fact, as I alluded to earlier, both chambers of the Congress decisively rejected cuts that measured just a small fraction of the total cuts ultimately sustained in the recently concluded SRA. Moreover, the SRA authorized by the Congress in the farm bill was about two things: (1) rebalancing the sharing of risk between companies and the Federal Government; and (2) avoiding sharp spikes in administrative and operating expense payments as experienced in 2008. Unfortunately, however, the SRA devolved into a treasure hunt to pay for other programs and, only when that hunt failed, eventually into an effort to cut the budget.

Thanks to the efforts of many Members of this Committee and other Members of the House and Senate who recognize the importance of Federal crop insurance to our farmers and ranchers and to our rural communities and jobs, some ground was made up between the first and the third USDA drafts of the SRA, not only in terms of the aggregate level of cuts but also in regards to substantive policy. For example, administrative and operating expense payment levels were brought within the realm of reason and total cuts were reduced from $8.4 billion down to $6 billion. We certainly want to acknowledge and thank you for your efforts.

But, frankly, speaking directly to the point of this hearing, the state of the crop insurance industry has been severely battered after what amounts to a 3 year political storm that culminated in an SRA that gambles dangerously with the future strength and viability of Federal crop insurance. For instance, the cuts to administrative and operating expense payments will come at the very same time that the COMBO policy is being introduced; at the same time that complex discounts like "BYE" are churned out; at the same time that cuts made in the 2008 Farm Bill are realized; as common land unit requirements are added; as greater interaction occurs between farm bill programs (*i.e.,* SURE, ACRE) and crop insurance policies; and as the financial stakes grow bigger and bigger and, consequently, more and more is being asked by producers of their agents—agents whose commissions are about to be cut under the SRA by as much as 50% when commission caps are factored in.

For agents, the commission caps contained in the SRA are a gratuitous punch. First, the caps save no taxpayer money. Second, the caps are wholly unnecessary to the goal of ensuring the financial health of companies. In USDA's own words: "As a regulator, RMA performs a rigorous financial analysis each year on each company to ensure that it has the financial capacity to withstand 2 consecutive years of significant losses." These review procedures, which were revamped and strengthened in the wake of a 2002 company failure, which actually had absolutely nothing to do with agency commissions, provided appropriate means to ensure that a company's commission expenses are not out of line. But, while we may never know the

real motive behind the commission caps, we can know the following about the commission caps: (1) that they represent an unprecedented intrusion by the Federal Government into private contracts between companies and agents; (2) that they will undermine service competition and service to underserved producers; (3) that they will mean a 4.8% commission on CAT policies (an end-around on specialty crop producers in states like California and Florida after Congress has repeatedly rejected OMB attempts to eliminate CAT coverage altogether); and (4) that they will cut some agents, including those in Iowa, by as much as 50%, meaning lost economic activity and jobs in rural communities.

For the record, I am not an agent with a commission higher than the percentage of administrative and operating expense payment. But I do not resent those who do receive higher commissions—in fact I aspire to be one of those guys and I believe the signals that I process from this free and open market are healthy in that they make me want to do the things I need to do to be a better agent. But moving from the philosophical to the practical, I also know that cutting someone's income stream by as much as 50% from one year to the next is not a responsible thing to do to anyone, much less in an economy like ours. It requires little imagination on the part of anybody who runs a business or meets a payroll to tell you what happens in the wake of cuts of this magnitude.

In fact, the commission caps, the cut in the administrative and operating expense payment, and the covenant not to sue that was entered into by the government and the companies but which also presumes to bind agents were enough for CIPA to seek outside legal counsel from a prominent law firm on the legality of the SRA, something that is evidently very much in doubt given the excessive efforts to insulate the contract from any legal challenge. To date, CIPA has declined to seek redress in Federal court mainly because the organization did not wish to put in jeopardy the contracts of our agent members.

In this vein, it is appropriate to observe that the agents are increasingly regulated by the Risk Management Agency not only in terms of how we sell and service policies but now how we are compensated financially despite the fact that there has been no privity of contract between RMA and agent, and agents have no seat at the table when the SRA that they are no less bound to is negotiated.

The bottom line is that the recently concluded SRA process marked a missed opportunity to strengthen Federal crop insurance for producers while saving on delivery costs. Instead, spin and cynicism trumped aspiration—and everybody lost in the process. Producers lost the opportunity for better coverage at lower cost. Congress lost funds to write a new farm bill. And, yes, agents lost revenue needed to cover payrolls and sell and service policies to our farmers and ranchers.

Fortunately, for everybody, our industry is dynamic and creative and it will find a way to make the most of what it has been given despite the deep cuts. In the coming days under this SRA, there is certainly going to be some economic upheaval and adjustment, just as the Administration apparently envisioned. But we will get through it, just as we have in the past, and we will continue to strive to provide the best service possible to our growers.

And, as we head into the 2012 Farm Bill debate, it is important to consider what has and has not worked for the American producer. Some may want to push lawmakers in the direction of group risk protection, even though farmers cannot take this sort of protection to the bank, something especially hard on the beginning farmer who is the very producer Washington wishes to protect. Others may want to push Congress into a whole farm revenue approach although the examples of this on the ground have left an awful lot to be desired. Still others may wish to push lawmakers into a one-size-fits-all kind of crop insurance or a crop insurance delivered by the Federal Government, despite the chills each of these propositions sends down the backs of farmers due to their track records.

In the swirl of these new ideas, I would simply ask that you consider what you have in Federal crop insurance, which works exceptionally well for so many, is the only game in town for so many others. And I would also ask that you consider what it can be—even absent legislative action—if we join together to act and press USDA to use its authorities to expand quality coverages for all crops in all areas and improve the existing policies so that all producers would have viable options to buy-up at the 85% level.

Next year, the 112th Congress will walk into the next farm bill in a deep budgetary hole, given the baseline that has been lost through this SRA process, and the expiring budget baseline associated with the SURE program. Yet, expecting to further whittle an already shaved-down farm safety net in order to pay for other things may well jeopardize the coalitional efforts long necessary to pass a farm bill. Moreover, offering new fangled ways to provide producers with less will not work either.

While the *status quo* offered by the commodity title of the farm bill today offers some comfort to producers, I would just say we can do better.

By encouraging USDA to aggressively use its authority under the Federal Crop Insurance Act to expand and improve the quality of coverage and address some of the problems producers face under the program, we can at least lower the very high stakes of what is bound to be a tough and contentious farm bill process.

Thank you once again for the opportunity to testify before this Subcommittee. I look forward to answering any questions Members may have.

ATTACHMENT 1

February 12, 2010

Hon. THOMAS J. VILSACK,
Secretary,
U.S. Department of Agriculture,
Washington, D.C.

Dear Secretary Vilsack:

On behalf of the Crop Insurance Professionals Association (CIPA), an organization comprised of veteran crop insurance agents from across the nation, I write to express our grave concern regarding the provisions of the first draft of the new Standard Reinsurance Agreement (SRA), issued December 4, 2009.

We strongly support efforts to improve and expand the access to quality coverage for producers under Federal Crop Insurance and to build upon its accelerated record of success since passage of the Agricultural Risk Protection Act (ARPA) of 2000. To this end, we are persuaded that the Federal Crop Insurance Corporation should set an ambitious goal of ensuring that, within 5 years, all U.S. producers have the same affordable access to quality coverage as enjoyed by producers best served under Federal Crop Insurance today.

Unfortunately, we are equally persuaded that that goal will never be achieved under the terms of the draft SRA. Instead, the SRA regrettably represents the single greatest retreat of Federal Crop Insurance in its 72 year history and a sharp reversal of ARPA, tabling deep and destabilizing cuts to private sector delivery that will, in the end, result in fewer companies, less access, lower coverage, and lost jobs.

The President, in his State of the Union address, stated that, "Jobs must be our number one focus in 2010." We wholeheartedly agree and respectfully submit that the private sector delivery system of Federal Crop Insurance is already the source of thousands of good-paying jobs and economic stability in rural communities across this nation.

Beyond its inestimable value to farmers—*i.e.,* allowing them to obtain credit, manage their price and production risks, and ultimately recover from a loss—the private sector delivery system of Federal Crop Insurance has added thousands of jobs in the last 10 years as sales have roughly tripled, covering $80 billion in liability with $3.5 billion in producer-paid premiums in 2009.

Mr. Secretary, in your remarks to the U.S. Conference of Mayors, you observed that the Supplemental Nutrition Assistance Program (SNAP), formerly known as Food Stamps, is an economy-driver, helping truckers, grocery stores, and farmers. In the same manner, but to a far greater extent, the two or four agents leasing office space and adding staff to compete in small towns, the adjuster in his or her vehicle travelling at all hours to adjust claims, and the company actuaries, computer programmers, and clerical staff in mid-sized communities all help drive the economy in the heartland—and all are tied directly to Federal Crop Insurance. At the end of the day, everyone can agree that moms and dads will measure an economic recovery not by whether they are eligible for SNAP but by whether they have a job.

Yet, notwithstanding the importance of Federal Crop Insurance, the draft SRA proposes to cut investment in private sector delivery by fully ⅓, imperiling this economy-driver and thousands of jobs that depend on it. Even as jobs legislation to incentivize hiring of new employees is under active consideration in Congress, including tax incentives for small businesses that hire new employees, the mere unveiling of the draft SRA has already had the opposite effect on jobs, chilling the hiring of new employees, putting into question the maintenance of current workers, and putting off computer upgrades and other kinds of investments that create economic activity and jobs throughout rural communities. It is only reasonable to conclude that the actual imposition of these cuts would prove far more detrimental than the mere prospect of them.

Crop Insurance Successes

Federal crop insurance increasingly represents the single most relevant and reliable personal business risk management tool available to farm and ranch families, wherever the region and whatever the commodity. We believe that private sector delivery is integrally responsible for this, allowing Federal Crop Insurance to offer narrowly tailored risk protection that is based on actual price and production while fully protecting producer privacy, being wholly compliant with our nation's trade commitments, and being understandable to the taxpayer.

