



Federal Reserve Bank of Chicago Annual Agriculture Conference

**Thomas P. Zacharias, President
National Crop Insurance Services**

November 19, 2013

Taming Agricultural Risks

“...the race is not to the swift,
nor the battle to the strong...
but time and chance
happeneth to them all...”

Ecclesiastes 9:11

Production Risks, Contracting, and Insurance

Organization

- NCIS Background/Services (“Who Are You?”)
- Institutional/Regulatory Framework
- The Companies (“Who Are Those Guys?”)
- United States Profile
- Program Costs
- Farm Bill (and Beyond)

National Crop Insurance Services

Purpose

- Service Organization for Crop Insurance Industry

Structure

- NCIS Members are Crop Insurance Companies and Reinsurers

“...getting to know you, getting to know all about you....”

Membership

Involvement/Participation

- NCIS Governed by Board of Directors
- Industry Participates in Technical Committees

Industry Committees

- Loss Adjustment, Policy and Procedures
- Actuarial Analysis and Data Reporting
- Industry Training
- Industry Communications

Monthly Conference Calls/Formal Meetings with
United States Department of Agriculture/Risk
Management Agency (USDA/RMA)

Regional/State Committees





NCIS Services and Functions

2013 NCIS Crop Research



- **Economic and Actuarial Research**
- Individual Coverage Versus Area Schemes
 - American Journal of Agricultural Economics - 2012
- Ex Ante Crop Insurance Versus Ex Post Disaster
 - American Agricultural Economics Association Meetings - 2013
- Industry Rate of Return and Standard Reinsurance Agreement
 - NCIS *Today Magazine*
- Review of RMA's Actuarial Methodology Change
 - RMA Website
- Understanding Costs of Crop Insurance Program
 - NCIS *Today Magazine*



Schools and Education

2013 NCIS Major Conferences and Adjuster Schools



Major Conferences

- Train the Trainer Conference
- Claims Manager's Conference



Communications and Industry Promotion

A modern-day farm policy
for tomorrow's challenges

Securing America's food supply

Shielding taxpayers from unnecessary risk

Strengthening the economy

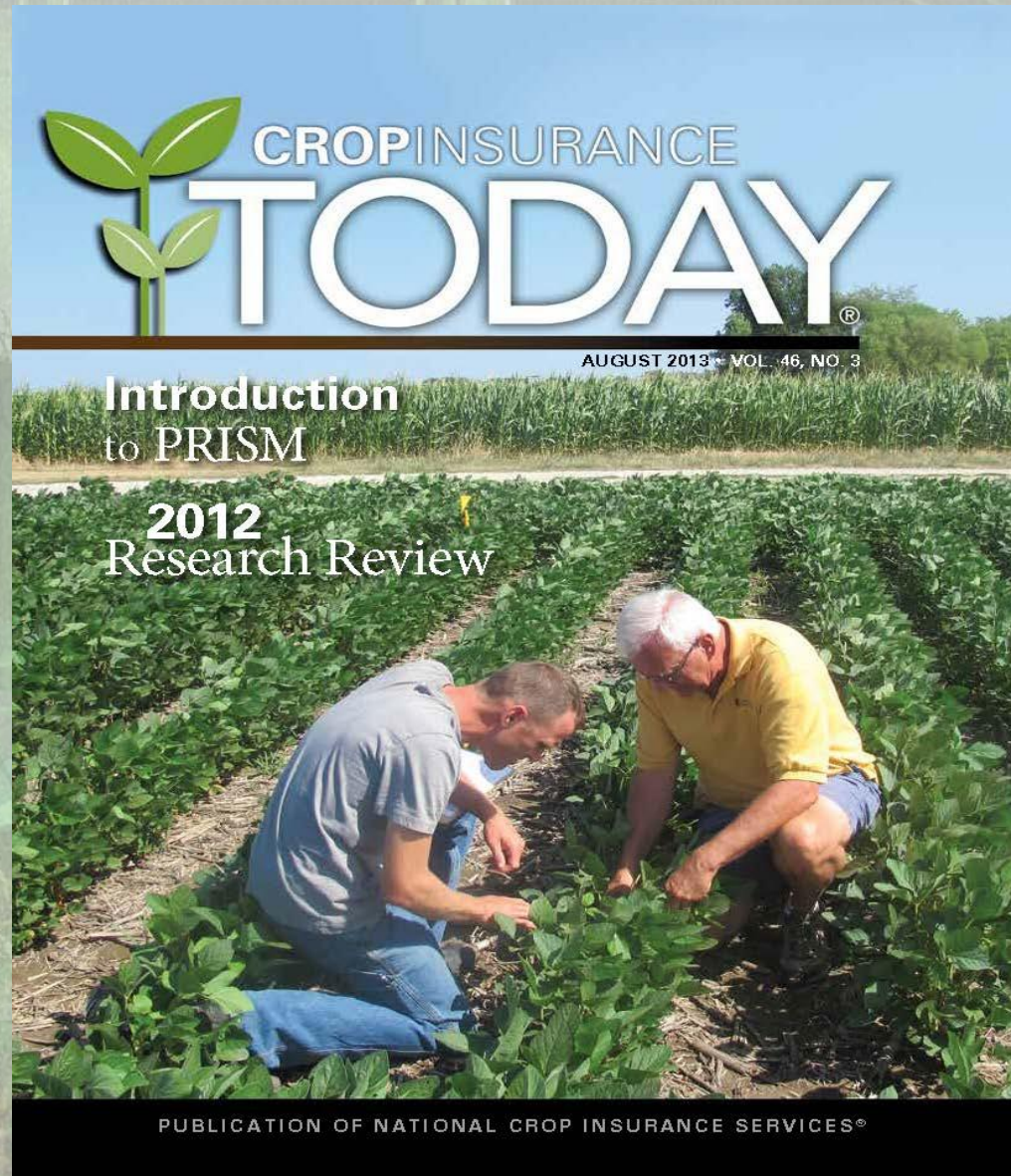
SUPPORT CROP INSURANCE



CropInsuranceInAmerica.org

CROP INSURANCE
Keeps America Growing

Communications and Industry Promotion



The background of the slide is a faded, semi-transparent image. It depicts a construction or agricultural site. In the center, a worker wearing a red hard hat and blue clothing is operating a piece of heavy machinery, possibly a tractor or a loader, which is carrying a large, rectangular object. To the left of the worker, there is a green recycling symbol (a triangle with arrows forming a circle). The overall scene is set in a field with some vegetation. The text 'Institutional/Regulatory Framework' is overlaid in the center in a large, bold, black font.

Institutional/Regulatory Framework

Federally Reinsured Crop Insurance Versus State Regulated Crop-Hail Insurance

	Federal Crop Insurance	State Regulated Crop-Hail Insurance
Regulator	Risk Management Agency (RMA) of USDA	State Departments of Insurance
Subsidized?	Yes	No
Premium Rate	Set by RMA	Set by Individual companies
Perils covered	All risk basis: Yield losses due to natural causes; Also revenue losses due to price movements and yield losses.	Named perils basis: Losses due to hail and others (fire, lightning, transit, etc)

The U.S. Partnership (Federally Reinsured)

	<i>Private Companies (AIPs)</i>	<i>Government (FCIC/RMA)</i>
Players	18 approved companies 16,000 agents & adjusters	450 staff - approximately \$80 mil annual budget
Products	May develop products	May develop products
Sales	Sell and adjust all policies; must sell to any farmer wanting coverage	Sells no policies; makes a payment to AIPs for delivery costs
Premiums	Collect premiums	Sets premium rates; subsidizes premiums
Underwriting	Bear underwriting risk; share gains/losses with gov.	Sets underwriting standards; shares gains/losses with AIPs
Claims	Pay all claims	Pays no claims
Education	Train agents, adjusters, informs producers	Informs producers

Standard Reinsurance Agreement (SRA)

- A Cooperative Financial Assistance Agreement between the Federal Crop Insurance Corporation (FCIC) and an Insurance Company.
 - FCIC – A Government Corporation of the USDA Authorized to Carry Out Programs of the Federal Crop Insurance Act.
- Risk Management Agency Acts on Behalf of FCIC to Administer all Federal Crop Insurance Programs.

