



**United States
Department of
Agriculture**

Federal Crop
Insurance
Corporation

1400 Independence
Avenue, SW
Stop 0801
Washington, DC
20250-0801

DATE: January 25, 2007

TO: Board of Directors
Federal Crop Insurance Corporation

FROM: Eldon Gould */signed/*
Manager

SUBJECT: Manager's Report
Exhibit No. 2878

This memorandum serves as the Manager's Report to the Board of Directors (Board), Federal Crop Insurance Corporation (FCIC), for the January 25, 2007 meeting. The report relates to program issues as outlined below:

Program Issues:

Pasture, Rangeland and Forage Pilot Program Sales – As of January 15, 2007, the sales of the new Pasture, Rangeland and Forage Rainfall and Vegetation Index pilot programs have exceeded first year sales projections. There have been a robust 7,737 Rainfall Index policies sold covering 23,125,534 acres with \$320,772,288 in total liability. As for the Vegetation Index pilot program, its sales are at 1,652 policies sold covering 3,828,234 acres and \$59,547,045 in total liability. This puts participation in the pilot program areas at approximately 16 percent, while the first year target goal was 10 percent.

Florida Fruit Tree Program – Recently, RMA issued Bulletin MGR-06-013 that extended the amount of time for an insured seeking coverage for Asiatic Citrus Canker (ACC) to submit an acceptable negative underwriting certificate from 30 days to 60 days and shifted responsibility for issuing destruction certificates to Approved Insurance Providers (AIP), which Florida's Department of Plant Industry (DPI) is no longer able to perform the task. To facilitate this change, DPI and RMA are providing training to affected AIP's in ACC identification, decontamination procedures and loss adjustment changes during the month of January. On December 18, 2006, the Board voted to remove ACC coverage for the 2008 crop year, but left open the potential for exploring other options to address losses due to ACC disease as the situation stabilizes and more effective disease management strategies are implemented. Appropriate changes are being made to policy documentation for the January 31, 2007 contract change date.

Cultivated Clams Pilot Program – On November 29, 2006, Research Triangle Institute presented its oral report for the Cultivated Clams Pilot Program Evaluation. Feedback was provided by RMA Regional Offices and staff on the information presented. A written report is due in February 2007.

Aquaculture Partnership – On December 13, 2006, Mississippi State University presented a draft report on the feasibility of insuring Farm-Raised Catfish, Atlantic Salmon, Trout, and Baitfish to RMA Regional Offices and staff. Comments are currently being solicited from within RMA about the report, which will be consolidated for presentation to the Board on its April 2007 scheduled meeting.

Premium Reduction Plan (PRP) – Currently, the PRP is not available during the 2007 reinsurance year (RY) due to language in the 2006 FY (Fiscal Year) Appropriations Bill. However, the Reinsurance Services Division (RSD) and Kansas City’s Financial and Overview staff are gearing up to evaluate up to eight requests from 2006 RY PRP-eligible AIPs after the 2006 RY annual settlement in February 2007. RSD is finalizing a Managers Bulletin that will provide clarification and guidance regarding PRP payment authorization requests for 2006.

An agriculture appropriations act was not enacted for the 2007 fiscal year. Therefore, RMA and most federal departments and agencies continue to operate under a “Continuing Resolution” (CR). The current CR expires in mid-February and Congress is considering a CR for the remainder of the 2007 FY. If Congress fails to include language in the next CR that restricts in some manner the administration of PRP for the 2008 RY, RMA would administer PRP under the terms of the PRP regulations promulgated in July 2005.

Regulatory Update:

Combination Regulation Update – The Product Administration and Standards Division (PASD) is in the process of responding to all public comments and making appropriate changes to the final rule. The final rule is targeted for Office of General Counsel (OGC) review and approval in late February 2007. The final rule is to be effective for the 2009 crop year.

Mustard Crop Provisions – On November 16, 2006, the proposed rule published in the *Federal Register* converts the Mustard pilot crop insurance program to a permanent program. The proposed rule comment period ended January 16, 2007. The final rule is targeted for the 2008 crop year.

Cabbage Crop Provisions – On November 16, 2006, the proposed rule published in the *Federal Register* converts the Cabbage pilot crop insurance program to a permanent program. The proposed rule comment period ended January 16, 2007. The final rule is targeted for the 2009 crop year.

Grape and Table Grape Crop Provisions – On September 29, 2006, the draft proposed rule was sent to AIPs for comment.. PASD is reviewing comments and incorporating appropriate changes into the draft proposed rule. The rule is targeted for the 2009 crop year.

Fresh Market Sweet Corn – On September 29, 2006, the proposed rule public comment period for Fresh Market Sweet Corn ended. PASD is preparing responses to the comments and drafting the final rule. The final rule updates the policy to reflect expansion of the program to select states and counties. The final rule is targeted for the 2008 crop year.

