

AGRICULTURAL ALTERNATIVES

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Agricultural Business Insurance

Whether you are currently in business or deciding to start an agricultural business, insurance should be part of your risk management strategy. Risk management can take many forms, including insurance, production diversification, and business structure. Insurance shifts some of the risk from the business to the insurance carrier.

There are many types of business insurance that you should consider. This publication will describe these types of insurance and some options to be considered to aid in the decision making process. This publication is not designed to provide recommendations for all types of agricultural operations. You should seek the advice of a trained insurance professional to determine the coverage that best suits your operation. Insurance companies offer many of the same basic coverages, but when tailoring an insurance package for your operation, you should talk to several insurance agents or brokers.

Insurance is available for the business, its employees, and the crops and livestock you may be producing. Depending on the state in which you live, insurance also may be available to cover the revenue of your operation. A single company may have policies for all of these items or you may have separate companies and policies for each form of coverage. Coverage and the cost of the coverage may vary from one company to another. You should explore all of your options when considering insurance alternatives.

Insurances covering the business include general liability, product liability, key person, business property, vehicle, and employee dishonesty. Each of these types of insurance has various options to consider. Insurance policies include statements regarding what is covered and what is excluded,



or not covered, written into the policy. These statements must be read closely and/or explained by the person selling the policy. Not knowing what is or is not covered will have no bearing on whether a claim will be paid. Also, policies will not cover damages above the limits set by the policy. A \$1 million liability policy will not pay \$2 million to an injured person.

Not all operations will need all types of insurance. For example, a business with the owner providing all of the labor and no employees will not need employee dishonesty or workers' compensation insurance. The business structure may also dictate some types of insurance coverage. A partnership may carry life insurance on both partners for

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the value of each partner's share of the business. For example, two equal partners in a business worth \$2 million may carry a \$1 million life insurance policy on each of the partners.

Insurance Covering General Liability

A general liability policy traditionally covers bodily injury and property damage, personal injury, product liability, and medical expenses. Each of these types of coverage is listed under separate sections of the policy and will generally have different limits of coverage. The insurance carrier or company will pay for the expenses that you become legally responsible to pay if the damages occur within the policy term and the incident was an accident. The company will only pay to the dollar limit of the policy.

Exclusions (losses that the company will not cover) are also spelled out in the policy. For bodily injury and property liability coverage, some of these exclusions may be, but are not limited to, use of livestock at shows or in competition and any damage caused by aircraft, watercraft, or by motor vehicle. Any injury to an employee while working will not be covered by the liability policy but will be covered under workers' compensation insurance. This type of injury would be covered under another policy.

Personal injury and product liability policies have many of the same requirements regarding the policy period and limits of coverage. The incident must come from activities usual to farming or the advertising of farm-related goods or services. An example of this activity is when a policyholder writes a published article about someone and that person considers the article offensive and sues. An exclusion to this coverage may be, but is not limited to, the insured knowing the information is false or written prior to the coverage being in effect. Another exclusion could be failure of the good or service to be as advertised in regard to quality or performance.

Under liability coverage medical payments are made regardless of fault. For most companies, the claim must be filed within three years of the accident for reasonable medical expenses to be paid. Reasonable expenses include first aid, medical, dental, or surgical services, and necessary ambulance, hospital, and funeral services. Exclusions for medical coverage may include anyone performing professional services (such as someone from an equipment dealer performing maintenance on equipment), a person performing duties within their normal work, or a member of the insured's household.

Additional coverages will be paid under the liability portion of the insurance. These may include expenses incurred by the insurance company, loss of earnings up to a specified limit, and any interest awarded to the injured party in the judgment.

If your operation uses pesticides, tell your insurance sales person or agent. In the case of a fire to pesticide storage facilities, extensive cleanup may be required if water is used to extinguish the fire. This may lead to runoff of pesticides and may come under the liability section of the policy. A fire company might not use water to extinguish a fire in a pesticide storage facility due to being held partially responsible for the cleanup procedure. If your operation uses or plans to use any hazardous materials, tell your insurance provider.