Standard Reinsurance Agreement

Cont'd

- Establishes the Terms Under Which FCIC Provides Reinsurance and Subsidies on Eligible Crop Insurance Contracts Sold by the Insurance Company.
 - By Regulation, Insurance Company Must be in Good Financial Standing and in Compliance with State Laws Where Domiciled and Writing Business Prior to being Considered for Approval of an SRA.

Standard Reinsurance Agreement

Con'd

“Except as specified below, the Company shall offer and market all plans of insurance for all crops in any State which it writes an eligible crop insurance contract and shall accept and approve applications from all eligible producers. The Company may not cancel so long as the policyholder remains an eligible producer.”

-- we take all comers --

Approved Insurance Providers (AIPs)

“Who are those guys?”

(Butch Cassidy and the Sundance Kid)

- Rain & Hail Insurance Services
 - “...ACE Buys R&H Ace Ltd...December 2010...”
 - “...ACE Group – operations in over 50 countries, employs more than 19,000 people...”
 - “\$92B in assets and \$21B gross written premium in 2012”

“Who are those guys?”

- ARMtech - Lubbock TX, subsidiary of Endurance
 - “Endurance is global provider of insurance and reinsurance, approximately \$9.6B in assets; \$2.7B in shareholders’ equity”
- ProAg – Amarillo TX, subsidiary of CUNA Mutual
 - “...insurance and financial services since 1935...”
 - 2012: approximately \$2.5B in GAAP Surplus; \$17.3B in assets

“Who are those guys?”

- QBE acquires Agro National November 18, 2010
 - Acquisition completed in March, 2011
 - June, 2010 QBE purchased NAU Country – Ramsey, Minnesota
 - QBE
 - Top 25 insurers/reinsurers
 - Headquartered in Sydney, Australia
 - \$46.7B in assets for 2011; approximately \$18.3B in U.S. gross premium

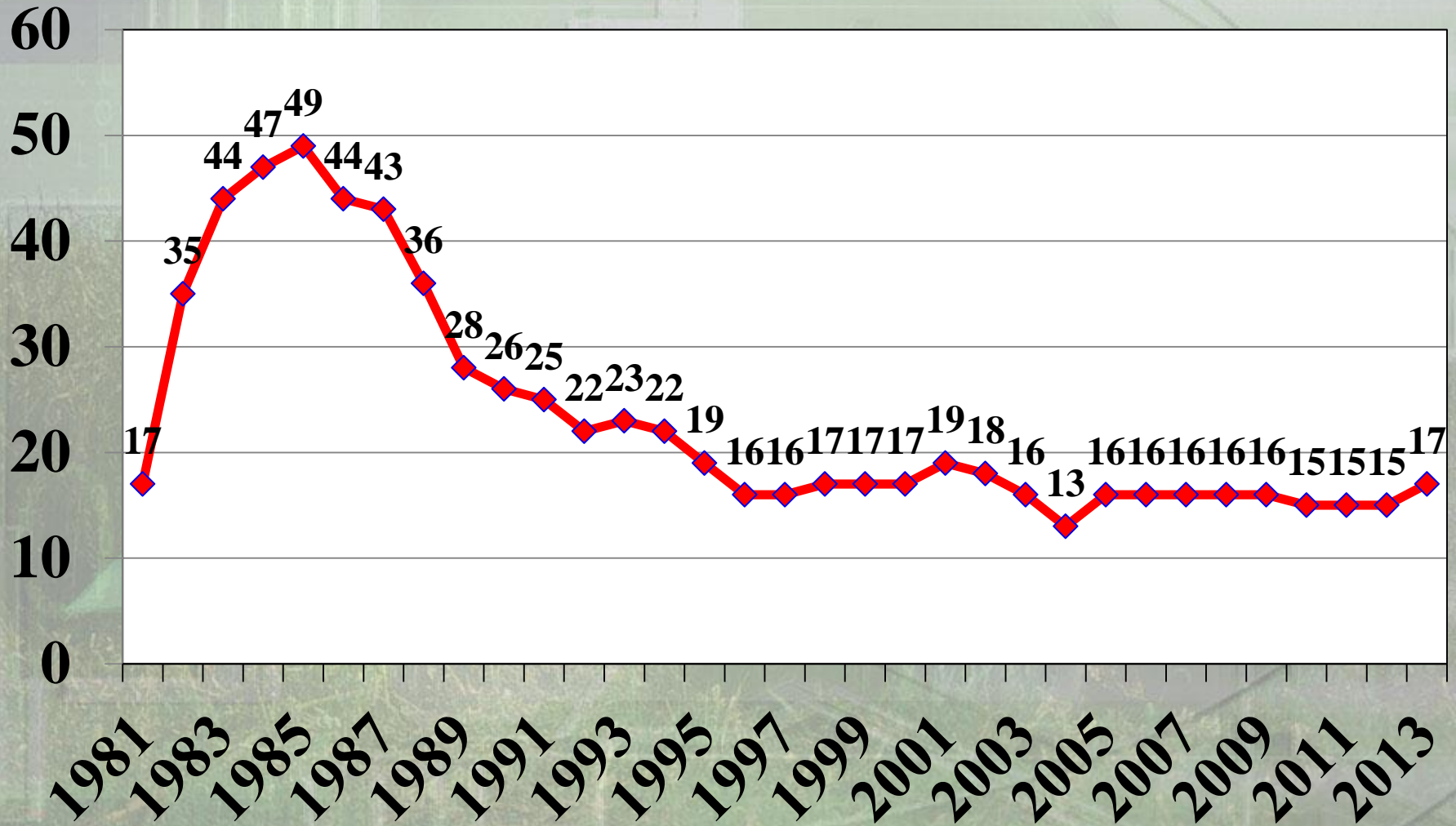
“Who are those guys?”

- Rural Community Insurance Services (RCIS) Anoka, MN
 - Wholly owned subsidiary of Wells Fargo and Company
- Great American
 - Founded 1872, 1st crop 1925
 - Owned by Great American Financial Group
- Farmers Mutual Hail – Since 1893

“Who are those guys?”

