REPORT OF THE
STATE CORPORATION COMMISSION'S
BUREAU OF INSURANCE ON

The Availability and Affordability of Diversification Crop Insurance

TO THE GOVERNOR AND
THE GENERAL ASSEMBLY OF VIRGINIA

HOUSE DOCUMENT NO. 21

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TO: The Honorable L. Douglas Wilder
Governor of Virginia
and
The General Assembly of Virginia

We are pleased to transmit this Report of the State Corporation Commission's Bureau of Insurance on The Availability and Affordability of Diversification Crop Insurance.

The study was initiated and the report prepared pursuant to House Joint Resolution 70 of the 1992 Session of the General Assembly of Virginia.

Respectfully submitted,

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EXECUTIVE SUMMARY

The State Corporation Commission's Bureau of Insurance (Bureau) was requested by the 1992 General Assembly, pursuant to House Joint Resolution No. 70, to study the availability and affordability of diversification crop insurance. The study resolution stated that increased knowledge of the availability and affordability of multiple peril crop insurance might assist farmers in obtaining this type of protection for their crops. The Bureau was asked to consider priv-te company policies reinsured by the Federal Crop Insurance Corporation (FCIC) as well as government policies sold directly through the FCIC. The Bureau sent surveys to the insurance companies that had premiums written in Virginia for multiple peril crop insurance during 1991. Surveys were also sent to the Federal Crop Insurance Corporation, the U.S. Agricultural Stabilization and Conservation Service (ASCS), the Virginia Department of Agriculture and Consumer Services, and several agents associations and crop insurance service organizations.

Multiple peril (multi-peril) crop insurance can be written directly through the FCIC or through policies which are written by private insurers and reinsured by the FCIC. Coverage under a multi-peril policy is generally written on an "all-risk" basis meaning that coverage is provided for all risks except those specifically excluded. Rates and coverages are the same whether directly insured or reinsured by the FCIC. However, rates and coverages vary by crop. Under the FCIC program, coverage is only available for certain crops in select counties. Insurance is not provided on any agricultural commodity in any county in which the income from the commodity constitutes an unimportant part of the total agricultural income of the county. The FCIC has specific guidelines to determine whether a crop may be insured under the program. These are as follows:

(1) Significant grower interest -- there must be an indication that producers are interested in growing the crop;

(2) Economic significance -- demonstration of the economic importance of the crop is required;

(3) Actuarial data sufficiency -- sufficient historical yield data must be available on the crop's production to determine adequate rates; and

(4) Acceptable risk profile -- this reduces the risk of the federal government bearing the costs for unavoidable crop failures.

The FCIC has recently created a research unit to study the expansion of the crop program to include more crops and counties under the program. Most of the companies that write multi-peril crop insurance in Virginia stated that they would be supportive of such an expansion if adequate premium volume were generated and adequate rates were charged to ensure the actuarial soundness of the program.

About half of the survey respondents indicated that the availability of multi-peril crop insurance would be improved if the federal program covered more crops. However, the ASCS reported that the availability of multi-peril coverage does not directly impact a farmer's decision to diversify since most diversification is done on a small scale. One respondent indicated that the affordability of coverage for additional crops insured or reinsured by the FCIC would depend on the rates developed for a particular county and crop. Others said affordability would not necessarily improve if new crops were added to the program.

The availability of multi-peril insurance coverage for crops which are currently insurable under the federal program does not appear to be a problem for farmers in Virginia. Most companies that write multi-peril crop insurance in Virginia indicated they insure all crops for which coverage is available under the federal program, and unless there is a history of payment problems, farmers are not refused coverage.

The affordability of coverage under the current FCIC program does not appear to be a problem either. The rates for crops covered under the FCIC program are subsidized by as much as 30 percent and are considered affordable by most growers according to the Virginia Department of Agriculture and Consumer Services.

According to the survey respondents, one of the biggest problems with the FCIC's insurance program appears to be the complexity of the administrative procedures involved in obtaining the insurance rather than the availability or affordability of the insurance. Another problem cited on the surveys was that many farmers are reluctant to participate in the program because disaster relief measures are often enacted by Congress on an ad hoc basis. It was also suggested that the program lacks accountability. A study conducted by the U.S. General Accounting Office (GAO) in 1991 stated that excessive losses were being paid which could lead to morale hazards (i.e., circumstances which increase the likelihood of loss due to indifference on the part of the insured). One survey respondent suggested that the program tends to encourage adverse selection because farmers with good loss experience often choose not to participate.

