



U.S. Department of Agriculture

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Office of Inspector General  
Financial and IT Operations

## **Audit Report**

### **Federal Crop Insurance Corporation/Risk Management Agency's Financial Statements for Fiscal Years 2003 and 2002**

Report No. 05401-12-FM  
November 2003

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UNITED STATES DEPARTMENT OF AGRICULTURE

OFFICE OF INSPECTOR GENERAL

Washington D.C. 20250



DATE: NOV 07 2003

REPLY TO  
ATTN OF: 05401-12-FM

SUBJECT: U.S. Department of Agriculture Federal Crop Insurance Corporation/Risk Management Agency's Financial Statements for Fiscal Years 2003 and 2002

TO: Ross Davidson  
Administrator  
Risk Management Agency

This report presents the auditors' opinion on the Federal Crop Insurance Corporation (FCIC)/Risk Management Agency (RMA) principal financial statements for the fiscal year ending September 30, 2003. Reports on FCIC/RMA's internal control structure and its compliance with laws and regulations are also provided.

Deloitte & Touche LLP, an independent certified public accounting firm, conducted the audit. We monitored the progress of the audit at all key points, reviewed the workpapers, and performed other procedures, as we deemed necessary. We determined the audit was conducted in accordance with generally accepted auditing standards, Government Auditing Standards (issued by the Comptroller General of the United States), and the Office of Management and Budget's Bulletin No. 01-02, "Audit Requirements for Federal Financial Statements."

It is the opinion of Deloitte & Touche LLP, that the financial statements present fairly, in all material respects, FCIC/RMA's financial position as of September 30, 2003, and its net costs, changes in net position, budgetary resources, and reconciliation of net costs to budgetary obligations for the year then ended, in conformity with generally accepted accounting principles. The consolidated financial statements of FCIC/RMA for the year ended September 30, 2002, were audited by other auditors whose report, dated December 15, 2002, expressed an unqualified opinion on those statements and included an explanatory paragraph that described the change in accounting policy discussed in Note 14 to the consolidated financial statements. The report on FCIC/RMA's internal control structure over financial reporting identified two material weaknesses related to information technology.

The report on compliance with laws and regulations disclosed two instances of noncompliance with financial management system requirements.

In accordance with Departmental Regulation 1720-1, please furnish a reply within 60 days describing the corrective actions taken or planned, including the timeframes to address the report's recommendations. Please note the regulation requires a management decision to be reached on all findings and recommendation within a maximum of 6 months from report issuance.

A handwritten signature in cursive script that reads "Richard D. Long". The signature is written in dark ink and is positioned above the printed name and title.

RICHARD D. LONG  
Assistant Inspector General  
for Audit



## INDEPENDENT AUDITORS' REPORT

The Inspector General  
U.S. Department of Agriculture and the  
Board of Directors of the Federal  
Crop Insurance Corporation

We have audited the accompanying consolidated balance sheet of the Federal Crop Insurance Corporation/Risk Management Agency ("FCIC") as of September 30, 2003 and the related consolidated statements of net cost, changes in net position, and financing, and the combined statement of budgetary resources (collectively referred to as the consolidated financial statements) for the year then ended. The consolidated financial statements are the responsibility of FCIC management. Our responsibility is to express an opinion on the consolidated financial statements based on our audit. The consolidated financial statements of FCIC for the year ended September 30, 2002 were audited by other auditors whose report, dated December 15, 2002, expressed an unqualified opinion on those statements and included an explanatory paragraph that described the change in accounting policy discussed in Note 15 to the consolidated financial statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the Office of Management and Budget ("OMB") Bulletin No. 01-02, *Audit Requirements for Federal Financial Statements*. Those standards and OMB Bulletin No. 01-02 require that we plan and perform the audit to obtain reasonable assurance that the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the 2003 consolidated financial statements present fairly, in all material respects, the financial position of FCIC as of September 30, 2003, and its net costs, change in net position, reconciliation of net costs to budgetary obligations, and budgetary resources for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

Our audit was conducted for the purpose of forming an opinion on the basic 2003 consolidated financial statements taken as a whole. The information in the Management's Discussion and Analysis, Supplementary Stewardship Information, and Required Supplementary Information sections are presented for the purpose of additional analysis and are not a required part of the basic 2003 consolidated financial statements, but is supplementary information required by accounting principles

generally accepted in the United States of America or OMB Bulletin No. 01-09, *Form and Content of Agency Financial Statements*. This supplementary information is the responsibility of FCIC management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit such information and, we do not express an opinion on it.

In accordance with *Government Auditing Standards*, we have also issued reports, dated October 30, 2003, on our consideration of FCIC's internal control over financial reporting and its compliance with certain provisions of laws and regulations. Those reports are an integral part of an audit performed in accordance with *Government Auditing Standards*, and should be read in conjunction with this report in considering the results of our audit.

Deloitte & Touche LLP

October 30, 2003



## INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

The Inspector General  
U.S. Department of Agriculture and the  
Board of Directors of the Federal Crop Insurance  
Corporation

We have audited the consolidated balance sheet of the Federal Crop Insurance Corporation/Risk Management Agency ("FCIC") as of September 30, 2003, and the related consolidated statements of net cost, changes in net position, and financing, and the combined statement of budgetary resources (collectively referred to as the consolidated financial statements), and have issued our report thereon dated October 30, 2003. We conducted our audit in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget ("OMB") Bulletin No. 01-02, *Audit Requirements for Federal Financial Statements*.

In planning and performing our audit, we considered FCIC's internal control over financial reporting by obtaining an understanding of FCIC's internal control, determined whether internal controls had been placed in operation, assessed control risk, and performed tests of controls in order to determine our auditing procedures for the purpose of expressing our opinion on the consolidated financial statements. We limited our internal control testing to those controls necessary to achieve the objectives described in OMB Bulletin 01-02. We did not test all internal controls relevant to operating objectives as broadly defined by the *Federal Managers' Financial Integrity Act of 1982*, such as those controls relevant to ensuring efficient operations. The objective of our audit was not to provide assurance on internal control. Consequently, we do not provide an opinion on internal control over financial reporting.

Our consideration of internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be reportable conditions. Under standards issued by the American Institute of Certified Public Accountants, reportable conditions are matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect FCIC's ability to record, process, summarize and report financial data consistent with the assertions of management in the consolidated financial statements. Material weaknesses are reportable conditions in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course

of performing their assigned functions. Because of inherent limitations in internal controls, misstatements due to error or fraud may occur and not be detected.

We noted certain matters, described in Exhibit I, involving the internal control over financial reporting and its operation that we consider to be reportable conditions. We believe that all of the reportable conditions are considered material weaknesses.

#### ADDITIONAL REQUIRED PROCEDURES

In addition, we considered FCIC's internal control over Required Supplementary Stewardship Information by obtaining an understanding of FCIC's internal control, determined whether these internal controls had been placed in operation, assessed control risk, and performed tests of controls as required by OMB Bulletin No. 01-02. Our procedures were not designed to provide assurance on internal control over Required Supplementary Stewardship Information, and, accordingly, we do not provide an opinion on such controls.

With respect to internal control related to performance measures reported in the Management's Discussion and Analysis section of the consolidated financial statements, we obtained an understanding of the design of significant internal controls relating to the existence and completeness assertions, as required by OMB Bulletin No. 01-02. Our procedures were not designed to provide assurance on internal control over reported performance measures, and, accordingly we do not provide an opinion on such controls.

We also noted other matters involving internal control and its operation that we have reported to management of FCIC in a separate letter dated October 30, 2003.

This report is intended solely for the information and use of FCIC management, the Department of Agriculture's Office of the Inspector General, OMB and Congress, and is not intended to be and should not be used by anyone other than these specified parties.

*Deloitte* : *Turned up*

October 30, 2003

FEDERAL CROP INSURANCE/RISK MANAGEMENT AGENCY  
MATERIAL WEAKNESSES IN INTERNAL CONTROL

***Finding No. 1 - Information Technology Security Controls***

The security of FCIC's financial data is considered to be at risk due to weaknesses related to its control and oversight over access to its information systems. These security weaknesses subject the agency to the risk of inadvertent or deliberate misuse, fraudulent use, improper disclosure, or destruction of data, which may occur without detection. These weaknesses occurred because policies and procedures either were not in place or were not functioning adequately.

Our testing of key controls over security administration and review of work performed by the Office of Inspector General noted security related control weaknesses in the areas of (1) ineffective user access administration controls over the computing environment, (2) inappropriate use of generic account IDs, (3) excessive super user access privileges and (4) inadequate control of physical security to the data center.

In addition, control weaknesses related to IT security were noted at NFC in the areas of (1) inadequate review of access controls and violation monitoring, (2) inadequate security policies and plans and (3) lack of certification and accreditation of general support systems.

**Recommendation No. 1 - We recommend the following actions to FCIC management:**

- a. Enforce newly implemented security policies, formalize drafted policies and continue developing additional identified policies. Responsibilities addressed in the security policies should reflect appropriate segregation of duties and oversight functionality. Security policies were not in place for the majority of the fiscal year; however significant progress was noted at the time our testing. Three policies had been formalized and several more were drafted.
- b. Define and adhere to strict access administration controls. Management has made significant progress in access administration. In addition to administration controls, security procedures should include a periodic review of user IDs and access levels to monitor the effectiveness of existing controls.
- c. Continue to increase efforts to eliminate generic and/or shared user IDs. Generic and shared user IDs do not provide appropriate accountability. FCIC management has implemented procedures to request, approve and document user IDs with super user and domain administrator access rights. These procedures should prohibit the use of shared IDs with extended privileges.
- d. Re-evaluate agreements with the Farm Services Administration ("FSA") regarding access to the data center. Contracts should include appropriate measures to verify the effectiveness of FSA controls in place to restrict physical access to the data center.
- e. Formalize security violation monitoring procedures. Formal procedures should include defining and assigning responsibilities, logging violations and follow up, and appropriate escalation procedures and notifications. Scheduled vulnerability scans should be required and stated in the policy. At the time of our testing, FCIC management had conducted an internal



vulnerability scan. Additionally, informal procedures were in place to review violation reports daily and escalate exceptions to the system administrator.

### ***Finding No. 2 - Application Program and System Software Change Controls***

Material weaknesses were noted in application program change controls which cover specific application systems. Weaknesses include: (1) inappropriate access capabilities by application programmers and system support staff to production data; (2) inadequate test environments that are not separate of production systems (3) inadequate segregation of duties for approving, performing, testing and documenting application program changes; and (4) inadequate version controls. These weaknesses may cause unauthorized or invalid program and operating system changes to be placed into production. These weaknesses occurred because policies and procedures were either not in place or not functioning adequately.

The OIG performed a review of the internal control structure of the NFC and identified control weaknesses related to (1) system software change controls (2) inadequate controls to test system software changes; and (3) inadequate configuration controls for the mainframe environment.

**Recommendation No. 2 - We recommend the following actions to FCIC management:**

- a. Implement enterprise-wide application change management procedures. Consistent procedures and levels of documentation should be required across all development teams. Informal change management procedures are followed for each application group. The Project Tracking System has been implemented and is utilized to centralize documentation for most groups, but the level of documentation varies by application.
- b. Structure formal application change management procedures to provide appropriate segregation of duties. Programmers should not be allowed access to production environments. Increased efforts to restrict access were noted, and should be continued. Management should ensure test environments exist separate of the production environment to provide further means of restricting programmer's access.
- c. Implement stricter version control procedures for application change management. Management identified the need for version control prior to our testing and is in the process of incorporating Synergy software.



## INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH LAWS AND REGULATIONS

The Inspector General  
U.S. Department of Agriculture and the  
Board of Directors of the Federal Crop Insurance  
Corporation

We have audited the consolidated balance sheet of the Federal Crop Insurance Corporation/Risk Management Agency ("FCIC") as of September 30, 2003, and the related consolidated statements of net cost, changes in net position, and financing, and the combined statement of budgetary resources (collectively referred to as the consolidated financial statements), and have issued our report thereon dated October 30, 2003. We conducted our audit in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget ("OMB") Bulletin No. 01-02, *Audit Requirements for Federal Financial Statements*.

The management of FCIC is responsible for complying with laws and regulations applicable to the agency. As part of obtaining reasonable assurance about whether FCIC's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of financial statement amounts, and certain other laws and regulations specified in OMB Bulletin No. 01-02, including the requirements referred to in the *Federal Financial Management Improvement Act of 1996* ("FFMIA"). We limited our tests of compliance to provisions described in the preceding sentence, and we did not test compliance with all laws and regulations applicable to FCIC. However, providing an opinion on compliance with all laws and regulations was not an objective of our audit and, accordingly, we do not express such an opinion.

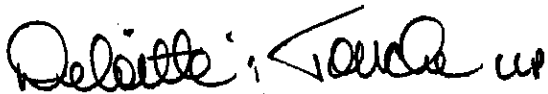
The results of our tests of compliance with the laws and regulations described in the preceding paragraph, exclusive of FFMIA, disclosed instances of noncompliance, described in Exhibit II, that are required to be reported under *Government Auditing Standards* and OMB Bulletin No. 01-02.

Under FFMIA, we are required to report whether FCIC's financial management systems substantially comply with the Federal financial management systems requirements, applicable Federal accounting standards, and the United States Government Standard General Ledger at the transaction level. To meet this requirement, we performed tests of compliance with FFMIA Section 803(a) requirements.

The results of our tests disclosed instances, described in Exhibit II, where FCIC's financial management systems did not substantially comply with Federal financial management systems requirements.

The results of our tests disclosed no instances in which FCIC's financial management systems did not comply with Federal accounting standards or the United States Government Standard General Ledger at the transaction level.