Insurance Covering Property

Most people are familiar with insurance covering personal property. This same type of insurance also may be used to cover the property of your farm operation. Some of the basic covered losses may include, but are not limited to, fire/lightning, theft, vandalism, and wind/hail. Most policies will cover anything that is not specifically excluded in the policy. Be sure to consult your insurance agent and carefully read your policy.

There are three basic ways of calculating the value of something that has been lost or damaged due to insurable losses. These are actual cash value (ACV), replacement cost value (RCV), and functional replacement cost (FRC). Your policy may use any one or a combination of these to value the cost of the item damaged.

ACV is the cost to replace the item, less accumulated depreciation. For example, if a tractor that originally cost \$50,000 is lost in a fire, the value of the tractor will be \$50,000 minus whatever depreciation is attributed to the tractor. If the accumulated depreciation for the tractor is \$20,000, the insurance payment will be \$30,000. The depreciation used in this calculation does not necessarily match the depreciation used for tax purposes.

RCV is the amount needed to repair or replace the damaged item. For example, if a building damaged by fire or wind is repairable, the value received will be the cost of the repairs to that building. If the building is a total loss, the value received will be the cost to replace the building up to policy limits. The value will be for a building of the same construction and size.

FRC is similar to RCV in that the item will be repaired or replaced with similar kinds and quality materials. FRC is designed to protect property that is somewhat obsolete, but still usable. However, if it was damaged or destroyed, you would not want to rebuild an obsolete building. FRC coverage assigns a "value" to the obsolete building's usability and applies that value to a new structure that is functional. For example, a "bank barn" on a fruit farm has limitations. FRC would provide a "pole building" as a replacement. Fruit farmers cannot store bulk bins in the loft and the lower level may have ceilings too low to store equipment, so they might only use 25 percent of the structure. In this case a \$50,000 pole building would provide more usable space than a \$150,000 to \$200,000 bank barn.

Damage to buildings, structures, and dwellings are covered under the property section of insurance policies. Many companies will have different coverages for different types of buildings. Structural makeup and/or condition will determine which type of coverage the company will allow. The company may also elect not to insure a structure if they determine that the structure is not in adequate condition. The insured may also elect not to insure a specific structure if the structure is not worth replacing if damaged.

Barns, nonattached buildings, and other structures will be covered under their own section of the policy. This section may include silos, portable buildings, and pens. Traditionally, pasture fences are not covered under your policy. Extensions or additions under this section cover private power and light poles, water damage caused by plumbing, heating, air conditioning, or fire protection.

Dwellings and any structures attached to the dwelling may be considered as a type of structure. Dwellings should be insured for from 80 to 100 percent of their value. The items contained in the dwelling are traditionally covered under the household property section of the policy and these items are usually valued at ACV. Policies usually specify the value limits of personal property. Additional coverages are available and will be listed in the policy. These may include credit card theft, water damage, and tree removal.

The insurance company will ask you to list all property including machinery, any crop or supplies inventory, and livestock or poultry. This list is considered the "schedule." When a policy refers to "scheduled property," the items on this list are what are being referenced. Unscheduled property that is still covered under the policy may include items such as fertilizer, pesticides, and grain stored off of the insured's property. If you purchase a piece of equipment or machinery, companies may automatically insure that item for a specified period. It is recommended that any new purchases be included on your schedule as soon as possible. This may be accomplished with a telephone call to your sales person or agent.

There are coverage extensions or additions that may cover property such as grain being transported by a common carrier or not being transported by the owner. Miscellaneous equipment and small equipment such as shovels and tools will be covered under this section of the policy. Blanket coverages may be available to cover any farm property owned by the insured.

Insurance Covering Employees

Before hiring any employees, contact your insurance carrier to determine if they offer workers' compensation insurance. This pertains to all employees, including part-time and after-school or summer employees. Having workers' compensation insurance is critical to any operation or business before hiring any employees. Traditional farmowners' policies will not cover an employee injured on the job.

