

Promoting Conservation Within the Federal Crop Insurance Program

Reforming highly subsidized program to deliver environmental and taxpayer benefits

Taxpayers are expected to spend nearly \$10 billion annually over the next decade on the Federal Crop Insurance Program. As evidenced by past legislative and administrative reform efforts, the highly subsidized program is well-positioned for reform – particularly to *promote* effective agricultural conservation instead of *discouraging* the adoption of risk-reducing, cost-saving practices. Ample opportunities exist to better assist producers in increasing resilience to financial and production challenges, in addition to better preparing for future climate risks.

While some conservation strings were added to crop insurance subsidy eligibility in the past, the program was not designed to promote conservation practices – such as cover crops, no-till, and grassed buffers – that reduce the risk of crop losses, sequester carbon, provide other environmental benefits, and ultimately improve farmers’ bottom lines.

Since crop insurance subsidies are tied to planted acreage, researchers have linked crop insurance to the destruction of carbon-rich wetlands and native grasslands – the opposite of what is needed to combat climate change and improve water quality. Without reforms, federal crop insurance will continue to promote risky planting decisions at taxpayer expense. Instead, the program should help reduce the risk of crop losses rather than deploying payments when crop losses occur. Producers should be rewarded for implementing best management practices that improve long-term resilience of their land and better prepare for inevitable future droughts and floods, which ultimately save taxpayer dollars through lower indemnities. This can be accomplished by removing barriers to increased adoption of conservation practices known to reduce risk, in addition to engaging crop insurance companies in efforts to aid producers aiming to increase their resilience.

As both Republican and Democratic Administrations have acknowledged, crop insurance reform is direly needed. Past budget requests under both Presidents Obama and Trump identified several tens of billions of dollars in crop insurance and farm subsidy reforms. Unfortunately, the most recent Fiscal Year 2022 budget request from President Biden found \$0 in proposed savings. Previous budget requests recommended bringing high crop insurance industry rate of returns in line with other industries, reducing administrative and operating (A&O) subsidies for crop insurance companies that total approximately \$1.5 billionⁱ annually, reducing premium subsidy levels, and other common-sense reforms. Crop insurance premium rates should be updated to reflect real risks on the ground, in addition to future climate risks. Furthermore, risk sharing agreements that dictate the share of losses that taxpayers cover versus private insurance companies should be updated to ensure taxpayers are not shouldering undue risk, particularly during years of severe drought and floods.

Total government payments to agriculture, in addition to the cost of crop insurance, reached record levels in 2020 due to the COVID-19 pandemic, remnants of the Trump trade bailout, and the cost of ad-hoc disaster aid.ⁱⁱ Recent farm bills shied away from ad-hoc disaster aid in favor of taxpayer-subsidized crop insurance, but disaster aid costs have risen in recent years, and the costs of climate change are expected to further increase over time. As policymakers negotiate ways to reduce climate risks and sequester carbon, reforming crop insurance risk rating and sharing should be a tool to promote resilience in agriculture through the adoption of cost-saving conservation measures. These reforms can

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contribute to a more cost-effective, accountable, and transparent farm safety net that is responsive to true need instead of increased dependence on federal subsidies.

Background: What is Crop Insurance?

Crop insurance is a highly subsidized federal program touted as the cornerstone of the farm financial safety net. It includes three distinct pots of taxpayer subsidies:

Premium subsidies: Federal taxpayers are expected to spend approximately \$7-8 billion annuallyⁱⁱⁱ over the next decade reducing the purchase price of crop insurance policies. These premium subsidies are paid directly to companies, reducing out-of-pocket costs to farm businesses. On average, for every \$10 of insurance premium, taxpayers foot the bill for \$6. Both yield and revenue policies are available, meaning farmers can purchase policies that cover crop losses or revenue losses (the latter paying out for a loss of crop or price declines, or a combination of the two).

- **Administrative and operating (A&O) subsidies:** Approximately \$1.5 billion^{iv} is spent each year to cover the costs of private crop insurance companies (and agents) that sell policies and process claims.
- **Underwriting gains or losses:** Most responsibility for loss claims in excess of premiums is borne by the federal government. Taxpayers disproportionately cover more losses in years of severe drought or flooding, such as the 2012 drought when indemnities totaled \$17 billion and the loss ratio was 1.57, meaning producers received significantly more in indemnities than premiums paid (not to mention taxpayers' portion of premium subsidies as well).^v In FY20, underwriting gains for taxpayers totaled \$1.2 billion, but in certain years – such as 2011 – companies received underwriting gains while taxpayers experienced underwriting losses.^{vi}

Because of the way crop insurance revenue subsidies are structured, many farmers plant crops in the spring knowing they will be guaranteed a profit at harvest time – thanks to taxpayers. Farmers admit this reality themselves:

“This is the first time since probably 2012 that, with our guarantees, we’re going to the field with a profit locked in for next fall” – South Dakota farmer Chad Schooley ([Quoted in AgWeek May 10, 2021](#))

Crop Insurance’s Impact on Land, Climate, and the Environment

Because crop insurance subsidies are tied to current planted acreage, the more acres a farmer plants, the more subsidies he or she is eligible for. Thus, farmers can receive subsidies to plant on former grassland or pastureland that was recently plowed (in states outside the Prairie Pothole Region), former tree-lined or grassed buffers near waterways, and other carbon-rich, environmentally sensitive land. While certain minimum conservation accountability standards were added to crop insurance eligibility in the 2014 farm bill, standards have not been implemented consistently or effectively in practice from state to state or county to county.^{vii}

For these reasons, researchers found that crop insurance subsidies can lead to farmers making riskier planting and production decisions at taxpayer expense. Planting crops on marginal land—those that are highly erodible, subject to frequent flooding, or with naturally low nutrients—ultimately leads to more

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taxpayer costs as these acres are more prone to crop failure. Crop insurance subsidies also lead to more acres being in production than would otherwise be planted without taxpayers bearing the risk of crop losses on these acres. This leads to increased climate, water, economic, and other risks as sensitive land is plowed under to plant more commodity crops. Specifically, researchers have identified the following links between the availability of crop insurance subsidies and impacts on land, water, climate, and the environment:

- **Subsidies influence planting decisions:** Unlike commodity subsidies which are generally based on historic acreage levels, crop insurance subsidies increase as more acres are planted. A Goodwin et al. (2004) study^{viii} estimated that one additional acre enrolled in crop insurance brought an extra 0.09-0.6 acres into agricultural production. Depending on crop type, researchers have estimated that up to three percent of this cropland expansion occurs on land eligible for or currently enrolled in the Conservation Reserve Program (CRP), a land set-aside conservation program, with negative impacts on wildlife habitat, water quality, etc.
- **More plantings on marginal land:** Cambridge researchers found that “[c]rop insurance subsidies lower the out-of-pocket expense of insurance relative to potential losses, making environmentally sensitive cropland more attractive for planting insurable crops” and warned that the federal “government may be effectively competing with itself over sensitive cropland by sponsoring conflicting interests.”^{ix}
- **Increase in soil erosion and nitrogen pollution:** The Cambridge study also found that a one percent increase in crop insurance use can “increase soil erosion by nearly 20,000 tons, nitrogen loss by over 72,000 lbs, and phosphorus loss by about 16,000 lbs. per year nationwide.”^x Nitrogen runoff from increased fertilizer use is associated with water pollution in agricultural growing areas, leading to health problems in rural communities, hypoxia and a dead zone in the Gulf of Mexico each year, the loss of wildlife habitat, and other negative impacts.

Farmers planting crops in riskier growing areas – such as dry areas of Texas, Oklahoma, and much of the Dakotas – disproportionately receive more benefits from federally subsidized crop insurance. In these states, farmers routinely receive \$2-5 back for every \$1 paid into crop insurance whereas in Corn Belt states like Iowa, Illinois, and Indiana, the annual ratio is closer to one (or negative), meaning crop insurance in these states is more actuarial sound.^{xi} In riskier areas, taxpayers not only end up subsidizing outright risk up front, plus the environmental degradation tied to farmers frequently planting on new, risky land, but when disasters ultimately hit, taxpayers are on the hook for a greater portion of losses, as compared to crop insurance companies bearing their fair share of risk. To make matters worse, in recent years, additional ad-hoc disaster aid has been layered on top of these indemnities, without strings attached or any policies to promote future resilience or reduced dependence on federal farm programs.

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Payments per/\$ of farm business premium 2016-2020

Nebraska	\$0.84	Arkansas	\$4.53
Illinois	\$0.88	Georgia	\$3.43
Iowa	\$0.98	Texas	\$3.42
Indiana	\$1.01	South Dakota	\$2.54
Kansas	\$1.05	North Dakota	\$2.29

Crop Insurance as a Tool for Conservation Adoption

While crop insurance has a history of spurring the loss of sensitive land, harming the environment, and being a barrier to the uptake of conservation through the use of cover crops in particular, the program is also uniquely positioned to promote climate, water, and economic resilience for farmers. Currently, the federal crop insurance program does not provide incentives for producers to reduce risk of crop loss through the uptake of smart, cost-saving conservation practices. The U.S. Department of Agriculture (USDA) recently announced \$5 per acre payments to producers who planted cover crops, as part of a post-COVID-19 economic package. However, this announcement was not authorized by Congress nor part of the farm bill which normally authorizes changes to crop insurance and other farm subsidy programs, meaning it would have to be extended through legislation to be continued.