This report is intended solely for the information and use of FCIC's management, the Department of Agriculture's Office of Inspector General, OMB, and Congress, and is not intended to be and should not be used by anyone other than these specified parties.

Handwritten signature in cursive script, appearing to read "Deloitte Touche".

October 30, 2003

FEDERAL CROP INSURANCE/RISK MANAGEMENT AGENCY  
NONCOMPLIANCE WITH LAWS AND REGULATIONS

***Finding No. 3 - Establishment of a Continuous Monitoring System over Financial Management Systems***

The FFMLA does not establish financial system requirements. However, it does establish a statutory requirement for agency-heads to assess, on an annual basis, whether their financial management systems comply with the three requirements of the FFMLA. If they do not comply, agencies are required to develop remediation plans and file them with OMB. In addition, OMB's Revised Implementation Guidance for the FFMLA, dated January 4, 2001 recognizes OMB Circular A-127, *Financial Management Systems*, as a reference document for government-wide financial management systems. Reviews of financial management systems performed in accordance with OMB Circular A-127 provide the basis for agency management's annual assurance statements for Section 4 of the *Federal Managers' Financial Integrity Act (FMFLIA)* and the FFMLA.

OMB Circular A-127, Section 7, paragraph G provides that agency financial management systems shall conform to existing applicable functional requirements as defined in the Federal financial management systems requirements issued by the Joint Financial Management Improvement Program ("JFMIP"). Section 9, paragraph A3 of OMB Circular A-127 provides that each agency shall ensure appropriate reviews are conducted of its financial management systems and these reviews must determine whether agency financial management systems comply with the Federal financial management systems required by the JFMIP.

OMB Circular A-123, Section III, Assessing and Improving Management Controls, provides that agency managers should continuously monitor and improve the effectiveness of management controls associated with their programs. OMB Circular A-123 also provides that this continuous monitoring, and other periodic evaluations, should provide the basis for the agency head's annual assessment of and report on management controls, as required by the FMFLIA.

FCIC management has not fully implemented a continuous monitoring effort to ensure that its financial management systems comply with the Federal financial management system's requirements in support of its annual assurance statement made under Section 4 of the FMFLIA. As a result, FCIC management cannot provide reasonable assurance that its financial management systems comply with Federal financial management systems requirements as required by the FFMLA. During fiscal year 2003, FCIC management has reviewed its financial management systems using JFMIP checklists and has committed to implement an independent, comprehensive monitoring effort to ensure financial management systems comply with Federal requirements by December 31, 2003.

**Recommendation No. 3** -We recommend that management continue to refine and implement its continuous monitoring effort in order to ensure its financial management systems comply with the requirements of FFMLA and OMB Circular A-127.

***Finding No. 4 - Financial Management Systems Five Year Plan***

FCIC management has not completed a financial management systems five-year plan, as required by OMB Circular A-127. FCIC management has completed a draft of its financial management systems five year plan and is currently reviewing it internally for completeness and compliance with OMB Circular A-127 before it is finalized.

**Recommendation No. 4** -We recommend that FCIC management finalize the financial management systems five year plan, once all necessary reviews have been completed.

FEDERAL CROP INSURANCE CORPORATION  
RISK MANAGEMENT AGENCY  
CONSOLIDATED FINANCIAL STATEMENTS  
AS OF SEPTEMBER 30, 2003 and 2002

## MANAGEMENT'S DISCUSSION AND ANALYSIS

### Mission and Organizational Structure

#### Organizational Structure

The Federal Crop Insurance Corporation (FCIC) is a wholly-owned government corporation created February 16, 1938 (7 U.S.C. 1501). The program was amended by Public Law (P.L.) 96-365, dated September 26, 1980, to provide for nationwide expansion of a comprehensive crop insurance program.

The Risk Management Agency (RMA) was established under provisions of the Federal Agriculture Improvement and Reform Act of 1996 (1996 Act), P.L. 104-127, signed April 4, 1996. The 1996 Act amended the Department of Agriculture Reorganization Act of 1994 (1994 Act), P.L. 103-354, Title II, by requiring the Secretary of Agriculture (the Secretary) to establish within the U.S. Department of Agriculture (USDA) an independent office responsible for supervision of the FCIC, administration and oversight of programs authorized under the Federal Crop Insurance Act, such as any pilot insurance plans or other programs involving revenue insurance, risk management education, risk management savings accounts, or the use of the futures markets to manage risk and support farm income that may be established under the Federal Crop Insurance Act or other law; and any other programs the Secretary considers appropriate. The Federal Crop Insurance Act as amended through 2002, is hereafter referred to as the Act.

#### Mission

The purpose of the FCIC and RMA, (hereafter the combined entities will be referred to as the FCIC), is to promote the national welfare by improving the economic stability of agriculture through a sound system of crop insurance and other risk management tools. Stabilizing rural communities through an actuarially sound system of crop insurance has been an important public policy of the United States for over half a century. The FCIC is committed to transforming yesterday's crop insurance program into a broad-based safety net for producers to assure American agriculture remains solid, solvent, and globally competitive through the twenty-first century.

The objectives include the following items:

- Increase the number of economically sound risk management tools that are available and utilized by producers to meet their needs;
- Increase the agricultural community's awareness of risk management alternatives; and
- Improve program integrity and protect taxpayers' funds.

#### Regulatory Acts Impacting the FCIC

The Farm Security and Rural Investment Act of 2002 (2002 Farm Bill) was signed into law on May 13, 2002. Major provisions of this new legislation included: Authorization for sweetpotato insurance to extend beyond the time the crop is in the field (as in the case of tobacco and potatoes) and expansion of the Adjusted Gross Revenue Insurance pilot program into additional counties in California and Pennsylvania.

The President signed the Agricultural Risk Protection Act of 2000 (ARPA) into law on June 20, 2000. Major provisions of this new legislation included: expanded use of contracts and partnerships for the research and development of policies and other risk

management tools; revised Catastrophic Risk Protection (CAT) administrative fees and loss adjustment expense reimbursements; significantly revised premium subsidies; livestock coverage authorization; reimbursement of research, development, and maintenance costs for products submitted to the Corporation; expanded risk management education and assistance; funds to address under-served areas, States, and commodities; an expert review panel and procedures for reviewing policies, plans of insurance, and related material or modifications; improved program compliance and integrity provisions; acceptance of electronic information; limitations of multiple insurance benefits on the same acreage in the same crop year; prevented planting; substitution of yields in a producer's actual production history; provisions specifying that good farming practices include scientifically sound sustainable and organic farming practices; a reconsideration process regarding good farming practice determinations; and others not included herein.

On June 30, 2000, FCIC published an Interim Rule in the Federal Register to amend the regulations for the Common Crop Insurance Policy and Group Risk Plan of Insurance Basic Provisions and the CAT Endorsement, effective for the 2001 crop year, to implement the changes in the administrative fees and subsidies and the substitution of yields in the producer's actual production history mandated by ARPA. These changes were also made in the crop insurance policies for other plans of insurance, such as Crop Revenue Coverage (CRC), Revenue Assurance (RA), and Income Protection (IP).

On September 18, 2002, FCIC published a Proposed Rule followed by a Final Rule published in the Federal Register on June 25, 2003, effective for the 2004 crop year for all crops with a contract change date on or after June 30, 2003. The Final Rule amended the Common Crop Insurance Policy and Group Risk Plan of Insurance Basic Provisions to implement the remaining policy changes required by ARPA. These changes included limitations of multiple insurance benefits on the same acreage in the same crop year, prevented planting, good farming practices including organic and sustainable farming practices, and a reconsideration process regarding good farming practice determinations. These changes were incorporated in the crop insurance policies for other plans of insurance, such as CRC, RA, and IP.

### **Business Overview**

Federal crop insurance is available to producers through private insurance companies that market and service policies upon which those companies also share in the risk. The amount of risk they share is defined by reinsurance agreements with the FCIC. Under these agreements reinsured companies agree to deliver risk management insurance products to eligible entities under certain terms and conditions. Reinsured companies are responsible for all aspects of customer service and guarantee payment of premium to FCIC. In return, FCIC reinsures the policies and provides a subsidy for administrative and operating expenses associated with delivering the insurance products and/or programs. FCIC also provides a subsidy for producer's premium. This constitutes a joint effort between the Government and the private insurance industry for program delivery.

Approximately 1.3 million policies were written in crop years 2003 and 2002 with an estimated \$1.40 billion and \$1.21 billion in farmer paid premium for crop years 2003 and 2002 and an estimated \$2.09 billion and \$1.79 billion in estimated premium subsidies for crop years 2003 and 2002. For the 2003 and 2002 crop years, an estimated \$4.0 billion and \$4.3 billion were to be paid in indemnities. For 2003 and 2002 crop year, \$ .6 billion and \$ 1.3 billion of appropriations were estimated to be used to pay indemnities in excess of premiums. Crop insurance was available for 88 different commodities (approximately 600 commodities as enumerated for disaster assistance purposes) for crop year 2003 and crop year 2002. Crop year 2003 and 2002 coverage was available in over 3,000 counties covering all 50 states and Puerto Rico.



The FCIC maintains two separate funds, one for administrative and operating purposes (A&O Fund), and one for the crop insurance and livestock program (Insurance Fund). The A&O Fund is used to pay salaries and other administrative expenses. The Insurance Fund is used to pay for crop and livestock losses specified in the policies. The Insurance Fund also pays for the reinsured companies administrative expenses associated with marketing and fully servicing the crop insurance policies written. Operating expenses of the reinsured companies are reimbursed by the FCIC. The premium costs of insured persons are also subsidized. The FCIC encourages future crop insurance participation by offering premium discounts to purchasers of crop insurance.

The reinsured companies process insurance documents, bill and collect premiums, and pay losses according to stipulations within the insurance policy and reinsurance agreement with the FCIC. The reinsured companies electronically transmit to the FCIC, at least monthly, all data required under the reinsurance agreement in order to receive their contracted reimbursements. R&D divisions, assist in processing all insurance data, record detailed accounting and statistical data, prepare the required accounting, statistical, and management reports for business from all sources, and collect all crop and accounting data needed for policy determinations, underwriting decisions, and financial management.

Ten regional offices formulate and recommend policies specific to the needs of the region for which each is responsible. They provide customer service, problem identification, resolution and/or referral, as well as assistance to delivery system partners regarding program issues related to underwriting and claims administration.

Six regional compliance offices provide assurance of program integrity by conducting program reviews and audits to assure mandates, policies and procedures are effective and are followed by persons involved in delivering crop insurance. The six field offices also conduct investigations into complaints alleging fraud or abuse of existing insurance programs. This ensures fair and equitable treatment of the farmer, taxpayer, and the FCIC.

### **Federal Crop Insurance Program - Activities**

The Federal crop insurance program comprises the following major activities:

- (1) Program Management includes the FCIC Board of Directors, the RMA Administrator's office and staff offices that report directly to the RMA Administrator.
- (2) Research and Development (R&D) involves the design and development of crop insurance programs, policies and standards, and the establishment and maintenance of rates and coverages for crops in each county. This activity also includes: 1) analysis of insurance experience and risk; 2) evaluation and establishment of setting crop insurance price elections; 3) production and dissemination of actuarial data, documents, and files; 4) the evaluation of current crop insurance plans and policies; and 5) development of strategies for increasing participation in the crop insurance program. This function handles products submitted under section 508(h) of the Act that must be reviewed and evaluated and if enacted, must be deployed and maintained like other risk management

products. With the passage of the Agricultural Risk Protection Act of 2000, effective fiscal year 2001, the design and development of risk management commodity programs are now done through contracts and partnerships with other organizations under RMA's oversight.

- (3) Insurance Services has responsibility for delivering FCIC programs through a system of ten Regional Offices and reinsured companies. It provides support, information, and advice to the Office of the Administrator; delivers risk management education programs to producers through private and public education partners; coordinates FCIC responses to emergency situations; maintains existing FCIC products through field underwriting assessments; assists in new product development; and supports FCIC civil rights and outreach initiatives. Headquarters staff complement field activities by ensuring consistent application of actuarially sound insurance principles in field-level underwriting and by monitoring a uniform system of loss adjustment.
- (4) Compliance provides program oversight and quality control of the reinsured companies. It ensures the integrity of the crop insurance program through reviews of reinsured companies' operations and ensures the delivery of crop insurance is in accordance with applicable laws, regulations, and procedures. There are six Regional Compliance Offices that provide assurance of program integrity by conducting program reviews and audits to assure mandates, policies and procedures are effective and are followed by persons involved in delivering crop and livestock insurance. The Compliance offices conduct investigations into complaints alleging fraud or abuse of existing insurance programs. This ensures fair and equitable treatment of the farmer, taxpayer, and the FCIC.
- (5) Ten Regional Offices formulate and recommend policies specific to the needs of the region for which each is responsible. They provide customer service, problem identification, resolution and/or referral, as well as assistance to delivery system partners regarding program issues related to underwriting and claims administration.

## **Federal Crop Insurance Program – Insurance Plans**

### **Revenue Based Crop Insurance Plans**

CRC was developed by a private insurance company and first submitted to the FCIC Board for approval in 1995 for the 1996 crop year. RA was developed by another private insurance company and submitted to the FCIC Board for approval in 1996 for the 1997 crop year. IP was developed in 1997 by the FCIC. These plans respond to the directive of the 1994 Act which directed the FCIC to develop a pilot crop insurance program which provided coverage against reduced gross income as a result of a reduction in yield or price, and has generally been improved and/or expanded each year. The FCIC Board of Directors approved, for the 1999 crop year, a fourth plan, Group Risk Income Protection (GRIP), submitted by another private company.

