

## PolicyPennings by Daryll E. Ray & Harwood D. Schaffer

# Crop insurance cost and who pays for it

At a time when farmers have become more reliant on crop revenue insurance than ever, it is coming under increasing challenges. With the end of Direct Payments in the 2014 Farm Bill, crop insurance became the primary farm commodity risk management program. The United States Department of Agriculture (USDA) estimates that crop insurance will account for 45 percent of the spending under the farm portions of the 2014 Farm Bill. The spending devoted to the Agricultural Risk Coverage and Price Loss Coverage commodity programs is expected to account for 23 percent though recent low prices may increase the overall cost of ARC and PLC.

The administration's 2016 Budget calls for \$16 billion in savings from federal crop insurance over the next ten years. The bulk of the savings would accrue as the result of cutting the premium subsidy by 10 percentage points. This would result in projected savings of \$14.6 billion over the next decade. Other savings would come from tightening up on prevented planting rules, providing farmers with the incentive to plant a second crop. The administration would also restrict farmers from buying additional coverage above 60 percent of a crop's guarantee for prevented planting.

Needless to say, the administration's proposal has not gone over well among farm groups. On Wednesday, February 4, 2015, a group of 31 organizations sent a letter to the House and Senate Budget Committee Chairs and Ranking Members (<http://tinyurl.com/pyn455n>) arguing that "crop insurance has been contributing more than \$1.2 billion a year towards reducing government spending since the 2008 Farm Bill."

But the administration's budget proposal is not the only threat to federal crop insurance on the horizon. A recent article, "The political economy of the 2014 Farm Bill," (<http://tinyurl.com/nomcm78>) by David Orden and Carl Zulauf argues that "insurance products do not address multiple year price and revenue risks." They also reference a paper by Cooper et al. that "find[s that] an average subsidy rate of approximately 35 percent is sufficient to have 80 percent of land insured."

In addition, Orden and Zulauf provide ammunition for those who would call for a cut in the government's subsidy level for crop insurance by suggesting that "systemic risk [long periods of low prices for all farmers as opposed to random risk] is at most 45 percent of total risk in US crop production. The rule of thumb argument is that the average subsidy rate should not exceed the share of risk that is systemic." Using either the 35 percent or the 45 percent rate, crop insurance subsidies by the federal government would fall dramatically.

Before he left the Senate in January, Tom Coburn of Oklahoma and the then Ranking Member of the

Committee on Homeland Security and Governmental Affairs asked the GAO (Government Accountability Office) to "look at the cost of the federal crop insurance program, specifically concerning the costs associated with revenue insurance policies." The GAO conducted a study and issued an August 2014 report "Crop insurance: Considerations in reducing federal premium subsidies" (<http://tinyurl.com/oagavey>).

In that study, the GAO's analysis showed that "reducing premium subsidies for revenue policies could potentially result in hundreds of millions of dollars in annual budgetary savings with limited costs to individual farmers. For example, the federal government would have potentially saved more than \$400 million in 2012 by reducing premium subsidies by 5 percentage points, and the savings would have been nearly \$2 billion by reducing these subsidies by 20 percentage points. Although such reductions would have required farmers to pay more of their premiums, the impact on their average production costs per acre would have been limited, usually less than 2 percent, and often less than 1 percent."

In the US Senate, Jeanne Shaheen and Patrick Toomey introduced S.345 "A bill to limit the level of subsidy provided by the Federal Crop Insurance Corporation to agricultural producers" on February 3, 2015. According to Shaheen's Senate website (<http://tinyurl.com/ma3e3yy>) the legislation "would save taxpayers more than two billion dollars by capping federal crop insurance premiums for the largest farm businesses. The bill would cap crop insurance premium subsidies at \$50,000, which the Congressional Budget Office estimates would reduce the deficit by about \$2.2 billion over 10 years."

And then there is the ongoing set of budget issues and the desire of some in Congress to reduce the Supplemental Nutrition Assistance Program (SNAP). What is clear to the farm sector is that if SNAP is cut, then an equivalent cut will be required of the farm program. Otherwise farmers will be forced to respond to those who will argue that they are taking food out of the mouths of hungry people to provide subsidies to farmers who have earned record profits in recent years.

It seems likely that crop insurance program will continue to be under pressure in the coming months. Whether any legislation will result is another issue.

Daryll E. Ray holds the Blasingame Chair of Excellence in Agricultural Policy, Institute of Agriculture, University of Tennessee, and is the Director of UT's Agricultural Policy Analysis Center (APAC). Harwood D. Schaffer is a Research Assistant Professor at APAC. (865) 974-7407; Fax: (865) 974-7298; [dray@utk.edu](mailto:dray@utk.edu) and [hdschaffer@utk.edu](mailto:hdschaffer@utk.edu); <http://www.agpolicy.org>.