This is certainly true in the case of fruit and vegetable production and the production of other specialty crops that policymakers in Washington increasingly seek to promote in combating childhood obesity and, more generally, in promoting healthier diets. It is also more and more the case with respect to livestock producers who have not, until more recently, participated in standing Federal policies designed to indemnify losses. And, finally, it is most certainly true for producers of many staple crops that are able to utilize tailored yield and revenue coverage to stay in business, relying on quality service and products and a timely adjustment and indemnification in the event of a loss.

As such, the negotiation of the SRA—which may very well decide whether Federal Crop Insurance continues to expand access to quality coverage, contracts in its services to producers or otherwise just treads water—must be a careful process neither driven by extraneous budget demands nor a convulsive response to a 1 year anomaly.

Critics of the current method of determining administrative and operating (A&O) payments make considerable issue about the increase of such payments from just under $1 billion in 2006 to $1.3 billion in 2007 and $2 billion in 2008, before receding to $1.58 billion in 2009. But what is truly remarkable in this set of facts is the tremendous positive growth in sales of insurance behind that A&O increase. Between 2006 and 2008, farmer-paid premiums (based on prices set by RMA) increased at an even faster pace than A&O, rising from $1.9 billion to $4.2 billion. This more than doubling of sales certainly speaks to the value and importance of crop insurance to producers, but it is also a testament to the quality of the sales force and the service that is currently provided by our competitive private sector delivery system.

Equally impressive is the nearly $8.7 billion in claims in 2008 that were timely assessed by adjusters and paid by companies and the $4.5 billion in claims from the 2009 crop that are also already adjusted and paid. As you know from your own experience in delivering benefits to millions of Americans who are served by the policies carried out by the Department of Agriculture, the labor, capital, and time involved in the timely processing of benefits should not be underestimated. For instance, despite a great deal of hard work and diligence, the Department is just now assessing losses and issues relative to the 2008 crop with respect to the benefits it delivers, and will only begin examining 2009 crop losses months from now. Only those who have never delivered benefits on the ground would dismiss the extraordinary cost and effort involved.

In sum, Federal Crop Insurance is relied upon by producers facing extraordinary risks precisely because protection can be tailored to individual risk management needs, with the guidance of a quality sales force, and it is reliable when disaster strikes, providing timely adjustment and indemnification. Unfortunately, by proposing to slash private sector delivery by fully ⅓, the draft SRA strikes at the very heart of Federal Crop Insurance.

Needed Improvements

Notwithstanding the substantial gains made in the quality of service and products to producers under Federal Crop Insurance since 2000, CIPA believes there is room for improvement. As such, we wholeheartedly agree with the nation's leading farm organizations that to the extent any savings can be generated from the SRA renegotiation without doing violence to private sector delivery such savings ought to be reinvested into Federal Crop Insurance. Specifically, we support the following:

➢ Improvements to Actual Production History (APH) so producers that have seen rapid technological advances and producers in areas that have experienced multiple year losses can insure more of the crop they expect to make in any given year. Existing APH requirements that often rely on outdated or artificially low yields have left many farmers with a "double-deductible" (*i.e.,* a deductible reflected in the difference between what the producer reasonably expects to yield and his or her APH, and the additional minimum 15% deductible required under a policy). Producers ought to be able to insure 85% of what they can reasonably expect to produce based on actuarially reliable data.

- ➢ Coupled with the APH issue, improvements to the rating of certain crops or practices should be pursued. For instance, advanced varieties now dominate planted acreage in the United States. As such, would not lowering rates generally for these crops be a more efficient means to recognizing lower risk than the current piecemeal approach of approving endorsements?
- ➢ Improvements to policies for crops that are relatively underserved, whether in the context of improved access to higher coverage levels, greater access to revenue products, or through new policies that better address the unique nature of the perils faced by such crops. In the past 10 years, there has been a significant increase in the quality of coverage for producers of many crops. In the next 5 years, the goal of the Federal Crop Insurance Corporation should be to ensure a similar increase for crops still underserved.
- ➢ Expansion of policies that are working, including the Pasture Rangeland and Forage policy, but which have been withheld from certain areas due to obstacles that are not imposed by statute.
- ➢ Development of new products to support the growth of advanced fuels under the new RFS2 regulation just released (*e.g.,* EPA projects over 11 billion gallons of biodiesel from corn stover and switchgrass will help meet the 36 billion gallon mandate for renewable fuels by 2022).
- ➢ Finally, the streamlining of compliance mechanisms so that integrity is ensured without placing undue burdens on the delivery system or producers.

As agents serving our farmer customers on a day to day basis, we believe these issues should be addressed and we would be pleased to work with the Risk Management Agency, producer groups, and companies in this regard.

Problems With the Draft SRA

Unfortunately, the cuts proposed under the draft SRA would not only do great violence to private sector delivery but, based on the Administration's proposed budget, the money taken from crop insurance would be channeled to government programs rather than toward better meeting the risk management needs of producers under Federal Crop Insurance.

The obvious jaw-dropping issue from an agent's point of view is the sheer magnitude of the cuts to A&O that appear wholly untethered to reality. It does not require an especially trained eye to discern that the crop reference prices used to calculate A&O discriminate against certain crops, are outdated and artificially depressed, are capped but not cupped, and bear no relationship whatsoever to either crop prices today or those forecast for the effective period of the next SRA. Based on industry analysis, we understand the draft would effectuate a 32% cut to companies and agents in the most recent crop year, atop the 12% cut sustained a little more than a year ago.

That a product or benefit can be effectively delivered at a certain cost in 2011 and beyond simply because it was delivered at that level 4 years ago is, we would contend, a rationale that ignores the realities of managing a competitive business. This is true even if one overlooks the virtual doubling of sales of Federal Crop Insurance since 2006.

Moreover, with respect, the assertion that, "these changes will result in more stability for agents, loss adjusters, company employees and others in rural America that are affiliated with and dependent upon the crop insurance industry" is a fantastically Orwellian description of the kind of devastation common sense dictates anyone to expect from a 32% cut, especially when stacked on top of a 12% cut sustained a little over a year ago.

As is usually the case, the more candid assessment is also the more accurate one. In its assessment, NCIS observed: "[the proposed funding reductions] would dramatically reduce the companies' returns on premium and invested assets and put current business at risk, force sharp reductions in payments to agents, expenditures on offices and other inputs, and reduce service to producers." More candid yet, the draft SRA will put more Americans out of work.

Yet another issue of serious concern under the draft SRA is the upfront denial of potential underwriting gains to companies despite the ostensible purpose of the SRA renegotiation which was to rebalance the sharing of risk. The draft SRA at least appears to take a private sector delivery system in a decidedly public direction, with all of its adverse implications to producers. We agree with farm organizations that contend that adjusting rates is the more logical approach to any perceived excess in underwriting gains. We would note that such an approach would also result in reduced A&O and lower premiums for both the producer and the Federal Government.

The Realities of A&O

While we understand the concern RMA and others have expressed with regard to the way A&O is currently structured, we submit that a solution that is designed to solve the problem of a 1 year anomaly in the past by creating more serious problems in every year thereafter is no solution at all.

While the current practice used to calculate A&O as a percent of premium may not avoid a 2008, it works cost-effectively in the other years and over time and beats every alternative floated to date.

The decoupling of A&O from crop prices or premiums, as proposed under the draft SRA, would militate against the most fundamental objective of Federal Crop Insurance: encouraging high sales of high coverage.

Because the Federal Crop Insurance Corporation establishes the rates of each policy for each crop based on a 1:1 loss ratio (such that producers are not charged for delivery costs), some method has to be used in order for companies to recoup the cost of selling and servicing policies. In the business of insurance, the denominator for allocating delivery costs has always been the premium.

Other factors fluctuate too wildly (*e.g.,* commodity prices) or can be manipulated too easily (*e.g.,* the number of policies sold), but premium is the one constant. Premium is ultimately what we are selling and it is the only figure that reflects both the value of what is covered and the probability that a loss may occur.

If the policy is properly rated, more premium is always a good thing for the business of insurance. This is why commissions for the sale of insurance have always, across all lines of insurance, been based on premium—to incentivize the sale of more premium. By the same token, if the public policy goal of Federal Crop Insurance is still to encourage more producers to insure their risks and to do so at higher levels of protection, then it still makes eminent sense to compensate for the sale of premium in the same way—as a percentage of premium.

Citing statistics that show A&O costs per policy increasing over the past 5 or 10 years as a basis for cutting A&O is neither probative nor helpful to the process because this statistic bears no relation to actual workload. The reality is that all policies are different and, thus, the notion of a per policy commission or A&O reimbursement is simply divorced from what is actually happening on the ground. One policy may cover thousands of acres with multiple tracts and multiple practices, all carrying their own set of data and needs, while another may cover a very simple tract of 40 acres planted to the same crop every year.

While it is true that the overall number of policies sold has decreased over the past several years, reflecting a trend of consolidation, this can hardly be translated to mean less workload on the delivery system. To the contrary, total acres covered under Federal Crop Insurance have actually increased significantly (by 30 million acres from 2006 to 2008), and given that every tract of additional acreage carries its own set of data and needs, this translates into to greater workload and cost of delivery.

While actual costs vary and are as difficult to quantify as a crop's cost of production, what we know from actual experience is that the time and expenses involved in providing a quality service to customers have in fact increased significantly in recent years; in part due to the increased needs and expectations associated with the higher costs to the farmers who rightly expect a commensurate level of service, and in part due to the added requirements, regulations and other changes to Federal Crop Insurance initiated by RMA.

Page 17 of the NCIS response to the first draft contains an important list of changes and developments that have added to the cost delivering a quality service to producers. To this list, we would add the following:

- ➢ Increased training time for agents and staff relative to:
  - ✓ New policies and pilot programs.
  - ✓ Computer programming and quoting software changes.
  - ✓ Changes and new wrinkles to existing policies.
  - ✓ The new "COMBO policy" or common crop policy.
  - ✓ New endorsements and complex discounts, including BYE.
  - ✓ Compliance directives.
  - ✓ Changes in FSA-delivered farm programs that are connected to crop insurance.
  - ✓ The use of the Comprehensive Information Management System.
  - ✓ The use of Common Land Units.

- ✓ Gaining and maintaining solid knowledge of markets and interacting Federal policies to provide a comprehensive service to the customer in the increasingly high stakes and complex business of agriculture.