CRC, RA, and IP have many similar features. These programs guarantee revenue by insuring yield and price variability. Indemnities are due when any combination of yield and price result in revenue that is less than the revenue guarantee. CRC, RA, and IP plans are similar because they use many of the same policy terms and conditions of the Multiple Peril Crop Insurance (MPCI) plan of insurance that uses Actual Production

History (APH). APH provides the yield component and a yield forecast through the insureds records of historic yields. It also provides a documented process to determine the yield for the insurance period.

GRIP offers producers a guarantee against decline in county revenue, which is based on the Chicago Board of Trade futures prices and National Agricultural and Statistics Service county yields as adjusted by the FCIC. The GRIP policy provides coverage on an enterprise unit basis. The amount of any loss will be finalized when the final county yields and harvest price are known in the spring following the crop year. The GRIP policy contains no replant, late, or prevented planting provisions.

The extension of the traditional MPCII protection that includes price variability allows FCIC to provide revenue protection for all products. The price component common to the CRC, RA, IP, and GRIP plans is that these plans use the commodity futures market for price discovery. Price discovery occurs twice in the CRC, RA, IP and GRIP plans: first, before the insurance period (Projected, Base or Expected Price) to establish the revenue guarantee and premium, and second, at harvest time (Fall Harvest Price, Harvest Price). CRC provides increased protection when the Harvest Price is above the Base Price. The RA plan of insurance has the Fall Harvest Price Option available. If selected by the producer, it provides increased protection when the Fall Harvest Price is greater than the Projected Harvest Price. All revenue insurance plans pay the insured producer an indemnity when any combination of harvested and appraised yield and Harvest Price (Fall Harvest Price) results in revenue that is less than the revenue guarantee.

#### Adjusted Gross Revenue:

AGR is a whole-farm revenue pilot program that bases the revenue coverage on 5-years of farm income tax records (Schedule F). It covers revenue from all agricultural commodities except for animals raised for sport, show, or pets and timbers, forest or forest products produced by the insured. It provides revenue coverage for producers with a limited amount of income from animals and animal products (35 percent). AGR is currently available in 230 counties in 18 states. In 2003, participation data indicates 979 policies written, a \$292.6 million liability and \$12.6 million in premiums.

#### Crop Revenue Coverage Insurance plan:

For the 2004 crop year, the CRC plan of insurance will offer coverage for corn in 45 states, cotton in 19 states, grain sorghum in 25 states, rice in 7 states, soybeans in 32 states, and wheat in 39 states.

#### Group Risk Income Protection:

Prior to 2003, GRIP corn and soybean insurance had been available only for the states of Illinois, Indiana, and Iowa. The GRIP program was expanded to include counties in Michigan and Ohio that have been approved for GRP coverage for corn and soybeans. The expansion will add 36 GRIP corn counties and 34 GRIP soybean counties in Michigan, and will add 61 GRIP corn counties and 52 GRIP Soybean counties in Ohio. The expansion extended coverage to approximately 210,000 acres of corn in the two states and approximately 200,000 acres of soybeans.

#### Income Protection:

IP is designed to protect producers against reductions in gross income when either a crop's price or yield declines from early-season expectations. For the 2004 crop year, the IP plan of insurance will offer coverage for barley in 7 states, corn in 3 states, grain sorghum in 1 state, soybeans in 4 states, and wheat in 8 states.

#### Revenue Assurance:

For the 2004 crop year the RA plan of insurance will provide coverage for feed barley in 6 states, malting barley in 5 state, canola/rapeseed in 3 states, corn in 19 states, cotton in 5 states, soybeans in 19 states, sunflowers in 6 state, rice in 2 states, spring wheat in 7 states and winter wheat in 15 states.

#### Revenue Products under section 508(h) of the Act

The following crop insurance products were submitted by private companies under the provisions of section 508(h) of the Act and approved by FCIC for the 2003 crop year:

- AGR-Lite is based on the AGR policy with some modifications. For example, AGR-Lite is available only to producers whose liability does not exceed \$100,000 and the 35 percent income limitation from animals and animal products has been removed. AGR-Lite is available in all counties in Pennsylvania with the exception of Philadelphia. In 2003, participation data indicates 75 policies written, a \$2.5 million liability and \$175,000 in premiums.
- Livestock Risk Protection (LRP) Fed and Feeder Cattle – As of July 10, LRP Feeder Cattle had 52 groups of cattle insured, for a total of 3,985 head of cattle. The total liability was \$2,407,163 with \$34,924 in total premiums. Policies had been sold in Iowa (2 policies in 2 counties), Kansas (14 policies in 10 counties), Nebraska (4 policies in 4 counties), Oklahoma (1 policy in 1 county), South Dakota (24 policies in 11 counties) and Texas (7 policies in 7 counties). Endorsements averaged 77 head of insured cattle, ranging from 3 head to 650 head at an average weight of 777 pounds. The average coverage level purchased was 93 percent.

As of July 10, LRP Fed Cattle had 4 groups of cattle insured, for a total of 224 head of cattle. The total liability was \$99,819 with \$1,907 in total premiums. Policies had been sold in Illinois (2 policies in 1 county) and Nebraska (2 policies in 2 counties). Endorsements averaged 56 head of insured cattle, ranging from 22 to 140 head at an average weight of 1,225 pounds. The average coverage level purchased was 94 percent.

- LRP Swine – For the 2003 reinsurance year LRP Swine had 588 groups of hogs insured, for a total of 183,916 head of hogs. The total liability was \$13,315,293 with \$692,779 in total premiums.
- Livestock Gross Margin (LGM) – LGM is a gross margin index, designed to protect profit margins for swine producers, and is based on three futures contracts: lean hog prices traded on the Chicago Mercantile Exchange (CME) minus feed costs using corn and soybean meal futures settlement prices at the Chicago Board of Trade (CBOT)).
- For the 2003 reinsurance year LGM has provided coverage for 148,273 head of

slaughter hogs with a liability of \$8,330,000. To date LGM premium is \$606,745 and total indemnities are \$19,493.

- Nutrient Best Management Practice (N-BMP) - The N-BMP insurance policy provides insurance protection from crop production loss when a producer applies a rate of fertilizer (nitrogen and/or phosphorus) recommended by a Best Management Practice (BMP). Except for fertilizer, producers must use the same farming practices on both the check strip and management unit. Based on an appraisal, if the production per acre on the check strip is greater than adjacent strips within the management unit, less a deductible (5 percent), the producer receives an indemnity.

## **Yield-based (APH) Insurance Plans**

### **Multiple Peril Crop Insurance**

These policies insure producers against losses due to natural causes such as drought, excessive moisture, hail, wind, frost, insects, and disease. The farmer selects the amount of average yield he or she wishes to insure; from 50 to 85 percent. The farmer also selects the percent of the predicted price he or she wants to insure; between 55 and 100 percent of the crop price is established annually by RMA. If the harvest is less than the yield insured, the farmer is paid an indemnity based on the difference. Indemnities are calculated by multiplying this difference by the insureds' percentage of the established price selected when crop insurance was purchased.

### **Group Risk Plan of Insurance:**

The GRP was created by FCIC as a risk management tool to insure against widespread loss of production of the insured crop in a county. It is primarily intended for use by those producers whose farm yields tend to follow the average county yield. Producers may select a coverage level of 65 percent for CAT, or a percentage ranging from 70 to 90 percent for buy-up coverage. The producer's coverage level percent is multiplied by the expected county yield shown on the actuarial documents to determine the trigger yield. If the payment yield that FCIC publishes for the insured crop year falls below an insured's trigger yield, they will receive a payment.

Producers may select a dollar amount of protection between 60 and 100 percent (except for CAT which is 45 percent) of the maximum protection per acre shown on the actuarial documents. This protection is provided for each acre of the crop planted by the acreage reporting date and shown on a producer's acreage report. The premium rates, practices, types, maximum protection per acre, and maximum subsidy per acre are also shown on the actuarial documents. FCIC issues the payment yield in the calendar year following the crop year insured. This yield is the official estimated yield published by the National Agricultural Statistics Service (NASS). Producers are paid if the payment yield falls below their trigger yield. The amount of payment per net insured acre is calculated by subtracting the payment yield from the trigger yield, dividing that quantity by the trigger yield, and multiplying that result by the producer's protection per acre for each net acre insured.

Covered crops currently include: barley, corn, cotton, forage, peanuts, sorghum, soybeans, wheat, and rangeland. All GRP crops are permanent programs, with the exception of rangeland, which remains a pilot program. For the 2003 crop year, one or more GRP crop programs were offered in 22 states. There were a total of 16,640 policies sold nationwide. The most policies were sold in Wisconsin with 2,218. Other states with significant GRP participation include: Illinois, Indiana, Iowa, Kentucky, Michigan, Ohio,

and Tennessee. The total acreage insured under GRP for 2003 was 12,472,178, with a total liability of \$1,137,455,138, and premium of \$35,624,030.

#### Dollar Plan:

RMA offers three different kinds of dollar plans: dollar revenue, dollar yield, and dollar asset. Typically, these plans set the amount of coverage using county average figures such as costs of production (COP) or other indicators. Indemnities are calculated using the actual results of each producer.

The dollar revenue plan provides protection against loss of revenue. Crops covered include blackberries, cherries, chili peppers, citrus (California), fresh-market tomatoes, beans, and sweet corn, peppers, processing cucumbers, raspberries, strawberries, and winter squash.

The dollar yield plan provides protection against a decline in the amount of the crop produced. Crops covered include hybrid seed corn and sorghum.

The dollar asset plan provides protection against the loss of a crop-producing asset, such as fruit trees, as well as certain crops. Coverage is provided for citrus trees (Texas), citrus fruit (Florida), clams, forage seeding, fruit trees (Florida), macadamia trees, nursery, raisins, and tropical fruit trees (Florida).

#### Pilot Programs

The FCIC currently has 32 pilot programs underway that implement legislation or test new and innovative crop insurance concepts. Pilot insurance plans and other risk management tools available for the 2003 crop year include AGR and AGR-Lite, apple pilot quality option, avocado actual production history, avocado revenue, avocado/mango trees, blueberries, cabbage, cherries, citrus (dollar), corn rootworm integrated pest management, coverage enhancement option, crambe, cultivated clams, cultivated wild rice, dairy options, Florida fruit trees, forage seed, fresh market beans, the IP plan of insurance, mint, mustard, onion pilot stage removal option, pecan revenue, processing chile peppers, processing cucumbers, rangeland (GRP), raspberry/blackberry, strawberries, sweet potatoes, and winter squash (including pumpkins).

#### Increase Participation and Program Growth

The FCIC continues to encourage producer acceptance and program participation through outreach and educational activities directed at informing the agricultural community of the "new risk environment" and how crop insurance is one component that can be used to mitigate potential losses. The FCIC's goals include ensuring that producers have sufficient information to adequately assess their own risk in today's uncertain agribusiness environment. Activities include participation in agricultural related events and expositions around the country and distributing the crop insurance industry's guide entitled, "Managing Risk - Being Prepared" Outreach and education on the crop insurance program and other risk management tools will increase under the mandate found in the 1996 Act.

### **Risk Management Education**

RMA continues to partner with the Cooperative State Research, Education, and Extension Service (CSREES), the Commodity Futures Trading Commission (CFTC), and the USDA National Office of Outreach, to provide Risk Management Education (RME) to U.S. farmers and ranchers, as mandated in Section 192 of the 1996 FAIR Act. In addition, the Agricultural Risk Protection Act of 2000 significantly increased RMA's role in delivering education and outreach programs.

The RME Division provides farmers with information and with educational opportunities to become more aware of risk, know the tools available to manage risk, and learn strategies for making sound risk management decisions.

RMA seeks to increase the agricultural community's awareness of risk management alternatives through education and information programs, an effort that was bolstered significantly with the passage of ARPA. ARPA provided RMA with the opportunity to expand its educational programs on several fronts.

- *Risk Management Education for Specialty Crops.* ARPA directs RMA to establish partnerships for the purpose of providing producers of specialty crops and under-served commodities with risk management training.
- *Crop Insurance Education for Targeted Region States.* ARPA authorizes and directs RMA to establish crop insurance education and information programs in states that have been historically under-served by the Federal crop insurance program. The 15 states designated by the Secretary that are eligible for this program are Maine, New Hampshire, Vermont, Connecticut, Massachusetts, Rhode Island, New York, New Jersey, Pennsylvania, Delaware, Maryland, West Virginia, Utah, Nevada, and Wyoming.
- *Competitive Grants for Risk Management Education.* This is a cross-cutting program administered by the CSREES using funding from the Federal Crop Insurance Fund.
- *Agricultural Management Assistance (AMA) Program.* This is another cross-cutting program authorized by ARPA that RMA administers jointly with the Natural Resource Conservation Service and the Agricultural Marketing Service.

### **Performance Goals, Objectives, and Results**

The key performance goals and results that follow were selected from RMA's revised fiscal year 2002 and initial fiscal year 2003 Annual Performance Plan and RMA's Strategic Plan for fiscal years 2000-2005.

