



Have and Have-Nots in Federal Crop Insurance

Federally subsidized crop insurance has become the largest taxpayer support for agriculture. But not all parts of the agriculture industry share in the benefits from this Washington-based program. Subsidies for crop insurance disproportionately benefit growers of a small number of crops. In addition, many small scale, niche, and diversified producers have low participation rates or few options under federal crop insurance.

Both the Senate and House farm bills, S. 3240 and H.R. 6083, include programs to increase Washington's role in managing the market risks faced by agricultural businesses. Yet neither bill reforms crop insurance into a more efficient, equitable, and fiscally sound program. In fact, both bills propose expanding subsidized crop insurance by mandating development of new insurance policies and creating new programs to cover smaller losses not currently covered by crop insurance. As Congress debates a new farm bill in the long shadow of a \$16 trillion national debt, lawmakers should seize this opportunity to improve crop insurance and find savings in what is by far the most expensive and fastest growing part of the agricultural safety net.

Federal Crop Insurance

The federal crop insurance program, first created in 1938, was designed to help farmers get back on their feet after severe flooding or drought, while reducing the frequency and cost of *ad hoc* emergency aid bills coming out of Congress. But through changes made by Congress and the U.S. Department of Agriculture (USDA), the program has essentially morphed into a cash guarantee scheme for a select group of agricultural businesses. Crop insurance has now outgrown its original mandate to create a safety net for producers. With many crops experiencing record or near record prices, farm country is estimated to achieve a record \$122 billion profit in 2012¹, while taxpayers are hit with a record high price tag for the federal crop insurance program that could easily cost taxpayers more than \$20 billion in 2012 alone.

Unfortunately, making common-sense reforms to the farm subsidy maze is not easy. Opposition to reforming crop insurance has arisen from two special interests benefiting from billions in taxpayer subsidies. Special interest commodity groups including those representing corn, soybeans, wheat, and cotton (the "big four") are mobilizing in defense of lucrative subsidies that help producers lock in annual business income. In addition, crop insurance companies and agents seek to retain billions of dollars in subsidies for administrative expenses, underwriting gains, and sales commissions that are consistently higher than the industry average.

The "big four" crops got 80 percent of all crop insurance subsidies from 1995 to 2010.² Meanwhile, smaller, diversified, organic, livestock, and specialty crop producers do not substantially purchase crop insurance or receive pennies on the dollar compared to traditional beneficiaries. Separating the haves from the have-nots and identifying the should-nots - crops or producers that are already managing risk without government intervention and taxpayer subsidies - is important when trying to make common sense reforms to crop insurance.

Taking a Step Back

First, one should ask whether it is taxpayers' role to subsidize farmers' purchase of crop insurance in the first place. Before 1998, crop insurance premium subsidies cost taxpayers less than \$1 billion annually.³ Enrollment rates in the program were fairly low since subsidies were not overly generous, Congress provided regular disaster aid, and producers relied on other more financially advantageous ways of managing their business risk. The latter include such options as purchasing private crop insurance, utilizing crop diversification and economies of scale, adopting technological advances (often developed through publically financed research), hedging, forward-contracting, reducing input costs, and obtaining off-farm income. As Congress increased subsidy rates and

encouraged producers to select policies that insured revenue (expected price multiplied by expected harvest size) instead of simply insuring against a loss of crops, the total annual taxpayer cost for premium subsidies skyrocketed to \$7 billion today and the entire program cost will likely exceed \$20 billion this year.

Second, one should ask whether or not the private sector is already providing or, in the future, could provide crop insurance coverage to help producers manage their business risks. Taxpayers currently pay, on average, 62 percent of an individual producer's crop insurance premiums, creating a significant hurdle for development of a robust private crop insurance industry. In addition, despite the existence of a number of companies offering unsubsidized crop insurance policies for "shallow" losses not covered by federal crop insurance, the House and Senate Agriculture Committees are attempting to expand crop insurance to cover even modest dips in revenue.