The Virginia Department of Agriculture and Consumer Services stated that the expansion of the FCIC crop insurance program would encourage greater crop diversification which, in turn, would improve the economy of Virginia. If the farmers of Virginia feel that, in order to encourage further crop diversification, the federal program should be expanded to provide coverage for crops not currently insured by the FCIC, a request should be made on their behalf by the Virginia Department of Agriculture and Consumer Services with the necessary data to support the need for program expansion.

The Commonwealth of Virginia may also wish to consider the possibility of establishing a state-funded program to subsidize farmers who purchase privately insured crop-hail policies for crops which cannot be insured by the FCIC. Such a program could be set up to promote crop diversification by providing a subsidy to farmers who grow crops which are considered important to the economy of Virginia.

GENERAL ASSEMBLY OF VIRGINIA--1992 SESSION

HOUSE JOINT RESOLUTION NO. 70

Requesting the Bureau of Insurance of the State Corporation Commission to examine the availability of insurance for diversification crops.

Agreed to by the House of Delegates, January 27, 1992
Agreed to by the Senate, March 4, 1992

WHEREAS, the A. L. Philpott Southside Economic Development Commission, through its Task Force on Agriculture, Forestry, and Natural Resources, has recognized that agriculture continues to play a vital role in the economic development of Southside Virginia and the entire Commonwealth; and

WHEREAS, while increased diversification efforts are necessary to ensure the continued survival and prosperity of farms throughout the Commonwealth, many farmers are reluctant to invest in diversification crops; and

WHEREAS, although many farmers now recognize multiple-peril crop insurance as a cost effective method of risk management, increased knowledge of the availability and affordability of these insurance packages might assist Virginia farmers in obtaining this protective tool; and

WHEREAS, although the Bureau of Insurance within the State Corporation Commission has no jurisdiction over rates for crop insurance, it is responsible for the administration of insurance laws pursuant to § 12.1-16 of the Code of Virginia; now, therefore, be it

RESOLVED by the House of Delegates, the Senate concurring, That the Bureau of Insurance of the State Corporation Commission is hereby requested to examine the availability and affordability of diversification crop insurance. The Commission shall include in its study consideration of private company policies reinsured by the Federal Crop Insurance Commission (FCIC) and government policies sold through the FCIC.

The Commission shall submit its findings and recommendations to the House Committee on Agriculture and the Senate Committee on Agriculture, Conservation and Natural Resources during the 1993 Session of the General Assembly.

INTRODUCTION

Legislative Request

The State Corporation Commission's Bureau of Insurance (Bureau) was requested by the 1992 General Assembly to study the availability and affordability of diversification crop insurance. This study was the result of House Joint Resolution No. 70 and was requested because many farmers are reluctant to invest in diversification crops even though diversification efforts are necessary to ensure the continued survival and prosperity of farms throughout Virginia. The study resolution stated that many farmers recognize multiple peril crop insurance as a cost effective method of risk management; however, increased knowledge of the availability and affordability of multiple peril crop insurance might assist farmers in obtaining this type of protection for their crops. The Bureau was asked to consider private company policies reinsured by the Federal Crop Insurance Corporation (FCIC) as well as government policies sold directly through the FCIC.

Methodology

The Bureau began its study by sending questionnaires to the insurance companies that had premiums written in Virginia for multiple peril crop insurance during 1991. Eight companies were surveyed. These are shown in descending order of premiums written:

NAME	PREMIUMS WRITTEN
Century Indemnity Company	$3,539,723
Empire Fire and Marine Insurance Company	1,353,705
Virginia Farm Bureau Mutual Insurance Company	727.281
International Business and Mercantile Reassurance	547,271
CIGNA Property and Casualty Insurance Company	265,946
John Deere Insurance Company	16,603
State Farm Fire and Casualty Company	1,528
Redland Insurance Company	1,489

Responses to the surveys were received by or on behalf of all companies except International Business and Mercantile Reassurance Company and John Deere Insurance Company. John Deere Insurance Company indicated that they do not write multiple peril crop insurance and that this information was reported incorrectly on the Virginia annual financial statement. National Ag Underwriters, Inc. responded as the managing general agent for Empire Fire and Marine Insurance Company. Rain and Hail Insurance Service, Inc. responded as the managing general agent for CIGNA Property and Casualty, Century Indemnity, State Farm Fire and Casualty, and Virginia Farm Bureau.

The Bureau also sent questionnaires to the following organizations to obtain additional information on the availability and affordability of multiple peril crop insurance:

(1) Federal Crop Insurance Corporation, U.S. Department of Agriculture;
(2) Agricultural Stabilization and Conservation Service, U.S. Department of Agriculture;
(3) Virginia Department of Agriculture and Consumer Services;
(4) National Crop Insurance Services;
(5) Crop Insurance Research Bureau;
(6) American Association of Crop Insurers;
(7) National Association of Crop Insurance Agents;
(8) Independent Insurance Agents of Virginia; and
(9) Professional Insurance Agents Association of Virginia and the District of Columbia, Inc.