Because crop insurance does not incentivize the uptake of risk-reducing conservation practices, neighboring farmers can employ drastically different agricultural practices but receive the same crop insurance subsidies. For instance, one farmer can utilize cover crops, no-till, grassed buffers, terraces, and other conservation measures – leading to better water quality, less soil erosion, and more carbon sequestration – but a neighboring farmer may use none of these. Crop insurance treats them the same, providing the same level of subsidies regardless of the use of risk-reducing practices to mitigate against financial downturns, climate-related disasters, and other challenges.

Several studies have documented the link between long-term use of agricultural conservation practices and better resilience and lower risk of crop losses, which lead to lower taxpayer costs and other measurable benefits. Examples include:

- **Reduced drought risk:** A USDA Economic Research Service (ERS) report found that conservation practices – such as “retirement of sensitive lands, investment in technology that improves irrigation efficiency, and adoption of tillage practices that conserve soil moisture” - reduce the risk of crop loss due to drought.^{xii}
- **Lower long-run costs for farmers:** While conservation practices can take time to provide financial benefits, conservation measures – such as cover crops and no-till - have been documented to lower costs for fertilizer, labor, and fuel and equipment costs, leading to more resilient yields – particularly in years of severe drought and floods.^{xiii}
- **Less government spending:** Several studies have linked cover crops, practices leading to increased soil carbon, and the use of no-till to lower insurance indemnities in crop insurance, which results in lower taxpayer costs and ultimately better financial resilience for farmers as they can better manage their own risk in the face of climate, water, and other challenges^{xiv}.

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Recommended Reforms

To better incorporate cost-saving, risk-reducing conservation practices into the federal crop insurance program, policymakers must reform the highly subsidized program. First, perverse underlying subsidies must be eliminated – particularly those that provide taxpayer subsidies for farmers planting on risky land without the use of smart conservation practices. Only then can other reforms lead to real, lasting climate, water, and economic resilience.

Overall Reforms to Reduce Undue Risk for Taxpayers, Agricultural Producers, and the Environment

- **Covering yield – instead of revenue – losses:** Taxpayers should not be in the business of guaranteeing business profits for farming or any other businesses. Therefore, subsidies for crop revenue insurance policies should be eliminated, and crop insurance should instead focus on helping farmers recover from deep, systemic losses due to severe drought, for instance, that are otherwise not covered by private insurance. Producers would still have skin in the game, but taxpayers would subsidize a lower percentage of risk, leading to producers making decisions that reflect real risks facing their pocketbooks, land, and futures.
- **Other common sense crop insurance reforms implemented at a minimum:** At a minimum, policymakers should implement the plethora of reforms that have been recommended in recent budget requests and legislative proposals to scale back the riskiest and costliest portions of the federal crop insurance program. Reforms such as means testing, subsidy limitations, lower premium subsidies, have routinely gained bipartisan support.
- **Elimination of subsidies on unsuitable land:** Rep. Blumenauer’s bill^{xv} to reform farm bill programs, leading to better climate and environmental outcomes, recommends eliminating crop insurance subsidies for planting on unsuitable land. Farmers can rather take on this risk at their own expense through private insurance policies. Crop insurance should help promote resilience instead of reducing the ability of producers’ land to be able to withstand future floods and droughts, for instance. Some safeguards were built into crop insurance – specifically native grassland protections and conservation compliance provisions – but these have not led to the level of conservation that is needed to improve resilience in the long-run.
- **Elimination of subsidies for separating fields into separate units to maximize insurance payouts:** Currently, farmers can receive more subsidies to separate out high- and low- risk land for insurance purposes (through optional units, for instance), leading to greater taxpayer-subsidized payouts. Subsidies for these should be eliminated, in addition to those for other high-risk policies.

Risk Rating Reforms and Better Integrating Conservation within Crop Insurance

The federal crop insurance program can better integrate cost-saving, risk-reducing conservation practices and reform crop insurance program risk ratings to align premiums with current risks farmers face on the ground, in addition to future risks from climate change, for instance. Specific recommended reforms include the following:

- **Incorporating the latest climate and other risks into crop insurance premiums:** Crop insurance should be comprehensively reformed to incorporate current and future risks – including climate

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risks – into premium rates. A USDA-ERS report recommends options such as adding a “drought risk factor” through an Environmental Benefits Indicator (EBI) adjustment, and other recommendations include better integration of soil health data to improve the accuracy of insurance rates.^{xvi} USDA has begun studying the risks of climate change within crop insurance, but this should be expanded to include how conservation practices reduce risk and improve resilience in the face of future disasters.