#### **Strategic Goal: To strengthen the safety net for agricultural producers through sound risk management programs and education.**

The FCIC develops and delivers (in coordination with and through the private sector) a variety of risk management products to enable agricultural producers to manage their risks. These products help producers protect themselves from yield risks, market risks, or other risks faced in their farming operations. The FCIC's new legislative initiatives resulting from the passage of the ARPA further contribute to producers' ability to protect their financial stability, and comprise the major component of the safety net for agricultural producers. The ARPA includes significant changes in the manner in which

the FCIC accomplishes its goal, including expanded use of contracts and partnerships. These changes will expedite and strengthen the research and development process to enable new and innovative risk management tools to be utilized by producers. These tools go far beyond traditional crop insurance programs which in the past, have been the primary focus of the FCIC. These efforts, and the resulting new FCIC tools for producers will truly enable the FCIC to achieve its vision of transforming yesterday's crop insurance program into a broad-based safety net for producers through the 21<sup>st</sup> century. An expanded, comprehensive risk management education and outreach program will increase agricultural producers' awareness of their new and improved risk management opportunities. The FCIC's goal provides a solid foundation and direction for the future and is directly linked to the Secretary's Overview on Goal 1.1, "Provide an effective safety net and promote a strong and sustainable U.S. farm economy."

**Objective: 1.1 Increase the availability and utilization of economically- sound risk management tools to meet producers needs.**

Producers' needs are continuously being assessed by the FCIC and its private sector partners to ensure new and innovative risk management alternatives are available to meet producers' needs.

**Strategies for Achieving the Objective**

1. Assess needs and interest for risk management tools for producers of specific agricultural commodities.
2. Lead the contracting and partnership efforts to assist agricultural partners in the research, development, implementation, and maintenance of new tools such as revenue coverage, underserved commodities and areas, specialty crops, livestock, cost of production plans, and other non-traditional risk management products.
3. Maintain and continuously improve existing products.
4. Evaluate products and take appropriate actions.
5. Evaluate and improve process for private companies submitting and gaining approval/disapproval of alternative products.

**Performance Goal and Indicators:**

The following outcomes assess the effectiveness of the FCIC's contribution to the safety net for agricultural producers through utilization of risk management tools related to increasing the availability and utilization of economically-sound risk management tools to meet producers needs.



	Crop Year <sup>1</sup> 1999 Actual	Crop Year <sup>1</sup> 2000 Actual	Crop Year <sup>1</sup> 2001 Actual	Crop Year <sup>1</sup> 2002 Actual	Crop Year <sup>1</sup> 2003 Estimated
<b>Performance Goal:</b> Increase the availability and utilization of economically-sound risk management tools to meet producers needs.					
<b>Indicators:</b>					
Net acres insured (acres in thousands) 2005 Target = 226,163 acres insured	196,377 <sup>2</sup>	206,444 <sup>2</sup>	211,810 <sup>2</sup>	215,529 <sup>2</sup>	221,516
Number of insurance plans available (crop year data). 2005 Target = 149 insurance plans	138	146	147	147	149
Total insurance in force (dollars in thousands). 2005 Target = \$42,175,500 insurance in force	30,864,958	34,436,731 <sup>2</sup>	36,730,027 <sup>2</sup>	37,312,679 <sup>2</sup>	41,118,175
Total crop insurance premium (dollars in thousands). 2005 Target = \$3,743,900	2,304,695	2,540,022 <sup>2</sup>	2,961,225 <sup>2</sup>	2,915,870	3,485,000
Loss Ratio	105.00	102.00	98.92	139.00	116.00
Participation rate for acres covered by revenue insurance plans (percent) <sup>3</sup>					
- Under-served States	8.2	18.2	23.8	23.8	23.9
- Nationwide	27.0	31.8	42.2	42.2	42.4

**Objective 1.2: Increase the agricultural community's awareness of risk management alternatives.**

Through contracts and partnerships, the agricultural community will have available a comprehensive risk management education and outreach program. The FCIC will provide leadership, funding, and a strategy for institutionalizing this risk management program.

**Strategies for Achieving the Objective:**

1. Enhance the process to identify and reach underserved areas, States, commodities, producers, and other members of the agricultural community (e.g., farm publications, education courses, etc.).
2. Prepare and deliver RME products.

<sup>1</sup> For most crops, crop year is defined as: The period within which the insured crop is normally grown and designated by the calendar year in which the insured crop is normally harvested.

<sup>2</sup> Reflects actual to date. Source: 10/27/2003 FCIC Summary of Business Report.

<sup>3</sup> Revenue plans: CRC, GRIP, IP, RA -- Underserved States: CT, DE, ME, MD, MA, NH, NJ, NY, NV, PA, RI, UT, VT, WV, WY.

**Performance Goal and Indicators:**

The following outcomes assess the effectiveness of the FCIC's contribution to the safety net for agricultural producers through utilization of risk management tools related to increasing the agricultural community's awareness of risk management alternative.

	FY 2000 Actual	FY 2001 Actual	FY 2002 Actual	FY 2003 Estimated
<b>Performance Goal:</b> Increase the agricultural community's awareness of risk management alternatives.				
<b>Indicators:</b>				
Number of producers participating in RME activities being coordinated or facilitated by RMA throughout the U.S.	30,095	40,232	50,000	62,000
Total number of crop insurance policies in force (in thousands – crop year to date)	1,286	1,298	1,300	1,300
Total number of RME sessions being coordinated or facilitated throughout the U.S.	1,200	1,500	1,200	1,200

**Objective 1.3: Improve program integrity and protect taxpayer's funds.**

This objective is achieved by conducting internal and external reviews, investigations, program evaluations, and audits to address inherent program vulnerabilities, deter abuse, and minimize program costs. This will be done in coordination with private sector delivery partners, oversight bodies, and appropriate contracts and partnerships with others.

**Strategies for Achieving the Objective:**

1. Develop and maintain a system to continually evaluate and improve internal and external management controls.
2. Expand the use of contracts and partnerships in the evaluation of new and existing risk management tools, including the implementation of an expert panel to review products before they are sent to the FCIC Board of Directors, in accordance with the requirements of ARPA.
3. Implement the process identified in the Concurrence Process and Signature Authorities memo signed by the RMA Administrator to the Deputy Administrator for Research and Development on October 4, 2000, to ensure adequate review and concurrence of new risk management tools.
4. Review, improve, and maintain performance standards for delivery partners.
5. Implement and maintain a process to ensure evaluation of financial performance measures of various reinsurance agreements.
6. Develop and apply data mining and other state-of-the-art technology to compliance methodology.

**2003 and 2002 Crop Year Performance Measurements**

The FCIC's total estimated premium level for its reinsured business was \$3.49 billion for the 2003 crop year, with insured producers paying \$1.40 billion and the remaining \$2.09 billion paid in premium subsidies. The FCIC provided approximately \$41.1 billion of

insurance protection on about 1.3 million policies for approximately 837,000 insureds. These crop policies provide coverage for over 221.5 million acres, which are approximately 77.7% of the insurable acres nationwide. For the 2003 crop year policies, the FCIC estimates that approximately \$4.0 billion of indemnities will be paid to insureds on approximately 292,000 indemnity claims. For crop year 2002 policies, the FCIC paid approximately \$4.058 billion to insureds on approximately 293,000 indemnity claims. The loss ratio for 2003 is estimated to be 116.00% compared to the FCIC's actual loss ratio of 139.00% in 2002.

The FCIC has pursued several initiatives to improve actuarial soundness and contain costs within the MPCIC program. The FCIC has steadily followed direction provided by the Act, to increase the share of risk to private insurance companies. Also, the FCIC has gradually reduced the rate of reinsured company administrative expense reimbursement. FCIC continues to work with the private insurance industry to review issues under contract. The objectives of this effort include:

- To seek changes which will strengthen the program through greater participation,
- To determine more accurately the approximate cost of required activities to effectively deliver crop insurance,
- To identify currently required activities that may be prudently eliminated, and
- To identify activities which can be accomplished more efficiently.

The FCIC has increased the risk to private sector in the reinsurance agreement since passage of the Act. Following the major losses of the 1993 crop year when reinsured companies lost approximately \$83 million, the FCIC elected to make only minor changes to the reinsurance agreement so the FCIC could observe the performance of the reinsurance agreement under less severe conditions. The reinsured companies' net underwriting loss for the 2002 crop year was \$52.2 million, and the reinsured companies underwriting gains for the 2003 crop year are estimated to be \$166.7 million.

#### 1994-2003 Crop Years in Retrospect

An overall review of the period 1994 crop year through 2003 crop year reveals a substantial change in delivery of the MPCIC product and unusually turbulent weather patterns. The FCIC's authorizing legislation was amended prior to the 1990 fiscal year to improve its ability to administer an actuarially sound program. In 1995, farmers were required to purchase crop insurance in order to obtain linkage to other USDA programs.

This is the reason for the substantial premium increase from the 1994 crop year to the 1995 crop year. In the 2000 crop year premium also increased substantially due to \$400 million in premium discounts being offered to producers.

10 Year Summary of Premiums and Losses  
(in millions)

	<u>1994</u>	<u>1995</u>	<u>1996</u>	<u>1997</u>	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>10 Yr. Total</u>
Premiums	950	1,542	1,837	1,775	1,879	2,304	2,540	2,961	2,916	3,485	22,189
Losses	598	1,566	1,487	991	1,673	2,420	2,591	2,949	4,058	4,043	22,376
Loss Ratio	63%	102%	81%	56%	89%	105%	102%	100%	139%	116%	101%

For the crop years 1994 through 2003, the program has paid out an average of \$1.01 for every dollar of premium. In addition to the cost of the excess losses, administrative expenses of the program and premium subsidy have averaged \$514 million and \$1,180 million respectively over the past ten years. Premium subsidies have increased significantly since the 1995 crop year due to the 100% subsidization of catastrophic insurance premiums by the U.S. government.

There are significant efforts underway that have shown early signs of loss ratio improvements, such as implementation of the nonstandard classification system (NCS), GRP, and the analysis of premium rates as discussed under the "2002 Program Performance" section.

#### **2003 and 2002 Fiscal Year Financial Performance**

Premium revenue is comprised of producer paid premium and premium subsidy appropriated by the federal government. Producer paid premium is recognized as earned ratably over each crop's growing season. The portion of producer premium not recognized at the conclusion of the fiscal year is classified as unearned revenue in the consolidated balance sheet. Premium subsidy is recognized as earned when expended. The unexpended premium subsidy remains an unexpended appropriation in the consolidated balance sheet.

The sum of producer paid premium and premium subsidy has been calculated using generally accepted actuarial methods to attain a break-even loss ratio of 100%. Premium subsidy is not considered written to the extent a portion remains unexpended and no unearned revenue is recorded in the consolidated balance sheets. As a result, the expected claim costs and claim adjustment expenses exceed the related unearned revenue. A premium deficiency is therefore recognized in the consolidated balance sheet by accruing a liability recorded as an other liability for the excess amount.

The following are measures of the FCIC's financial performance:

<u>Net Operating Cost</u>		
(in millions)		
	2003	2002
Total Program Costs	\$ 4,661	4,885
Less Earned revenues	(1,073)	(1,419)
Net cost of operations	\$ 3,588	3,466

The previous measure indicates the FCIC's net operating cost.

<u>Operating Results</u>		
(in millions)		
	2003	2002
Beginning Balance	\$ (678)	\$ 82
Prior Period Adjustment	---	(319)
Beginning Balance, as Adjusted	(678)	(237)
Appropriations and other financing sources used	2,928	3,025
Less net cost of operations	(3,588)	(3,466)
Net change in Cumulative Results of Operations	\$ (1,338)	\$ (678)

The previous measure indicates that future funding will be required for the 2003 fiscal year.

Financial Obligations

(in millions)

		2003	2002
Entity Assets	\$	3,249	3,710
Liabilities covered by budgetary resources	\$	2,348	2,841
Ratio of entity assets to liabilities covered by budgetary resources		1.39	1.31

Net Position

(in millions)

		2003	2002
Total assets	\$	3,249	3,710
Total liabilities		(3,687)	(3,519)
Net Position	\$	(438)	191

The above measures provide an indication of the net position of the FCIC as of September 30, 2003 and 2002.

**Financial Highlights**

The FCIC has prepared its financial statements in accordance with the accounting standards codified in the Statements of Federal Accounting Standards and the Form and Content requirements contained in the Office of Management and Budget (OMB) Bulletin 01-09 and its updates.

**Financial Statements****Limitation on Financial Statements**

The financial statements have been prepared to report the financial position and results of operations of the entity, pursuant to the requirements of 31 U.S.C. 3515 (b). While the statements have been prepared from the books and records of the entity in accordance with the formats prescribed by OMB, the statements are in addition to the reports used to

monitor and control budgetary resources, which are prepared from the same books and records. The statements should be read with the realization that they are a component of the U.S. Government, a sovereign entity. One implication of this is that liabilities cannot be liquidated without legislation that provides resources to do so.

### Consolidated Balance Sheet

The FCIC's total assets as of September 30, 2003 were \$3.2 billion and as of September 30, 2002 were \$3.7 billion. The Fund Balance with Treasury and Accounts Receivable Net, \$3.1 billion and \$3.6 billion, respectively, are 97.0 and 98.0 percent, respectively, of total assets. The Liability for Estimated Losses on Insurance Claims, \$2.8 billion in fiscal year 2003 and \$2.9 billion in fiscal year 2002, respectively, are approximately 76 percent of total liabilities in fiscal year 2003 and 82 percent of total liabilities in fiscal year 2002.

### Statement of Net Cost

The FCIC's net cost of operations for fiscal year 2003 was \$3.6 billion, a 3.5 percent increase over the fiscal year 2002 net cost of operations that was \$3.5 billion. The indemnity costs and program delivery costs are 96.8 percent of the FCIC's cost of operations in fiscal year 2003 and 97.6 percent in fiscal year 2002.

### Statement of Net Position

The net cost of operations of the corporation increased in fiscal year 2003. Our loss ratio was an estimated 142 percent in fiscal year 2002 and an estimated 116 percent in fiscal year 2003.