Responses were received from all organizations except the National Crop Insurance Services, the American Association of Crop Insurers which no longer exists, the National Association of Crop Insurance Agents, and the Independent Insurance Agents of Virginia.

MAJOR FINDINGS

Role of the Federal Crop Insurance Corporation

One of the first objectives of the study was to determine the role of the federal government in (i) providing multiple peril crop insurance coverage on a direct basis and (ii) providing reinsurance coverage for multiple peril crop insurance policies sold through the private sector.

The federal government writes multiple peril (multi-peril) crop insurance through the Federal Crop Insurance Corporation (FCIC). The FCIC is a wholly government-owned corporation which offers protection for participating farmers against unavoidable causes of loss. All farmers are eligible to participate if an insurance program exists for a particular crop in their county. Multi-peril crop insurance generally provides coverage for drought, flood, hail, wind, frost, winterkill, lightning, fire, excessive rain, snow, wildlife, hurricane, tornado, insect infestation, and plant disease.[1] It is usually written on an "all-risk" basis, meaning that it will cover all risks except those specifically excluded under the policy. However, some crops (principally fruits and vegetables) are written on a "named perils" basis.

According to the questionnaire completed by the Insurance Services Division of the FCIC, the purpose of the FCIC is to promote the national welfare by improving the economic stability of agriculture through a sound system of crop insurance. The FCIC was created in 1938 (7 USC §1501) as a result of the severe droughts of the 1930s. The program was originally limited to one commodity, wheat.[2] Over the years the program grew and, in 1980, was amended under Public Law 96-365. The intent of the 1980 amendment was to make the private insurance sector the primary writer of multi-peril coverage with the federal government acting as reinsurer.[3]

The FCIC reinsures business written through the private sector under the terms of a standard reinsurance agreement. (Reinsurance is a type of insurance that insurers buy for their own protection.) Under the FCIC program, the reinsured companies

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1. William H. Rodda, et al., Commercial Property Risk Management and Insurance, Vol. II, (Malvern, PA: American Institute for Property and Liability Underwriters, 1983), p. 219.

2. Bernard L. Webb, "Reinsurance as a Social Tool," Issues in Insurance, Vol. I, Everett D. Randall, Editor (Malvern, PA: American Institute for Property and Liability Underwriters, 1987), p. 449.

3. Rodda, p. 219.

market and service multi-peril crop insurance policies and share a portion of the risk on those policies. The FCIC also contracts with private agency sales and service contractors (referred to as master marketers) who sell and service FCIC crop insurance but do not assume any risks on policies sold. In April of 1992, employees of the Agricultural Stabilization and Conservation Service (ASCS) of the U.S. Department of Agriculture were given the authority to begin selling and servicing multi-peril policies for the FCIC.

Objectives of the Federal Crop Insurance Corporation

As reported on its questionnaire, the FCIC's insurance program was considered experimental from 1938 to 1980. The program did not cover a substantial portion of agricultural production in the United States, and most relief to farmers was provided through disaster assistance payments and emergency loans. When Congress passed the 1980 legislation, a number of objectives were established for the program. They were as follows:

(1) increase farmer participation in the insurance program and abolish disaster payments;
(2) improve program efficiency by taking advantage of the private sector's expertise;
(3) operate within budget;
(4) provide federal subsidies to reduce costs for farmers;
(5) increase private sector involvement; and
(6) offer coverage for more commodities.

Another goal of the 1980 Act was to make the program operate on an actuarially sound basis. According to a report issued by the U.S. General Accounting Office (GAO), this legislative expectation has not been met as there have been large and consistent gaps between premiums received and losses and expenses incurred.[1] The GAO report pointed out that the FCIC is paying out excessive insurance indemnities and this can create morale hazards. As stated in the report, morale hazards occur when a farmer suffers a partial loss on a crop and does not try to prevent further loss because the insurance benefits outweigh any attempts to salvage and harvest the crop.[2] The FCIC lost $2.7 billion from 1983 to 1989 which translates into about $391 million annually. The report stated that a combination of increasing revenues from growers as well as lowering program expenses was needed to ensure actuarial soundness.[3]

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1. Crop Insurance: Inaccurate FCIC Price Forecasts Increase Program Costs (GAO/PEMD-92-4, December, 1991), p. 14.