If your company does not offer workers' compensation insurance, ask for a recommendation of a company that does. A company or business can elect to self-insure for workers' compensation. However, the company or business will have to prove that they have enough resources to be able to self-insure. Self-insuring is not recommended for agricultural or small businesses.

Most states have programs that offer workers' compensation insurance. State-sponsored coverage is traditionally more expensive than that from private companies. However, private companies may elect to not cover a start-up business due to the company not having a history of employing workers. Some farmers' associations may offer a group workers' compensation insurance package for their members.

Workers' compensation insurance is based on the type of operation or work that employees will do and the amount of your annual estimated payroll. For example, a horticultural operation using migrant harvest labor for short periods may have a higher premium than a grain operation with one or two full-time employees. Also, an operation with only \$20,000 in payroll will pay a lower premium than an operation with \$150,000 in yearly payroll. There are experience deductions available for employers who have been in business for several years. Also, your history of claims will have an effect on the amount of premium you may pay.

Workers' compensation carriers will require an audit of your payroll records each year to determine the amount of premium due for the expiring year. Fluctuations in payroll are adjusted for in the expiring year and any additional premium is due immediately. The results of the expiring policy audit are a good resource for future estimates. If you add additional employees during the year, contact your agent to make adjustments to the policy. Companies will require payroll records to be kept on file for a specified time (usually three years) for audit purposes.

In the event of an injured employee, you must follow all guidelines established in the policy. Document any injury or event that may result in a future claim, and keep all records pertaining to the claim or injury on file for future reference. Past injuries may resurface at a later time, which may result in prior claims needing to be revisited. For example, an employee being affected by a pesticide exposure may have adverse effects from that incident several years from the occurrence of the accident. In this case, prior documentation will be critical in determining the history of the claim.

Insurance Covering Over-the-Road Vehicles

Any vehicle licensed by a state should be insured. In fact, many states require proof of insurance before issuing a license for a vehicle. You may be required to provide copies of the driver's licenses to the insurance company for anyone who will drive a business vehicle. Each state has specific laws governing who may operate which vehicles within that state. For example, some states require a Commercial Driver's License (CDL) to operate a large truck covered under a farm license plate.

Some companies may offer discounts for a fleet of vehicles used in the operation. These vehicles may be required to be owned by the business and not the owner, depending on business structure. If the business operates under a fictitious name, the business must be listed on the registration as the owner of the vehicle.

Insurance covering over-the-road vehicles will have liability insurance covering that vehicle included in the policy. This liability insurance may cover the driver, parties involved in an accident, and property, to name a few examples. This does not mean that a farm liability policy is not needed. This coverage will only be for the vehicle and the contents or load of that vehicle. For commercial vehicles, cargo coverage is required for the contents or load the vehicle is carrying. Cargo coverage is an additional coverage added to the existing policy.

Insurance Covering Crops or Income

Since the 2000 Farm Bill, the crop insurance industry has made dramatic changes. Crop insurance is a program with both private and public controls. Individual policies are written by private companies and the policies are regulated and guaranteed by the Risk Management Agency (RMA), which is under the control of the U.S. Department of Agriculture (USDA). The RMA is governed by the Federal Crop Insurance Board of Directors, which has broad responsibilities to administer, regulate, and oversee new policies and coverages. Most crops are now covered under some form of crop insurance. Even minor crops are insurable as part of a whole farm revenue coverage.

Producer premiums are subsidized by USDA with the higher coverage levels receiving a larger dollar amount of subsidy. The more coverage a producer purchases, the more subsidy USDA offers. Pennsylvania also offers additional premium subsidies for its producers.

Crop insurance has two basic components: coverage level for production and coverage level for price. A policy with 75/85 percent yield coverage will cover 75 percent of the producer's average production and 85 percent of the price determined by the federal government for that crop. For

example, if a producer has a historical production level of 100 bushels per acre, a producer with 75 percent coverage will have a claim if production goes below 75 bushels per acre. If the price for that crop is determined to be \$10 per bushel, the producer will receive \$8.50 for the amount of production below 75 bushels per acre.

