



U.S. Department of Agriculture
Office of Inspector General
Audit Report

RISK MANAGEMENT AGENCY
INDEMNITY PAYMENTS TO PRUNE
PRODUCERS IN CALIFORNIA -
PRODUCER B



**Report No.
05099-5-SF
August 2001**



UNITED STATES DEPARTMENT OF AGRICULTURE

OFFICE OF INSPECTOR GENERAL

Washington D.C. 20250



DATE: August 15, 2001

REPLY TO
ATTN OF: 05099-5-SF

SUBJECT: Indemnity Payments to Prune Producers in California – Producer B

TO: Phyllis Honor
Acting Administrator
Risk Management Agency

ATTN: Garland Westmoreland
Deputy Administrator

This report presents the results of our audit of indemnity payments made to prune producers in California. Your August 2, 2001, response to the draft report is included as exhibit D of the report. Excerpts from your response have been incorporated into the relevant sections of the report.

We are unable to accept your management decision for all recommendations. In accordance with Departmental Regulation 1720-1, we will be able to accept your management decision on Recommendation Nos. 1 and 3 when you provide us with documentation that the insurance provider was billed for errors on unit 102 totaling \$504 for crop year 1998 and \$6,678 for crop year 1999. We will be able to accept your management decision on Recommendation Nos. 2 and 4 after reviewing your final determination.

Please furnish a reply within 60 days describing the corrective action taken or planned and the timeframes for implementation of all of our recommendations. Please note that the regulation requires a management decision to be reached within a maximum of 6 months from report issuance. Follow your internal agency procedures in forwarding final action correspondence to the Office of the Chief Financial Officer.

We appreciate the assistance and cooperation of your staff during this review.

/s/

RICHARD D. LONG
Assistant Inspector General
for Audit

EXECUTIVE SUMMARY

RISK MANAGEMENT AGENCY INDEMNITY PAYMENTS TO PRUNE PRODUCERS IN CALIFORNIA – PRODUCER B

REPORT NO. 05099-5-SF

RESULTS IN BRIEF

This is one of a series of audits that we have conducted to resolve questions about the amount of production reported by prune producers in connection with indemnity claims filed with the Risk Management Agency (RMA) for losses during the period 1997 through 1999. In a survey of the program, we had identified six producers for whom the information on file raised questions about the amount of production. Five of the six producers also received disaster payments from the Farm Service Agency (FSA).¹ This report covers our review of one of these producers, whom we have identified as “producer B.”

During our audit, we found that the insurance provider made errors in both the 1998 and 1999 insurance claims for producer B as follows:

- An incorrect unit structure and overstated acreage were used to calculate the 1998 indemnity. The insurance provider initially paid indemnities on two optional units that should have been combined into one unit. In addition, the acreage was overstated because noncropland acres were inadvertently included in the total acreage of 75.0 acres.
- Understated yields were used to calculate the 1999 indemnity. When adjusting the 1999 insurance claim, the insurance provider discovered that it had used an incorrect unit structure and gross acreage. To correct the errors, it combined the two units and re-measured the land as 58.6 acres. The insurance provider then re-calculated new yields for the combined unit but failed to use the new acreage amount.

¹ Report No. 03006-7-SF discusses the results of our review of Producer B’s 1998 disaster claim.

- Understated production was used to calculate the 1999 indemnity. The insurance provider understated production by 8.4 tons because the insurance provider (1) failed to use the final settlement sheet to verify that total production had been included in the claim and (2) failed to apply a quality loss factor to a second production report.
- Incorrect yields were used to re-calculate the 1998 and 1999 indemnities. The insurance provider updated the yields using 58.6 acres, which were later determined to be in error. Based on the updated records, the insurance provider determined that the producer had been overpaid in 1998 indemnities and underpaid in 1999 indemnities. The insurance provider netted the two amounts and erroneously disbursed additional funds to the producer.
- Acreage was understated by 11.2 acres for the re-calculated 1998 indemnity and the 1999 indemnity. After we completed our analysis, we noted that the reduction for noncrop acres appeared to be excessive and requested that the FSA measure the acreage. FSA determined that the correct cropland acreage was 69.8. Therefore, the recalculated 1998 indemnity and the 1999 indemnity were based on acreage that was understated by 11.2 acres.