2. Ibid., p. 3.

3. Ibid., p. 8.

Market Distribution

Over the past ten years, the portion of business written by the private sector has grown substantially. In fact, most multi-peril crop insurance business is now written by private insurers. The FCIC indicates that in Virginia, during 1991, premiums written directly through the FCIC accounted for five percent of the total book of business. During the same year, premiums written by private insurance companies and reinsured by the FCIC accounted for 95 percent of the total book of business. This compares with 1981 figures showing 99.9 percent of the premiums written directly by the FCIC and less than one percent written by the private sector. Although more business is being written by the private sector and being reinsured by the FCIC, the total book of multi-peril crop insurance business has decreased six percent over the past ten years.

Rates

The FCIC regulates the rates and the policy forms for all multi-peril crop insurance policies sold directly by or reinsured through the FCIC. The Bureau of Insurance also reviews and approves multi-peril policy forms used by private insurers in Virginia. Rates promulgated under the FCIC program are not required to be filed with the Bureau. Multi-peril crop insurance rates are subsidized by the federal government to encourage participation in the program. The rates as well as the amount of subsidy are the same for policies sold directly by or reinsured through the FCIC.

Most multi-peril policies guarantee a certain yield per acre for insured crops. (For some crops, the guarantee can be stated in a dollar amount per acre rather than a yield per acre.) If production on the insured acreage falls short of the guarantee, the policy pays the difference up to the dollar amount of coverage stated in the policy. Guarantees based on yield are calculated from average historical production, using the insured's records as well as yields that reflect the county average for any years the insured does not have records. This becomes the actual production history yield or APH yield. Each insured decides what percentage of the APH yield he wants his policy to guarantee. The options are 50 percent, 65 percent, and 75 percent. A 35 percent coverage level has recently been approved and will become available for the 1993 crop year.

The FCIC subsidizes up to 30 percent of the total premium for all policies, not to exceed the amount of subsidy calculated for the 65 percent coverage level. The following example was provided on the questionnaire completed by the Insurance Services Division of the FCIC:

Yield Per Acre:	100 bushels
Price Election:	$1.00 per bushel
Insured Acreage:	100 acres

Amount of Insurance	
75% coverage:	$7500
65% coverage:	$6500
50% coverage:	$5000

Premium Rates ($ per $100)	
75% coverage:	$10.00
65% coverage:	6.50
50% coverage:	4.70

Premium Cost ($)	
75% coverage:	$750.00
65% coverage:	$422.50
50% coverage:	$235.00

Amount of Subsidy ($)	
75% coverage (16.9%):	$126.75
65% coverage (30%):	$126.75
50% coverage (30%):	$ 70.50

As pointed out on the survey completed by the FCIC, the percentage of subsidy at the 75 percent coverage level is not constant since it depends on the premium rates at the 65 percent coverage level. In no event may the dollar amount of subsidy at the 75 percent coverage level exceed that of the 65 percent level.

In addition to the direct premium subsidy, an additional subsidy is given in the form of reimbursement to companies for their expenses. As a result, expense costs are not loaded into the rates paid by insureds.

Crops Covered Under the FCIC Program

The FCIC indicated on its questionnaire that not all crops are insurable in all counties. In Virginia, the following crops are insurable:

Insurable Crops	Number of Counties
apples	22
barley	99
corn, grain, & silage	99
cotton, upland	8
green peas	2
grain sorghum	81
oats	90
peaches	18
peanuts	10
potatoes	2
soybeans	80
sweet corn, processing	2
tobacco	51
tomatoes, fresh market	2
tomatoes, processing	2
wheat	99

When asked which crops in Virginia were excluded from coverage under the FCIC program, the following response was given on the questionnaire:

> No crops are specifically excluded, although the FCIC Act provides that the Board of Directors may limit or refuse insurance in any county or area, or on any farm, on the basis of the insurance risk involved. The Act further provides that insurance shall not be provided on any agricultural commodity in any county in which the Board determines that the income from such commodity constitutes an unimportant part of the total agricultural income of the county, except that insurance may be provided for producers on farms situated in a local producing area bordering on a county with a crop insurance program.