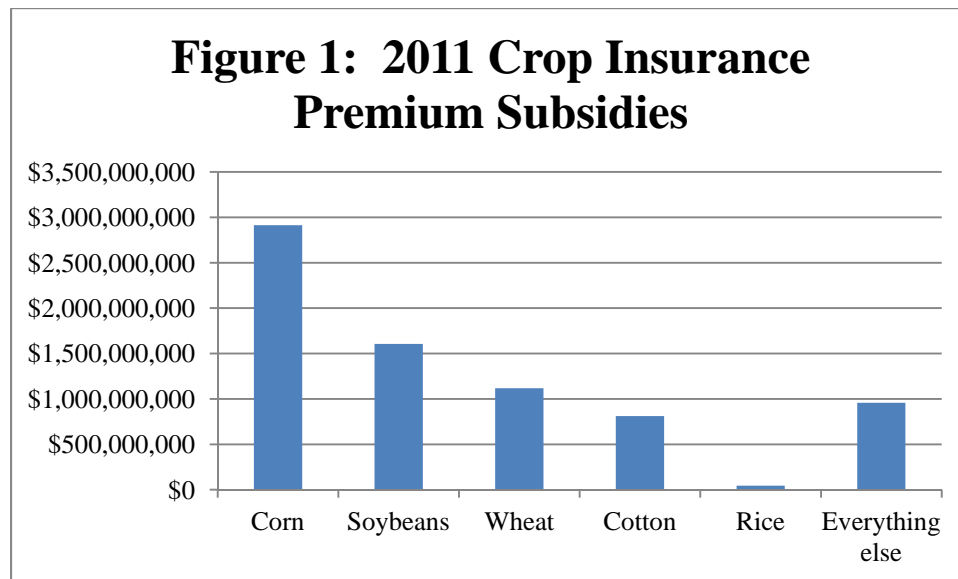
This leads to the final set of questions:

- (1) Which farmers or crops are benefiting from the current program and which are left out?
- (2) Which should receive taxpayer-subsidized crop insurance in the future?

The Haves, Have-Nots, and Should-Nots

The Haves

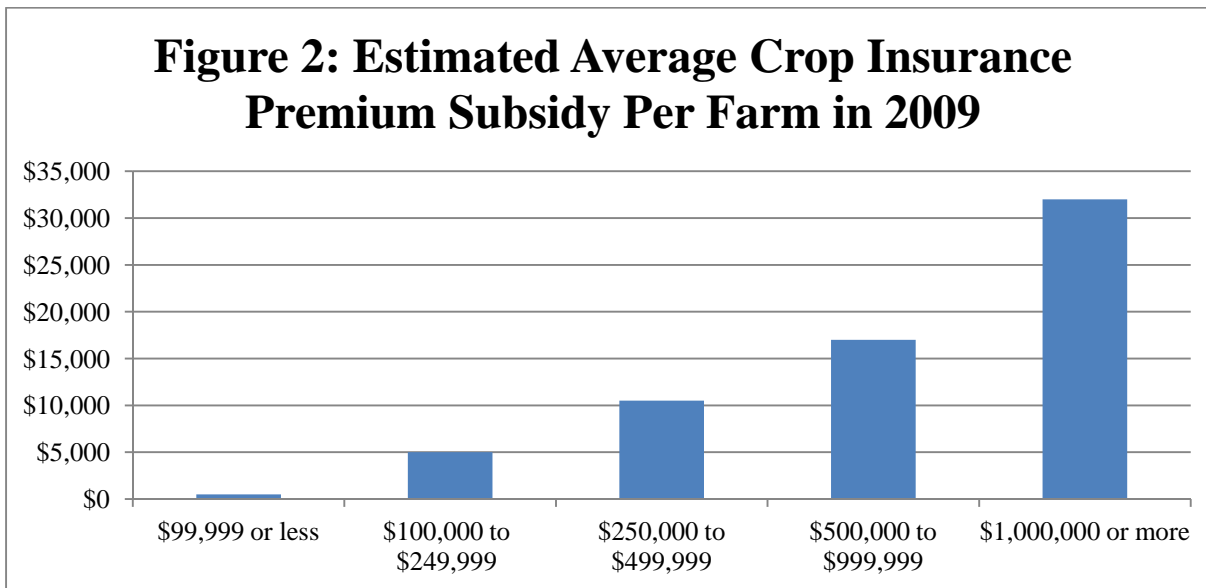
The federal crop insurance program does not treat all crops equally. Corn, soybeans, wheat, and cotton benefit the most, receiving 80 percent of all insurance premium subsidies over the past 15 years while representing just 30 percent of national commodity sales and 50 percent of cropland.^{4,5} Corn was the biggest winner, collecting \$13 billion in crop insurance subsidies from 1995 to 2010, or one out of every three taxpayer dollars in the program. Figure 1 shows this skewed distribution of crop insurance premium subsidies. In 2010, 86 percent of corn acres were covered by the federal program, and about 75 percent of all corn acres were enrolled in coverage levels above the 50 percent free catastrophic level.⁶ As the coverage level increases (up to 85 percent of income), so too does the overall cost to taxpayers.



Reference: USDA's Risk Management Agency⁷

In addition, insuring revenue (expected price multiplied by expected harvest size) as opposed to simply insuring against loss of crops increases taxpayer costs, especially since the cost of premiums are tied to the price of commodities, currently at or near record highs. By 2011, 83 percent of the total cost of premium subsidies went to policies guaranteeing revenue instead of protecting against loss of crops to natural disasters like floods or drought. Of these revenue policies, about 95 percent were for producers of the "big four" crops.