➢ Increased service time per customer because of:

- ✓ The expectations that come with paying more for better coverage.
- ✓ The complexity and number of policy options, including many new policies or endorsements.
- ✓ The increased use of revenue policies that involve greater volatility.
- ✓ The increased market volatility and higher stakes that have increased producer demands for time, information, and counseling.
- ✓ The consolidation of policies with more crops and more acres added to existing policies.
- ✓ The increased interaction with FSA programs (*i.e.,* ACRE and SURE) that inevitably lead to questions and demands on an agent's time.
- ✓ The increased compliance requirements that involve more record keeping, authorizations, *etc.*

➢ Increased direct costs to agencies in the form of:

- ✓ Investments made in staff and office space to meet increased demands associated with increased sales.
- ✓ Investments in computer systems and technology to quote policies and maintain records.
- ✓ Costs of sales and advertising in an increasingly competitive business.
- ✓ Costs associated with Errors & Omissions insurance for agencies as the value of insurance coverage written has increased and penalties for non-compliance have grown more severe.

In terms of both time and money, agencies have, in fact, seen a substantial increase in the cost of doing business in the last few years as sales have increased. As such, to arbitrarily cut and freeze the A&O reimbursement at 2006 levels or lower for major crops will meet with what one should reasonably expect: a freeze on new hiring, the lay-off of existing workers, finding ways to cut corners, and no new investment.

As agents, we take a long-term view of the business, knowing there will be bad years but trusting these will be offset by good years. Business decisions in agriculture should not be based on a single year's experience, nor should A&O calculations be driven by a 1 year anomaly. One needs look no further than 2009, when premium-based A&O and commissions retreated by 21% from the year before, to illustrate the danger in such an approach. In fact, based on lower volatility factors, lower commodity prices and the full implementation of farm bill cuts, we are bracing for yet another drop in 2010.

In short, while it is true that, alongside our producer customers, agents experienced the high of 2008, we also shared the experience of a protracted string of lows in the late 1990s and the early years of the past decade when there was no intervention to help us. We accept this as a reality of doing business. It has been suggested that the A&O calculation contained in the first draft of the SRA locks in greater certainty. We would agree. It locks in certain failure.

The Legality of Reference Prices

While our chief concern regarding the A&O calculation proposed under the draft SRA deals with its reliance on arbitrary and inappropriately low reference prices, we concur with the legal analysis of NCIS that the proposed calculation violates the Federal Crop Insurance Act.

We will not recite here the legal analysis already provided by NCIS. We understand that the Department believes it is on solid legal grounds. As such, we simply provide notice to the Federal Crop Insurance Corporation that we believe we would have no alternative but to seek relief in Federal court to prevent the implementation of the plan contained in the first draft of the SRA.

Conclusion

To ensure all America's farmers and ranchers have the risk management tools they need, to create and save jobs, and to spur economic growth in rural communities, the Administration should build upon Federal Crop Insurance's record of accomplishment since 2002.

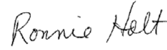
Any savings that can be achieved in the SRA renegotiation without doing violence to Federal Crop Insurance or its private sector delivery system should be reinvested

into Federal Crop Insurance to provide greater access to higher coverage, rather than diverted from the budget baseline of the farm safety net.

The proposal to decouple A&O from the value of policies (premiums and liability) runs counter to the goals of Federal Crop Insurance and violates the law. The specific A&O proposal tabled in the first draft of the SRA would result in fewer companies, fewer agents, less access, lower coverage, and lost jobs.

In sum, the magnitude of the cuts and the means to achieving such cuts are unnecessarily destructive when more sensible, nondestructive means of achieving efficiencies while fully protecting Federal Crop Insurance are clearly available.

Sincerely,



RONNIE HOLT,
Chairman,
Crop Insurance Professionals Association.

CC:

Hon. JAMES W. MILLER;
Hon. WILLIAM J. MURPHY;
Hon. BLANCHE L. LINCOLN;
Hon. SAXBY CHAMBLISS;
Hon. COLLIN C. PETERSON;
Hon. FRANK D. LUCAS;
Members of the Senate Committee on Agriculture, Nutrition, and Forestry; and
Members of the House Committee on Agriculture.

ATTACHMENT 2

April 22, 2010

WILLIAM J. "BILL" MURPHY,
Administrator,
Risk Management Agency, U.S. Department of Agriculture,
Washington, D.C.

Dear Administrator Murphy:

Please accept this letter as a supplement to our letter, dated February 12, which fully sets forth the views of CIPA with respect to the First and Second SRA drafts, generally.

We are compelled to make a statement relative to a provision contained in the February 23 draft SRA referred to as the "soft cap" on agent commissions.

First, we are deeply concerned that the "soft cap" on commissions represents an unprecedented interference by the agency into what are currently wholly private contracts—sometimes multi-year contracts—between companies and agents. We believe the combined effects of the imposition of a "soft cap" and reference prices used to calculate A&O would have severe practical as well as legal implications.

Second, the government imposed cap runs against the principle of service competition that is vital to the success of this public-private partnership. Commissions are a critical way for companies to reward agents who do an exceptional job in servicing their farmer customers.

To eliminate this point of competition will reduce the incentives for agents which will in turn and over time reduce the quantity and quality of competition. While this effect is somewhat mitigated by a company's ability to profit share, the "soft cap" still presents great uncertainties for small businesses that will have a negative impact upon jobs in rural communities across the nation.

On this note, we have read the RMA's argument that a soft cap is needed to prevent another company failure like the one seen in 2002. However, on p. 13 of the RMA's FAQ piece respecting the 2nd draft, you also state, "As a regulator, RMA performs a rigorous financial analysis each year on each company to ensure that it has the financial capacity to withstand 2 consecutive years of significant losses." These review procedures—which were revamped and strengthened in the wake of the 2002 failure—seem very appropriate, and provide a means by which RMA can ensure that a company's commission expenses are not excessive. We believe this proven method is far preferable to the commission cap, which we see as tantamount to an elementary school teacher penalizing the whole class because the teacher fears the possible misbehavior of one student.

Finally, believing the cap is more about taking money out of the private delivery system than anything, we must note that the 80% cap on commissions, when com-

bined with other cuts to A&O for companies, would effectuate a deep and unsustainable cut for many agents in many regions, and make the sale and servicing of certain policies that are already unprofitable even less so.

Based on the NCIS's April 9 comment, A&O for the 2010 crop year in the State of Iowa under provisions of the 2nd Draft SRA will be down 45% from the 2009 A&O, which is already down 25% from 2008. This, of course, is before the cap is applied. If, one assumes that average commissions in Iowa are around 20%, one would be looking at an additional 30% cut generally just to come into compliance with the cap.

To put numbers on this, in 2008 Iowa received $185 million in A&O, in 2009 it received $128 million and in 2010 it is expected to receive $105 million; and based on current commissions all of this money or perhaps even more would have stayed in the state, and gone to people and businesses in rural communities to sustain jobs.

Under the combined provisions of the 2nd Draft (applying the 80% cap on commissions to the expected $70 million in A&O payments, going forward), those same Iowa communities would be limited to roughly $56 million. In short, this cut is simply too deep and we respectfully warn that the economic repercussions will be real, painful and directly tied to this SRA.

Another area that highlights the problem with the 80% cap is with respect to the sales and servicing of CAT policies, which currently provide LAE equal to 6% of the imputed premium.

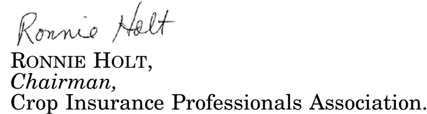
The cap would make the maximum commission on a CAT policy equal to 4.8% of imputed premium, which is simply too low to justify the work associated with the sale to many specialty crop producers or smaller growers of crops where buy-up is simply not viable.

Generally, we applaud and encourage efforts to move growers away from CAT toward higher coverage, and if buy-up were a viable option for growers of all crops, we would not be as concerned.

But CAT remains the only viable option for some crops, and the growers of these crops should not be further penalized by a commission structure that makes it unprofitable for any agent to provide them service.

For these reasons, CIPA strongly recommends that the cap on agent commissions contained in the 2nd Draft be eliminated.

Sincerely,



RONNIE HOLT,
Chairman,
Crop Insurance Professionals Association.

ATTACHMENT 3

June 16, 2010

Hon. THOMAS J. VILSACK,
Secretary,
U.S. Department of Agriculture,
Washington, D.C.

Dear Secretary Vilsack:

On behalf of the Crop Insurance Professionals Association (CIPA), I write to convey our grave concern over the third draft of the Standard Reinsurance Agreement (SRA) and respectfully request that the Administration address these concerns in a fourth draft.

First, we reiterate our sincere hope that you will reinvest the savings resulting from the SRA negotiations into Federal crop insurance in order to help farmers and ranchers by expanding access to quality coverage. For examples, developing and approving quality policies for all crops and regions and addressing certain problems, such as lagging actual production histories, are vitally important.

Unfortunately, the third draft redeploys only a small fraction of the total savings from the SRA negotiations for this purpose. As a consequence, farm and ranch families are seriously shortchanged in this process, Congress is left in a fiscal lurch as reauthorization of the farm bill approaches, and Federal crop insurance is left to somehow deal with combined cuts of more than $12 billion in a matter of just 2 years.

The emergence of Federal crop insurance as a primary and essential safety net for producers began in earnest in 2000 and the public private partnership has proved a remarkable success. Unfortunately, innovation in aggressively meeting pro-

ducer risk management needs seems to have taken a back seat to seemingly endless rounds of cuts that show no signs of letting up until the cuts reach the bone and irreparable damage is done. If this occurs, Washington will have cut through the one thread of policy that, to date, has not generally been politicized and which has offered producers a semblance of stability in these uncertain economic and policy times.

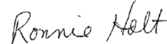
For the sake of producers, we hope that this does not occur. As you know, it certainly does not have to. The Administration's stated objectives of deficit reduction and reducing the cost of delivery can be achieved in another way that is not harmful. As we have observed many times, simply bringing down premiums that producers pay *in lieu of* an SRA renegotiation would achieve both objectives without injury to Federal crop insurance.