As a result of the above errors, the producer was overpaid \$504 for crop year 1998 and overpaid \$6,678 for crop year 1999 (see exhibit A.)

KEY RECOMMENDATIONS

We recommend that RMA collect the 1998 overpayment of \$504 and the 1999 overpayment of \$6,678 for unit 102 from the insurance provider. We also recommend that RMA instruct the insurance provider to correct the acreage and yields to reflect 69.8 cropland acres.

AGENCY RESPONSE

In its response to the draft report dated August 2, 2001, RMA conditionally concurred with the findings. RMA will complete a review and will issue either an initial determination to the insurance company or reasons for non-concurrence by October 31, 2001. The response is included in its entirety as exhibit D to this report.

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INTRODUCTION

BACKGROUND

The Federal Agriculture Improvement and Reform Act of 1996 established RMA. RMA is responsible for supervision of the Federal Crop Insurance Corporation (FCIC), administration and oversight of programs authorized under the Federal Crop Insurance Act of 1980, and other programs designed to manage risk and support farm income. FCIC provides crop insurance through a network of approved private insurance companies that are reinsured by FCIC. With the implementation of the single delivery system in 1998, these companies have sold and serviced all crop insurance policies that insure producers against losses due to natural causes such as drought, excessive moisture, hail, wind, frost, insects, and disease.

A producer suffering an insured loss reports the loss to his insurance provider and will generally provide copies of "Inspection Report And Certification Forms" (form P-1's) as proof of production. To determine the amount of the loss and verify that the producer's total production is accounted for, the insurance provider is required to obtain final settlement sheets from handlers, such as packinghouses. If the amount of production is less than the guaranteed level of production per the insurance policy, the producer is entitled to an indemnity, i.e., a reimbursement against loss or damage. This is calculated by multiplying the production loss amount by the price elected by the producer.

In California, the Dried Fruit Association (an independent third party) inspects the prunes and generates the form P-1's. After the prunes have been dried and delivered to a packinghouse, the Dried Fruit Association inspects a sample from each lot and determines its weight, size, and quality. The inspection results are reported on the form P-1 and distributed to the producer, handler, and the Prune Marketing Committee (PMC). PMC maintains records for all dried fruit production in California.

OBJECTIVES

Our objective was to resolve questions that were raised due to discrepancies identified between the production reported to PMC and the production reported by producer B to the insurance provider. We also reviewed producer B's claim to determine if the indemnity was calculated in accordance with RMA procedures.

SCOPE

During the survey phase of our audit, we looked at concerns about the inaccurate reporting of production by prune producers, which could be, among other things, an indicator of shifting production to increase indemnities. We limited our review to California producers because California prune orchards produce 99 percent of U.S. production. We selected a judgmental sample of 20 producers to review based on the following criteria: (1) the policy had multiple units or parcels of land (which would allow shifting of production), (2) at least one of the units received no indemnity payment (which might indicate that production had been falsely assigned to that unit), and (3) the indemnity was among the largest paid.

We found discrepancies in the production reported by 6 of the 20 producers in our sample. Based on the survey results, we decided to conduct audits of each of the six producers to resolve the questions about the discrepancies. Producer B is one of the six producers.

Our scope covered crop years² 1997 through 1999. However, due to an acreage error that affected prior year yields, we expanded our scope to include a review of yield determinations completed for producer B for crop years 1994 through 1996.

Audit fieldwork was performed from April through August 2000 at RMA's Regional Office located in Davis, California; the Rain and Hail Insurance Service Inc. office (insurance provider) located in Fresno, California; and the Sutter/Yuba FSA County office located in Yuba City, California.

This audit was performed in accordance with generally accepted government auditing standards.

METHODOLOGY

To accomplish our objectives and support our findings, we performed the following procedures:

- We compared form P-1's obtained from PMC to production amounts used by the insurance provider to calculate producer B's indemnities.
- We analyzed producer files obtained from the insurance provider to determine if producer B's indemnities were adjusted in accordance with approved procedures.