- John Deere – the green tractors, right?
 - Founded in 1837
 - 2012: \$36.2B revenue (entire company)
- ADM
 - Enters in 2010
 - 30,000 staff; 265 processing plants; 140 countries
- Climate Corp – Recently approved for SRA
 - San Francisco-based
 - High-tech weather insurance platform
 - Acquired by Monsanto for approximately \$1B

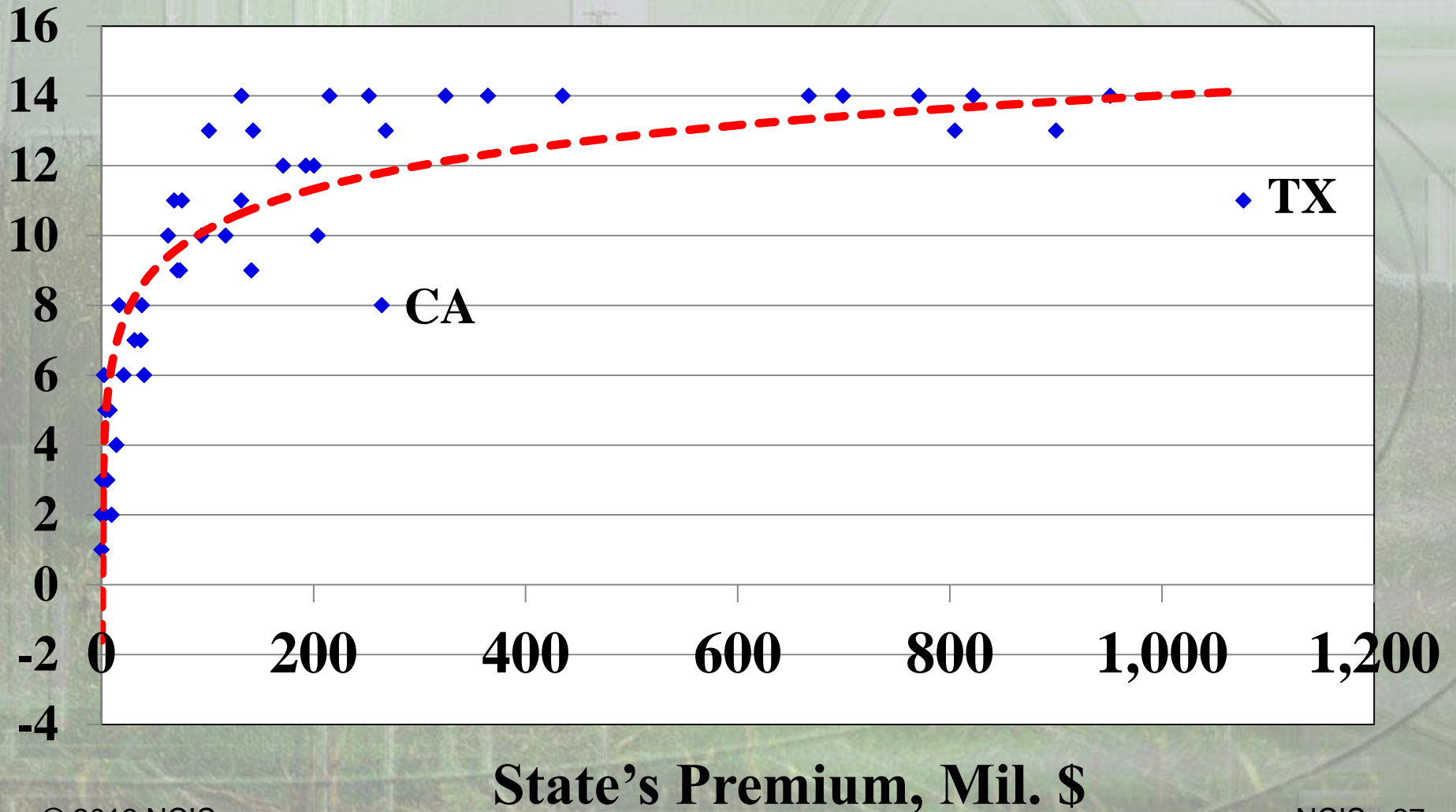
Number of AIPs



Source: 1981-84, RMA; 1985-2013, NCIS

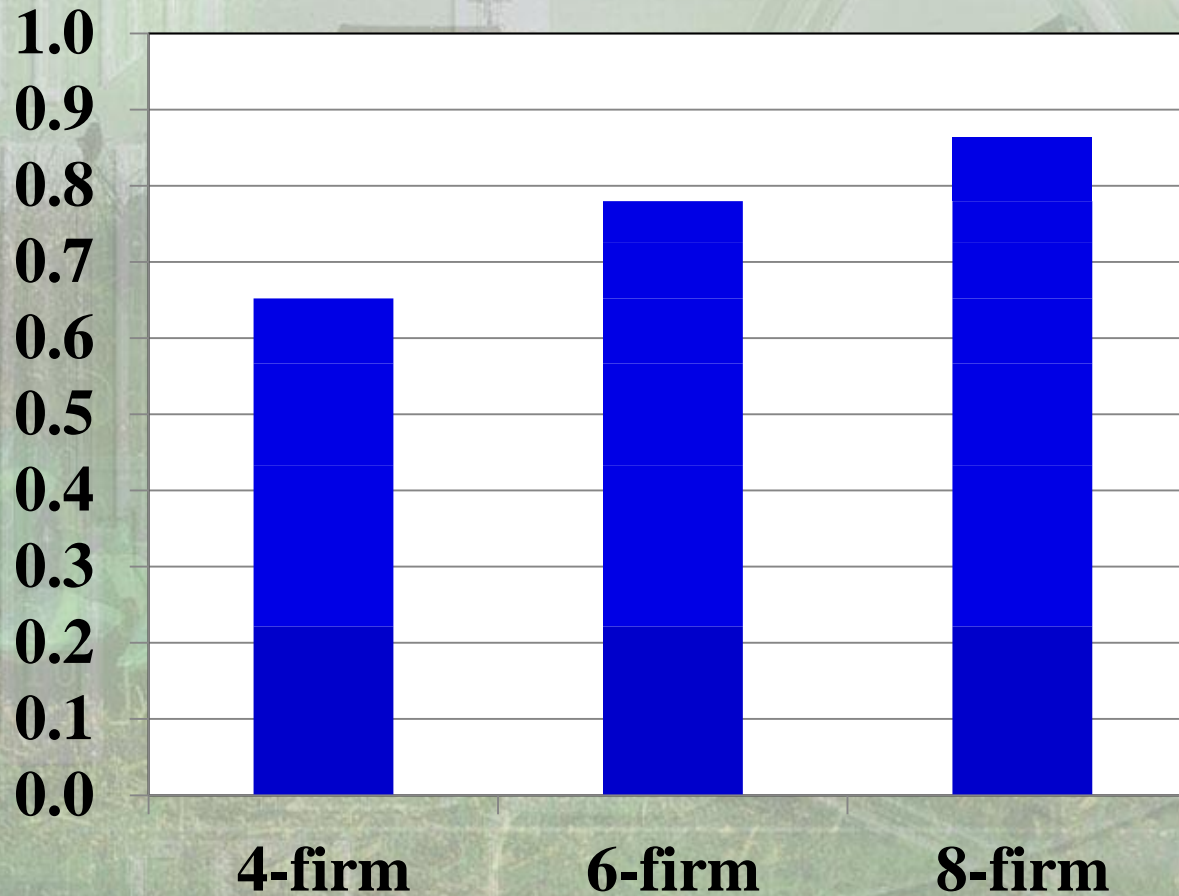
Premium and Number of AIPs per State, 2012