Second, we wish to strongly caution the Department that the unprecedented introduction of caps on agent commissions will, in point of fact, work to undermine the Administration's stated objective of better serving underserved producers. We also strongly caution that as much as a 50% cut on commissions anticipated in some states, including Iowa, is going to expand unemployment lines in many mid-sized and small towns.

There are other unsettling parts to the third draft. One example is a provision that actually states that if a company or even a third party litigates a provision of the SRA because they believe that it violates the law and they prevail in a court that the costs to the Department stemming from the lawsuit be borne by the companies signing the SRA. The provision raises a serious question about the SRA's compliance with the law and the Department's confidence in its answer to that question.

We sincerely hope that the Department and other parties to the SRA will look before they leap and address these and other serious concerns in a fourth draft.

Sincerely,



RONNIE HOLT,
Chairman,
Crop Insurance Professionals Association.

The CHAIRMAN. Thank you. It has been an interesting presentation here this morning.

I will start off with a couple of questions. We have votes coming up. If they come too quick, we will just recess and come back.

I am concerned—and Mr. Murphy knew this; we have talked about this—about the caps, getting into the business between the company and the agent and so on. I am also concerned about the legal aspect of it.

Some of you have heard me tell this story. I was just sharing it with Ms. Botts just a moment ago. We are going to look into this a little further.

My last overseas assignment, I was in a NATO headquarters in Iberian Command Atlantic. I had a senior position. At our mess table, we had a big round table, and we had quite an international meeting at noon every day, and I was in the hot seat quite a bit. I discovered after some time—and it kind of set me back a little because I have sort of been a critic—that other nations around the world envy our judicial system. They envy it very much. I thought that was kind of unique. It made an impression on me at that time, that many years ago.

Back when we were developing the last farm bill and we got into the mandatory arbitration, some of you remember that, that sparked me to think that fair is fair. I am not comfortable with that. So so much for that for this moment.

I would like to address maybe a question to Mr. Frerichs of Rain and Hail. Last weekend, I flew my little puddle-jumper around southern and central Iowa. I saw a lot of water everywhere. The

floods are going down. The dikes and levees didn't break, we sweated that out. But I saw a lot of standing water in a lot of spots in corn fields and bean fields that are not going to grow a thing. Of course, there are so many acres overall, I am not saying we are going to have a short crop, but there will be a lot of individuals, at least in those areas, that will really be impacted.

I just wonder if you might address, a company like Rain and Hail in Des Moines, because I flew right over their headquarters as I went from Saylorville down river. I had my chief of staff with me. We were kind of looking things over and thinking, wow, this is pretty bad, but it could have been worse.

But what would the impact be if—and I will use some years where Iowa experienced flooding or drought. In your written testimony, you mentioned RMA uses good weather, consistent good yields to base their cuts. With that point, what would be the impact if they had used years when Iowa experienced flooding or drought? They have been through both of them quite a little bit, in my experience. I have accused Jerry that those Chinook winds that he sends up once in a while from south, southwest Iowa, gets you in trouble sometimes.

But anyway, your comments.

Mr. FRERICHS. Chairman Boswell, thank you for the question.

I just came back from Iowa last night on a commercial flight, and going in and out of Iowa I saw the same water you saw. I saw the rivers out of the banks. It does look pretty bad from the air.

First and foremost, I would like to tell you that Rain and Hail will make sure that every one of those claims that farmers have this year, or in back-to-back loss years gets worked, gets worked quickly, and farmers get the payments that they are required to receive under the crop insurance policies. Rain and Hail prides itself on service, and we will make sure that happens.

This program requires capital standards, capital requirements, unlike any other Federal program. We are required to have surplus roughly equal to two times what we write in premium. So back-to-back losses obviously would affect us. We would have underwriting losses, presumably, on a nationwide basis. If it is just one state, perhaps not. Every year somewhere in the U.S. crops fail, and we make those payments. Say it was a drought like 1988 back to back, obviously, that would impact a company's financial reserves, and it may impact how much over time a company can write.

I would submit to you that is what happened to the company that Administrator Murphy mentioned in his testimony earlier today. That company did not fail because of excess expenses. Sure, excess expenses added to it at the tail end. That company failed 2 or 3 years earlier because of bad risks. Insurance companies don't generally fail because of excess expenses. They fail because they take on bad risks, and that is what happened to this company.

The CHAIRMAN. I recognize Mr. Moran.

Mr. MORAN. Mr. Chairman, thank you.

Mr. Frerichs, you just addressed one of the questions, and I was going to address it to Mr. Dalton. I wanted to make sure that we got on the record that Mr. Murphy, in response to a question that I asked in a prior hearing about the justification for the commission caps, used the failure of an insurance company as the expla-

nation for why this is important. I want to make sure that I understand if there is more to it than this issue, and if company commissions, or expenses, had anything to do with its failure.

Mr. FRERICHS. Mr. Moran, as you may well know, I worked for that company for a year, the year that they went under. I would submit to you and to the Subcommittee that there were a lot of issues that resulted in that company going under.

It looked—it actively sought for a buyer. One of the potential buyers was Rain and Hail, as it turns out. That deal went pretty far along, and then RMA put some terms on the conditions of the sale that Rain and Hail could not agree to, and so they walked away.

Ultimately, that company failed because of bad risks that it took. Its capital eroded over time. It was allowed to purchase another company a year or 2 prior to that, so it expanded, and it did not adjust its expenses. So expenses were clearly an aspect of this. But it was at the very tail end of it. I think that is what RMA is missing.

They put significant financial requirements on the companies. We provide anything and everything to them that they want to know about a company. That is part of the SRA. You shall provide whatever we ask for, and we do that. Clearly, at some point, they missed the capital health of that company, and agreed to let them write premiums that they probably should not have been writing.

Mr. MORAN. Thank you very much.

Mr. Parkerson, let me turn to you. You brought the graphic in front of you, the stack of regulations. Your testimony is that the handbook has grown from 309 pages and appendix 3 has grown by 621 pages. Do you have any estimate of the additional financial cost to companies, given these new administrative costs? And I don't know whether you know the answer to that question, but whatever that amount is would increase the loss or the reduction in support for companies by more than the $6 billion that the SRA agreement—that we attribute to the SRA agreement. Any comments or response to that?

Mr. PARKERSON. Yes. Thank you, Mr. Moran.

We did take a survey. As I said, all 16 SRA holders are members of our organization. We did a survey of those companies. We found that, according to those companies, that we would probably end up spending pretty close to $100 million in trying to pay for, not only on computers, but training and all of the aspects in supporting the program over the next couple of years.

So those are not in total from any expenses. That is what those companies say it will cost them to put in the new computers.

Obviously, to match, RMA is putting in their new computers and to match that the requirements of the new program that is coming out, the COMBO policy that they are doing. All of that came up to, as I understand, about $100 million that they estimate over the next couple of years to spend.

Mr. MORAN. Thank you, Mr. Parkerson.

And, finally, to those who represent the agents, shouldn't there be a legitimate concern about the cap on agent commissions could lead to a decrease in the number of—I am sorry, a decrease in the service to those that you write policies for, your customers? Is there

a concern that the commissions all become standardized, and there is no reason then to compete for better service among those you serve?

Mr. DALTON. Thank you.

I know in our agency that we are looking this coming year to about a 30 percent cut in our agency revenues, which would amount to about $180,000. When you talk about the service end of this thing, this is scary to me, because we are looking at probably having to close an office and lay off a couple of employees.

We service a lot of small farmers; and, in Iowa, a small farmer is someone who is farming 300 or 400 acres. They are doing this on the weekend. Those people actually require more of my time than the guy that is farming 3,000 or 4,000 acres because they are doing it as a business. Very seldom do I spend less than 8 hours a year with a customer. That usually equates to four or five different visits.

I am concerned that if I have to lay off people because of these cuts that I am not going to be able to service these people; and, consequently, the service is going to go down. And what we are trying to accomplish is better service for our people, rather than less. This is definitely going to have a devastating effect on my office.

I started this agency from scratch in 1983. I had one customer, and it was me. We have now grown where we have four offices and 13 employees. We have never had a layoff. We provide stable jobs. I think our people are well paid. Having to lay off people because of these substantial cuts bothers me, and we are talking about people who have been with me for 20 years and are experts in the field. When you start getting rid of people, your service is going to go down the tube, no matter what you do.

Mr. MORAN. Thank you, Mr. Chairman.

The CHAIRMAN. Mr. Walz.

Mr. WALZ. I, too, would like to address my condolences to our Ranking Member. I never had the opportunity to meet your mother, but I have seen the product of her work, and it is all positive.

Mr. MORAN. I was going to say, I didn't realize we were going to get so partisan so quickly.

Mr. WALZ. I was going to say, we often use the term *gentleman* around here, but the gentleman from Kansas embodies that. While this place can bring out the worst in people, it oftentimes brings out the best. And I can tell you my experience here, that is always true with the gentleman from Kansas. He is always dignified and a thoughtful Member. I am sorry for your loss.

Thank you all for being here. I do truly appreciate you all being here.

Ms. Fowler, you mentioned this is a program that farmers understand. I was thinking, I was watching a program last night on TV on quantum physics and time travel, and it is easier for me to understand that than this program. So I am trying to piece it all together. I think we are all here for the same reasons, trying to figure out how to make this thing work.

I think Mr. Frerichs brought up a fair point. We are all concerned with budgets. It is important, but we have a lot of folks that need to be honest. This idea of a budget freeze or something, that

is lazy legislating. You are going to freeze bad programs and you are going to freeze good programs that return money.

I think it is important to put everything in perspective. Since July 1 to this day, we have spent more in Iraq and Afghanistan than the $12.5 billion we would save on this, and it is important for the American public to have a open discussion on cost benefits.

I would also like to say, we are all here trying to make this work, and Mr. Deal gave us the history of this as he moved this thing into the private sector. This is a true public-private partnership. We have to be careful about demonizing.

I heard several of you say an unprecedented intrusion by the Federal Government. No, that was the internment of the Japanese in World War II. It is probably a stretch to use that rhetoric.

I think we need to be careful. You have a great argument. You have points to make. We want to make it work, and we are listening.