² A crop year is designated by the calendar year in which the insured crop is normally harvested.

- We compared the producer's disaster application at the Sutter/Yuba FSA County office with loss records submitted to the insurance provider.
- We interviewed RMA and FSA officials, producers, handlers, and other persons to resolve production discrepancies.

FINDINGS AND RECOMMENDATIONS

CHAPTER 1	INSURANCE PROVIDER MADE NUMEROUS ERRORS IN CALCULATING INDEMNITY PAYMENTS
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For crop year 1998, the insurance provider incorrectly included noncropland acres in its measurement of a prune orchard resulting in overstated acreage being used to calculate the indemnity payment. It later discovered the error and re-measured the acreage. However, the insurance provider made an additional error when it failed to include all cropland in the second measurement, resulting in an understated acreage amount of 11.2 acres. Consequently, the producer was overpaid \$504.

For crop year 1999, the above understated acreage amount was used to calculate the indemnity. In addition, the insurance provider did not comply with RMA regulations related to procedures for verifying production resulting in production being understated by 8.4 tons. These errors resulted in the producer being overpaid \$6,678.

FINDING NO. 1

INSURANCE PROVIDER UNDERSTATED ACREAGE WHEN DETERMINING THE PRODUCER'S 1998 INDEMNITY

In calculating the 1998 indemnity for unit 102, the insurance provider understated the producer's 58.6 acres by 11.2 acres. This occurred due to a series of inadvertent errors related to acreage measurements. As a result, the yields were inaccurate and the producer received a net overpayment of \$504 for crop year 1998 (see exhibit B).

The Loss Adjustment Manual (LAM)³ states that the insurance provider must "ensure that all documentation, determinations, and calculations are completed as specified in the FCIC-approved LAM and crop handbooks." The Crop Insurance Handbook⁴ states "all acreage measurements for perennial crops will be based on land acres (i.e., planimetered, wheeled/taped) with deductions for noncrop areas."

³ FCIC-25010-1, paragraph 7(C) dated May 1998.

⁴ FCIC-18010, section 7(D)3, effective for the 1998 crop year.

Producer B experienced low yields as a result of excessive rain during crop year 1998. Based on a 75.0-acre orchard, the producer received \$53,235 in crop insurance payments for losses sustained. In determining the crop losses for the following year (1999), the insurance provider discovered that it used an incorrect unit structure and had used total acreage without deducting noncrop areas such as roads and buildings.

The insurance provider corrected the unit structure by combining two units (102 and 103) into one unit (102) and re-measured the land to remove noncropland acres, resulting in 58.6 acres. The insurance provider calculated new yield and actual production history (APH)⁵ figures for the combined unit. During our preliminary review, we were unable to confirm the yield calculations and questioned their accuracy. During the audit, the insurance provider realized that it had incorrectly used the 75.0 acres in calculating the yields and took immediate action to correct them by using 58.6 acres. The insurance provider determined that the 1998 APH yield was 3.6 tons per acre. The insurance provider then recalculated the 1998 indemnity and determined that producer B was overpaid \$2,583 for crop year 1998. See table 1. To recover the overpayment, the insurance provider reduced the 1999 indemnity by this amount.

After we completed our analysis, we noted that the reduction for non-crop acres appeared to be excessive and requested that FSA measure the acreage. FSA determined that the correct cropland acreage was 69.8. The insurance provider agreed that the FSA measurement was accurate and that its own acreage measurement was understated by 11.2 acres. The insurance provider stated that it had inadvertently omitted part of the orchard when it measured the cropland. Consequently, the APH was overstated by .6 ton per acre because it appeared that more prunes were produced on less land. As a result, the producer was overpaid \$504 for crop year 1998.

⁵ The actual production history (APH) yield is the sum of the annual yields divided by the number of years in the database. The approved APH may contain up to 10 consecutive crop years of actual and/or assigned yields. The 1998 APH for producer B was calculated using the annual yields from crop years 1994 through 1997.