Mint Crop Provisions - The rule converts the mint program from a pilot program to a permanent program based upon FCIC Board action. Also, PASD is working to address OGC’s comments to the

final rule. The final rule is targeted for the 2008 crop year.

Northern Potato Crop Provisions and Southern Potato Crop Provisions – On September 26, 2006, the proposed rule public comment period for Northern Potato Crop Provisions and Southern Potato Crop Provisions ended. PASD is in the process of preparing responses to the public comments and drafting the final rule. The rule makes changes to the Storage Coverage Endorsement and the process for determining production to count for claim purposes intended to improve program integrity and address audit recommendations. The final rule is targeted for the 2008 crop year.

Almond and Walnut Crop Provisions – The rule will reduce the age requirements for almond and walnut trees for crop insurance purposes. Currently, the final rule is with OGC for review and approval. The final rule is targeted for the 2008 crop year.

Millet Crop Provisions – On December 27, 2006, the proposed rule was published in the *Federal Register* that removes the indemnity reductions for unharvested acreage that has caused some producer concern for several years. The proposed rule comment period ends on February 26, 2007. The final rule is targeted for the 2008 crop year.

Florida Citrus Fruit – On November 27, 2006, the public comment period for the proposed rule for Florida Citrus Fruit ended. The proposed rule clarifies insurable citrus crops and provides coverage for wind damage on fresh fruit when in conjunction with a hurricane or tornado. Due to issues raised by comments to the proposed rule, RMA must conduct additional analysis before preparing the final rule. The final rule is targeted for the 2009 crop year.

Nursery Provisions – On December 12, 2006, the final rule was published in the *Federal Register* that clarifies the definition of nursery liners for insurance purposes and that the peak amount of insurance under the Peak Inventory Endorsement is limited to 200 percent of the amount of insurance established under the Nursery Crop Insurance Provisions. The final rule will be in effect for the 2008 crop year.

Coverage Enhancement Option (CEO) – The proposed rule is with OGC for review and approval. The proposed rule would convert the pilot program to a permanent program option. Currently, the CEO is only offered in Texas for citrus trees. The final rule is targeted for the 2008 crop year.

Cultivated Wild Rice – Comments from Approved Insurance Providers to the draft proposed rule for Cultivated Wild Rice are under review with appropriate changes incorporated to the proposed rule. The rule converts the cultivated wild rice program from a pilot program to a permanent program. The projected implementation is for the 2009 crop year.

Contracted Tobacco – Currently, the proposed rule rewrites and renames the current Guaranteed Tobacco Crop Provisions to the Contracted Tobacco Crop Provisions reflecting the elimination of tobacco quotas. The revised regulation will eliminate the Quota Tobacco Crop Provisions as well. Right now, the proposed rule is with OGC for review and approval. The final rule is targeted for the 2008 crop year.

Program Highlights/Announcements:

California Freeze Update: Over the weekend of January 14, 2007, a freeze swept through the state of California bringing record low temperatures and heavy damage to the citrus crop. Damage has been reported in San Joaquin valley (Madera, Fresno, Tulare, and Kern Counties) in addition to the town of Porterville (in Southern Tulare County). For the California citrus crop, there are 3,109 policies earning premium. RMA has 202,679 citrus acres insured with a total liability of \$311,181,568 for the state of California. In addition to citrus, damage has been reported on avocados, strawberries, and nursery. The agency continues to assess and investigate the freeze damage that occurred.

FFA Risk Management Writing Contest - RMA sponsored the FFA Risk Management Writing Contest that was kicked off at the National Convention last Fall in Indianapolis, Indiana. The deadline for essay submissions is January 31, 2007. A panel of reviewers will review the top 33 essays mid-February 2007. The top 10 winners will be recognized by RMA in May 2007 when they visit Washington, DC.

Florida State Department of Insurance Hurricane Assessment - The Florida State Board of Administration (SBA) issued a draft rule authorizing the Office of Insurance Regulation (OIR) to impose an assessment to replenish the funding for the Florida Hurricane Catastrophe Fund (FHCF). The proposed assessment is one percent of the insured's premium, must be paid by the insured, and was to take effect January 1, 2007. RMA and some of the approved insurance providers filed written challenges to the assessment against Federally reinsured MPCCI premium asserting that it is actually a premium tax, which is precluded by section 511 of the Federal Crop Insurance Act. In November 2006, the companies were granted a motion for temporary injunction and have filed a motion for summary judgment.

Improving Program Access - To improve access to crop insurance services and programs for persons with limited English proficiency, RMA and NCIS have developed plans to capture, disclose, and increase awareness of agents who speak multiple languages as well as reaching the hearing impaired and blind. The Agent Locator on the RMA website will note the languages or services that the agent speaks or accommodations the agent is able to provide. Participation in the program by agents is voluntary. It is anticipated that software modifications will be completed by May, followed by notices to the companies and a promotional pieces in NCIS publications and through the Regional Offices.