AIPs/State



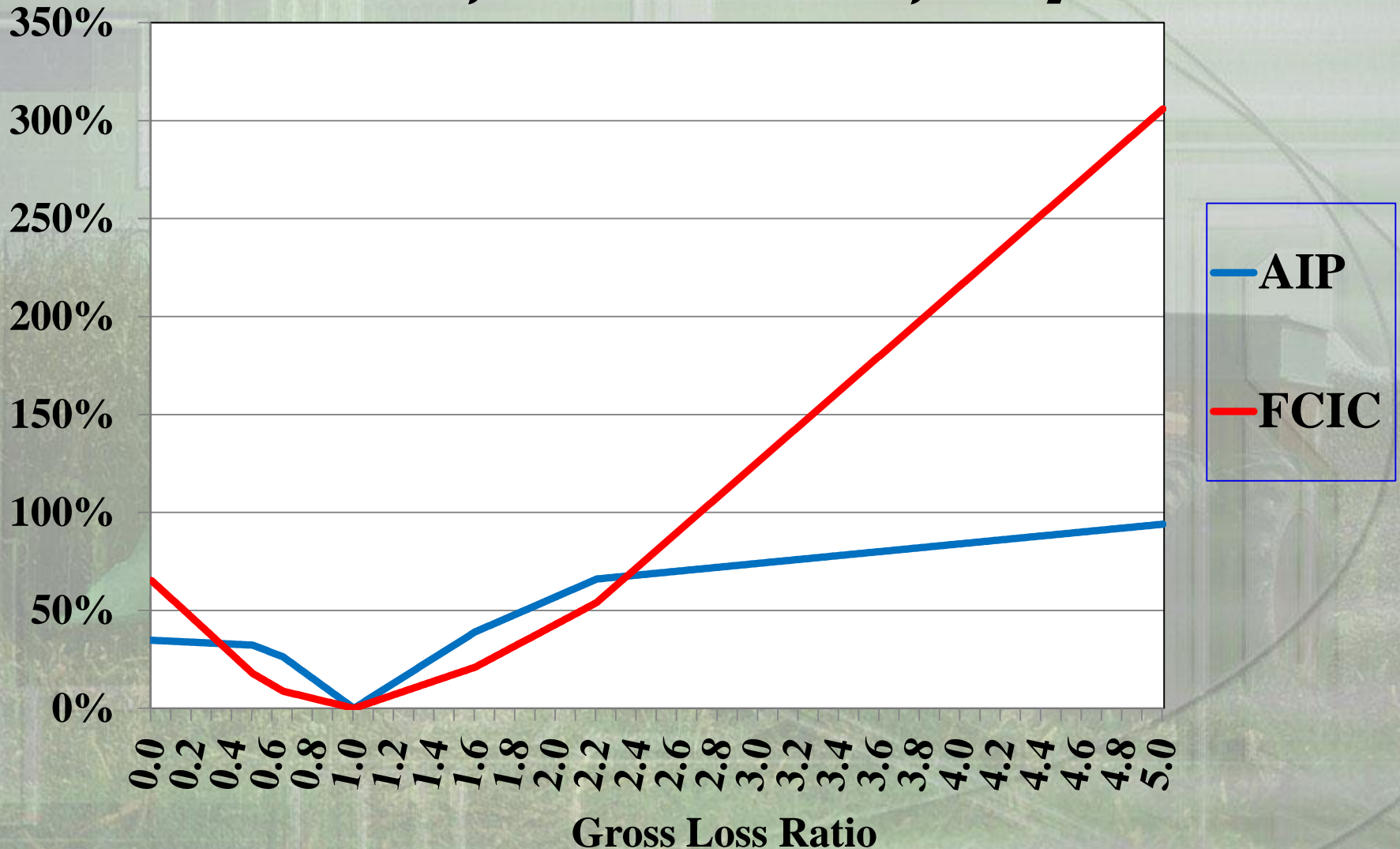
AIP Concentration Ratios, 2012

1.0=100% of Industry Premium



How Companies and FCIC Share Gains/Losses

*Share of Premium, Commercial Fund, Group 1 States **





U.S. Profile

“the numbers please”

A green tractor with a combine harvester attachment is shown in a field. A person is operating the tractor. The background is a blurred field of crops.

Where is Crop Insurance Bought and Sold?

Crop Hail Premium Totals

US Premium Volume

2013	\$926.4 million*
2012	\$954.1 million

Top 5 Premium Written States*

2013	<u>Premium</u>
• Nebraska	\$177.5 million
• Iowa	\$116.2 million
• Minnesota	\$ 92.1 million
• North Dakota	\$ 88.6 million
• Illinois	\$ 82.6 million

*Preliminary Verified Total as of 9/23/2013

Nationwide Summary*

	<u>Liability</u>	<u>Premium Volume</u>
2012	\$117.1 billion	\$11.1 billion
2011	\$114.1 billion	\$ 12.0 billion

Top 10 Liability States

2012	<u>Premium</u> (\$millions)	<u>Liability</u> (\$billions)	<u>Acres</u> (millions)	<u>Liability per Acre</u> (\$/acre)
Iowa	902.8	\$14.9	21.7	688
Illinois	772.7	\$12.1	18.0	678
Minnesota	824.8	\$10.0	17.5	574
Nebraska	668.8	\$ 8.7	15.7	557
North Dakota	968.4	\$ 6.3	23.3	272
Indiana	437.6	\$ 5.8	8.7	659
Kansas	808.7	\$ 5.7	18.3	310
California	261.0	\$ 5.4	4.6	1172
South Dakota	701.2	\$ 5.4	15.0	360
Texas	1,082.4	\$ 5.2	48.2	109
- Texas PRF	114.8	\$ 0.5	33.3	15
- Texas – All Other	967.6	\$ 4.7	14.8	320

*Source: RMA Summary of Business as of 9/23/2013; Texas as of 10/11/2012

Liability as a Share of Production Value

2011-12 avg.

	Production Value (bil \$)	Insured Liability (bil \$)	Liability as a % of Prod. Value
Grains	84	66	79%
Oil crops	41	27	66%
Fruits & nuts	25	7	28%
Vegetables & melons	21	3	14%
All other	41	14	34%
Total crops	212	116	55%

Major Plans of Crop Insurance Sold, 2012

(% of total liability)

Individual
Yield

- Yield Protection (18.2%)

Individual
Revenue

- Revenue Protection (70.2%)
- Revenue Protection—Harv. Price Excl. (2.6%)

Area Yield
& Revenue

- Group Risk Plan (>1%)
- Group Risk Income Protection (>0.5%)
- Group Risk Income Prot.—Harv. Rev. Opt. (2.2%)