### Statement of Budgetary Resources

Appropriations, combined with other budgetary resources made available and adjustments totaled \$4.8 billion in fiscal year 2003 and \$5.0 billion in fiscal year 2002, while total outlays were \$3.3 billion in fiscal year 2003 and \$3.0 billion in fiscal year 2002.

#### Budgetary Resources

(in millions)

		2003	2002
Appropriations	\$	2,977	2,894
Unobligated balance brought forward		1,027	1,234
Offsetting Collections and Adjustments		834	835
Total	\$	4,838	4,963

**Statement of Financing**

The total budgetary and non-budgetary resources used to finance operations totaled \$3.6 billion in fiscal year 2003 and \$3.5 billion in fiscal year 2002. The fiscal year change in undelivered orders was not part of the net cost of operations, and totaled \$16 million in fiscal year 2003 and \$1 million in fiscal year 2002.

**Systems, Controls, and Legal Compliance****Risk Compliance**

The focus of the compliance function continues to ensure the integrity of the crop insurance program and its delivery by increasing effectiveness, efficiency and timeliness of reviews performed on the companies which participate in the delivery of MPCCI.

ARPA mandated new requirements in the areas of program compliance and integrity but the act did not cause a change to Risk Compliance's overall mission, goals, or business objectives. Instead ARPA impacted existing business processes and provided additional management tools.

The role of Risk Compliance is to ensure that laws, policies, and procedures are followed and administered effectively. Risk Compliance seeks to maintain program integrity. This is accomplished through a systematic review process for the detection and prevention of crop insurance program abuse. Properly done, this requires a proactive approach in which the FCIC and the industry work together to increase awareness, develop programs, identify systems and processes, and take other actions to minimize the potential for crop insurance program abuse. Such an approach is ultimately aimed at the proactive prevention of fraud and abuse, rather than reactive.

Risk Compliance's goal is to reduce taxpayer and producer burden generated by fraud and abuse, contract noncompliance, and program vulnerabilities. The reinsured companies counter fraud and abuse in program delivery by performing growing season inspections, reviewing reported producer yields, performing on sight inspections, avoiding conflicts of interest, and initiating and engaging in litigation on issues important to the MPCCI program. The reinsured companies are also an important source of information concerning program vulnerabilities.

Risk Compliance's efforts are focused on investigation work generated by Office of the Inspector General (OIG) Hotline complaints, a variety of other external sources, and National Operations Reviews (NOR) of companies to determine compliance with the Standard Reinsurance Agreement (SRA) requirements and to determine MPCCI program vulnerabilities.

Ultimately, Risk Compliance produces a positive impact on MPCCI program integrity through its findings of noncompliance. Risk Compliance provides information and evidence to the FCIC Contracting Officer and other key operating and policy elements of the FCIC. This material provides a basis for action against wrong doers and for MPCCI program modification. Risk Compliance works with the Department of Justice through the USDA OIG's criminal division and the Office of General Counsel (OGC) (civil) where matters indicate a need for litigation.



### **Federal Managers' Financial Integrity Act**

The FCIC takes measures to conduct self-assessments, identify material weaknesses, and implement timely corrective action through the annual Federal Managers' Financial Integrity Act (FMFIA) reporting process.

The FCIC addresses audit findings and recommendations timely and works closely with the OIG, GAO, OCFO, Department of Justice (DOJ), and Assistant US Attorneys (AUSA) to timely implement effective, responsive corrective actions and improvements.

The compilation of these activities has enabled FCIC to identify and reduce program vulnerabilities, which has contributed to improved program integrity and protection of taxpayer's funds. A reduction in program vulnerabilities, improved program integrity, and protection of taxpayer's funds, in turn, enhance the economic safety net for farmers and ranchers.

The Federal Financial Management Improvement Act (FFMIA) requires that agencies implement and maintain financial management systems that comply substantially with federal financial management system requirements, applicable federal accounting standards, and the U.S. government standard general ledger at the transaction level. During its financial statement audit, the OIG and independent auditors report on whether or not financial management systems comply substantially. If the systems do not, then a plan is required to bring the systems into compliance.

Through review of its programs and the use of OIG and GAO evaluations, RMA strives to ensure government resources are used efficiently and effectively to achieve the intended program results. Improvement to programs following these reviews are designed to further minimize the potential for waste, fraud, and mismanagement.

Additionally our auditors noted an instance of noncompliance with certain laws and regulations applicable to the FCIC. The finding noted that management has not established a continuous monitoring system over financial management systems.

### **Agricultural Risk Protection Act of 2000**

The Agricultural Risk Protection Act (ARPA) of 2000, Section 515, mandated new requirements in the area of program compliance and integrity. These new requirements once fully implemented should enhance management information systems and facilitate the detection and enforcement of program fraud, waste, and abuse.

With the resources provided in the ARPA for data warehousing, data mining and other information technology capabilities, RMA continues to improve its compliance enforcement capabilities and reduce overall program vulnerabilities. Cooperative agreements and contracts are in place to greatly supplement this already existing effort in incremental phases over the next 5 years. Using the trends, indicators and analyses provided by these systems, we will be more proactive and aggressive in managing and monitoring program integrity issues.

RMA has entered into a contractual agreement to establish a pattern recognition system, enabling the Agency to identify trends signaling poor performance and/or potential/actual fraud, waste, and abuse of resources. The objectives of the contract are to identify trends, patterns, anomalies and relationships between reinsured organizations, insurance agents, adjusters, and producers in crop insurance data indicative of excess claim adjustment over actual crop loss. The vendor shall incorporate Data Analysis and Data Mining techniques to accomplish this objective. Implementation of this system will enable the Agency to target review efforts in those areas deemed the most vulnerable, thereby enhancing program integrity and protecting taxpayers' funds. To manage both the increased span of

control within the internal components of the agency and to ensure unity of authority without compromising the necessity for decentralized operations, RMA reviewed and updated its delegations of authority from the Administrator to the Deputy Administrator for Compliance. The revised delegation provides for the separation of authority at the various levels within Compliance that ensures that the processes for reviews and investigations, adjudication and appeals provides for administrative due process and are conducted fairly and impartially. By tailoring its management functions to meet and exceed the requirements of ARPA, RMA maintains the integrity of the compliance business processes and in doing so, is in a better position to maintain the integrity of crop insurance programs.

RMA conducts reviews designed to evaluate reinsured company performance, detect and correct program vulnerabilities, and collect underpaid premiums and overpaid indemnities. We also conduct investigations into complaints and allegations received from various sources such as producers, agents, and OIG hotline.

RMA's key partner in maintaining program integrity are the reinsured companies. We will continue to foster these relationships while emphasizing the need for the companies' quality control programs to improve and assisting the companies in that improvement process. Our objective is to develop within the companies the same stewardship of taxpayer's funds as our own values and beliefs.

As RMA implements the many changes specified and implied by ARPA requirements over the next several years, the agency will maintain close liaisons and partnerships with other government agencies and private sector companies to keep abreast of technological changes and innovative best practices especially in the areas of combating insurance fraud, investigative tactics and techniques, information management systems, or any other worthwhile venture that may assist the agency in its quest to save the taxpayers' dollars.

### **Actuarial and Underwriting Performance**

The systematic adjustment of premium rates and coverage's by the FCIC is producing additional cost savings for the federal government by reducing crop losses and placing the MPCI program on a more actuarially sound basis. These annual adjustments were initiated beginning with the 1991 crop year as a result of the Act and have stabilized the financial performance of the crop insurance program. The FCIC adjusts premium rates as necessary and appropriate for actuarial soundness. Annual premium rate increases are limited by law to no more than 20%. If rate increases greater than 20% are necessary for actuarial soundness, the FCIC will move toward the target rates over the following years, thus adhering to the 20% rule, but still moving toward the actuarially sound target rate.

The FCIC continues to review the premium rate making methodologies to increase the integrity and performance of the crop insurance program. In addition, the Economic Research Service (ERS), an agency of the USDA, is reviewing the FCIC's crop insurance program rates, financial elements of the standard reinsurance agreement, and yield coverage. Independently, the ERS has entered into a cooperative agreement with the actuarial firm of Milliman and Robertson to review the FCIC's actuarial processes. Additionally, the ERS provides feasibility studies of crops that represent opportunities for expansion of the crop insurance program. The FCIC also uses the resources of the CSREES to provide information about the financial situation of farmers so the FCIC can make more informed decisions for program improvement. During fiscal years 2001, 2002, and 2003, the FCIC has issued several contracts for completion of actuarial studies that will be evaluated and implemented to modify, update, and enhance actuarial methodology and the ratemaking process.

**Actual Production History Underwriting**

The FCIC's Actual Production History (APH) underwriting procedure of MPCII requires APH guarantees to be calculated with emphasis on the producer's actual yield records versus proxy yields. Yield guarantees are calculated using 4 years of actual records, building to a 10-year database. For producers who do not provide 4 years of actual yield records, the yield guarantee is a percentage of the proxy yield, which is calculated for each year's missing yield record. The percentage of the proxy yield is 100% when 3 years of records are provided, 90% for 2 years, 80% for 1 year, and 65% when no records are provided. New producers of crops who do not have records of actual yields may use 100 percent of the proxy yield. For APH yield calculation purposes, ARPA allows producers to substitute 60 percent of the applicable proxy yield for actual yields that are less than 60 percent of the applicable proxy yield to mitigate the effect of catastrophic years. Insureds may elect the APH Adjustment and substitute 60 percent of the applicable proxy yield for low actual yields caused by drought, flood, or other natural disasters.

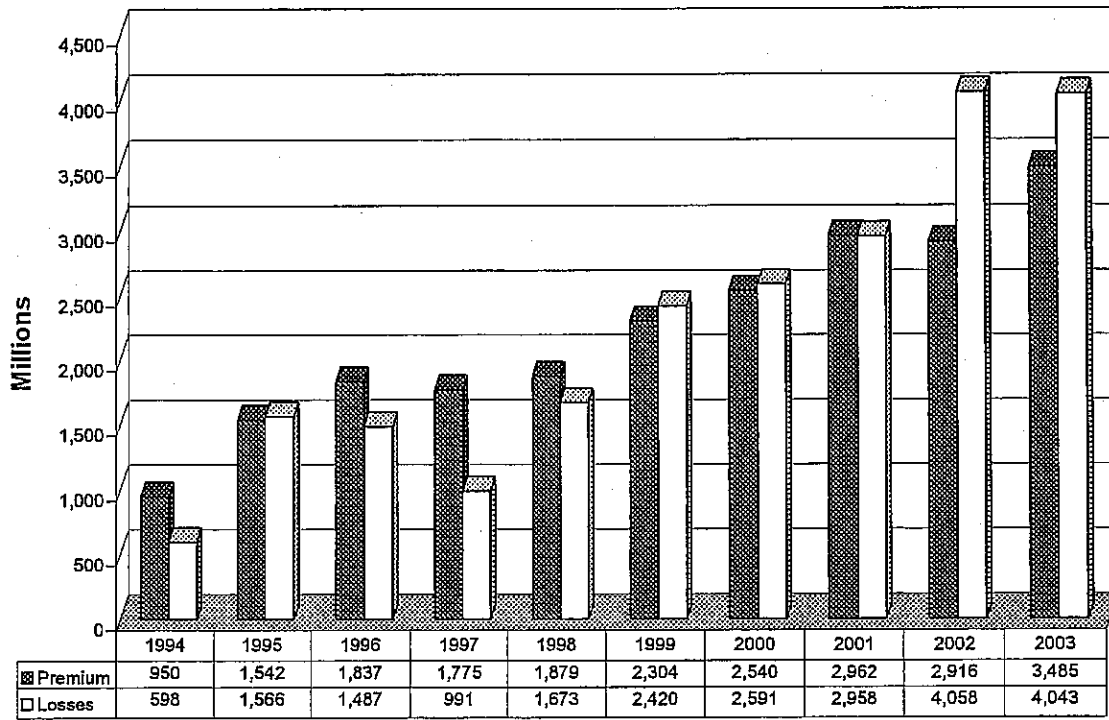
**Policyholder Tracking System**

The FCIC's Policyholder Tracking System (PHTS), a process within the DAS, uses the policyholder's Social Security Number or Employer Identification Number to track the policyholder's insurance history. The FCIC utilizes the PHTS to create a nationwide database to track producer participation in crop insurance programs, develop adequate production documentation, identify high-risk producers, assess the performance of insurance providers and other activities to improve the integrity and fiscal responsibility of the federal crop insurance program.