I want to get to the point where this works so our agents can deliver the kind of service I know that they do. I talk to them every day, I hear them out there, and I know they are doing that, and I know our producers want that. And we are trying to get where this country makes the best use of its tax dollars to protect those producers. We can do that here.

I, too, am a little disappointed that this SRA did not have the input you needed. I want to hear from you. I am listening. The question I have for you is that this continues to trouble me, and I don't know how we get there with all of the different programs we have, countercyclical direct payments, all of these things. Is this crop insurance—is this a model for where we can get?

And the thing I have, the *ad hoc* disaster assistance, we keep trying, and Mr. Deal talked about Jimmy Carter trying to get away from that. Well, we are still here with the *ad hoc* disaster assistance. Is there a way that we strengthen this program that can pull in and make up for some of that, and we start to use a market-based approached to solving that?

I really want to make this thing work. I know producers love this program, and you have all been part of making this work. Let's make it better now. Let's figure out how to make it better. Is there a way to do that?

I know that question is pretty broad, but it is helping me understand my role of where we should ask the questions.

Mr. RUTLEDGE. Thank you for the question.

To begin with, if you were to ask the farmers of our nation if they had to give up everything but keep one agricultural program, I think they would say crop insurance. As far as a way to strengthen that, RMA, along with the industry, has worked to increase the available coverage to the producers and that would be one way that you could go about that.

I will pass the mike on to the next person.

Mr. PARKERSON. I would echo what Mr. Rutledge said, but I would also like to throw in the fact that, because we do represent all of the companies and oftentimes we are in Kansas City and foreign delegations come in to talk to the RMA group, they often come by NCIS and ask us about this partnership that you have mentioned. It is obviously very envious of what we have here. We have

had German delegations, Chinese, all the Europeans, and they want to know how this works. We are definitely trying to help them understand that. But it is a truly enviable program from around the world, and it needs to be protected for our producers now.

Mr. WALZ. That is my point on this. I think we all come in this together. I know there is a frustration on this. It certainly isn't a sinister takeover by the government to try and get involved in this or anything. But if there is an overstep, we need to know where it was, and we need to figure out how to step back from that. Because I hear this from people. I think, Mr. Rutledge, your statement was dead on. I hear that from people: Well, I don't know what is going to happen, but don't take away crop insurance. I do hear that.

Anyone else?

Mr. Dalton.

Mr. DALTON. Congressman, I would like to give you my firsthand experience on this disaster program. We own some farm ground in southern Iowa, 2008 was not a good year. Obviously, I am involved in the crop insurance business, and I carry that for my own risk management. I was pretty well made whole by the crop insurance in 2008. We have a land manager that takes care of the ground for us, and the county we are in was declared a disaster area in 2008.

This spring I get a call from him; and he says, I have a rather substantial check here for you.

And I said, For what?

Disaster money.

I said, I don't have any disaster. I have already received my money back from the insurance company for my claim.

So why are we paying this twice? It seems to me if we have our growers putting money into an insurance pool, if all of them are involved in that and we focus our efforts toward that, you have money to pay the claims without this *ad hoc* disaster thing which seems to keep popping up.

Mr. WALZ. Mr. Roach.

Mr. ROACH. Crop insurance in California is the only safety net available. There are no direct payments or countercyclical or loan deficiency. But we don't even have 85 percent coverage available in California either on crop insurance. Still looking for improvements, I would say push towards 85 percent revenue coverage for all producers, regardless of what type of crops that they have.

Mr. DEAL. May I make a comment, Congressman.

Mr. WALZ. Yes. I'm sorry to run over.

Mr. DEAL. I would give the same answer I gave in 1978. The courage has to come from you in Congress to eliminate the *ad hoc* disaster program.

Mr. FRERICHS. Mr. Walz, as a St. Olaf graduate, I appreciate the question. Built on a hill and run on a bluff, right.

Are there model aspects to there program? Absolutely. To use Chairman Boswell's terms, did RMA step too far, did USDA step too far in this agreement? Absolutely. That is the nature of the beast, though. We give and take, and we go back and forth. And, hopefully, over time, we have a successful partnership; and clearly that has been the case over the last 30+ years.

So, yes, there are aspects of this program. I am a firm believer in the private delivery of this program. I believe it results in competition. And, yes, it results in competition at the agent level, not at the farmer level.

We take what we are given from USDA in terms of rates. We cannot change them. That is unlike any other insurance program in the world, but that is the way this works. So, yes, there are aspects that are very, very successful, and there are awards, too. It is a process.

Mr. WALZ. Well, I appreciate all your candidness and help.

Thank you, Mr. Chairman.

The CHAIRMAN. Good discussion.

Mr. Schrader.

Mr. SCHRADER. Thank you, Mr. Chairman.

Mr. Rutledge, you indicate in your testimony some concern over changing business models as the SRAs renegotiated, why this wasn't phased in over time. I guess I would ask you why aren't the changes phased in over a period of time to allow the insurance companies to adjust their business models.

Mr. RUTLEDGE. Well, I expressed in my oral testimony that this would lead to fewer companies, fewer agents, *et cetera.* I think if it was phased in over a 2 year period, especially some of the changes in the Group 1 states, it might give companies more of a time frame to prepare for the changes. It might give them a few more opportunities to continue to stay in business.

Mr. SCHRADER. So why aren't the changes phased in, from your understanding.

Mr. RUTLEDGE. It was discussed during the negotiations with RMA, and it was initially viewed favorably. At the end of the day, they felt that, given the other changes—I can't speak for RMA, of course, but I think they just felt it wasn't needed, maybe. So I don't really have an answer for why it wasn't.

Mr. SCHRADER. Maybe Mr. Murphy will get to me later on that when he gets a chance.

Mr. FRERICHS. Congressman Schrader, $6 billion in savings, that was the target. If you phase it in, you don't hit it, simple as that.

Mr. SCHRADER. Very good.

Mr. Parkerson, you and others have indicated that the Milliman study is flawed in a number of areas in some of the assumptions made. Can you elaborate on that.

Mr. PARKERSON. Yes. We had in the process—first of all, I will say this and, quite candidly, RMA, Bill Murphy and his people, we had a respectful negotiation. But I truly believe that there was a number set, and we even asked this in this negotiation. There was a number set. They knew what they wanted, and we went about trying to answer those, but they got what they wanted.

And I will say that in some of the respects that were mentioned to the studies, we had asked for background information, we had asked for data and information and have not received exactly what we have asked for. We still were not able to run some of the models. Nor were we able to get the baseline that RMA used. And that would be key to fully understanding the cuts and the process.

Mr. SCHRADER. Okay, very good.

I guess the question to Ms. Fowler or anyone on the panel, my home State of Oregon, particularly western Oregon, doesn't really participate, at least to my knowledge, in a great degree to a lot of these programs. What is the rationale behind that? You pointed out the vegetative program is not going to be working. That is probably more the eastern side of my state.

Ms. FOWLER. It totally depends on the program in that particular area, depending on what the rates may be, the price elections, different things that are in your particular area.

Mr. SCHRADER. Why is the vegetative program not being picked up on in the——

Ms. FOWLER. Oh, I am sorry.

On the vegetative program, it is very difficult to understand the infrared data that comes; and, also, it appears there is somewhat of a lag time, and a lack of trust and understanding that program. There is just very little participation in that program. Much easier are the rainfall, the NOAA records. If it rains in your 12 x 12 grid, you are going to know.

Mr. SCHRADER. Mr. Frerichs, the testimony from Mr. Murphy indicated that the agents in "I" States are paid significantly higher than, say, Texas or some other states. Is there a reason that that should be the case? And I assume that is the reason the "I" States take a bigger hit, obviously, under the new SRA.

Mr. FRERICHS. Yes, there is a reason for that. The underwriting—the expected underwriting gains in the "I" States have traditionally been higher than other parts of the country.

Traditionally, when Iowa goes, it goes big, like the drought of 1988. But the frequency of it, even though it is very severe, the frequency of it is much lower than a state like Texas, or a state like North Dakota, or any of the states in the Great Plains where the risk of farming is greater. You have more frequent loss events and, therefore, more indemnity payments and, as a result, lower expected underwriting gains over time.

In theory, if the program—if all the crops were rated correctly, you would have equal expected underwriting gains, in theory. But it doesn't quite work out that way because once you take frequency into account—and this was one of the goals of the negotiation, was to take that under consideration, and we think that RMA did that but went a little bit too far. But once you start taking frequency into account, then your expected underwriting gains are not equal. And so the business in Iowa is expected to return more to an insurance company than, say, the business in Texas. Is that an equity issue? No, that is a Mother Nature issue.

Mr. SCHRADER. Very good.

Thank you. I yield back.

The CHAIRMAN. Thank you.

Mr. Pomeroy.

Mr. POMEROY. Thank you.

The CHAIRMAN. About 10 minutes to vote, so we are going to try to wrap up. I wouldn't want to cut you off.

Mr. POMEROY. What are you telling me, Mr. Chairman.

The CHAIRMAN. I am telling you I want to yield the gavel.

Mr. POMEROY. Okay. I got the message. Let me be quick.

I find this panel very interesting, and I am not surprised by the thrust of the comment. Adjustment in what we are paying our private partner to crop insurance has been changed significantly with this SRA renegotiation.

The reason for my remarks on the prior panel were to try to put into the record the very real threat to crop insurance posed by others in this Congress. This bill does not begin and end in this Committee room. We are part of the process. And so I believe that some adjustment had to be made.

As an old insurance commissioner, I can't understand how we don't weaken our arguments completely when we look at commissions paid over and above A&O expenses for example. It would seem to me that you, on the one hand, are having a threat to company solvency or, on the other hand, you are acknowledging that you are overpaying for the actuarial portion of the program; because companies can casually cut into it to pay agent commission for purposes of bidding for a given agent for purposes of expanding market share.

When confronted with those arguments by GAO and the oversight committee—these are tough questions. So my own opinion is companies shouldn't pay more than A&O; and, if they are, something is wrong with that.

Mr. Deal, your long time experience in the program might be helpful on offering some perspective on that question. Is it ever justified for a company to pay more than 100 percent of A&O on agent commission.