Table 1: 1998 Overpayment (see exhibit B)

	Per Insurance Provider	Per Audit
Original indemnity payment @ 75 acres	\$ 53,235	\$ 53,235
Recalculated indemnity @ 58.6 acres and an APH of 3.6	<u>50,652</u>	
Recalculated indemnity @ 69.8 acres and an APH of 3.0		<u>\$ 50,148</u>
Overpayment	2,583	3,087
Less amount used to reduce indemnity	2,583	<u>2,583</u>
Overpayment outstanding		<u>\$ 504</u>

Based on the recalculated indemnity, RMA should collect the overpayment from the insurance provider. In addition, RMA should instruct the insurance provider to correct the acreage and yields for unit 102.

RECOMMENDATION NO. 1

Collect the 1998 overpayment of \$504 for unit 102 from the insurance provider.

Agency Response

RMA conditionally concurred with our finding and recommendation. RMA will conduct an internal review by October 31, 2001, at which time it will make a final determination regarding the overpayment for unit 102.

OIG Position

We are unable to accept your management decision until you provide us with documentation that the insurance provider was billed for \$504.

RECOMMENDATION NO. 2

Instruct the insurance provider to correct the acreage and yields for unit 102.

Agency Response

RMA conditionally concurred with our finding and recommendation. RMA will conduct an internal review by October 31, 2001, at which time it will make a final determination regarding the acreage and yield figures for unit 102.

OIG Position

We are unable to accept your management decision until we review your final determination.

FINDING NO. 2

INSURANCE PROVIDER UNDERSTATED PRODUCTION AND ACREAGE WHEN DETERMINING THE PRODUCER'S 1999 INDEMNITY

In determining the 1999 indemnity payment for unit 102, the insurance provider understated the producer's 44.7 tons of production by 8.4 tons. This occurred because the insurance provider failed to (1) collect the final settlement sheet to verify that total production had been included in the claim and (2) apply a quality loss factor to the tonnage. In addition, the acreage error discussed in Finding No. 1 also affected the 1999 indemnity. As a result, the producer received an overpayment of \$6,678 for crop year 1999 (see exhibit C).

The LAM⁶ states that the insurance provider should "follow up and verify harvested production records documented by receipts from... packing houses..., verify receipts against the entries on the summary/settlement sheets [and] obtain GROSS PRODUCTION for the unit from the summary and/or settlement sheets after verification."

In addition, Prune Crop Provisions⁷ state, "any production of substandard prunes resulting from damage by insurable causes will be adjusted..." This adjustment, or quality loss factor, reduces the total tonnage for damages sustained.

To ensure that the producer reported all production, we attempted to reconcile the production amount that was used to calculate the 1999 indemnity with production data maintained by the Prune Marketing Committee (PMC). In PMC records, we found that one Inspection

⁶ FCIC 25010, paragraph 106(B and C), dated January 1998.

⁷ FCIC 99-036, section 11(b,c, and e), effective for the 1999 crop year.

Report and Certification Form (form P-1) representing 8.7 tons was excluded from the insurance claim for unit 102.

To determine how the insurance provider overlooked the 8.7 tons, we asked if it had collected a copy of the 1999 final settlement sheet to verify total production. The insurance provider stated that it does not collect final settlement sheets as a standard practice. Instead, it collects form P-1's and verifies producers' total production by contacting packinghouses. We told the insurance provider that LAM requires that final settlement sheets be collected to verify total production. The insurance provider agreed that it should have collected these forms but could not explain why it did not collect them.

We also found that a second form P-1 used to calculate the indemnity was overstated by 0.3 ton because the insurance provider failed to apply a quality loss factor. These errors resulted in the total of 44.7 tons of total production being understated by 8.4 tons (8.7 tons – 0.3 ton).