- **Risk Management Agency’s (RMA) good farming practices:** The Government Accountability Office’s (GAO) recent high-risk report recommended that USDA better account for climate risks within the federal crop insurance program, in addition to better integrating conservation – beyond the recent addition of cover crops - within RMA’s list of good farming practices.^{xvii}
- **Promoting the use of conservation practices through minimum level of conservation and lower premiums:** A minimum level of conservation should be required in exchange for taxpayer subsidies in any farm safety net program – including crop insurance. These provisions should be effectively implemented and verified by third parties such as local conservation districts, local USDA offices, or university extension agents so crop insurance can become more accountable to taxpayers. Implementing a second tier of best management practices could qualify farmers for reduced crop insurance premiums,^{xviii} after actuarial data is compiled and analyzed, which would better align conservation with crop insurance instead of the two working at odds with one another. As recommended by Jonathan Coppess of the University of Illinois, farmers could alternatively receive higher premium subsidy rates for better use of risk-reducing conservation practices such as cover crops.^{xix} Private crop insurance companies must have skin in the game and help promote risk-reducing conservation practices.
- **Prioritization:** USDA has begun the process of announcing additional incentives for climate-smart practices within CRP. This model could be expanded to crop insurance and other farm bill programs to prioritize federal funding toward programs and practices that deliver the best return on taxpayer investment.

Crop Insurance Risk Sharing Reforms

While more attention has been paid to better integrating conservation within crop insurance and better aligning premium rates to reflect true risks, crop insurance companies also have a role to play in ensuring the federal crop insurance program promotes resilience instead of dependence on Washington. A few reforms to this end – for an industry that is unlike car, homeowners, or other insurance - include the following:

- **Allow crop insurance companies to bear more risk:** Currently, taxpayers bear a disproportionate share of risk and costs during years of severe disasters in particular. Allowing the federal government to renegotiate the Standard Reinsurance Agreement (SRA) to reform the share of underwriting gains/losses borne by taxpayers versus crop insurance companies should be a top priority in the next farm bill. Bringing crop insurance industry returns in line with other industries should also be a priority, or else the industry stands to benefit at taxpayer expense with little accountability or preparation for future risks to the program, as identified by GAO. Past renegotiations of SRAs have led to better risk sharing, in addition to taxpayer savings, and this should be continued regularly in the future.

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- **Allow private crop insurance and other risk management tools to thrive:** Promoting the use of private risk management tools and private insurance will involve first eliminating overly generous taxpayer subsidies in the federal crop insurance program. Other reforms in the commodity title of the farm bill will also be necessary to eliminate subsidies that promote the plantings of certain subsidy-eligible crops over others. Ultimately allowing private risk management tools to thrive, alongside a thinned down, actuarial sound crop insurance program that only kicks in during true times of need instead of guaranteeing profits, will lead to better economic, environmental, and climate resilience in the future.

Conclusion

Last year, government payments to agriculture reached a record high of \$47 billion. The federal crop insurance program added another \$9.4 billion to taxpayer spending on agriculture in FY20.^{xx} With this record spending came no new strings attached or resilience measures to enable farmers and ranchers to better prepare for the next economic downturn or natural disaster. Instead of continuing the status quo with crop insurance providing barriers to conservation adoption, the program should be reformed to promote cost-saving, risk-reducing conservation practices that ultimately improve farmers' bottom lines and better prepare agriculture for the next inevitable disaster. The program should also ensure that taxpayers are not shouldering undue risk, particularly during years of severe droughts or flooding, and that private crop insurance companies cover a greater share of losses to bring the program in line with other industries.

With a drought creeping into the Corn Belt^{xxi} from the West and climate challenges front and center in Washington, policymakers should ensure that any future infrastructure, energy, climate, agriculture, and other spending does not work at cross purposes with other federal programs in the way that conservation programs and crop insurance have done in the past. Crop insurance can help solve climate, environmental, and other challenges by promoting carbon sequestration, soil retention, water quality benefits, etc. but significant reforms are necessary to achieve these goals. Simply throwing more money at crop insurance, conservation, carbon banks, or other programs – without reforms - will fail to achieve climate and environmental solutions while wasting taxpayer dollars. Conservation practices should be rewarded through lower premiums and other measures to incentivize adoption of measures that reduce risk, promote resilience, and improve farmers' bottom lines.

Federal farm policy – crop insurance included - should lead to a more cost-effective, transparent, and accountable safety net that is responsive to real need. Federal policies should promote – instead of inhibit – the adoption of smart conservation practices. The current crop insurance program is currently doing more harm than good by subsidizing risky production practices at taxpayer expense, but common sense reforms - including better accounting for risk-reducing conservation practices - can lead to better resilience for producers, the environment, and taxpayers alike.

ⁱ <https://www.cbo.gov/system/files/2021-02/51317-2021-02-usda.pdf>

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ⁱⁱⁱ <https://www.cbo.gov/system/files/2021-02/51317-2021-02-usda.pdf>

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