Mr. DEAL. I think the issue gets back to what is the true amount that is needed for service. I don't argue that the amount that they are doing is right. I think a study has to be done to really define the service that the companies are rendering and the service that the agents are rendering, and that there is ample compensation for that.

You are right. The publicity out in the company is not good on the path of some of these agents. It isn't kept quiet. It is in the community.

So I agree with you. The new SRA gives good discipline to the issues that you are talking about. I think the study will determine what the numbers are and what the numbers should be. I think the new SRA goes a long ways to squelching some of the negative terms you are hearing out there. And I grant you have a big job ahead of you, because there is much of Congress that does not look at whole agriculture as an expenditure and say maybe this ought to be. So I don't envy your job of moving ahead with this deficit that we have and where do you pull numbers from and how you do that. I mean, we are just a little piece of that.

Mr. POMEROY. On the cuts that were in the farm bill, many of them are related to timing of payments. Because you can gain basically a scoring window, and the Chairman put those in for purposes of protecting just as much of this program as he possibly could under what we were given.

Was there a $6 billion marching order, Mr. Parkerson? I think that is an important point. I asked it in the privacy of my office of RMA. Did OMB give you a figure? And they have told me no.

And I see Keith Collins in the audience. We remember when he was here as head of FCIC.

And we know that there had been a number given from the Office of Management and Budget, and it was wrong. That is not what this SRA was ever supposed to be about. They indicated this is a bottom-up process looking at program review. Believe it or not, but that is the information they told me. And I actually don't believe this one came from the Office of Management and Budget.

Relative to the role played by agents—so I don't want to just sound like I am not sympathetic to what is going on out there—the products are more complicated than ever before and more essential to the survival of the family farm than ever before. I believe it reflects the success of the program. But, on the other hand, there is a good bit of work.

I call our insurance agents risk counselors. Because, basically, they help understand where is the exposure, how do we protect it. And we have to be cognizant there is an awful lot of terrific work done in the delivery of the product by our private-sector partners. It comes around and around. Maybe we just ought to deliver this product in the FSA office. I have heard it many times during my years in Congress.

Clearly, the product is much more complicated than can be competently delivered, in my opinion, in a crammed session of an already overworked FSA office, supported by bad computers. If we are going to rely on private-sector partners, we have to treat them fairly.

I cannot conclude that the ultimate result of the SRA is an unfair result. It is a dramatic result. You have not convinced me it is an unfair result in light of the external pressures of the program that could have produced much more horrific results.

I have found what you said very interesting and understand where you are coming from.

Thank you. I yield back, Mr. Chairman.

The CHAIRMAN. Thank you very much.

That concludes our—we have had a very good discussion. I say this to my Ranking Member and the rest of the panel. It was a good discussion. I think we are going to have to have more. So, Mr. Murphy, Mr. Moran and I have decided we want to invite you up for a visit. We will do that, and we hope it will happen soon. So our schedulers will work on that.

With that, I would like to recognize Mr. Moran for any closing comments he might want to make.

Mr. MORAN. Mr. Chairman, thank you very much for the hearing you conducted today.

I appreciate the witnesses. I look forward to having additional conversations with the witnesses, the people they represent, as well as Mr. Murphy at the Risk Management Agency.

The only thing that I would add is that Mr. Frerichs has indicated at some point in time maybe we ought to look at the process and the outline by which the SRA renegotiations proceed, with the desire of making certain that there are better checks and balances than maybe exist today.

And Mr. Pomeroy's comment, in my view, somehow we have to get the OMB out of this, where the goal of SRA negotiations is not

some set dollar amount of savings. Because that then drives the process as compared to a lot of other factors that are very important. So I look forward to working with you and others to see that we reach that in the long term.

The CHAIRMAN. I certainly concur with your comments, and we will do that. We are all in this for the same reason. We want to make this safety net as good as we can make it and available and affordable, and that is our common goal.

So, with that, under the rules of the Committee, the record of today's hearing will remain open for 10 calendar days to receive additional material and supplements, as well as written responses from the witnesses to any questions posed by Members.

This hearing is about to adjourn. I would like to thank every one of you for taking the time. Thank you very much for coming and spending this time and sharing your concerns, your expertise. And I also want to thank Administrator Murphy for the time you spent with us today. I think this has been a good hearing. I appreciate it, and we will continue to work together. Thank you very much.

[Whereupon, at 11:50 a.m., the Subcommittee was adjourned.]

[Material submitted for inclusion in the record follows:]

SUBMITTED QUESTIONS

Questions Submitted by Hon. Leonard L. Boswell, a Representative in Congress from Iowa??

Response from William J. "Bill" Murphy, Administrator, Risk Management Agency, U.S. Department of Agriculture

Question 1. You mention in your testimony that RMA plans to provide a performance-based discount, or refund, as part of the savings from the SRA. What is the plan for providing this discount?

Answer. The Federal Crop Insurance Act contains a provision that allows for a performance-based discount to be provided to a producer who has good insurance or production experience relative to other producers of that agricultural commodity in the same area. RMA is currently evaluating producer experience and developing a program that places emphasis on longevity of program participation and overall good demonstrated loss experience within the Federal Crop Insurance Program. While many details are currently being worked out, RMA plans to provide some preliminary information on this program in the near future with the goal of implementing the program later this year.

Question 2. Please explain the rationale behind the insertion of the covenant not to sue into the final draft.

Answer. The new SRA requires the companies to covenant against bringing legal action against RMA regarding the A&O subsidy structure, and to include such a covenant in agent contracts. This provision was included in the new SRA because of potential legal challenges by companies and other parties if any changes were made to the A&O subsidy structure. In particular, Congress included two separate provisions regarding how A&O can be established in the Federal Crop Insurance Act (Act) and there was honest disagreement over which provision had precedence.

To ward off potential legal challenges, in the third draft of the SRA RMA elected to include an economic disincentive to sue but it did not prohibit such suits. Companies argued that this provision might have been too broad and too severe. On reflection, RMA agreed. The companies offered, as an alternative, a draft of the covenant not to sue. Such covenants are not uncommon in the private sector when parties wish to resolve the dispute and complete the negotiation of a deal. Because the situation was similar here, RMA was not opposed to using the covenant not to sue to resolve its dispute with the companies.

With respect to the application of the covenant not to sue to the agents, RMA had a legitimate concern that while the companies had agreed to include a covenant not to sue, they could still negate the agreed-to financial provisions in the SRA by encouraging their agents to sue. Although agents do not sign the SRA, they are included in the definition of "affiliate" in the SRA, which is mentioned at least 20 times, not including the Appendices. Further, their function in the crop insurance program is to act on behalf of the companies. As representatives of the companies, the agents are regulated to the same extent as the companies. Therefore, agents are not truly independent entities with respect to the crop insurance program and, as representatives of the companies, they should be bound by the same terms and conditions that bind the companies, including the covenant not to sue.

Question 3. USDA has indicated that funds saved as part of the SRA negotiations would be used to meet OMB's Administrative PAYGO requirements that the costs of expanding crop insurance pilot programs be offset by cuts in other programs/provisions.

Isn't it true that under the Crop Insurance Act, FCIC has the statutory authority to implement new crop insurance programs (including expanding pilot programs) without the need to find additional funding as long as the programs fit within the statutory cost framework? In other words, aren't OMB's Administrative PAYGO requirements to offset program costs internal Administration requirements that are not required by law?

Answer. Currently the annual appropriation provides "such sums as are necessary" for the administration and delivery of FCIC's programs, provided the FCIC does so within the statutory authorization and funding provided by the Federal Crop Insurance Act. The Administrative PAYGO requirement is an initiative to incorporate fiscal discipline into administrative decisions that increase mandatory spending. Yes, FCIC has the statutory authority to implement new crop insurance programs or expand pilot programs. The Administrative PAYGO requirements are not statutory, but guidance, which are incorporated in section 31.3 OMB Circular. A–11, Preparation and Submission and Execution of the Budget. When FCIC is directed in statute to implement a new program or pilot, it does so without regard to Administrative PAYGO. However, under its general statutory authority, it is at

FCIC's discretion to implement new programs and pilots, when they are not expressly directed to carry them out in statute. The cost of implementing new programs is a reason FCIC may not exercise its discretion to implement such new programs. FCIC previously considered cost before the Administrative PAYGO requirements were in place when deciding to implement new programs. Administrative PAYGO only formalizes having to consider cost when deciding to implement new programs where the spending is mandatory, and FCIC is compliant with these requirements.

Question 3a. Did FCIC expand pilot programs before OMB introduced its internal, Administrative PAYGO requirements in 2005? How many crop insurance pilot programs have been expanded since Administrative PAYGO was introduced in 2005?

Answer. Yes, prior to the Administrative PAYGO requirements, FCIC expanded pilot programs either by adding new or additional counties within a pilot program, or by expanding various features or coverage to provide additional benefits and risk protection. As noted before, however, cost was always a consideration when deciding to approve new or expansion of programs. RMA expanded the Sugar Beet Stage Removal Option pilot program, and expanded the Forage Seed pilot program while also converting it to a permanent program.

Question 3b. What pilot programs has FCIC wanted to expand but was prevented from doing so because it could not find the Administrative PAYGO offsets that OMB required?

Answer. To date, RMA has not been prevented from expanding any program under the Administrative PAYGO requirements. Funding has been available for all pilot program expansions including for the Pasture, Rangeland, and Forage pilot program, which was recently funded and expanded for the 2011 crop year.

Question 4. How do you address the concerns raised about the Milliman study on the companies' rate of return on equity, specifically the time horizon used and the fact that the model did not take into account actual firm equity and crop insurance requirements for equity?