As discussed in Finding No. 1, the insurance provider used 75.0 acres when it calculated the yields for the combined unit. An incorrect APH of 2.3 tons and acreage of 58.6 were used to calculate a 1999 indemnity of \$34,587. Later, the insurance provider recalculated the APH using the 58.6 acres, resulting in an APH of 3.0 tons per acre. Based on the recalculation, the insurance provider determined that producer B was underpaid \$22,176 for crop year 1999 (see Table 2). The insurance provider netted this underpayment with the 1998 overpayment and dispersed additional funds to the producer. However, FSA determined that the correct acreage was 69.8 acres. Based on 69.8 acres, we recalculated an APH of 2.5 tons per acre.

As a result of all the errors discussed above, the producer was overpaid \$6,678 for the 1999 loss.

Table 2: 1999 Overpayment (see exhibit C)

	Per Insurance Provider	Per Audit
Original indemnity payment @ 58.6 acres, APH of 2.3, and 44.7 tons of production	\$ 34,587	\$ 34,587
Recalculated indemnity @ 58.6 acres, APH of 3.0, and 44.7 tons of production	<u>56,763</u>	
Recalculated indemnity @ 69.8 acres, APH of 2.5 and 53.1 tons of production		<u>\$ 50,085</u>
Underpayment	22,176	15,498
Underpayment per insurance provider		<u>22,176</u>
Overpayment outstanding		<u>\$ 6,678</u>

RMA should collect the 1999 overpayment from the insurance provider. In addition, RMA should remind the insurance provider to collect final settlement sheets for all future loss claims in order to verify production.

RECOMMENDATION NO. 3

Collect the 1999 overpayment of \$6,678 for unit 102 from the insurance provider.

Agency Response

RMA conditionally concurred with our finding and recommendation. RMA will conduct an internal review by October 31, 2001, at which time it will make a final determination regarding the overpayment for unit 102.

OIG Position

We are unable to accept your management decision until you provide us with documentation that the insurance provider was billed for \$6,678.

RECOMMENDATION NO. 4

Instruct the insurance provider to collect final settlement sheets to verify that total production is accounted for, or to document the facts if a handler will not provide the form.

Agency Response

RMA conditionally concurred with our finding and recommendation. RMA will conduct an internal review by October 31, 2001, at which time it will make a final determination regarding the collection of settlement sheets by insurance providers.

OIG Position

We are unable to accept your management decision until we review your final determination.

EXHIBIT A – SUMMARY OF MONETARY RESULTS

RECOMMENDATION NUMBER	DESCRIPTION	AMOUNT	CATEGORY
1	Insurance provider paid producer B's 1998 indemnity claim using understated acreage.	\$504	Questioned Costs – Recovery Recommended
3	Insurance provider paid producer B's 1999 indemnity claim using understated acreage and production amounts.	\$6,678	Questioned Costs – Recovery Recommended
TOTAL OVERPAYMENT		\$7,182	

EXHIBIT B – 1998 CLAIM COMPUTATION WORKSHEET

-A- Unit No.	-B- APH Yield ⁷	-C- Coverage Level ⁸	-D- (B x C) Guarantee Per Acre ⁹	-E- Acres	-F- (D x E) Unit Guarantee	-G- Production to Count ¹⁰	-H- (F - G) Unit Loss	-I- Price Election ¹¹	-J- (H x I) Indemnity Amount ¹²
Original Indemnity Calculation Per Insurance Provider:									
102	2.3	0.5	1.2	47.0	56.4	17.0	39.4	\$ 630	\$ 24,822
103	3.7	0.5	1.9	28.0	53.2	8.1	45.1	\$ 630	\$ 28,413
Totals:				75					\$ 53,235
Recalculation of Indemnity by Insurance Provider:									
102 ¹³	3.6	0.5	1.8	58.6	105.5	25.1	80.4	\$ 630	\$ 50,652
Indemnity Calculation Per Audit:									
102	3.0	0.5	1.5	69.8	104.7	25.1	79.6	\$ 630	\$ 50,148
1998 Overpayment									\$ 504

⁷ The actual production history (APH) yield is the sum of the annual yields divided by the number of years in the database. The approved APH may contain up to 10 consecutive crop years of actual and/or assigned yields. In this case, the APH was based on 4 years of data (1994 - 1997).