Other

- Pasture/Rangeland, Aquaculture, Others

Revenue Policies Rationale

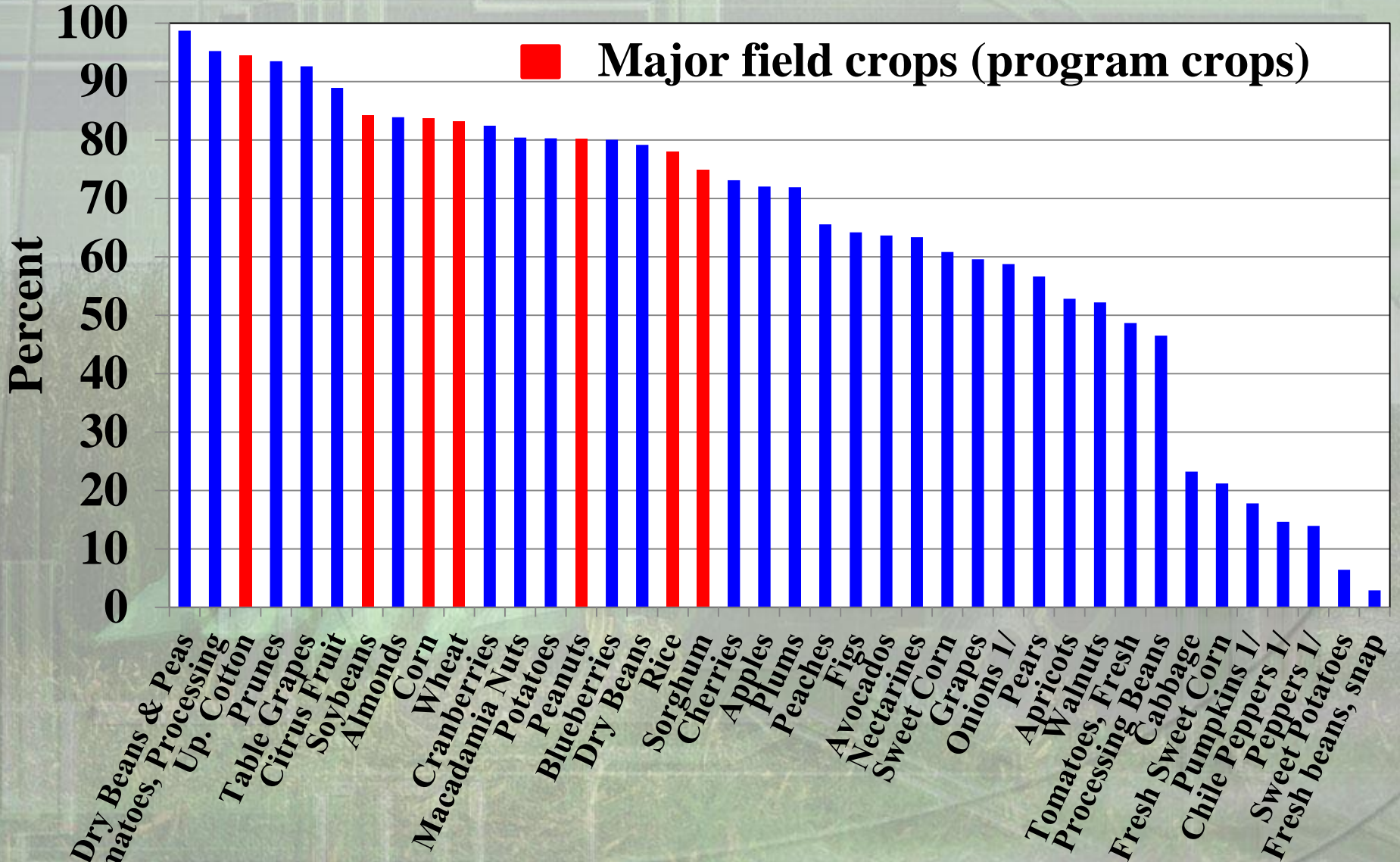
- Farmers Face Income Risk

Harvest Price Option

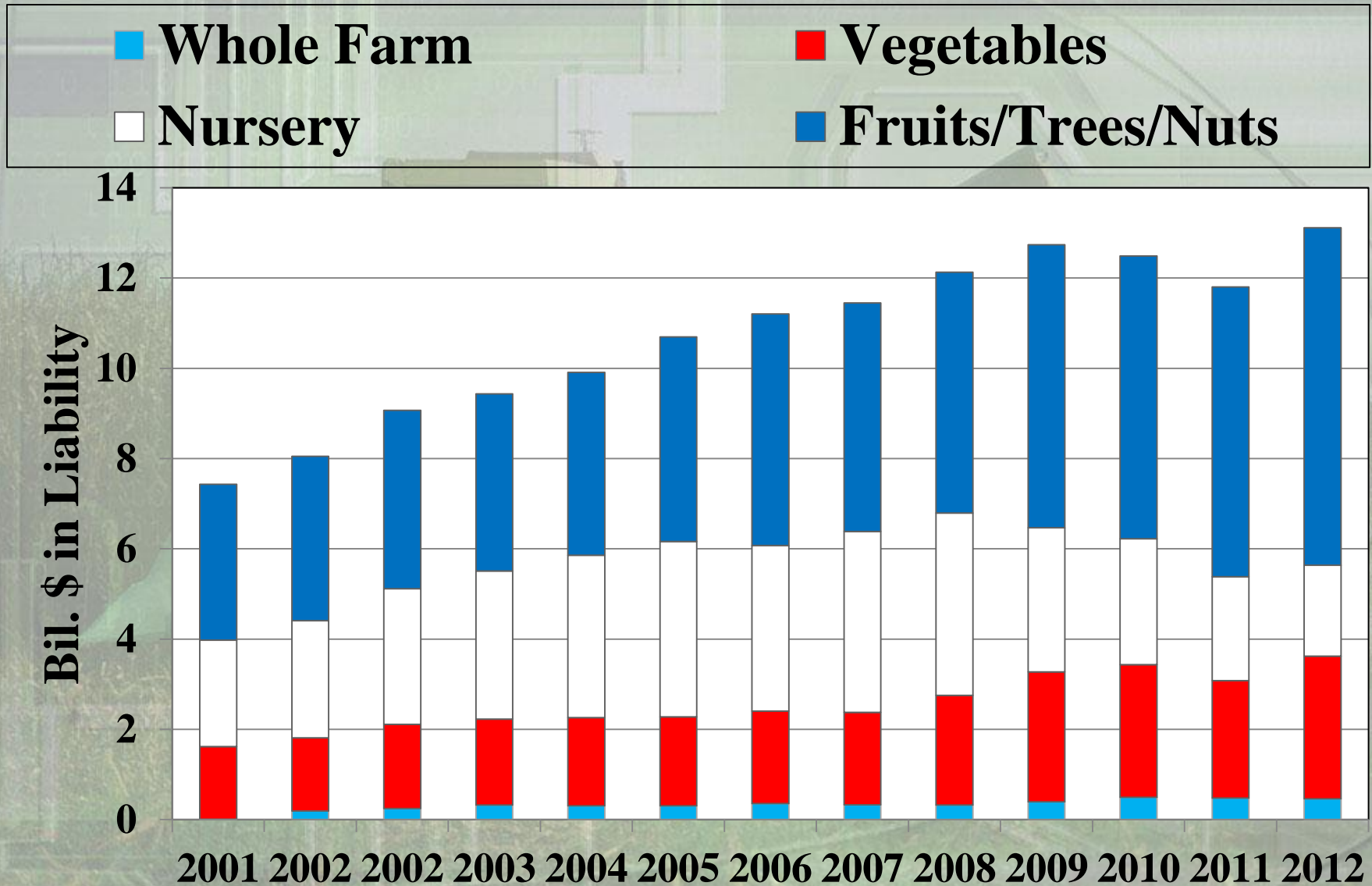
(Replacement Value Contract)