Answer. Regarding the time horizon used in the Milliman study, the Data Acceptance System (DAS) used by RMA to monitor policy-level crop insurance data was established in 1989. The time period analyzed by Milliman encompasses the entire DAS data set currently available at RMA. Although a longer historical time period may have been desirable, the Milliman analysis reflects the longest historical data set of all Approved Insurance Providers (AIP) the profitability studies currently have available. Indeed, the study sponsored by the crop insurance industry and conducted by Grant Thornton, LLP (Grant Thornton), examines data only back to 1992. Milliman acknowledged in its report that surveying only 20 years limits the conclusions one may draw as to the likelihood of potential catastrophic events. To fully consider this possibility, it performed a hypothetical analysis in which the 20 year span includes a second "disaster" year, similar to that of 1993 in place of an average year. The result of this hypothetical exercise is an average historical rate of return which still exceeds the reasonable rate of return by 2.3 percent. Regarding firm equity assumptions, Milliman correctly observes that for a multi-line insurer, policyholder surplus is shared by all lines of insurance written by the company. Consequently, being able to attribute any portion of the surplus to a particular line of insurance is complicated and requires a method for allocating the surplus across lines of insurance. Despite the difficulty, one must consider allocations of surplus to specific lines of insurance to solve an extensive range of financial and regulatory problems common to the insurance industry. Milliman employs the National Association of Insurance Commissioners (NAIC)-sanctioned method for allocating surplus across lines. Milliman finds that investment earnings from policyholder surplus are a significant element of AIP profitability. Properly accounting for these earnings is not possible without a credible surplus allocation method. Milliman assumes that investments earned from policyholder surplus are the same rate for crop insurance as for other property and casualty (P&C) lines of the company. Investment earnings are an important contributor to the profits of all insurance companies, including those of crop insurance companies. However, the two major sources of investment earnings—(a) operations and (b) policyholder surplus—should be treated differently between crop insurance and other lines. Milliman recognizes that crop insurance companies do not collect premiums upfront for investment prior to claims being paid, as with other lines. The resulting assumption by Milliman is that the companies do not earn any investment income from operations. On the other hand, crop insurance inherently shares investment earnings from policyholder surplus with the company's other insurance lines. Milliman uses the guidance provided by the NAIC for allocating policyholder surplus across lines of insurance to properly attribute these investment earnings to AIPs.

Question 5. Where is RMA at with regard to the study of agent business costs?

Answer. The Government Accountability Office study GAO–09–445 "CROP INSURANCE: Opportunities Exist to Reduce the Costs of Administering the Program" recommended that RMA conduct an evaluation of the costs of program delivery. RMA is committed to contracting for such a study. However, the 2008 Farm Bill authorized RMA and the companies to negotiate a new SRA effective for the 2011 reinsurance year, which began July 1, 2010. Given this deadline, it was not possible for a contracted study of program delivery costs to be completed in a timely manner to be relevant for the negotiation. RMA will now begin an effort to contract for a study of program delivery costs that would provide meaningful and timely information and analysis for future negotiations of the SRA. We anticipate that a Statement of Work will be completed in the fall of 2010, such that the Agency can begin to solicit proposals from outside parties to conduct the evaluation.

Question 6. The Adjusted Gross Revenue (AGR) insurance product has not been very successful in attracting farmer interest, despite the fact that farmers with diversified production enterprises have long wanted an option that works for them. It has also been a struggle for organic farmers to find crop insurance options that work for them, especially in light of higher premium charges on the front end and payouts at the conventional price at the back end if there has been a significant loss. Is the Department giving any consideration to improving AGR coverage or to fixing problems with insurance for organic producers as part of its strategy on using the portion of the $2 billion designated for RMA program improvement? If so, could you share with the Committee the contours of the options being discussed? If not, why not?

Answer. RMA understands and appreciates the need for a product that will cover the multitude of specialty and organic crops that do not have conventional crop insurance programs. Both of the AGR programs insure all commodities on the farm on a whole farm basis. These two programs rely heavily on historic, farm, tax forms for underwriting purposes.

For 2010, only 410 farms nationwide are insured with the AGR product and 540 farms, nationwide, are insured with AGR-Lite. Organic producers are covered under both AGR products.

The AGR products have not been widely popular. This is primarily due to the complexity of accounting, records, and reporting necessary to convert tax information into an insurance guarantee and to account for a multitude of commodities under one policy.

At this time, the AGR products continue to be the only risk management product available for some commodities. RMA is currently evaluating the effectiveness and future of the AGR and AGR-Lite plans of insurance to determine if the potential exists for improving these products, or better specifying the target market best suited for these products to work most effectively for producers. However, the AGR program is not one of the initiatives currently being considered under the $2 billion designated for RMA improvements. RMA continues to move forward in improving crop insurance coverage for organic producers so they will have viable and effective risk management options like many of the conventional crop programs. Consistent with the 2008 Farm Bill, RMA contracted for research into whether or not sufficient data exists upon which RMA could determine a price election for organic crops, and if such data exists, to develop a pricing methodology using that data. Also included in the contract was research into the underwriting, risk, and loss experience of organic crops as compared with the same crops produced in the same counties during the same crop years using nonorganic methods. Three reports have been completed from this study, and RMA plans to make them available in the near future.

RMA intends to establish dedicated price elections for organic crops that are supported by data and sound economic pricing principles. The first of these organic price elections may become available for the 2011 crop year. In addition, RMA will continue to capitalize on improved data collection and sharing of organic production and price data occurring throughout USDA, an initiative to better leverage the resources of all of our agencies to address this important segment of agriculture.

Question 7. Concerns have been expressed about the impact of RMA's current policy of allowing producers to transfer their current Actual Production History or APH to new lands that they may acquire. These concerns range from assigning blame for breaking out grass and pastureland for crop production to causing an increase in cash rental rates and making it harder for beginning farmers to compete with established producers who have better APHs. Can you explain how the APH transfer provision works? And do you think it is exacerbating either of these two situations, increasing cash rents or incentivizing the breaking out of new land?

Answer. Producers customarily add land to their farming operations and RMA procedure allows producers to use the average of their approved APH yields for a crop/practice/type on land newly added to their operation (commonly referred to as added land), if certain criteria are met. This allows producers to use their production history to establish the approved APH yield instead of using the county transitional yield (T-Yield) on newly added land. However, if the land being added exceeds RMA's established acreage limitation of 640 acres, a review by the RMA Regional Office is required or the approved yield for the land being added is limited to the county T-Yield. If the land being added exceeds 2000 acres, the approved yield for the added land is limited to the county T-Yield. Generally, APH yields cannot be transferred to a different person unless both parties share in the production of the crop for the current crop year, or when a farming operation is transferred and the transferee assisted in the establishment of the approved APH yields. The Basic Provisions stipulate acreage that has not been planted and harvested or insured in at least one of the three previous crop years is generally uninsurable unless a written agreement is authorized by RMA. For a written agreement to be approved for newly broken land, the crop planted on the recently broken acreage must be appraised by the approved insurance provider to yield 90 percent or greater of the approved yield used to determine the production guarantee provided by the written agreement. The approved yield for these written agreements for newly broken land are generally a percentage of the county established T-Yield for the crop with approximately 70 percent of these written agreements providing a production guarantee per acre equal to, or less than the county T-Yield. Additionally, over the last nine years, acreage with these written agreements had an average loss ratio of about half compared to the same crops, producers, and counties for acreage that was not subject to a need for a written agreement. The restrictions of the production guarantee to be based generally on a percentage of the county T-Yield and other requirements placed on newly broken land to obtain crop insurance on such land minimizes any incentive crop insurance may have to break out new land for a profit.

Question 8. Given the tremendous interest in revenue products for many different enterprises, how can we get more revenue protection for producers through the approval process at USDA? What are your constraints with regard to the pricing information necessary to have a viable revenue product?

Answer. Section 522(e)(4) of the Federal Crop Insurance Act (Act) prohibits the Federal Crop Insurance Corporation (FCIC) from conducting research and development for any new policy for an agricultural commodity offered under the Act. Many new insurance programs are developed and submitted by private entities to the FCIC Board of Directors (Board) for approval under section 508(h) of the Act. If the Board determines that the product is actuarially appropriate, follows sound insurance principles and is in the best interests of producers and taxpayers, it will be approved for sale. RMA also contracts for certain development efforts, and Board approval is generally consistent with that of privately submitted products.

Regarding constraints on pricing information, data utilized in establishing prices for revenue products must be credible, reliable and consistently available, as with all insurance products. In addition, data must be available to project a price and to calculate an actual price at harvest, and generally must be from independent sources or collected in a way that does not allow undue influence or manipulation that could cause program vulnerabilities.

Existing revenue products for the major commodities utilize the futures market to establish the projected and harvest prices. The futures market provides extensive historical prices that are appropriate to use in evaluating price risk and in establishing projected and harvest prices. In the absence of data from the futures market, there are often very limited sources of data that can be obtained in a manner that provides independent, unbiased results that will accurately reflect market expectations that producers can rely upon. Research into potential sources of price data for new revenue products have to be conducted on an individual crop basis to assure a consistent and reliable source of data and methodology can be established.

Questions Submitted by Hon. K. Michael Conaway, a Representative in Congress from Texas

Question 1. The Federal Crop Insurance Corporation Board of Directors approved a Cottonseed Pilot Endorsement program in 2009. It was the hope of many producers that the program would be implemented for the 2010 crop year; unfortunately it was not. Can you update the Subcommittee on the status of this program and when it will be implemented?

Answer. RMA intends to release the Cottonseed Pilot Endorsement program for sale to producers beginning with the 2011 crop year.

Question 2. I have heard from many producers who utilized the Group Risk Income Protection or GRIP. This year GRIP was discontinued for many crops in many counties across the country. Why was this program discontinued and since it was a very popular program, what is RMA doing to possibly reinstate or revamp the program?

Answer. The Group Risk Plan (GRP) and Group Risk Income Protection (GRIP) plans of insurance utilize information collected and reported by the National Agricultural Statistics Service (NASS) county estimates program. NASS implemented modifications to their publication standards that requires estimates for a given crop be supported by at least 30 reports where the respondent reported both harvested acreage and yield, or production from respondent reported yields must account for a minimum of 25 percent of the current year's production estimate for that county or district. Implementation of these standards has increased the reliability of NASS' published county level estimates, but has resulted in fewer publishable county estimates.