The FCIC also stated that a Crop Value Assessment had recently been completed. This assessment indicates, on a state-by-state basis, the economic value each crop contributes to the state. The following crops which are not currently covered under the FCIC program were assessed for Virginia:

Crop	Dollar Value
hay, other	$180,441,000
hay, alfalfa	64,960,000
nursery crops, other	10,480,000
sweet corn, fresh	1,683,000
sweet potatoes	960,998
rye	588,999
cottonseed	253,000
canola	128,000

When asked if there had been any requests by state agencies in Virginia or by the private sector to include under the FCIC program additional crops which are grown in Virginia, the FCIC indicated that requests had been received to expand the program to include the following crops but that the FCIC had not implemented programs for these crops:

broccoli
beans, green fresh
beans, green processing
cabbage
canola
cantaloupe
trees, Christmas
vegetables
watermelon

FCIC Guidelines

In order to determine whether a particular crop may be insured under the FCIC program, certain criteria must be met. The FCIC applies the following guidelines to evaluate crop expansion requests:

(1) Significant grower interest -- there must be an indication that producers are interested in growing the crop;

(2) Economic significance -- demonstration of the economic importance of the crop is required;

(3) Actuarial data sufficiency -- sufficient historical yield data must be available on the crop's production to determine adequate rates; and

(4) Acceptable risk profile -- this reduces the risk of the federal government bearing the costs for unavoidable crop failures.

To further explain the FCIC's position on program expansion, the following comment was given on the questionnaire:

> The strategy is to offer insurance on those crops that contribute the most to the economy of a county, so FCIC has the best chance possible of dedicating its scarce resources of people, money, and time to develop crop programs that will serve the broadest cross-section of farmers. In that process, the Crop Value Assessment... is used to place the crops on a priority scale.

Any state that wishes to make requests to include additional crops under the federal program can contact the FCIC's regional service office in Raleigh, North Carolina for more information. Requests should be directed to Mr. Larry Atkinson, Director, 4407 Bland Road, Suite 150, Raleigh, North Carolina 27609. Mr. Atkinson's telephone number is (919) 790-2990.

Role of the ASCS

In April of 1992, the Agricultural Stabilization and Conservation Service (ASCS) of the United States Department of Agriculture became involved in the marketing of multi-peril crop insurance for the FCIC. Marketing efforts conducted through the ASCS is strictly on behalf of the FCIC with no connection to the private sector. According to the questionnaire completed by the ASCS, the availability of multi-peril crop insurance depends on the companies operating in a particular area and the number of available agents. Since ASCS offices are located in over 2,800 counties throughout the country, the ASCS feels that crop insurance should become more readily available to farmers. Two ASCS employees in Virginia have been trained by the FCIC, but no policies have been sold to date. When asked if crop diversification was being hampered in Virginia because of farmers' inability to obtain multi-peril crop insurance either directly or indirectly through the FCIC, the following response was given:

> We do not believe the availability of crop insurance is much of a factor in a farmer's decision whether or not to attempt to grow different crops. Generally, crop insurance is available for the major crops grown on a large scale. Producers experimenting with other minor crops usually start on a smaller scale.

Role of the Private Sector

Rain and Hail Insurance Service, Inc. (RHIS), which is a managing general agent for crop insurance for four of the companies surveyed, indicated on the questionnaire that they insure under multi-peril policies all crops for which the FCIC offers a program in Virginia. When asked if there were any circumstances under which they would refuse to offer coverage, they stated they do not refuse to write multi-peril crop insurance for farmers in Virginia except for individuals who have unpaid, past due amounts from prior years. When asked if there would be a change on their part if the FCIC expanded its program to include crops not currently covered, they stated that they would write the additional crops covered under the program. They also indicated that they would be supportive of the FCIC developing programs to insure and reinsure more crops if the crops were of significant importance to agriculture and if adequate data were available to assure that a sound program could be established. They also stated that they support the FCIC's recent creation of a research unit to study systematically the expansion of the program to include new crops and counties.

National Ag Underwriters, Inc. (NAU), managing general agent for Empire Fire and Marine, indicated on the questionnaire that they insure under multi-peril policies all crops for which the FCIC offers a program in Virginia. When asked if there were any circumstances under which they would refuse to write coverage for farmers in Virginia, they gave the following reasons why coverage would not be offered:

(1) Debt owed to the FCIC, their company, or another company;
(2) Land not insurable;
(3) Crop has no approved program.

When asked if there would be any changes on their part if the FCIC expanded the program to include more crops, they stated that they would write coverage for the new crops. They also indicated that they would be in favor of the FCIC reinsuring more crops grown in Virginia if the premium volume warranted the expense involved.

Redland Insurance Company indicated on their questionnaire that 1991 was the first year they wrote multi-peril crop insurance in Virginia and that they only insured tobacco. The sole reason for refusing to write coverage, as noted on the survey, would be non-payment of previous years' premiums. When asked if there would be any change on their part if the FCIC expanded its program, they stated that they generally do not reject any applications for new crops. They also stated they would be in favor of the FCIC reinsuring more crops if the proper development of rates, forms, and rules were implemented.