⁸ The coverage amount is the insurance provided by the crop insurance policy against insured loss of production or value, by unit, as shown on the producer's summary of coverage. Producer B elected a coverage level of 50 percent of the APH.

⁹ The guarantee per acre is shown in tons of production.

¹⁰ The total production to count (in tons) will include all harvested and appraised production of natural condition prunes that grade substandard or better and any production that is harvested and intended for use as fresh fruit.

¹¹ RMA established a price election of \$630 per ton for California prunes for crop year 1998.

¹² The indemnity amount is the reimbursement against loss or damage.

¹³ The original indemnity payment was issued based on an incorrect unit structure. Subsequently, the insurance provider discovered the error and it corrected the unit structure by combining two units (102 and 103) into one unit (102).

EXHIBIT C – 1999 CLAIM COMPUTATION WORKSHEET

-A- Unit No.	-B- APH Yield ¹⁴	-C- Coverage Level ¹⁵	-D- (B x C) Guarantee Per Acre ¹⁶	-E- Acres	-F- (D x E) Unit Guarantee	-G- Production to Count ¹⁷	-H- (F - G) Unit Loss	-I- Price Election ¹⁸	-J- (H x I) Indemnity Amount ¹⁹
Original Indemnity Calculation Per Insurance Provider:									
102	2.3	0.75	1.7	58.6	99.6	44.7	54.9	\$ 630	\$ 34,587
Recalculation of Indemnity By Insurance Provider:									
102	3	0.75	2.3	58.6	134.8	44.7	90.1	\$ 630	\$ 56,763
Totals:				58.6		44.7			\$ 56,763
Indemnity Calculation Per Audit:									
102	2.5	0.75	1.9	69.8	132.6	53.1	79.5	\$ 630	\$ 50,085
Differences:				<u>11.2</u>		<u>8.4</u>			
1999 Overpayment									<u>\$ 6,678</u>

¹⁴ The actual production history (APH) yield is the sum of the annual yields divided by the number of years in the database. The approved APH may contain up to 10 consecutive crop years of actual and/or assigned yields. In this case, the APH was based on 5 years of data (1994 - 1998).

¹⁵ The coverage amount is the insurance provided by the crop insurance policy against insured loss of production or value, by unit, as shown on the producer's summary of coverage. Producer B elected a coverage level of 75 percent of the APH.

¹⁶ The guarantee per acre is shown in tons of production.

¹⁷ The total production to count (in tons) will include all harvested and appraised production of natural condition prunes that grade substandard or better and any production that is harvested and intended for use as fresh fruit.

¹⁸ RMA established a price election of \$630 per ton for California prunes for crop year 1999.

¹⁹ The indemnity amount is the reimbursement against loss or damage.

EXHIBIT D – RMA’S WRITTEN RESPONSE TO THE DRAFT REPORT



United States Department of Agriculture
Farm and Foreign Agricultural Services
Risk Management Agency

AUG - 2 2001

TO: Ernest M. Hayashi
Director, Farm & Foreign Agricultural Division
Office of Inspector General

FROM: Garland D. Westmoreland
Deputy Administrator
Office of Risk Compliance

A handwritten signature in black ink, appearing to read "G. Westmoreland", written over a horizontal line.

SUBJECT: OIG Audit Discussion Draft 05099-5-SF – Indemnity Payments to Prune
Producers in California – Producer B, dated July 13, 2001

I have reviewed the subject report and conditionally concur with the findings and do not desire an exit conference. The Director of the Risk Management Agency's Western Regional Compliance Office (WRCO) will request copies of the audit working papers from your San Francisco Office. If the WRCO concurs with the audit findings and recommendations, they will issue an initial determination to the insurance provider. If the WRCO does not concur, they will provide the basis for the non-concurrence with recommendations for resolving them. The WRCO expects to complete its review and issue either an initial determination or reasons for non-concurrence by October 31, 2001.

If you have any questions, please contact Rich Steffens at (202) 720-0929.



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The Risk Management Agency Administers and Oversees
All Programs Authorized Under the Federal Crop Insurance Corporation

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