PolicyPennings by Daryll E. Ray & Harwood D. Schaffer

Revenue insurance: Adds a layer of middlemen and self-lowering safety net

Over the years, crop/revenue insurance has frequently been the focus of this column. With revenue insurance taking on an air of inevitability as the key element of the commodity section of the 2012 Farm Bill, it seems appropriate to look specifically at the arguments for revenue insurance that are currently in play.

A core argument for revenue insurance is that it is market-based. The idea being that revenue insurance provides a private-sector remedy to agriculture's price and income problems instead of the government-based remedy as has been the case in the past. The problem we have with that statement is that it is not true. The government is just as involved as it ever was only now there is a middleman in the process. And the middleman has to be paid a fee over and above the payments that are made to crop farmers.

If crop/revenue insurance were truly a private-sector venture, as it is with crop hail insurance, farm liability insurance, farm equipment insurance, and a host of other insurance products, there would be no need for the government to subsidize a significant portion of the premium and provide a profit to the insurance companies to boot.

But as it is, if crop/revenue insurance is the mechanism that Congress wants to use to provide protection to crop farmers, billions of dollars could be saved by eliminating the middlemen by having farmers sign up for it during one of their trips to the county offices of the Farm Service Agency. That's where much of the information required to apply for the insurance is housed anyway.

Another argument for the insurance approach to farm programs is that revenue insurance is market-following and thus does not distort the market by setting artificial price levels, as can be done with loan rates and target prices. Instead, of using loan rates and target prices set by Congress, insurance uses the market's price to set its protection level—it follows the market.

In making this argument, crop/revenue insurance proponents are assuming that, on average, the price being offered by the market is just fine. History suggests otherwise; just look at the season average prices for the 1998-2001 crop years. Besides, perfection in "market-following" means no protection at all.

As the House Ag Committee Chair and Ranking member have stated, crop/revenue insurance is not a safety net. When prices fall, so does the level of insurance protection.

One of the benefits of revenue insurance being talked about for the coming farm bill is protection against a change in the expected level of revenue between planting and harvest, even if the revenue at harvest is well above any reasonable measure of the cost of production. That is, there is the possibility of ensuring farmers "pure profits" during times when prices come off extraordinarily and unsustainably high levels.

Every business out there needs to be able to protect itself against short-term fluctuations in income. There are always ups and downs in a market economy and businesses need to provide themselves with a cushion to get them through minor fluctuations in income. In this respect farmers are no different than the small business on Main Street.

To the extent that the reduction in expected revenue between planting and harvest is price-related, farmers do not need the government to provide a service that is available in the marketplace. Farmers wanting to protect themselves against a change in price between planting and harvest have several mechanisms available to them: forward contracting and the futures market.

To us, it is difficult to make a convincing case that the public should provide crop farmers with protection that is readily available from the private sector without a subsidy. We have always thought that farm programs were to provide help during the hard times.

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