In addition to RHIS completing a survey on behalf of Virginia Farm Bureau, the insurer sent in its own response and stated on the survey that, beginning with the 1992 crop year, they now market through RHIS. When asked which crops they insured under multi-peril policies, they listed the following:

corn
grain sorghum
soybeans
barley
wheat
tobacco
peanuts
cotton

The company survey stated that, even though they never refused a farmer, they did not write coverage on select crops because of the lack of manpower and expertise to service these crops. When asked what types of changes they would anticipate if the program were expanded to include more crops, they indicated there would not be many changes. They did indicate, however, that there would be more programs which do not meet needs and are not manageable. They also stated they would be in favor of the FCIC expanding its program to include more crops if an actuarially sound program could be developed for these crops at affordable rates.

Crop Insurance Research Bureau, which is an organization whose services include providing information on crop research and lobbying on behalf of its member insurers (two of which write business in Virginia), stated that expanding the FCIC's program would cause companies to spend more money in all areas of doing business, such as inspections, loss adjustments, and premium collections, and there would be no assurance of an increase in premiums written.

Impediments to Program Participation

According to a questionnaire completed on behalf of the Professional Insurance Agents Association of Virginia and the District of Columbia, Inc. (PIA), the only impediment to obtaining crop insurance through a master marketer or a private insurer would be the farmer's history of not paying premiums or some type of fraudulent activity. The respondent indicated that multi-peril crop insurance is generally available even to those with poor loss experience and that there is a non-standard classification system in place to limit guarantees if the loss history warrants such action.

There is a concern, however, that in an effort to reduce government spending and balance the federal budget, the FCIC program may be reduced in scope or eliminated altogether and replaced with legislative authority for an ad hoc disaster payment program. At a March, 1992 hearing of the House Committee on Agriculture, discussions focused on the problems of having both a crop insurance program and a disaster assistance program. Representative Ron Marlenee (R-MT) noted that the current insurance program is complex, burdensome, and expensive. Criticizing the amount and complexity of paperwork confronting farmers, he reminded the committee that promises had been made in the past to make the program affordable and available. Written testimony was also presented at the hearing explaining how farmers were being penalized because of inelastic bureaucratic regulations imposed by the FCIC. Regulations, such as those requiring growers to sign contracts committing them to purchasing protection prior to planting, were cited as being counterproductive and served to discourage participation in the program.

Other impediments exist as well. The response on the PIA survey indicated that farmers do not always keep adequate records to obtain coverage guarantees that justify the premium. Some feel that the guarantees are too low. In most cases, farmers obtain insurance for the highest cost crops and self-insure the others. It was also noted that some farmers believe that disaster payments will be always be available, thus discouraging participation in the insurance program.

Availability and Affordability of Multi-Peril Crop Insurance

When asked if the availability and affordability of multi-peril crop insurance would be improved if the FCIC reinsured more crops grown in Virginia, Rain and Hail Service, Inc. stated that availability would be improved but affordability would depend on the rate required to assure a sound program as well as a grower's willingness to pay for the coverage. National Ag Underwriters, Inc. said there would be no change in the availability or affordability of crop insurance. Virginia Farm Bureau responded to the question by stating that availability and affordability would not necessarily improve unless there were a sound basis to build a program and rates. Without this, programs would be implemented that do not meet farmers' needs and which cost too much. Redland Insurance Company indicated that since each crop would be rated on its own, only the availability would improve. A questionnaire completed by the Crop Insurance Research Bureau contained the following statement:

> We do not believe that availability or affordability would improve. The rule of insurance is the rule of large numbers--large numbers paying premiums to offset the losses of a few. With crop insurance, the rule is a few paying premium with a large percentage receiving

paid losses.

The PIA was asked if multi-peril crop insurance was generally affordable to farmers who wish to purchase it. Their response was as follows:

> In Virginia crop insurance rates have been reasonable. We enjoy quality producers [who] have had a good loss ratio and had little abuse of the crop insurance program. Rates do vary crop to crop and county to county. This appears reasonable considering that crops vary by region and crop quality varies by region.

When asked if their agents were aware of any complaints by Virginia farmers that crop diversification was being hampered because of the inability to obtain multi-peril insurance on certain crops, the PIA gave the following response:

> Some crops are not included in the program. This is due to either lack of interest or insufficient volume to establish an actuarially sound program of insurance. FCIC has set up a crop program based on the impact in a county--not state. There is an ongoing study to change this theory to set up a program if there is an economic impact on the state.

Suggested Changes

Each company questionnaire asked what changes could be made to the way crop insurance is marketed and underwritten to make it more available or affordable. Redland Insurance Company stated that several task forces were currently in place to recommend changes to the program.