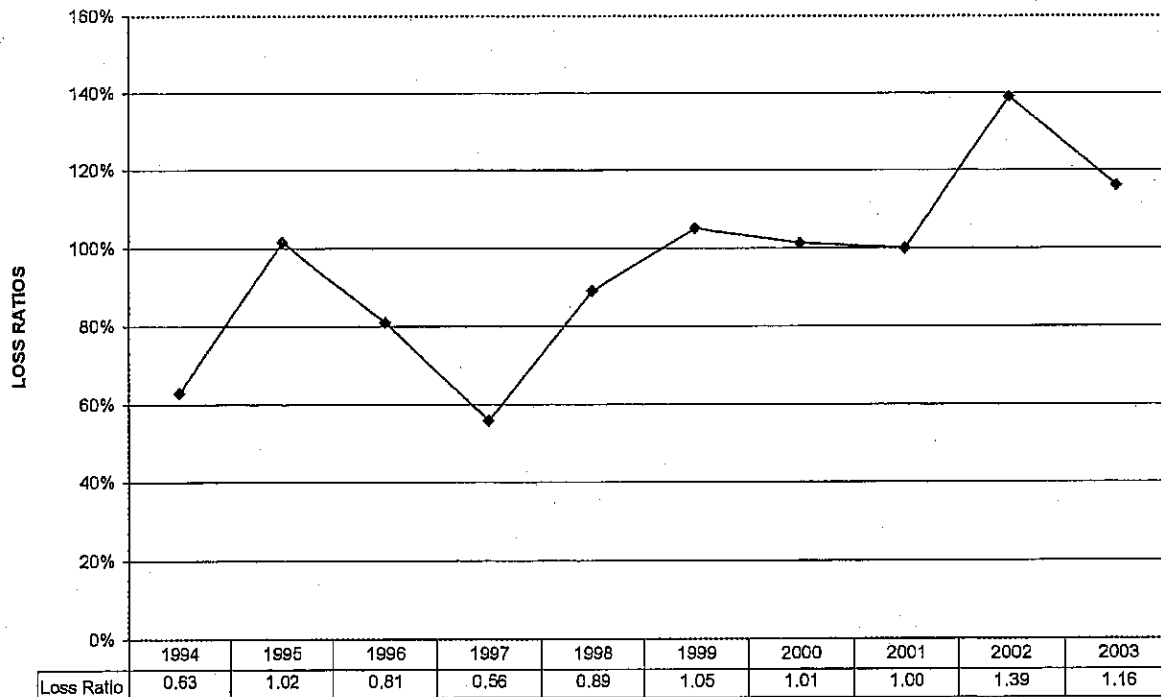
**Ineligible Tracking System**

The FCIC implemented the Ineligible Tracking System in October 1997, for the 1998 crop year. The ITS identifies persons who have rendered themselves ineligible for crop insurance benefits as a result of a violation of crop insurance policy provisions. The FCIC will not reinsure a crop insurance policy for a person identified as ineligible.

### SUMMARY OF PREMIUMS AND LOSSES



### SUMMARY OF LOSS RATIOS



**RISK MANAGEMENT AGENCY  
FEDERAL CROP INSURANCE CORPORATION  
CONSOLIDATED BALANCE SHEETS  
As of September 30, 2003 and 2002  
(in millions)**

	<u>2003</u>	<u>2002</u>
<b>Assets:</b>		
Intragovernmental		
Fund Balance with Treasury	\$ 1,996	\$ 2,352
Accounts Receivable, Net	1	1
Total Intragovernmental Assets	1,997	2,353
With the Public		
Accounts Receivable, Net	1,152	1,241
Advances	100	116
Total Public Assets	1,252	1,357
Total Assets	3,249	3,710
<b>Liabilities:</b>		
Intragovernmental		
Other Liabilities	4	(1)
Total Intragovernmental Liabilities	4	(1)
With the Public		
Accounts Payable	112	93
Other Liabilities:		
Estimated Losses on Insurance Claims	2,803	2,874
Unearned Revenue	235	207
Other Liabilities	533	346
Total Other Liabilities	3,571	3,427
Total Liabilities	3,687	3,519
<b>Commitments and Contingencies (Note 13)</b>		
<b>Net Position:</b>		
Unexpended Appropriations	362	331
Cumulative Results of Operations	(1,338)	(678)
Capital Stock	500	500
Paid-in Capital	38	38
Total Net Position	(438)	191
Total Liabilities and Net Position	\$ 3,249	\$ 3,710

See accompanying notes to consolidated financial statements.

**RISK MANAGEMENT AGENCY  
FEDERAL CROP INSURANCE CORPORATION  
CONSOLIDATED STATEMENTS OF NET COST  
For the Years Ended September 30, 2003 and 2002  
(in millions)**

	2003	2002
<b>Program Costs:</b>		
Intragovernmental Gross Costs		
Other Program Costs	\$ 49	\$ 61
	<u>49</u>	<u>61</u>
Intragovernmental Net Costs		
	<u>49</u>	<u>61</u>
Gross Costs With the Public		
Indemnities	3,768	4,114
Other Program Costs:		
Program Delivery Costs	743	656
Other Program Costs	101	54
Total Other Program Costs	<u>844</u>	<u>710</u>
Total Costs with the Public	<u>4,612</u>	<u>4,824</u>
Less: Earned Revenue from the Public:		
Premium Revenue	1,348	1,216
Net Gain (Loss) on Business Ceded to Reinsured Companies	(327)	145
Other Revenue	52	58
	<u>1,073</u>	<u>1,419</u>
Total Earned Revenue with the Public	<u>1,073</u>	<u>1,419</u>
Net Costs With the Public	<u>3,539</u>	<u>3,405</u>
<b>Net Cost of Operations</b>	<u>\$ 3,588</u>	<u>\$ 3,466</u>

See accompanying notes to consolidated financial statements.

**RISK MANAGEMENT AGENCY  
FEDERAL CROP INSURANCE CORPORATION  
CONSOLIDATED STATEMENTS OF CHANGES IN NET POSITION  
For the Years Ended September 30, 2003 and 2002  
(in millions)**

	<u>2003</u>			
	Cumulative Results of Operations	Capital Stock	Additional Paid-in Capital	Unexpended Appropriations
<b>Beginning Balances</b>	\$ (678)	\$ 500	\$ 38	\$ 331
<b><u>Budgetary Financing Sources:</u></b>				
Appropriations Received				2,982
Appropriation Transfers - in/out				(5)
Other Adjustments	-			(48)
Appropriations Used	2,898			(2,898)
<b><u>Other Financing Sources:</u></b>				
Transfers without Reimbursement	-			
Imputed Financing from Costs Absorbed by Others	11			
Other	19			
<b>Total Financing Sources</b>	<u>2,928</u>	<u>-</u>	<u>-</u>	<u>31</u>
<b>Net Cost of Operations</b>	<u>3,588</u>			
<b>Ending Balances</b>	<u>\$ (1,338)</u>	<u>\$ 500</u>	<u>\$ 38</u>	<u>\$ 362</u>
	<u>2002</u>			
	Cumulative Results of Operations	Capital Stock	Additional Paid-in Capital	Unexpended Appropriations
<b>Beginning Balances</b>	\$ (237)	\$ 500	\$ 38	\$ 432
<b><u>Budgetary Financing Sources:</u></b>				
Appropriations Received				2,896
Appropriation Transfers - in/out				(2)
Other Adjustments	-			20
Appropriations Used	3,015			(3,015)
<b><u>Other Financing Sources:</u></b>				
Transfers without Reimbursement	-			
Imputed Financing from Costs Absorbed by Others	10			
<b>Total Financing Sources</b>	<u>3,025</u>	<u>-</u>	<u>-</u>	<u>(101)</u>
<b>Net Cost of Operations</b>	<u>3,466</u>			
<b>Ending Balances</b>	<u>\$ (678)</u>	<u>\$ 500</u>	<u>\$ 38</u>	<u>\$ 331</u>

See accompanying notes to consolidated financial statements.

**RISK MANAGEMENT AGENCY  
FEDERAL CROP INSURANCE CORPORATION  
COMBINED STATEMENTS OF BUDGETARY RESOURCES  
For the Years Ended September 30, 2003 and 2002  
(in millions)**

	<u>2003</u>	<u>2002</u>
<b>Budgetary Resources:</b>		
Budget Authority		
Appropriations Received	\$ 2,982	\$ 2,896
Net Transfers	(5)	(2)
Unobligated Balances		
Beginning of Period	1,027	1,234
Spending Authority from Offsetting Collections		
Earned (Collected)	833	819
Recoveries of Prior Year Obligations	7	20
Permanently not Available	(6)	(4)
<b>Total Budgetary Resources</b>	<u>4,838</u>	<u>4,963</u>
<b>Status of Budgetary Resources:</b>		
Obligations Incurred		
Direct	2,983	3,936
Unobligated Balance		
Apportioned	1,509	718
Other Available	342	299
Unobligated Balance Not Available	4	10
<b>Total Status of Budgetary Resources</b>	<u>4,838</u>	<u>4,963</u>
<b>Relationship of Obligations to Outlays:</b>		
Obligations Incurred	2,983	3,936
Less: Spending Authority from Offsetting Collections and recoveries of Prior Year Obligations	(840)	(839)
Obligated Balance, Net, Beginning of Period	1,331	1,264
<u>Obligated Balance, Net, End of Period</u>		
Undelivered Orders	(87)	(71)
Accounts Payable	(57)	(1,260)
	<u>(144)</u>	<u>(1,331)</u>
<b>Total Outlays</b>	<u>3,330</u>	<u>3,030</u>
<b>Outlays Detail:</b>		
Disbursements	4,163	3,849
Collections	(833)	(819)
<b>Subtotal</b>	<u>3,330</u>	<u>3,030</u>
<b>Net Outlays</b>	<u>\$ 3,330</u>	<u>\$ 3,030</u>

See accompanying notes to consolidated financial statements.



**RISK MANAGEMENT AGENCY  
FEDERAL CROP INSURANCE CORPORATION  
CONSOLIDATED STATEMENTS OF FINANCING  
For the Years Ended September 30, 2003 and 2002  
(in millions)**

	<u>2003</u>	<u>2002</u>
<b>Resources Used to Finance Activities:</b>		
Budgetary Resources Obligated		
Obligations incurred	\$ 2,983	\$ 3,936
Less: Spending Authority from Offsetting Collections and recoveries	(840)	(839)
Obligations net of offsetting collections and recoveries	2,143	3,097
Other Resources:		
Imputed financing from costs absorbed by others	11	10
Other	19	-
Net Other Resources Used to Finance Activities	30	10
Total Resources Used to Finance Activities	2,173	3,107
<b>Resources Used to Finance Items Not Part of the Net Cost of Operations:</b>		
Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided	16	1
Total resources used to finance items not part of the cost of operations	16	1
Total resources used to finance the net cost of operations	2,157	3,106
<b>Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period:</b>		
Components Requiring or Generating Resources in Future Periods		
Change in exchange revenue receivable from the public	(89)	212
Other	1,520	148
Total components of Net Cost of Operations that will not require or generate resources in the current period	1,431	360
<b>Net Cost of Operations</b>	<b>\$ 3,588</b>	<b>\$ 3,466</b>

See accompanying notes to consolidated financial statements.

**RISK MANAGEMENT AGENCY  
FEDERAL CROP INSURANCE CORPORATION  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
SEPTEMBER 30, 2003 and 2002**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:**

**Reporting Entity**

The Federal Crop Insurance Corporation (FCIC) is a wholly-owned government corporation within the United States Department of Agriculture (USDA) and is not subject to federal, state, or local income taxes and, accordingly, no provision for income taxes is reported. These consolidated financial statements include the Risk Management Agency (RMA) and the FCIC; hereafter the combined entity will be referred to as the FCIC. The FCIC was established by the Federal Crop Insurance Act, which was enacted as Title V of the Agricultural Adjustment Act of 1938 (52 Statute 72). The FCIC manages a multiple-peril crop insurance (MPCI) program to assist in stabilizing and protecting the farming sector of the nation's economy. This program was restricted until the Federal Crop Insurance Act of 1980 (Public Law 96-365) expanded the program nationwide to eventually phase out the disaster payment program that was authorized by the Agriculture Act of 1949, as amended.

The RMA was established under provision of the Federal Agricultural Improvement and Reform Act of 1996 (the 1996 Act), Public Law 104-127, signed April 4, 1996. This act amended the Department of Agriculture Reorganization Act of 1994 (the 1994 Act), P.L. 103-354, Title II, to require the Secretary to establish within the USDA an independent office responsible for supervision of the FCIC, administration and oversight of programs authorized under the Federal Crop Insurance Act (7 U.S.C. 1501 *et seq.*), any pilot or other programs involving revenue insurance, risk management education, risk management savings accounts, or the use of the futures market to manage risk and support farm income that may be established under the Federal Crop Insurance Act or other law; and such other programs the Secretary considers appropriate.

On June 20, 2000 the President signed the Agricultural Risk Protection Act of 2000 into law effective starting with fiscal year 2001. Major provisions of this new legislation include: expanded use of contracts and partnerships for the research and development of policies and other risk management tools; prohibited research and development by the FCIC; revisions in CAT administrative fees and loss adjustment expense reimbursement; significant premium subsidy changes; livestock coverage authorization; reimbursement of research, development and maintenance costs for products submitted to the FCIC; expanded risk management education and assistance; provisions to address under-served areas, States, and commodities; establishment of an expert review panel and procedures for reviewing policies, plans of insurance, and related material or modifications; improved program compliance and integrity provisions; availability and acceptance of electronic information; good farming practices to include scientifically sound sustainable and organic farming practices; and others not included herein.

The objectives include the following items:

- Increase the number of economically sound risk management tools that are available and utilized by producers to meet their needs;
- Increase the agricultural community's awareness of risk management alternatives; and
- Improve program integrity and protect taxpayers' funds.

The Farm Security and Rural Investment Act of 2002 (2002 Farm Bill) was signed into law on May 13, 2002. Major provisions to this new legislation included: Authorization for sweet potato insurance to extend beyond the time the crop is in the field (as in the case of tobacco and potatoes), and expansion of the adjusted Gross Revenue Insurance pilot program into additional counties in California and Pennsylvania.

The FCIC has one delivery system in place to market the MPCCI program. The reinsurance business permits private insurance companies to write MPCCI that is reinsured by the FCIC. These companies were compensated by the FCIC for expenses associated with marketing and fully servicing (including claims adjustment, claims processing, billings, and premium collections) the MPCCI policies reinsured by the FCIC. The reinsurance business has been the FCIC's sole delivery system for the MPCCI since 1998. MPCCI is available for 88 different commodities (approximately 600 commodities as enumerated for disaster assistance purposes) in over 3,000 counties with policies covering all 50 states and Puerto Rico.

The FCIC is under the direction and control of a board of directors, which is appointed by the Secretary.

The FCIC receives all federal appropriations from the U.S. Department of Agriculture, budget classification (code 350).