Since crop insurance subsidies increase with planted acreage, the larger the farm is, the greater the taxpayer cost. With no eligibility tests or limits on the amount of subsidies that can flow to any one farm, larger, wealthier producers reap the most subsidies and enroll the most acres (and greatest percentage of their acres) in crop insurance.⁸ As Figure 2 shows, farmers with \$1 million or more in annual sales received an average of \$35,000 in 2009 – just in crop insurance premium subsidies.^{9,10} This in spite of the fact large producers should be better able to manage their risks since their land is spread across a wider area, economies of scale can increase efficiencies and reduce input costs, and their access to capital is greater.



Reference: Congressional Research Service and USDA’s Economic Research Service^{11,12}

The Have-Nots

The “have-nots,” commodities with low participation rates or fewer options under federal crop insurance, include organic, small-scale, and specialty crop producers, as well as the major commodities rice, peanuts, and livestock. From 1995 to 2010, except for corn, soybeans, wheat, cotton, sorghum, nursery crops, and potatoes, no single crop received more than one percent of total premium subsidies even though more than 100 crops are covered by at least one subsidized crop insurance policy.^{13,14,15}

These “have-nots” in fact often could be characterized as “have-less” since they have access to subsidized crop insurance policies, but the policies are often less generous yield as opposed to revenue based policies. Of all 2011 revenue insurance policies, only 5 percent covered barley, canola, cherries, sorghum, rice, and sunflowers. All other crops like tomatoes, apples, and potatoes only use yield programs which cost taxpayers relatively less while still protecting producers from loss of crops.¹⁶ Today, about 75 percent of all specialty crop acres are covered by federal crop insurance.

The “have-nots” include small and beginning farmers who not only enroll fewer acres in federal crop insurance, but also compete with unlimited subsidies flowing to large landowners who bid up farm prices and drive out competition.¹⁷ As Representative Tim Walz (D-MN) noted at a House Agriculture Committee hearing, beginning farmers face administrative hurdles like not having historic yield records on newly purchased land.¹⁸ As a result, lower average county yields may be used in these farmers’ crop insurance policy calculations leading to lower yield guarantees. The 2012 farm bill drafts addressed this, while also reducing beginning farmers’ crop insurance premium costs by 10 percent.¹⁹

Organic producers are also largely left out of the current system and hence, enroll fewer acres in federal crop insurance. In 2011, only 25 percent of organic farmland was enrolled in subsidized crop insurance policies,

compared to about 80 percent of all other cropland.²⁰ Since most crop insurance policies use conventional prices when calculating payments, while charging organic producers a surcharge on their premiums, these farmers note that their crops are undervalued.²¹ Organic farmers also tend to grow a greater diversity of crops, self-insure, or purchase unsubsidized private insurance to manage risk.

The largest producers not receiving much in crop insurance subsidies are growers of rice, peanuts, and livestock. Yet the reasons for low crop insurance participation may be because crop insurance is not needed or because other taxpayer-paid programs crowd out crop insurance. Livestock producers have access to subsidized crop insurance policies such as Livestock Risk Protection (LRP), Livestock Gross Margin (LGM), Adjusted Gross Revenue (AGR), Rainfall Index, and Vegetation Index. However, fewer acres of hay and rangeland are covered by the latter two since they are less susceptible to yield losses.²² Additional crop insurance products that meet the needs of livestock producers have not been established in part because of governmental programs that protect livestock producers for free. For decades, ad-hoc disaster payments subsidized livestock losses due to natural disasters like drought. In the 2008 farm bill, Congress created four disaster programs to cover the following types of losses:

- **Livestock Forage Program:** pasture and grazing losses due to drought or fires
- **Livestock Indemnity Program:** livestock deaths caused by hurricanes, floods, blizzards, disease, wildfires, extreme heat, extreme cold
- **Emergency Assistance for Livestock, Honeybees, and Farm-raised Fish:** losses due to disease, adverse weather, feed and water shortages, or other conditions like blizzards or wildfires
- **Supplemental Revenue Assistance Payments (SURE):** provides subsidies for shallow losses not covered by crop insurance; calculated on a whole-farm basis instead of per-crop

Peanut and rice producers are also two of the biggest beneficiaries of the discredited Direct Payments program which makes payments to landowners regardless of need or whether or not they are even growing the crop being subsidized. By its nature, irrigated rice production is not subject to swings in yield. The greatest risks faced by rice producers are fluctuations in prices on the world market and, like any other business, increased costs for inputs and raw products (seed, energy, and labor). Since price discovery mechanisms do not exist for many crops, including peanuts, developing revenue policies is difficult.²³ Most crop insurance revenue products are based on the price the crop is garnering on a futures market. The bulk of peanuts are produced and sold through contractual agreements, not traded on the open-market, thus it's difficult to create revenue insurance products for peanuts.