Virginia Farm Bureau said the program needed more accountability from farmers to prove their losses because too many claims were being paid that should not be paid. The insurer also stated that even though the program had many good points, it involved too many steps to insure a crop which, in turn, caused good producers to avoid the program. Farm Bureau also suggested removing the politics from the program and requiring it to operate as a sound business. They also suggested that the program would work better if guarantees were stated in a dollar value per acre and financial records were used to support losses.

National Ag Underwriters, Inc. suggested that the state offer a premium subsidy or low cost reinsurance. Rain and Hail Service, Inc. also suggested that the state consider providing some amount of subsidy to farmers who purchase either multi-peril crop insurance or a privately developed supplemental or alternative multi-peril crop insurance coverage to supplement the amount of premium and administrative expense cost currently paid for by the federal government. They stated on the survey that their organization has developed some products that supplement the federal program or serve as alternatives to the federal program. Rain and Hail Service, Inc. also made the following comment:

> We believe the basic MPCI [multi-peril crop insurance] policy provides good basic coverage for most growers. This coverage can be enhanced by privately developed products for growers who need or want additional coverage, and, in some cases, MPCI look-alike private programs which are more attractive or available at less cost than the basic program. These products, since they are privately developed and underwritten, can meet needs that are not met by the basic program. However, due to the risks involved, companies must underwrite them very carefully. Availability of these types of products could be broader if catastrophe reinsurance capacity were available from the government. This would allow combining the best product development, marketing and servicing skills (private sector) with catastrophe capacity (government) to broaden farmers' risk management opportunities.

According to the survey response received from the PIA, the federal crop program is not bad, and in terms of peanut and tobacco production, it has been successful both from a participation level and from an actuarial standpoint. Most problems, they suggested, exist due to administrative procedures and politics rather than from coverages and rates.

The Crop Insurance Research Bureau stated that the program has become too complicated for most producers and that a more simplistic administrative approach is needed. They also mentioned that because rates are not favorable to the better farmers, adverse selection is built into the program. In addition, they pointed out that many farmers question the necessity of paying a premium when they can wait for Congress to pass a relief fund. They suggested developing a program which would meet the following objectives:

(1) Be actuarially sound;
(2) Collect premium deposits up front;
(3) Provide better loss adjustment; and
(4) Require more accountability of producers.

Complaints Received

The Consumer Services Section of the Bureau's Property and Casualty Division was questioned to determine whether any complaints had been filed with the Bureau regarding the availability or affordability of crop insurance. According to Bureau staff, no complaints have been filed by farmers in Virginia with regard to the availability and affordability of crop insurance.

The Virginia Department of Agriculture and Consumer Services was contacted to determine how many complaints their department has received from farmers in Virginia who are unable to obtain or cannot afford to purchase multi-peril crop insurance. They indicated they receive approximately three or four complaints a year and these are usually presented by associations or cooperatives. Therefore, they were unable to determine the total number of individual complaints received. When asked whether complaints have centered around coverage for certain crops, the department answered "yes, typically vegetable crops." Other complaints have centered around the way losses are calculated. When asked why farmers in Virginia do not carry multi-peril crop insurance, the department said that the majority of farmers who do not carry multi-peril crop insurance find that coverage is not obtainable for certain crops. They indicated that about 10 percent of the farmers who do not carry multi-peril insurance find that coverage is too expensive.

The Department of Agriculture and Consumer Services mentioned on the questionnaire that they had requested the FCIC to include vegetable crops under the multi-peril insurance program but that no changes in coverage had been made to date. The department also mentioned that increased crop diversification would be beneficial for Virginia's economy because it would "allow for opportunities for increased income for Virginia farmers." The lack of available and affordable crop insurance, they indicated, could be detrimental to increased production and could result in significant economic loss to Virginia.

Crop-Hail Insurance

In addition to multi-peril coverage, protection to growers may also be obtained from private insurers through a crop-hail insurance policy. All crop-hail policy forms must be filed and approved by the Bureau of Insurance, and all rates for crop-hail policies must be filed with the Bureau before they can be used. National Crop Insurance Services, a rate service organization, may be authorized to file loss costs and policy forms on behalf of its member companies.