- Protects Farmer with Forward Contracts
- Protects Farmer with Livestock

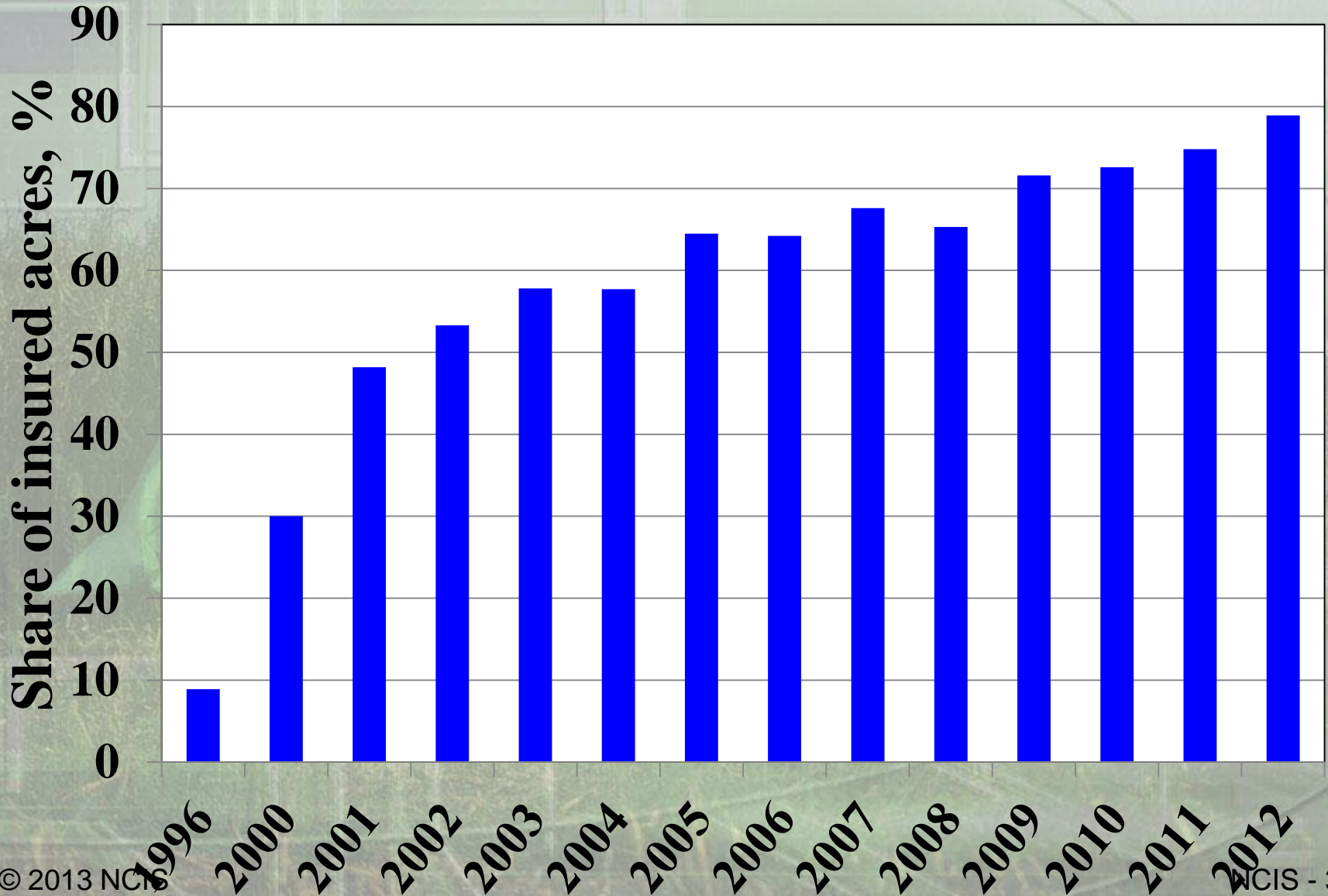
Insured Share of Planted or Bearing Acres