Although RMA has used county estimates provided by NASS that have not met NASS' publication criteria, doing so requires RMA to rely on information not generally available to the public. There have been two appeals in which the NAD. Director found against RMA in their review. The director of NAD held that RMA acted inconsistently with applicable regulations and calculating GRIP indemnity payments. 7 C.F.R. section 407.9 specifically provides that payment yield (which is the same as the final county yield) is the official estimated yield *published* by NASS. Thus, the applicable regulation, section 407.9, and the GRIP Coverage Insurance policy, require RMA to rely on *published* NASS figures, specifically the *published* NASS figure for the payment yield (or final county yield). In addition, as the result of an extensive program review, NASS has determined that in some cases they will no longer produce county estimates for a given crop and/or state, or cropping practice within a state. In order to ensure that the GRP/GRIP programs, especially the determination of the final county yields upon which indemnities are based, operate in a manner transparent to all affected policyholders, RMA reviewed the eligibility of all GRP/GRIP corn, grain sorghum, cotton, and peanuts county programs.

RMA considered several criteria in its review. These criteria include whether the most recent Census of Agriculture shows at least 50 farms in the counties producing the crop. In addition, concentration of acreage within the county, again based on the most recent *Census of Agriculture* (*http://www.agcensus.usda.gov/*), must score less than 1,000 on the Herfindahl-Hirschman Index, a measure of the concentration of acreage that assures that no single producer, or small group of producers, can unduly affect the county average yield and create indemnity payments. There also must be at least 30 of the most recent consecutive years of published NASS data available for the crop so that there is a sufficient basis to establish credible premium rates.

RMA also considers a minimum 15,000 planted acres in each of the last 10 years to assess the likelihood of credible NASS county estimates being available on an ongoing basis. Recent significant shifts in planted acreage were also considered, as this can reflect changes in production practices that may not be accounted for in establishing the expected county yield, the basis of the insurance guarantee.

Finally, RMA considered where policies have been sold and the resulting insurance experience. A significant proportion of counties have had no GRP or GRIP business in the last few years. The review resulted in RMA removing 1,062 counties, 752 of which have had no policies earning premium for the 2009 crop year. For the 2010 crop year, RMA deleted 469 counties for corn (137 with policies earning premium); 350 counties for soybeans (146 with policies earning premium); 75 counties for cotton (16 counties with policies earning premium); 125 counties for grain sorghum (11 with policies earning premium) and 43 counties for peanuts, none of which had policies earning premium.

RMA is in the process of reviewing information available for the GRP/GRIP programs for the 2011 crop year to evaluate counties where the program was deleted and whether any new information warrants reconsideration, and if any additional deletions are warranted.

Question 3. Obviously we all are very concerned about the baseline implications of the recently signed SRA. Of the $2 billion that you are reinvesting do you have a complete list of programs that those monies will be used for that you could share with the Subcommittee?

Answer. The savings from the SRA will be used to offset the cost of expanding several programs administered by RMA and FSA. With regard to those programs administered by RMA, savings from the SRA has already been used to offset the cost of expanding insurance coverage for pasture, rangeland, and forage (PRF) in the states of Colorado, Idaho, North Dakota, Texas, Oklahoma, Oregon, Pennsyl-

vania, South Dakota, Georgia, Utah, Florida, California, New Mexico, Arizona, and New York. PRF coverage will be expanded to Minnesota, Arkansas, and Nevada in subsequent years.

The SRA savings will also offset the cost of providing a performance-based premium refund to those growers with exceptionally good loss experience. The SRA savings will also allow the potential expansion of crop insurance coverage to strawberries, forage seeding, sugarbeets, pistachios, honeybees, aquaculture, poultry, and crops grown exclusively for bioenergy. Finally, a portion of the SRA savings will be used to offset the cost of revising or expanding the availability of current crop insurance products.

With regard to those programs administered by FSA, a portion of the SRA savings will be used to improve and enhance the availability of the Conservation Reserve Program (CRP) and the Conservation Reserve Enhancement Program (CREP).

Question 3a. Cotton is a very important crop in my district. It is my understanding that the cotton industry has contacted you about using some of these savings for programs such as redesigning the quality loss adjustment for cotton. This would come at a nominal cost and RMA has agreed in principle with the new program. Can you ensure me that RMA will carefully review this request?

Answer. RMA has been in discussions with the cotton industry regarding potential changes and improvements to the cotton quality loss adjustment provisions. Progress has been made but additional detailed information is likely needed to fully implement all desired changes. RMA is actively working with the appropriate USDA agencies to obtain the needed data. While there may be some administrative funding issues among the agencies, RMA is working to address or resolve those issues.

Questions Submitted by Hon. Jim Marshall, a Representative in Congress from Georgia

Question 1. How much money is budgeted annually for RMA to take acreage reports?

Answer. Insureds provide acreage reports to their agents, who in turn provide the reports to their companies. The acceptance and processing of acreage reports is a key aspect of servicing Federal crop insurance policies, and FCIC pays the companies an Administrative and Operating (A&O) subsidy to perform such required services.

Question 2. How can USDA refine the acreage reporting process so it will meet all the agencies' needs within USDA and eliminate the need for producers to make duplicate reports within USDA?

Answer. In July, USDA formed the Acreage/Crop Reporting Streamlining Initiative (ACRSI) as a joint effort between its offices for program administration and information technology to coordinate an effort with the vision to "have a common USDA framework for producer commodity reporting in support of USDA programs". The project intends to establish common USDA producer commodity reporting standards to meet the needs of the agencies that require the data in the administration of their programs, contribute to the elimination of duplication of information collection, and simplify producer reporting. The project looks to expand on the success of the Comprehensive Information Management System which compiles common producer, program, and land information collected by FSA, RMA, and approved insurance providers. The project has also engaged the precision agriculture industry in an effort to collaborate on establishing standards to enable producers to use these systems to meet USDA program requirements. USDA is committed to seeking greater efficiency and effectiveness in the administration of its programs through the use of technology and better in-house coordinated efforts among its various agencies.

Question 3. Would a separation of duties between selling insurance and processing claims inject more integrity into the crop insurance program and assure greater responsibility in the use of tax dollars?

Answer. Under the SRA's Conflict of Interest Provisions, sales agents and their relatives are prohibited from being involved in loss adjustment activities in the county or an adjoining county where the sales functions are performed. In addition, loss adjusters are not permitted to adjust losses for individuals with whom they have a business, financial or legal relationship, or for relatives. All agents and loss adjusters must submit annual Conflict of Interest disclosures to their companies which allows the companies to conduct mandatory and discretionary reviews to identify any activities prohibited under the SRA's Conflict of Interest provisions. Therefore, such separation of duty is already mandated.

Question 4. In response to a provision in the 2008 Farm Bill, RMA made several recommendations regarding pecans in its recent Report to Congress. As we wait to see how RMA intends to act on the report's finding, I would like RMA's comments

on the possible benefits of implementing the following changes for the 2011 crop cycle:

Changing the current 10 year history RMA uses in determining pecan coverage to 6 years.

Answer. This recommendation was put forth for perennial crops for which alternate bearing and downward trending yield adjustments are applicable. The pecan revenue policy is a 2 year coverage module, which negates the need for alternate bearing yield adjustments. RMA is evaluating the feasibility of using a shorter base period. However, this will require a legislative change and the use of a shorter base period may expose pecan producers to more variable insurance guarantees in any given year.

Question 4a. Allowing growers to obtain insurance once trees in a new grove produce 600 pounds or more of pecans rather than waiting 12 years prior to obtaining insurance on a new grove.

Answer. The current 12 year growing season requirement is an eligibility requirement before pecan acreage is insurable. RMA plans to propose removing the 12 year growing season requirement and to make pecan acreage insurable once a certain level of production is met. The production levels may vary from one region to another. Any change to the eligibility requirements must go through the regulatory process subject to public comment.

Question 4b. Establishing a 60 percent "catastrophic cup," which will ensure that producers will not have to report less than 60 percent of their actual production history average for the purposes of calculating losses.

Answer. The 60 percent "catastrophic cup" mentioned by Mr. Marshall is in regards to the yield substitution generally available to crops insured under the APH plan of insurance that provides individual yield coverage. Under APH, when the producer's recorded or appraised yield for the commodity was less than 60 percent of the applicable T-yield, the producer can exclude and replace such yield with a yield equal to 60 percent of the applicable T-yield. The Pecan Revenue policy is not under the APH plan of insurance. However, RMA is currently evaluating the feasibility of providing a similar adjustment for pecans.

Question 4c. Allowing growers to increase their covered acres by up to 25 percent with no production history rather than restrict it to 12.5 percent of their current coverage.

Answer. RMA requires approved average revenue per acre to be recalculated when a producer's acreage increases by more than 12.5 percent to ensure the correct revenue guarantee is established. Allowing producers to keep the same average revenue per acre when the insured acreage is increased by more than 12.5 percent may create program vulnerabilities. RMA has no plans to change this requirement.

Question 4d. Allowing growers to insure groves by farm number rather than their county average.

Answer. Currently producers can insure their acreage by enterprise or basic units. It has been requested that producers be allowed to insure optional units by farm serial number. RMA will review this optional unit recommendation as we work on revisions to the Pecan Revenue Policy. Any change to unit structure would likely require an adjustment in premium rates and must go through the regulatory process subject to public comment.

Question 4e. Raising the maximum production dollars per acre for growers from $1,350 to $1,800 per irrigated acre when determining premium payments.

Answer. Under RMA's current rating methodology for pecans, all pecan producers with an approved average revenue per acre of $1,350 or greater pay the same premium rate. RMA is researching alternative rating methodologies for calculating premium rates for pecans. One method under consideration is very similar to the methodology used for the APH plan of insurance. Under this rating methodology, each pecan producer's premium rate would be based on their own specific approved average revenue per acre and its relationship to the applicable county average revenue per acre. Producers with approved average revenues greater than the applicable county revenue per acre would have premium rates lower than the county average premium rate. In essence, the greater the individual pecan producer's approved average revenue per acre in relation to county average revenue per acre the lower the individual's premium rate. And, the lower the individual pecan producer's approved average revenue per acre is in relation to the country average revenue per acre the higher the individual's premium rate will be.

Based on its preliminary findings, RMA believes this rating methodology may provide more fair and equitable premium rates to pecan producers. However, RMA

must complete additional producer impact analyses before reaching a final decision. Any potential rate changes would not likely be applicable until the 2012 crop year.