Other forms of crop insurance are based on production but also have a revenue guarantee. The price is set by prices from contracts on the Chicago Board of Trade (CBOT). This is a combination of production- and revenue-based insurance. The price is determined by a price set for a period of time (usually an average of one month) on the CBOT.

Another form of insurance offered in some states is Adjusted Gross Revenue (AGR) insurance. This type of insurance is based solely on the revenue or income stream of the operation. The IRS's Schedule F tax form is used to determine the amount of protection available to the producer. AGR has limitations concerning the amount of income derived for livestock production that may make the insurance unavailable to some producers. Depending on the state in which the business is located, optional coverages are available under Adjusted Gross Revenue-Lite (AGR-Lite). AGR-Lite does not have the livestock restrictions but has several other restrictions that are the same as AGR concerning amount of income and where that income originates.

You will need to discuss all of your options concerning crop insurance with a crop insurance sales agent. The crop insurance package should be designed specifically for your operation. Several types of coverages may be used to maximize the benefits from the program. More information on crop insurance is available in the publications *Crop Insurance for Pennsylvania Field Crops*, *Crop Insurance for Pennsylvania Vegetable Crops*, *Crop Insurance for Pennsylvania Fruit Crops*, and *Crop Insurance for Northeast Nursery and Greenhouse Crops*, available from your local extension office or on the Pennsylvania Crop Insurance Education Web site, cropins.aers.psu.edu/.

Other Types of Insurance

Other types of insurance may apply to your business or operation. These types of insurance may range from health insurance as part of a benefit package offered to employees to business interruption insurance. Insurance may be a major expense on your yearly financial statements. However, a business should not operate without insurance coverage.

Business interruption insurance will cover the income of the business if a major loss occurs rendering the business unable to operate. For example, this may be due to the loss of a barn and marketable animals in that barn. The business will not have income until new animals can be raised to the same size as the lost animals. Property insurance should pay for the lost animals, but the business income flow should be covered under business interruption insurance.

Employee dishonesty insurance may cover a business that direct markets. If an employee is keeping some of the cash received during the marketing of the product, employee dishonesty insurance will cover this type of loss.

A business owner may use life insurance as a part of the plan to pass along the farm or business. Life insurance may provide a portion of an estate to a survivor who is not involved in the business. Life insurance may also be used in other types of personal plans for the business.

The business owner may offer health insurance to employees as a portion of the benefits package. Health insurance may help attract or retain key employees. For agricultural businesses to compete with other businesses, they need to offer attractive packages to employees.

Another type of insurance available is key employee insurance. This policy is written to cover a key employee that is very valuable to the business. The insurance will provide income to the business in the case of employees no longer being able to perform their duties. An example of this type of employee may be the farm or business manager. If the person who oversees the day-to-day operation of the business cannot fulfill the duties, the business will suffer. This insurance will provide coverage in this event.

You may want or need to consider other types of insurance for your operation. Some companies offer discounts on premiums if the insured uses one company for all of their insurance needs. Discounts are under the judgment of the company and not the insurance salesperson. Discounts may also have guidelines established by the company that will need to be met by the insured. Consult your insurance agent regarding any possible discounts the company may offer.

This publication has outlined some of the key types needed by agricultural businesses. For information specific to your business, contact an insurance professional or professionals, as one company or broker may not be able to provide for all of your needs. It is important to read the policy, fully document any claims, and talk to your insurance agent in the event of any changes to your operation.



For More Information

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Web Sites

Pennsylvania Crop Insurance Education
cropins.aers.psu.edu/

State and Federal Laws That Apply to Farm Labor
[extension.aers.psu.edu/FarmEconomics/
StateFedLawsApplyFarmLabor.pdf](http://extension.aers.psu.edu/FarmEconomics/StateFedLawsApplyFarmLabor.pdf)

USDA, Risk Management Agency
www.rma.usda.gov/

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