#### **Basis of Presentation and Accounting**

The accompanying consolidated financial statements have been prepared to report the balance sheet, net cost, changes in net position, budgetary resources, and financing of the FCIC. The consolidated financial statements have been prepared from the books and records of the FCIC in accordance with Accounting Principles Generally Accepted in the United States of America (GAAP). GAAP for Federal financial reporting entities recognizes the Federal Accounting Standards Advisory Board (FASAB) as the standard setting body. The financial statements are presented in accordance with the Office of Management and Budget (OMB) Bulletin 01-09, *Form and Content of Agency Financial Statements*. All significant transactions and balances among FCIC's appropriations have been eliminated in consolidation. These consolidated financial statements are different from the financial reports, prepared by the FCIC pursuant to OMB directives, which are used to monitor and control the FCIC's use of budgetary resources.

The FCIC records accounting transactions on both an accrual and budgetary basis of accounting. Under the accrual method, revenues are recognized when earned and expenses are recognized when incurred, without regard to receipt or payment of cash.

Budgetary accounting facilitates compliance with legal constraints and controls over the use of federal funds. All inter-fund balances have been eliminated in the accompanying consolidated financial statements.

### **Fund Balance With Treasury**

Fund Balance with Treasury represents the aggregate amount of funds in the FCIC's accounts with Treasury for which the FCIC is authorized to make expenditures and pay liabilities. The FCIC's Fund Balance with Treasury consists of appropriated funds and receipts collected from non-federal entities.

### **Accounts Receivable**

Accounts receivable with the public represent premiums from reinsured companies due to the FCIC for crop insurance written by the reinsured companies and reinsured by the FCIC. The reinsured companies are responsible for collecting the premium from the producer and paying the FCIC, whether or not the premium has been collected from the producer. Reinsured companies are also responsible for a portion of the underwriting losses.

Producers' accounts receivable represent amounts due from individual producers for interest, overpaid indemnities, and premiums which are payable directly to the FCIC. It also includes estimated buy-up and catastrophic fees turned over by reinsured companies to the FCIC for collection. The FCIC provides an allowance for uncollectible accounts based upon historical experience.

The allowance for uncollectible accounts also represents approximately \$12.1 million and \$4.8 million for reinsurance recoverables and \$0.6 million and \$0.2 million for uncollectible CAT and additional coverage fees in fiscal years 2003 and 2002, respectively.

### **Property and Equipment**

Property and equipment consists of office furniture, computer equipment, and computer software. Historically, property and equipment with an acquisition cost of \$5,000 or more and an estimated useful life of at least two years was capitalized. Property and equipment with an acquisition cost of less than \$5,000 was expensed when purchased. Beginning in fiscal year 2003, the threshold was increased to \$25,000. Property and equipment is depreciated using the straight-line method over useful lives that range from 6 to 10 years. There are no restrictions on the use or convertibility of the FCIC's property and equipment.

### **Accounts Payable**

The FCIC accounts for reinsurance administrative expenses as program costs because they vary with, and are directly related to, acquiring new and carry-over business. Due to loss ratios at or in excess of 100% of producer premium without regard to the premium subsidy appropriation, all reinsurance administrative expenses have been expensed in the period in which they were incurred.

Section 508 (k) of the 1994 Act authorizes the FCIC to enter into reinsurance agreements with private insurance companies. Under these agreements, the FCIC assumes the

majority of the risk of loss on Multi Peril Crop Insurance (MPCI) written by the reinsured companies.

The 1998 Standard Reinsurance Act (SRA) was renewed through the 2003 reinsurance year, and provides for both proportional and non-proportional means by which the risk of loss may be ceded to the FCIC. The reinsured companies elect the method to transfer risk to the FCIC through their plan of operation. The plan of operation becomes a part of the SRA for each reinsurance year (July 1 through June 30).

Proportional reinsurance provides for a one-to-one percentage exchange of losses and premiums between the reinsured company and the FCIC. A reinsured company may not cede to the FCIC, under proportional methods, premiums that exceed 65% of its total book of business for the 2003 and 2002 reinsurance contracts. The FCIC uses nonproportional reinsurance programs (stop loss) which limit losses in the reinsured's retained book of business after the cessions made under proportional methods. Stop loss reinsurance is applied by state and by fund, if necessary, based upon the ratio of the reinsured's ultimate net losses to its retained net book premium.

The SRA provides for reimbursement to the reinsured companies for administrative expenses, including loss adjustment expenses. The SRA's reimbursement rates (as a percent of premium) are as follows for the 2003 and 2002 reinsurance years: Group Risk Plans (GRP), 22.7%; revenue plans that could increase liability at harvest, 21.1%; and all other plans, 24.5%. Reinsured companies were also allowed an expense reimbursement for adjusting catastrophic claims of 8% for the 2003 and 2002 reinsurance years.

### **Retirement Plans**

Most employees hired after December 31, 1983 are covered by the Federal Employees Retirement System (FERS). FERS is a three-tiered retirement plan consisting of Social Security benefits, a basic plan benefit, and a thrift savings plan (TSP). The FCIC and the employee each contribute 6.2% of the employee's basic pay through payroll taxes for Social Security benefits. Under the FERS basic benefit plan, the employee contributes .8% of basic pay and the FCIC contributes 10.7% of basic pay for FERS employees. The cost of providing the FERS basic benefit is equal to the amounts contributed by the FCIC and the employees because the plan is fully funded.

A TSP account is automatically established for employees covered by FERS, and the FCIC makes a mandatory contribution of 1% of basic pay to this account. Employees are eligible to contribute up to 13% (12% in fiscal year 2002) of basic pay to their TSP account subject to a maximum overall yearly contribution of \$12,000 (\$11,000 in calendar year 2002). The FCIC makes matching contributions, ranging from 1% to 4%, for employees who contribute to their TSP accounts.

Most employees hired on or before December 31, 1983, participate in the Civil Service Retirement System (CSRS.) CSRS is a single benefit retirement plan. The FCIC and the employee each contribute 8% of the employee's basic pay. Employees covered under CSRS are eligible to contribute up to 8% of basic pay to a TSP account to a maximum overall yearly contribution of \$12,000 (\$11,000 in calendar year 2002). The FCIC makes no matching contributions to TSP accounts established by employees covered under CSRS.

The limits will continue to increase by one percentage point per year through fiscal year 2005, after which all participants will be eligible to contribute up to the Internal Revenue Code's annual deferral limit (\$12,000 in calendar year 2003).

The FCIC does not report FERS or CSRS assets, accumulated plan benefits, or unfunded liabilities on its consolidated financial statements. Reporting such amounts is the responsibility of the Office of Personnel Management (OPM).

SFFAS No. 5, *Accounting for Liabilities of the Federal Government*, requires Federal entities to recognize an expense for pensions and other retirement benefits at the time the employee's services are rendered. The purpose of recognizing this expense is to record and report the full cost of each entity's operation. A corresponding revenue, Imputed Financing Sources, is recognized to the extent pension and other retirement benefit expenses exceed the amount paid to the OPM.

#### **Fair Value of Financial Instruments**

In the case of the FCIC's financial instruments, the carrying values approximate fair values because of their short-term maturity.

#### **Use of Estimates**

The preparation of these consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The significant estimates made are in connection with the recognition of the losses on insurance claims liability.

#### **Reclassifications**

Certain reclassifications were made to prior year amounts to conform to the current year presentation.

#### **Net Position**

Net position is the residual difference between assets and liabilities and is composed of capital stock, additional paid-in capital, unexpended appropriations, and cumulative results of operations. Unexpended appropriations represent the amount of unobligated and unexpended budget authority. Unobligated balances are the amount of appropriations or other authority remaining after deducting the cumulative obligations from the amount available for obligation and undelivered orders. Cumulative results of operations are the net result of the FCIC's operations since inception.

#### **Unearned Revenue**

Premium revenue is comprised of producer paid premium. Producer paid premium is recognized as earned ratably over each crop's growing season. The portion of producer paid premium not recognized at the conclusion of the fiscal year is classified as "unearned revenue, with the public" in the consolidated balance sheets. Premium subsidy is recognized as earned when expended. The unexpended premium subsidy remains an unexpended appropriation in the consolidated balance sheets.

The sum of producer paid premium and premium subsidy has been calculated using generally accepted actuarial methods to attain a break-even loss ratio of 100%. Premium subsidy is not considered written to the extent a portion remains unexpended and no unearned revenue is recorded in the consolidated balance sheets. As a result, the expected claim costs and claims adjustment expenses exceed the related unearned revenue. A premium deficiency is therefore recognized in the consolidated balance sheets by accruing a liability recorded as an other liability for the excess amount.

Insurance Fund appropriations, Administrative and Operation (A&O) Fund appropriations, and other financing sources are recognized when expended, which corresponds to when the expenses are incurred. The amount of appropriations not expended is a component of unexpended appropriations in the net position of the Balance Sheet.

In fiscal years 2003 and 2002, the FCIC received appropriations for the Insurance Fund and the RMA received appropriations for the A&O Fund. The Insurance Fund appropriations are available until expended, while the A&O Fund appropriations are available to cover obligations incurred in a given fiscal year. These consolidated financial statements include all activity related to the Insurance Fund and A&O Fund appropriations.

### **Claims Recognition**

The liability for estimated losses on insurance claims represents those claims that have been incurred, but for the most part, have not been reported to the FCIC as of the Balance Sheet date. The estimation of these liabilities relies on calculations using historical experience adjusted for changes in crop growing conditions. Also, because of the significant uncertainties associated with the assumptions used, the ultimate liabilities may differ significantly from the recorded estimates.

Administrative expenses associated with claims adjusters and reinsured companies are paid through the FCIC's Insurance Fund. Indemnity costs are paid from premium proceeds, including premium subsidies and premium discounts, which are also a part of the FCIC's Insurance Fund.

The estimated aggregate loss ratio including the premium subsidy appropriation for 2003 crop year was approximately 116 % (\$1.16 of claims for every \$1.00 of premium and premium subsidy) and the actual aggregate loss ratio for 2002 crop year was approximately 139% (\$1.39 for every \$1.00 of premium and premium subsidy). In the 2003 and 2002 fiscal years, federal premium subsidy funded approximately 60% of the total premium with approximately 40% being paid by the producer. This translates to an estimated \$1.40 billion and \$1.21 billion in farmer paid premium in crop years 2003 and 2002 respectively, with an estimated \$2.09 billion and \$1.79 billion in estimated premium subsidies for crop years 2003 and 2002.

## 2. FUND BALANCE WITH U.S. TREASURY:

<u>2003</u> (in millions)			
	<u>Appropriated</u> <u>Funds</u>	<u>Revolving</u> <u>Funds</u>	<u>Total</u>
Obligated	\$ 18	120	138
Unobligated available	-	1,854	1,854
Unobligated unavailable	4	-	4
<b>Total</b>	<b>\$ 22</b>	<b>1,974</b>	<b>1,996</b>

<u>2002</u> (in millions)			
	<u>Appropriated</u> <u>Funds</u>	<u>Revolving</u> <u>Funds</u>	<u>Total</u>
Obligated	\$ 21	1,305	1,326
Unobligated available	1	1,017	1,018
Unobligated unavailable	8	-	8
<b>Total</b>	<b>\$ 30</b>	<b>2,322</b>	<b>2,352</b>

The FCIC maintains separate accounts for the A&O (appropriated) and Insurance (revolving) Funds. The A&O Fund is used to pay administrative and operating expenses. The Insurance Fund is used to pay losses, and can also be used to pay claim adjustment expenses, reinsured company expenses, and costs referenced in the Agricultural Risk Protection Act. The FCIC does not earn interest on funds maintained in U.S. Treasury accounts. All funds are currently available to the FCIC except for the unobligated appropriated (i.e., A&O) funds that were only available for obligations through September 30, 2003.

## 3. ACCOUNTS RECEIVABLE:

Accounts receivable, net, federal and non-federal is as follows:

<b>2003</b> (in millions)	<u>Gross</u> <u>Accounts</u> <u>Receivable</u>	<u>Allowance for</u> <u>Uncollectible</u> <u>Accounts</u>	<u>Net</u> <u>Accounts</u> <u>Receivable</u>
Intragovernmental	\$ 1	-	1
With the Public	1,165	13	1,152
<b>Total</b>	<b>\$ 1,166</b>	<b>13</b>	<b>1,153</b>



<b>2002</b> (in millions)	Gross Accounts <u>Receivable</u>	Allowance for Uncollectible <u>Accounts</u>	Net Accounts <u>Receivable</u>
Intragovernmental	\$ 1	-	1
With the Public	1,246	5	1,241
<b>Total</b>	<b>\$ 1,247</b>	<b>5</b>	<b>1,242</b>

#### 4. ADVANCES:

Advances consist of the following:

	2003	2002
	(in millions)	
Advances to reinsured companies for escrow losses	\$ 98	114
Advances to reinsured companies for state premium subsidy	2	2
<b>Total advances</b>	<b>\$ 100</b>	<b>116</b>

The FCIC's advances to reinsured companies represent amounts funded to escrow accounts for which the companies' loss checks have not yet cleared.

#### 5. ACCOUNTS PAYABLES

Accounts payable, with the public, is as follows:

	2003	2002
	(in millions)	
Reinsured companies	\$ 112	93
<b>Total accounts payable with the public</b>	<b>\$ 112</b>	<b>93</b>

Accounts payable to reinsured companies represent the reimbursement to the reinsured companies for administrative expenses, including claim adjustment expenses, as provided by the SRA.