Conflict of Interest Update - Section IV.f.4. of the Standard Reinsurance Agreement (SRA) outlines policies and procedures regarding conflict of interest with respect to loss adjustment. As part of these provisions, reinsured companies must disclose to FCIC any business, financial, legal, or familial relationship between anyone in the company or its affiliates and a policyholder or anyone with a substantial interest in the policyholder. On July 14, 2006, the Reinsurance Services Division (RSD) circulated a draft Managers Bulletin to provide guidance to approved insurance providers regarding Conflict of Interest disclosures by company employees, agents, and loss adjusters. RSD has received and evaluated comments from the industry and is finalizing a new draft based on industry feedback.

2007 Request for Applications (RFA) – Presently, the 2007 (FY) Request for Applications announcements for Targeted States, Commodity Partnerships, and Commodity Partnerships Small Sessions are being drafted. As discussed during the last Board meeting, there is a concern that

producers are not aware of the products, programs, and pilots that are available to them. The Board felt that Risk Management Education Division (RMED) should be complimenting R&D projects by providing “education and information” on the new tools and products. As recommended by the Board, RME has taken steps to revise the RFA to include priorities for each region that will compliment current products, programs, and pilots that have been approved for use by the Board.

Payment by Cooperatives and Trade Associations - Section 508(b)(5)(B) of the Federal Crop Insurance Act authorizes benefits to be provided to producers through cooperatives and trade associations as an exception to the Standard Reinsurance Agreement’s (SRA) anti-rebating provisions. The crop insurance industry has shown increasing interest in providing such benefits, especially in light of PRP developments. Therefore, on January 9, 2007, RMA sent a draft Manager’s Bulletin and procedures to all AIP’s for review and comment by January 19, 2007. These procedures, when finalized, would be used by RMA to administer benefits provided to producers under the authority of section 508(b)(5)(B).

Livestock Price Reinsurance Agreement (LPRA) - RMA contracted with Watts and Associates, Inc. to conduct a study of the Federal livestock insurance program, including the Livestock Price Reinsurance Agreement (LPRA). RSD is evaluating the recommendations of the study regarding the LPRA, and incorporating appropriate recommendations into a draft LPRA for the 2008 reinsurance year.

Financial Review Staff and National Association of Insurance Commissioners (NAIC) Coordinate Efforts - The Financial Review Staff enhanced and fostered a stronger ongoing reciprocal relationship with the National Association of Insurance Commissioners and State Insurance Regulators. A significant tangible benefit from these efforts is NAIC agreement to provide data directly to RMA, thus alleviating companies from providing duplicate data to RMA already being provided to NAIC. To quantify the effect, companies will have eight less reports to provide RMA in their Plan of Operations as a result. Also, the enhanced working relationship has yielded benefits to both RMA and NAIC in communication, training, and oversight of approved insurance providers. On a quarterly basis, NAIC provides vital and detailed regulatory information about AIPs that is incorporated to RMA’s review protocol.

National Financial and Operations Reviews (NFOR) – The Financial Review Staff provides financial and operational oversight over all AIPs and managing general agencies participating in the Federal crop insurance program. Financial and operational oversight includes analyzing and assessing the financial and operational performance of all AIPs. The staff continued to enhance its financial oversight of all 16 approved insurance providers by leading and conducting five full on-site National Financial Operations Reviews, 16 AIP annual financial analysis reviews, 64 AIP quarterly financial analysis reviews, two new company financial analysis reviews, and one new company orientation. The Financial Review Staff continues to be on target with its goal of conducting an on-site review of every AIP at least once every three years.

Financial Review Staff conducted on-site financial and operations reviews of the following companies for 2006:

- American Agri-Business Insurance Company/ARMtech Insurance Services
- Occidental Fire & Casualty Company of NC/Crop 1 Insurance Direct
- Farm Bureau Mutual Insurance Company
- Great American Insurance Company
- Westfield Insurance Company/John Deere Risk Protection

FY 2005 Agreement Closeout – The Risk Management Education Division (RMED) is reviewing final project reports from partners and the closeout process has begun for the FY 2005 agreements, which ended September 30, 2006.

FY 2006 Agreements - First quarter progress reports are being reviewed and quarterly conference calls are being conducted with the respective regional office, partner, and RMED staff.