Should-Nots: The Solution is Not More Subsidies

But just because the “big four” reap the most subsidies doesn't mean every crop needs a special program – especially if they are managing risk in other ways that cost taxpayers little or nothing. House and Senate Agriculture Committees have created new special-interest carve-outs like rice and catfish profit margin protection, peanut revenue insurance, and a cotton-only shallow loss program. If passed, they will further expand the government's role in managing individual farm business risks. Shallow loss programs, whether stand alone entitlement programs like Agriculture Risk Coverage (ARC), or add-ons to crop insurance, such as the Supplemental Coverage Option (SCO), are market- and trade-distorting entitlement programs that were created simply to add more layers onto an already overly generous suite of farm subsidies. They allow farm businesses to receive taxpayer checks if their income dips as little as 10 percent or even 5 percent below anticipated levels, not the original goal of crop insurance which was to only cover catastrophic losses that occur after widespread droughts or floods. In addition, proposals for extending crop insurance to potentially cover government-subsidized margin insurance for all crops should be a major red flag. Putting taxpayers on the hook for guaranteeing the profit margin of select businesses is a potentially costly and highly distorting practice that could have lasting negative consequences.

Unintended Consequences

In addition, several unintended consequences can result from providing unlimited subsidies to large producers growing just four main crops, including:

- Drain on the federal treasury,
- Less diverse crop rotations,
- Incentivized production on native grassland, pasture, wetlands, highly-erodible land, and others risky areas prone to drought or flooding, and^{24,25,26}
- More consolidation and hurdles for young and beginning farmers to overcome as land prices are bid up.

Conclusion

Farm businesses should use their own dollars to purchase private crop insurance or utilize other methods to protect against most yield and revenue risks. If the private market cannot adequately protect against widespread drought, flooding, or other severe losses, then a thoughtful level of taxpayer support should be considered for crops or producers who truly need the support. But expanding crop insurance to cover shallow losses that guarantee farm business income and transfer unnecessary risk to taxpayers should be rejected outright. As Congress debates a new five-year farm bill, reforms must be made so federal crop insurance does not continue to pick winners and losers while contributing to the ever mounting federal debt.

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¹ <http://www.ers.usda.gov/topics/farm-economy/farm-sector-income-finances/highlights-from-the-2012-farm-income-forecast.aspx>

² http://farm.ewg.org/cropinsurance.php?fips=00000&summpage=TC_BY_CROP&statename=

³ http://farm.ewg.org/cropinsurance.php?fips=00000&summpage=FP_BY_YEAR&statename=theUnitedStates

⁴ http://www.ers.usda.gov/Briefing/FarmIncome/Data/cr_t3.pdf

⁵ http://farm.ewg.org/cropinsurance.php?fips=00000&summpage=PS_BY_CROP&statename=

⁶ http://www.ers.usda.gov/Data/ARMS/app/default.aspx?survey_abb=CROP

⁷ <http://www.rma.usda.gov/data/sob.html>

⁸ <http://www.ers.usda.gov/Briefing/WellBeing/economicresilience.htm>

⁹ <http://www.nationalaglawcenter.org/assets/crs/R40532.pdf>

¹⁰ <http://www.ers.usda.gov/Briefing/WellBeing/economicresilience.htm>

¹¹ <http://www.nationalaglawcenter.org/assets/crs/R40532.pdf>

¹² <http://www.ers.usda.gov/Briefing/WellBeing/economicresilience.htm>

¹³ http://farm.ewg.org/cropinsurance.php?fips=00000&summpage=PS_BY_CROP&statename=

¹⁴ <http://www.rma.usda.gov/pubs/2011/decliningyields.pdf>

¹⁵ <http://www.rma.usda.gov/data/cropprograms.html>

¹⁶ <http://www3.rma.usda.gov/apps/sob/>

¹⁷ <http://www.gao.gov/assets/590/589305.pdf>

¹⁸ <http://sustainableagriculture.net/blog/house-commodities-hearing/>

¹⁹ <http://www.ag.senate.gov/issues/farm-bill>

²⁰ <http://www.rma.usda.gov/data/sob/organic/loss2011.pdf>

²¹ <http://www.mosesorganic.org/cropinsurance.html>

²² <http://www.rma.usda.gov/pubs/2010/specialtycrop.pdf>

²³ <http://www.rma.usda.gov/pubs/2010/specialtycrop.pdf>

²⁴ <http://ers.usda.gov/publications/err120/>

²⁵ <http://www.rma.usda.gov/data/indemnity/2011/42312map.pdf>

²⁶ http://www.ers.usda.gov/Data/ARMS/app/default.aspx?survey_abb=CROP#P6a5901646cbc4f0db12d3376d4c6fb75_45_66iT0R0T0R0x2