Growth in Specialty Crop Coverage

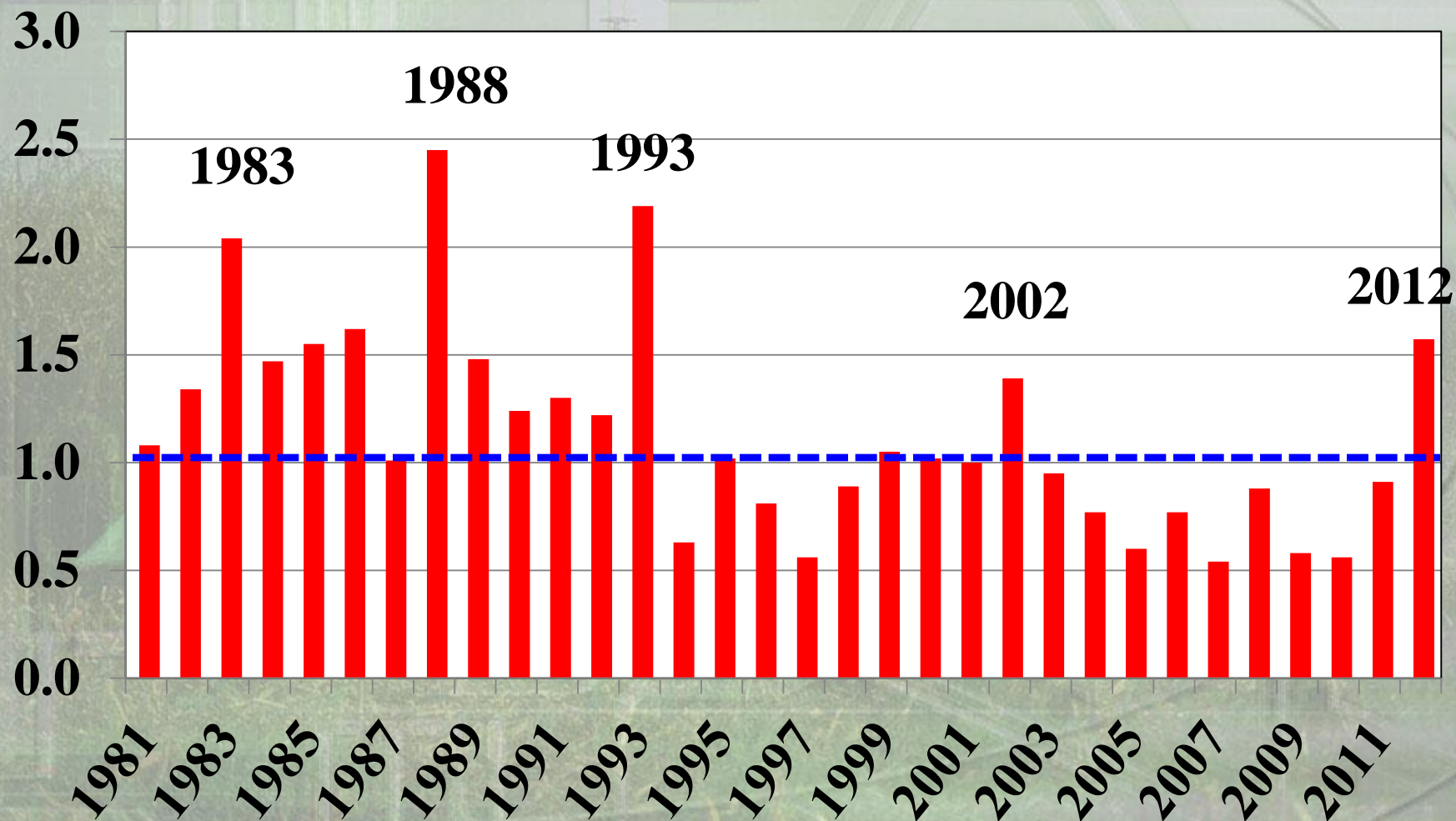


Growth in Share of Acres Covered at 70% or Higher



Actuarial Performance of Crop Insurance

Loss Ratio = Indemnities/Premiums



2012 Drought

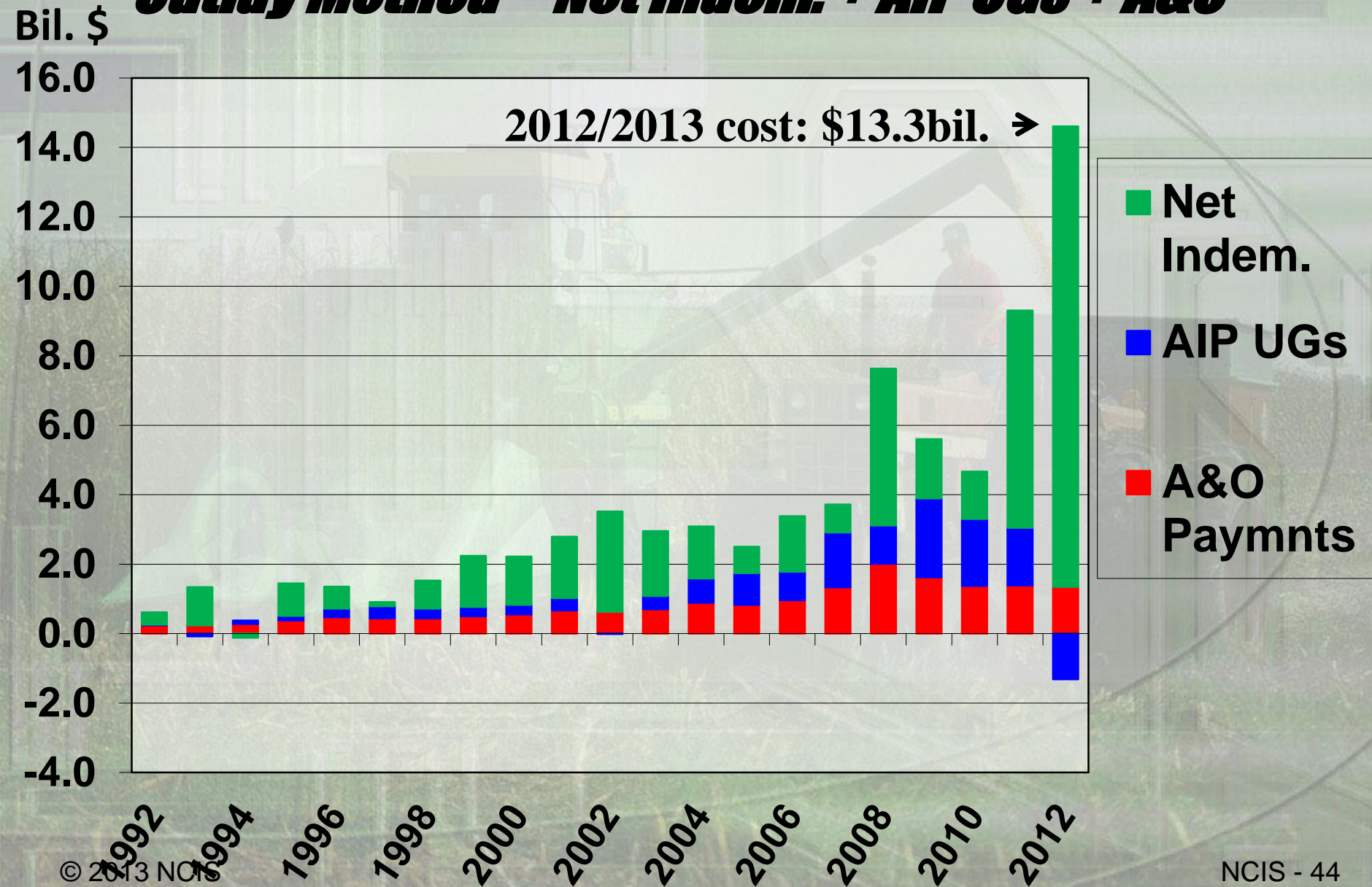
- \$17.4 Billion U.S. Indemnity
 - (Approximately 80% Drought-Related)
- \$4.1 Billion U.S. Farmer Premium
- \$12.7 Billion U.S. Uninsured Losses
 - (Approximately)