Compliance:

2007 Compliance Goals Announced – The Deputy Administrator for Compliance and the Regional Compliance Directors have set their goals for 2007 Fiscal Year as follows:

- Improve & Revitalize Farm Service Agency (FSA) Spot Check Program Implementation
- Better Control Over and Reporting Of Company Quality Control Reviews
- Enhance Stakeholder and Public Awareness of Program Integrity (Compliance) Activities
- Improve Internal Quality Control
- Strengthen and Support Company Efforts to Combat Waste, Fraud, & Abuse

National Crop Insurance Services (NCIS) National Claims Managers Conference – On January 11, 2007, the Deputy Administrator addressed the NCIS National Claims Managers Conference. At the event, the Deputy stressed the need for consistent and documented improvement in Approved Insurance Provider quality controls over crop insurance payments. The following are issues discussed:

1. National issues:

- Quality Controls:
- Data Mining:
- Resolution of the Montana GRP Rangeland dispute in favor of the AIPs;
- Peanut price lawsuit; and
- SRA violations and remedies.

2. Regional issues:

- Aflatoxin;
- Nursery salvage values;

- Hurricane Indemnity Program problems with causes of loss adjustments;
- Minimum yield restrictions; and
- Onion (and maybe Potato) sampling problems.

Hurricane Indemnity Program (HIP) Review – The Office of Inspector General for Audit (OIG) is continuing their review of the FSA administered HIP program. RMA provided loss data to FSA to assist with the determination of the disaster payments. RMA had initiated an inquiry into changes in the cause of loss data subsequent to the HIP announcement that made producers eligible for payments. RMA has shared the Cause of Loss Report with OIG and has further requested that CAE run a similar report to show policies where the “date of damage” was altered after the HIP program was announced. RMA will be distributing individual data mining results to each respective Approved Insurance Provider with a request for an explanation of why the cause of loss code was altered.

National Program Operations Reviews (NPOR) – Compliance has issued almost all of the initial findings on policies selected for the 2005 NOR reviews. These policy reviews help assess the insurance providers’ adherence to the Standard Reinsurance Agreement (SRA), quality control guidelines and approved policies and procedures. RMA conducts random policy reviews during the NOR to report an error rate to OMB under the requirements of the Improper Payments Information Act of 2002. RMA has issued the NOR procedures for conducting these reviews and will modify them as necessary based on the experience comments of the reviewers who have used them in the field.

Compliance offices conducted Operations Reviews of the following companies for 2006:

- Dallas – *Rain and Hail*
- Davis – *Crop USA*
- Indianapolis – *Country Mutual*
- Kansas City – *ProAg*
- Raleigh – *American Agricultural*
- St. Paul – *Farmers Crop Insurance Alliance (closeout)*

Compliance offices will conduct the following Operations Reviews for 2007:

- Dallas – *Farmers Mutual Hail of Iowa*
- Davis – *John Deere*
- Indianapolis – *Agriserve*
- Kansas City – *Heartland*
- Raleigh – *Agro National*
- St. Paul – *Farm Bureau Mutual*

Ongoing Investigations Update –

- In December 2006, Paul Wentworth, owner of Wentworth Agri Services of Loup City, Nebraska, was indicted in U.S. District Court on 33 criminal counts relating to more than \$6.7 million in falsified crop insurance payments from 1998 through 2002. This begins a new

chapter in an extensive effort by the Central Regional Compliance office in Kansas City to assist OIG and the US Attorney's office with this case.

- Bli Farms, Richard Bli, and the estate of James Bli were ordered to pay more than \$2.1 million for damages associated with false insurance claims in 1992, 1994 and 1995. The Blis were acquitted of criminal charges, but thanks to the efforts of the US Attorney's office, civil charges under the False Claims Act were brought against the Michigan Potato Farmer resulting in the civil judgment in which the actual damages to the government were trebled. Currently, RMA is considering the appropriate administrative sanctions to impose as a result of the judgment.

GAO Report on Fraud, Waste, and Abuse – This audit provided recommendations to RMA as to how we could improve compliance efforts. RMA agreed in principle with most of the GAO recommendations and agreed to proceed on the following items:

- Adjusting the producer spot-check list procedures to permit FSA to review fall seeded crops for the following year as opposed to the current year, which was ineffective. RMA discussed the possibility of separating the data mining algorithms for the fall and spring, but determined that essential data would be excluded in the process. Farm Service Agency has stated that without additional resources, it will be unable to perform 100 percent of the designated growing season inspections.
- Distributing to each AIP the listing of its policyholders whose tax identification numbers or shareholders with substantial beneficial interests did not reconcile with FSA's permitted entity file. RMA will formally require the AIPs to review the discrepancies under Appendix IV and report the results at some point in time
- Finalizing a quality control program for the AIPs intended to help RMA assess the effectiveness of the quality controls used by the AIPs. Also, RMA Compliance will continue to test AIP quality control programs during scheduled national operations reviews.
- Finalizing the ARPA-implemented sanctions regulations as soon as OGC has completed its review of the current draft. RMA informed GAO that the lack of these regulations had not hindered RMA from using the statutory authority to sanction some producers. However, getting the regulations in place should help improve the overall sanctions process.

###