



Crop Insurance Professionals Association LLC.

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February 12, 2010

The Honorable Tom Vilsack
Secretary
U.S. Department of Agriculture
200-A Jamie L. Whitten Building
1400 Independence Avenue, SW
Washington, D.C. 20250

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 five 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 ten 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 one-third, 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 one-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 one-third, 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 ten years, there has been a significant increase in the quality of coverage for producers of many crops. In the next five 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 RFS-2 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 four 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 one 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 to 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 five or ten 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 one-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

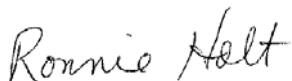
To ensure all America's farmers and ranchers have the risk management tools they need, to create and save jobs, and to spur economic growth in rural communities, the Administration should build upon Federal Crop Insurance's record of accomplishment since 2002.

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

The Honorable Tom Vilsack
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CC:

The Honorable James W. Miller
The Honorable William J. Murphy
The Honorable Blanche L. Lincoln
The Honorable Saxby Chambliss
The Honorable Collin C. Peterson
The Honorable Frank D. Lucas
Members of the Senate Committee on Agriculture, Nutrition, and Forestry
Members of the House Committee on Agriculture