Program Costs **(“The check please”)**

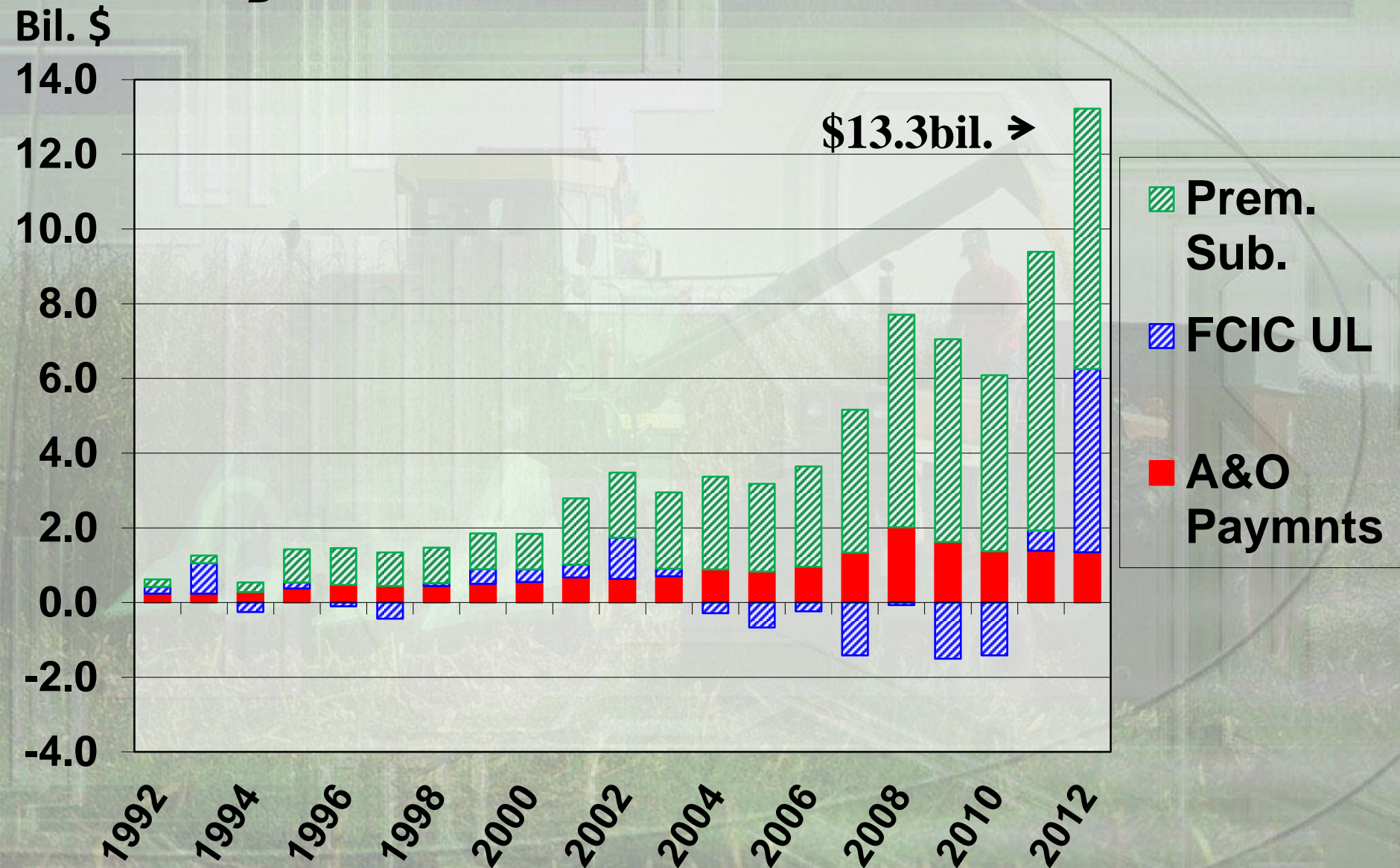
Components of CY Taxpayer Cost

Outlay Method = Net Indem. + AIP UGs + A&O



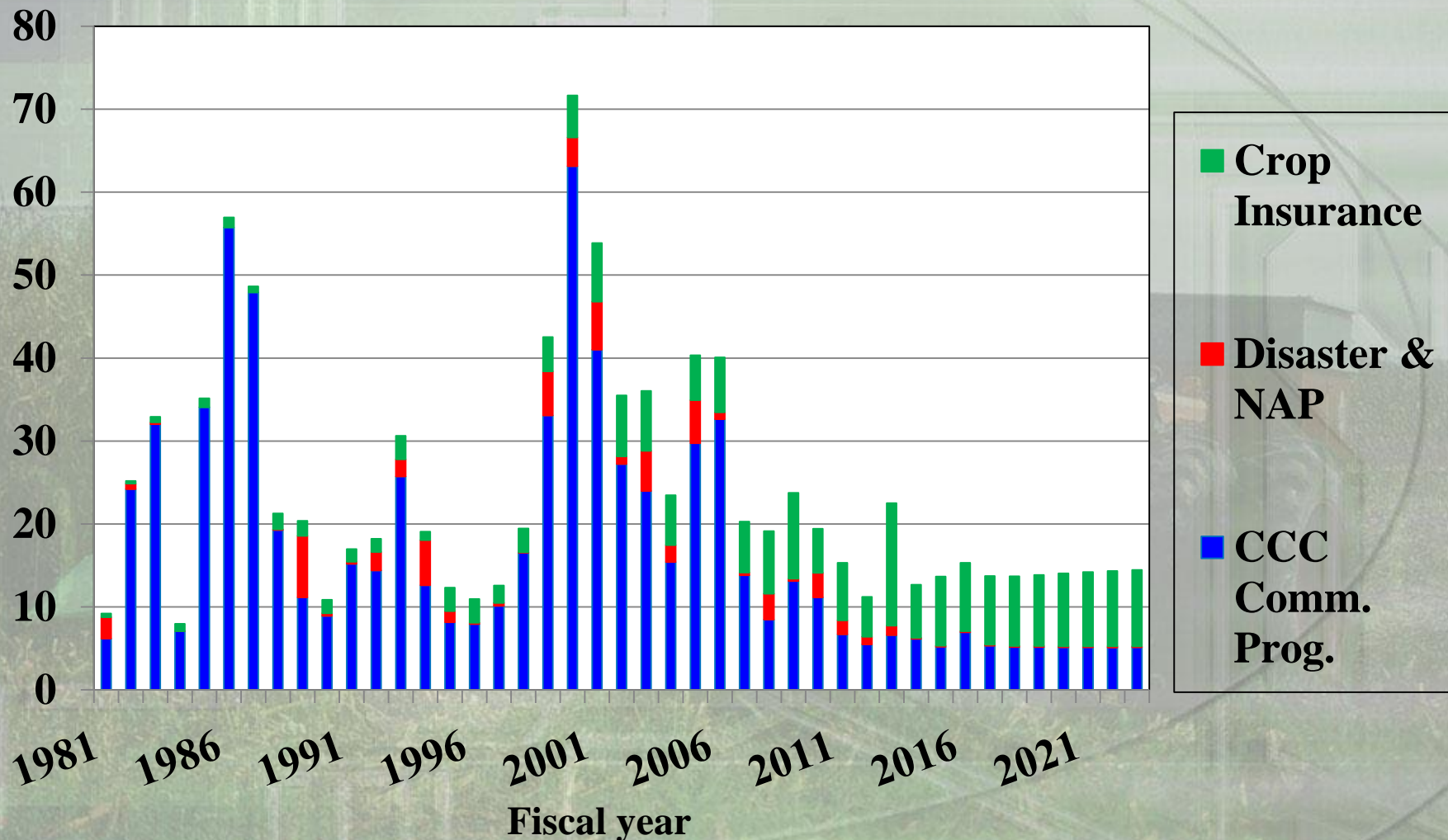
Components of CY Taxpayer Cost

Subsidy Method = Prem. Sub. + FCIC Un. Loss + A&O



Real Expenditures on CCC Commodity Programs, Disaster & NAP, Crop Insurance

Bil. 2013 \$



Source: USDA and Congressional Budget Office May 2013 Baseline; deflated using index of prices received for crops

The 2013 Farm Bill and Crop Insurance

Summary:

- 2013 Farm Bill (FB) authorizes most programs affecting food, feed, fiber and biofuel production.
 - Nutrition comprises 80% of the FB.
- Funds various farm programs, including conservation, trade, research and crop insurance.
- Lack of FB creates uncertainty in agriculture.
- Crop Insurance is separate from the FB.
 - Crop Insurance has permanent legislation, Federal Crop Insurance Act, so crop insurance program continues to operate despite expiration of 2008 FB on September 30, 2013.

2013 Farm Bill and Crop Insurance

Con'd

- Farm Bill *Does* Affect Crop Insurance
 - FB makes important improvements to crop insurance.
- House and Senate versions authorize two new insurance products that enable producers to buy coverage that supplements their underlying crop insurance policies.
- Supplemental Coverage Option or SCO for all crops except cotton.
- Stacked Income Protection Plan or STAX for cotton.
- These products protect farmers against larger area-wide disasters.

2013 Farm Bill and Crop Insurance Con'd

- Both bills direct development of provisions for peanuts, catfish, whole farm insurance and organic crops.
- Bills set research priorities.
 - Improve product development processes and increase funding for livestock insurance.
- Both bills strengthen crop insurance programs for beginning farmers, address producers' concerns with declining insurance yield guarantees and provide farmers with more flexibility for determining coverage on land to be insured.
- Key Difference: AGI test and Conservation Compliance in Senate bill but not House bill

2013 Farm Bill and Crop Insurance Con'd

Conclusion:

- Farm safety net spending has trended down over the past decade as farm program spending has declined and importance of crop insurance has risen.
- In this FB, producers have expressed a clear preference to give up traditional farm programs while urging Congress to put a great focus on crop insurance.
- While some resources have been shifted to strengthening crop insurance, overall funding for the farm safety net will be reduced under the FB.
- Since 2008, crop insurance funding has been cut by \$12 billion.

Why Crop Insurance is Now in a Position of Strength

- 1--Producers share program cost**
- 2--Producers take personal responsibility for risk management**
- 3--Producers get individual risk management solutions**
- 4--Producers receive indemnities in the timeliest way**
- 5--Program can be quickly adjusted and is self-correcting**
- 6--Payments are not in excess of losses**
- 7--Protection can be used as collateral for loans**
- 8--Program enables pre-harvest marketing**
- 9--Producers not subject to payment limits**
- 10--Producers benefit from the efficiencies of private sector delivery**
- 11--Crop insurance can be green box under the WTO and has flexibility to meet WTO support limits**
- 12--Crop insurance has contributed to deficit reduction**

Beyond the Farm Bill

Policy & Program Issues

- **Interaction of Crop Insurance and Farm Programs**
 - Interaction & implementation issues
 - Will farmers buy down?
 - Effectiveness of area plans
- **Private Delivery**
 - Concern over delivery cost (different regulatory model, less costly products, alternative approach?)
- **Underwriting Gains**
 - Degree of public/private risk sharing and returns
- **Premium Subsidies**
 - Level
 - Structure

Websites

NCIS

www.ag-risk.org

Crop Insurance in America

***Just the Facts Tab**

www.cropinsuranceinamerica.org

Support Crop Insurance

www.supportcropinsurance.org

Social Media



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