**6. OTHER LIABILITIES:**

Other liabilities covered by budgetary resources, federal and non-federal, are as follows:

	2003	2002
	(in millions)	
Federal		
Other accrued liabilities	\$ 4	(1)
Total other liabilities, federal subtotal	4	(1)
Non-Federal:		
Underwriting gain payable to reinsured companies	180	38
Reserve for premium deficiency	342	299
Federal Employees Compensation Act Liability	4	4
Annual leave liability	3	4
Other accrued liabilities	4	1
Total other liabilities, non-federal subtotal	533	346
Total other liabilities	\$ 537	345

The Dairy Options Pilot Program (DOPP) is a pilot program to determine whether futures and options can provide a meaningful reduction in market risk faced by milk producers. The program that is administered by the FCIC is funded by the Commodity Credit Corporation (CCC) funds that were advanced to the FCIC.

Premiums and losses are reported monthly under the SRA and a periodic settlement, as stipulated in the agreement is calculated whereby the results of the business written by the reinsured companies are determined and an experience-rated underwriting gain or loss is computed. Underwriting gains are paid to the reinsured companies while the reinsured companies pay underwriting losses to the FCIC. However, a portion of the underwriting gain payable includes amounts being held in reserve from prior years for any future underwriting losses incurred by the reinsured companies.

Included in other intragovernmental liabilities are liabilities that are not covered by budgetary resources that amount to approximately \$0.5 million and \$0.4 million for unfunded Federal Employees Compensation act (FECA) liability. Included in liabilities with the public are liabilities not covered by budgetary resources that amount to approximately \$3.4 million and \$5.3 million for unfunded annual leave, \$3.8 million and \$4.1 million for actuarial FECA liabilities for fiscal years 2003 and 2002. Additional liabilities not covered by budgetary resources are \$1,399 million and \$678 million as of September 30, 2003, and 2002 respectively. Liabilities not covered by budgetary resources are not funded by current appropriations from Congress. Annual leave is accrued as it is incurred and the accrual is reduced as it is taken. As of September 30, 2003 and 2002, the balance in the accrued annual leave account was adjusted to reflect current pay rates and annual leave balances.

A premium deficiency has been recorded as the expected claim costs and claim adjustment expenses exceed the related unearned revenue.

## 7. NET POSITION:

<b>2003</b> (in millions)	Revolving Funds	Appropriated Funds	Total
Capital stock	\$ 500	-	500
Additional paid-in capital	38	-	38
Unexpended Appropriations:			
Unliquidated obligations	-	16	16
Unobligated, not available	-	4	4
Unobligated, available	342	-	342
Subtotal, unexpended Appropriations	342	20	362
Cumulative Results of Operations:			
Donated capital	3,958	-	3,958
Results of operations	(5,289)	(7)	(5,296)
Subtotal, cumulative results of operations	(1,331)	(7)	(1,338)
Total net position	\$ (451)	13	(438)

<b>2002</b> (in millions)	Revolving Funds	Appropriated Funds	Total
Capital stock	\$ 500	-	500
Additional paid-in capital	38	-	38
Unexpended Appropriations:			
Unliquidated obligations	-	22	21
Unobligated, not available	-	8	8
Unobligated, available	300	1	301
Subtotal, unexpended Appropriations	300	31	331
Cumulative Results of Operations:			
Donated Capital	3,958	-	3,958
Results of operations	(4,629)	(7)	(4,636)
Subtotal cumulative results of operations	(671)	(7)	(678)
Total net position	\$ 167	24	191

Donated Capital:

Prior to the 1994 Act, the Secretary was authorized to use the funds of the Commodity Credit Corporation, (CCC) to pay claims of the FCIC if the funds available to the FCIC for that purpose were insufficient. The 1994 Act eliminated the need for the FCIC to request funds from the CCC. Although the authority to use the CCC funds still exists, the FCIC is now authorized to draw necessary funds directly from the U.S. Treasury (with USDA and OMB approval) to cover operating expenses including excess losses.

#### Capital Stock:

Section 504 (a) of the 1994 Act authorizes capital stock of \$500 million subscribed by the United States. There has been no change in the capital stock issued since August 15, 1985.

### 8. INDEMNITY COSTS:

Insurance indemnity costs are as follows:

		2003	2002
		(in millions)	
Catastrophic coverage	\$	80	28
Additional coverage		3,688	4,086
Insurance claims and indemnities	\$	3,768	4,114

### 9. PROGRAM DELIVERY AND OTHER PROGRAM COSTS:

Program delivery costs are as follows:

		2003	2002
		(in millions)	
Reinsurance administrative expenses	\$	743	656

Federal other program costs are as follows:

		2003	2002
		(in millions)	
Reimbursable costs	\$	32	46
Other retirement benefit, other post-employment benefit, FECA, and other costs		6	5
Imputed costs		11	10
Total federal other program costs	\$	49	61

Non-federal program costs are as follows:

	<u>2003</u>	<u>2002</u>
	(in millions)	
Other program fund costs	\$ 53	16
Administrative and other fund costs	48	38
Total non-federal other program costs	\$ 101	54

## 10. UNEARNED REVENUE

Unearned revenue is as follows:

	<u>2003</u>	<u>2002</u>
	(in millions)	
Unearned producer premium	\$ 235	207

## 11. FINANCING SOURCES:

In fiscal years 2003 and 2002, the FCIC received an Insurance Fund appropriation of \$2.9 billion and \$2.8 billion respectively, for premium subsidy, reinsurance administrative expenses and other program expenses and for research and development. In fiscal years 2003 and 2002, the RMA A&O Fund appropriation was \$70.7 million and \$75.3 million respectively.

Provisions of Agricultural Risk Protection Act (ARPA) place a major emphasis on contracting and partnering for development of risk management products. ARPA provides incentives for private parties to develop and submit new risk management products to the FCIC Board of Directors. In fiscal year 2003, \$68 million was appropriated for ARPA expenses with \$5 million being transferred to Cooperative State Resource, Education, and Extension Service (CSREES.) In fiscal year 2002 \$52 million was appropriated for ARPA expenses with \$2 million being transferred to CSREES.

The following table summarizes appropriations used:

	<u>2003</u>	<u>2002</u>
	(in millions)	
Net A&O appropriation used	\$ 77	82
Appropriation for premium subsidy	1,868	1,827
Appropriation for ARPA costs	33	31
Appropriation for delivery costs	730	656
Appropriation for excess losses	190	415
Appropriation for Emergency Financial Assistance (EFA) discount	-	4
Insurance fund appropriations, subtotal	2,821	2,933
Total appropriations used	\$ 2,898	3,015

## 12. ESTIMATED LOSSES ON INSURANCE CLAIMS:

The following table summarizes the activity in the accrual for estimated losses on insurance claims.

	<u>2003</u>	<u>2002</u>
	(in millions)	
Balance as of October 1	\$ 2,874	1,899
Incurred Related to:		
Current year	3,967	4,323
Prior year	(199)	(209)
Total Incurred	3,768	4,114
Less Paid Related to:		
Current year	(775)	(972)
Prior year	(3,064)	(2,167)
Total Paid	(3,839)	(3,139)
Net Balance as of September 30	\$ 2,803	2,874

The FCIC experienced positive loss development related to the prior crop years in fiscal years 2003 and 2002. As a result, incurred claims related to prior years decreased approximately \$199 million in fiscal year 2003 and \$209 million fiscal year 2002.

## 13. COMMITMENTS AND CONTINGENCIES

The FCIC is a defendant in various litigation cases arising in the normal course of business. Furthermore, in order to defend its policies and procedures, the FCIC may, in some instances, pay litigation expenses and judgments over and above indemnities found under the SRA for reinsured companies. For this reason, the FCIC is consulted with and approves significant decisions in the litigation process.

In fiscal year 2003, one of the reinsured companies, American Growers Insurance Company (AGIC), was placed under an order of supervision by the Nebraska Department of Insurance. On December 10, 2002, the FCIC signed a Memorandum of Understanding (MOU) with the Nebraska Department of Insurance that establishes the responsibilities and understandings between the FCIC and the Nebraska Department of Insurance with respect to AGIC. The FCIC is working with the Nebraska Department of Insurance and AGIC management to ensure that all outstanding policy claims will be paid and service to producers will continue.

The MOU establishes the framework to ensure that AGIC personnel, loss adjustors, and agents continue servicing policyholders. To achieve these goals, key employees at AGIC have been retained to finish servicing the 2002 crop year book of business. In addition, expenses related to loss adjustment, billing, and agents commissions associated with policies reinsured by the FCIC and paid to ensure the timely payment of crop insurance claims, adequate levels of service going forward, and the timely collection and transmission of premiums to the FCIC. Further, maintaining a viable agent network is essential to making sure that policyholders are quickly transferred to other crop insurance companies for subsequent crop years.

Approximately \$580 million of the estimated \$3 billion losses on insurance claims for the 2002 crop year were related to business written by AGIC. (19% of FCIC's total book of business.) Additional costs may be incurred by FCIC for other administrative costs of AGIC, however these costs are not quantifiable at this time.

#### **14. STATEMENT OF BUDGETARY RESOURCES:**

FCIC's Statement of Budgetary Resources serves as a tool to link budget execution data to information reported in the "actual" column of the Program and Financing Schedules in the Appendix of the Budget of the United States Government (referred to as the "President's Budget") as well as information reported in the Reports of Budget Execution and Budgetary Resources (SF-133). Some reporting differences do exist between comparable amounts in the Statement of Budgetary Resources, the President's Budget, and the SF-133. On an aggregate level, these differences amount to less than one-tenth of one percent of FCIC's total budgetary resources and are therefore considered immaterial. The differences are not due to error or omission; rather, the differences arise from timing and varying OMB reporting requirements.

#### **15. CHANGE IN ACCOUNTING POLICY FOR APPROPRIATIONS**

In fiscal year 2002, FCIC changed its accounting policy for recognizing appropriations as expended. Accordingly, the consolidated financial statements of all prior periods were restated. FCIC previously reported appropriations as expended when the liabilities were thought to be incurred, which corresponded to when the risk was underwritten. FCIC has now determined that the liabilities are incurred and the appropriation expended at the point in time the appropriation is used to subsidize a paid indemnity.

## SUPPLEMENTARY STEWARDSHIP INFORMATION (UNAUDITED):

### Schedule 1

In response to the Secretary's 1996 Risk Management Education (RME) initiative, and as mandated by the 1996 Act, the FCIC has formed new partnerships with the Cooperative State Research, Education, and Extension Service (CSREES), the Commodity Futures Trading Commission, the USDA National Office of Outreach, Economic Research Service, and private industry to leverage the federal government's funding of its RME program by using both public and private organizations to help educate their members in agricultural risk management. The RME effort was launched in 1997 with a Risk Management Education Summit that raised awareness of the tools and resources needed by farmers and ranchers to manage their risks. RMA has built on this foundation during fiscal year 2003 by expanding State and Regional education partnerships; encouraging the development of information and technology decision aids; supporting the National Future Farmers of America (FFA) foundation with an annual essay contest; facilitating local training workshops; and supporting Cooperative Agreements with Educational and outreach organizations.

During fiscal years 2003 and 2002, the RME worked toward the goals by funding approximately 1,200 risk management sessions. Most of these activities targeted producers directly. The number of producers reached through these sessions is approximately 62,000 in fiscal year 2003 and 50,000 in fiscal year 2002. In addition to reaching producers, some training sessions helped those who work with producers, such as lenders, agricultural educators, and crop insurance agents, better understand those areas of risk management with which they may be unfamiliar. Total RME obligations incurred by the FCIC were approximately \$9.4 million for fiscal year 2003 and \$4.9 million for fiscal year 2002. The following table summarizes the RME initiatives since fiscal year 1999.

	2003	2002	2001	2000	1999
	(dollars in millions)				
RME Obligations	\$ 9	6	5	1	1
Number of producers attending RME sessions	62,000	50,000	50,000	30,000	14,500
Number of RME sessions held	1,200	1,200	1,500	1,250	950

One of the directives of ARPA is to step up the FCIC's educational and outreach efforts in certain areas of the country that have been historically underserved by the Federal crop insurance program. The Secretary determined that fifteen states met the underserved criteria. These states are Maine, Massachusetts, Connecticut, Wyoming, New Jersey, New York, Delaware, Nevada, Pennsylvania, Vermont, Maryland, Utah, Rhode Island, New Hampshire, and West Virginia.



**REQUIRED SUPPLEMENTARY INFORMATION (UNAUDITED):**  
**Schedule 2**

Intra-governmental balances:

FCIC reports the following amounts as intra-governmental assets and liabilities, which are included in the September 30, 2003 and 2002 consolidated balance sheets:

Intra-governmental assets:

<u>2003</u> (in millions)		
<u>Agency</u>	<u>Fund Balance with Treasury</u>	<u>Accounts Receivable</u>
Department of the Treasury	\$ 1,996	-
Other Federal Agencies	-	1
Total intra-governmental assets	\$ 1,996	1

<u>2002</u> (in millions)		
<u>Agency</u>	<u>Fund Balance with Treasury</u>	<u>Accounts Receivable</u>
Department of the Treasury	\$ 2,352	-
Other Federal Agencies	-	1
Total intra-governmental assets	\$ 2,352	1

Intra-governmental liabilities:

<u>2003</u> (in millions)		
<u>Agency</u>	<u>Accounts Payable</u>	<u>Other Liabilities</u>
Department of Agriculture	-	5
Other Federal Agencies	-	(1)
Total intra-governmental liabilities	-	4

<u>2002</u> (in millions)		
<u>Agency</u>	<u>Accounts Payable</u>	<u>Other Liabilities</u>
Department of Agriculture	-	2
Other Federal Agencies	-	(3)
Total intra-governmental liabilities	-	(1)