A crop-hail policy is usually narrower in scope than a multi-peril policy in that coverage is provided for direct loss or damage by hail to the crops described in the policy. Crop damage due to fire is also often written with hail coverage. This provides insurance against damage to crops standing in the field. Such fire insurance may also cover damage during harvesting and while the crop is being transported to its first place of storage.[1] In the case where the insured chooses to purchase a multi-peril policy, coverage for hail and fire damage may be excluded by endorsement. This exclusion is usually

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1. Rodda, p. 216.

conditioned upon the existence of a separate hail and fire insurance policy. Excluding the hail and fire coverage and carrying at least an equal amount of protection under a separate crop-hail policy can reduce the cost of the multi-peril policy by as much as 30 percent according to information furnished by the FCIC.

The July, 1989 issue of the FC&S Bulletin, published by the National Underwriter Company, explained that crop-hail coverage may also include perils other than hail and fire depending on the crop and the state in which it is grown. This coverage may be in the form of a "named perils" policy. However, rates for coverage under such policies are not subsidized by the federal government. Therefore, a crop which is not insurable under the federal program may be considered insurable by the private sector, but insurance for that crop will not be subsidized.

A response to one of the questions on the PIA survey indicated that there was no privately offered multi-peril crop insurance program equivalent to the one sold by and reinsured through the FCIC. As stated on the survey, "insurance may be found in the private insurance industry to provide for certain perils of coverage but nothing to equal a multi-peril crop insurance contract." Therefore, a crop which is not insurable under the federal program may be considered insurable under a crop-hail policy, but coverage provided under a crop-hail policy will not be as comprehensive as a policy issued through the federal program.

Information obtained from Redland Insurance Company, however, indicated that the company's named perils policy can provide coverage which is just as comprehensive as the FCIC multi-peril policy and that they do offer this coverage in Virginia for certain crops not covered under the FCIC program. Rates are not subsidized though. Redland Insurance Company said that, depending on the individual risk, they will write coverage on a "named perils" basis for green beans, cabbage, cantaloupe, watermelon, sweet corn, and rye. Broccoli and vegetables are written on a selective basis depending on the number of acres insured.

According to National Ag Underwriters, Inc. (NAU), among the crops grown in Virginia which are not covered under the FCIC multi-peril program, NAU offers a crop-hail policy with fire coverage for canola, green beans, hay, sweet corn, and rye. The company does not offer coverage for any other crops grown in Virginia which are not covered under the FCIC program because of the adverse experience for those crops in other states.

Rain and Hail Service, Inc., on the other hand, offers crop-hail and fire coverage on all crops which are commercially grown in Virginia. Any producer that wants to insure a crop which is not insurable under the FCIC multi-peril policy can obtain coverage under a crop-hail policy. Rain and Hail Service, Inc. has been developing a privately insured multi-peril policy but is not offering this policy to Virginia growers yet. Rates, of course, are not subsidized for this type of policy.

CONCLUSION

Based on the findings contained in this report, there does not appear to be a problem with either the availability or affordability of multi-peril insurance coverage for crops which are insurable under the federal program. Generally, farmers are not refused coverage unless there is a past history of payment problems. Most companies that write multi-peril crop insurance in Virginia indicated that they insure all crops for which coverage is available under the federal program. The rates for these crops are subsidized by as much as 30 percent and are considered affordable by most growers according to the Virginia Department of Agriculture and Consumer Services. In addition, the FCIC has recently created a research unit to study the expansion of the crop program to include more crops and counties. Most of the companies surveyed stated that they would be supportive of such an expansion if adequate premium volume were generated and adequate rates were charged to ensure the actuarial soundness of the program.

The biggest problem with the FCIC's program, as noted by a number of the survey respondents, is not necessarily the availability or affordability of the insurance but the complexity of the administrative procedures involved in obtaining the insurance. It was also pointed out by several respondents that many farmers are reluctant to participate in the program if they can anticipate receiving disaster relief payments approved by Congress on an ad hoc basis. Another problem cited with the program was the lack of accountability. A study conducted by the U.S. General Accounting Office in 1991 suggested that excessive losses were being paid which could lead to morale hazards. One survey respondent also suggested that the program created a situation of adverse selection because farmers with good loss experience often chose not to participate.

The Virginia Department of Agriculture and Consumer Services stated that the expansion of the FCIC crop insurance program would encourage greater crop diversification which, in turn, would improve the economy of Virginia. If the farmers of Virginia feel that, in order to encourage further crop diversification, the federal program should be expanded to provide coverage for crops not currently insured by the FCIC, a request should be made on their behalf by the Department of Agriculture and Consumer Services with the necessary data to support the need for program expansion. The Commonwealth of Virginia may also wish to consider the possibility of establishing a state-funded program to subsidize farmers who purchase crop-hail coverage for crops not insurable by the FCIC. Such a program could be set up to promote crop diversification by providing a subsidy for farmers who grow crops which are considered important to the economy of Virginia.