LIVESTOCK GROSS MARGIN FOR DAIRY CATTLE INSURANCE POLICY QUESTIONS AND ANSWERS

1. Q: What is the Livestock Gross Margin for Dairy Cattle Insurance Policy?

A: The Livestock Gross Margin for Dairy Cattle Insurance Policy provides protection against the loss of gross margin (market value of milk minus feed costs) on the milk produced from dairy cows. The indemnity at the end of the eleven-month insurance period is the difference, if positive, between the gross margin guarantee and the actual gross margin. The Livestock Gross Margin for Dairy Cattle Insurance Policy uses futures prices and state basis for corn, soybean meal, and milk to determine the expected gross margin and the actual gross margin. The price the producer receives at the local market is not used in these calculations.

2. Q: Who is eligible for the Livestock Gross Margin for Dairy Cattle Insurance Policy?

A: Any producer who owns dairy cattle in Arizona, Colorado, Connecticut, Delaware, Illinois, Indiana, Iowa, Kansas, Maine, Maryland, Massachusetts, Michigan, Minnesota, Missouri, Montana, Nebraska, Nevada, New Hampshire, New Jersey, New York, North Dakota, Ohio, Oklahoma, Pennsylvania, Rhode Island, South Dakota, Texas, Utah, Vermont, West Virginia, Wisconsin, and Wyoming is eligible for Livestock Gross Margin for Dairy Cattle Insurance Policy coverage.

3. Q: What milk is eligible for coverage under the Livestock Gross Margin for Dairy Cattle Insurance Policy?

A: Only milk sold for commercial or private sale primarily intended for final human consumption from dairy cattle fed in any of the eligible states is eligible for coverage under the Livestock Gross Margin for Dairy Cattle Insurance Policy.

4. Q: What are the advantages of the Livestock Gross Margin (LGM) policy over traditional options?

A: LGM has two advantages over traditional options.

Convenience. Producers can sign up for LGM twelve times per year and insure all their milk production they expect to market over a rolling eleven-month insurance period. The producer does not have to decide on the mix of options to purchase, the strike price of the options, or the date of entry.

Customization. The LGM policy can be tailored to any size farm. Options cover fixed amounts of commodities, and those amounts may be too large to be used in the risk management portfolio of some farms.

5. **Q: How is LGM different from traditional options?**

A: LGM is different from traditional options in that LGM is a bundled option that covers both the price of milk and feed costs. The mix of target milk marketings per dairy cow and target feed rations are supplied by the producer. This feature allows the producer to select feed rations and production levels that best reflect their actual production situation. The resulting bundle of options effectively insures the producer's gross margin, milk revenue minus feed costs, over the insurance period.

LGM works as a bundle of options that pay the difference, if positive, between the value at purchase of the options and the value at the end of a certain time period. So, LGM would pay the difference, if positive, between the gross margin guarantee and the actual gross margin, as defined in the policy provisions.

6. **Q: Can LGM be exercised?**

A: No, LGM cannot be exercised during the insurance period. LGM pays the difference, if positive, between the gross margin guarantee and the actual gross margin, as defined in the LGM provisions, at the end of the insurance period.

7. **Q: Does LGM use the price the producer receives at the market?**

A: No. The prices for LGM are based on simple averages of futures contract daily settlement prices and are not based on the prices the producer receives at the market. Milk and corn prices are adjusted for state-specific and month-specific expected basis. The same basis levels used to adjust expected corn prices and expected milk prices are used to adjust actual corn prices and actual milk prices.

8. **Q: Does LGM make early indemnity payments?**

A: Yes. If an indemnity is due under LGM coverage, the company will send the producer a notice of probable loss after the last month of the producer's marketing plan. The last month of the producer's marketing plan is the last month in which the producer indicated target marketings on the application.

9. **Q: How is the underwriting capacity for LGM distributed?**

A: LGM has limited underwriting capacity that will be distributed through the Federal Crop Insurance Corporation's underwriting capacity manager. The underwriting capacity will be distributed on a first come, first served basis. LGM will not be offered for sale after capacity is full or at any time the underwriting capacity manager is not functional.

10. **Q: When is LGM for Dairy Cattle sold and how long do the sales periods last?**

A: LGM for Dairy Cattle is sold on the third to last business day of each month. The sales period begins as soon as RMA reviews the data submitted by the developer after the close of markets on the last day of the price discovery period. The sales period ends at 9:00 AM the following day. If expected milk and feed prices are not available on the RMA website, LGM will not be offered for sale for that insurance period

11. **Q: How are the feed quantities for LGM determined?**

A: Producers must supply the total number of tons of corn or corn equivalent and the tons of protein meal or protein meal equivalent that they expect to feed for each month in which they insure their milk. Feed quantities are bounded. The number of tons of corn or corn equivalent must be between 0.00364 and 0.02912 tons per hundredweight of milk. The number of tons of protein meal or protein meal equivalent must be between 0.000805 and 0.006425 tons per hundredweight of milk.

12. **Q: How can feed equivalents be determined?**

A: Producers can determine the corn and soybean meal equivalents of their feeds. The only restriction is that the feed rates must be within the bounds listed in Question 11. The LGM-Dairy Commodity Exchange Endorsement contains a table with suggested feed conversion rates. Below is an example feed conversion based on the suggested rates. If a producer fed 140 bushels of oats and 0.2 tons of meat meal, he/she would need to convert these to corn and soybean meal equivalents.

The conversion for the oats can be done in two steps:

Step 1. Converting feed to tons.
140 bushels of oats X (32 pounds/1 bushel of oats) X (1 ton/2000 pounds) = 2.24 tons

Step 2. Using the suggested conversion rates for corn and soybean meal equivalents.
2.24 tons of oats X 0.120 = 0.2688 tons of soybean meal equivalents
2.24 tons of oats X 0.779 = 1.7450 tons of corn equivalents

The conversion for the meat meal can be done in one step as the meat meal is already measured in tons:

Step 1. Using the suggested conversion rates for corn and soybean meal equivalents.
0.2 tons of meat meal X 1.227 = 0.2454 tons of soybean meal equivalents
0.2 tons of meat meal X -0.349 = -0.0698 tons of corn equivalents

So the corn and soybean meal equivalents for 140 bushels of oats and 0.2 tons of meat meal are 0.5142 tons of soybean meal (0.2688 + 0.2454) and 1.6752 tons of corn equivalent (1.7450 – 0.0698).

Feeds should be combined when creating corn and soybean meal equivalents. Please notice that many of the protein meal feeds have negative corn equivalent values.

13. Q: How are the feed costs for LGM determined?

A: Expected feed costs for a month equal the expected corn price times the tons of corn or corn equivalent (converted to bushels) specified by the producer for that month plus the expected soybean meal price times the tons of protein meal or protein meal equivalent specified by the producer for that month. Actual feed costs use actual prices for the month and the same producer-specified quantities of feed.

14. Q: What types of losses are covered by LGM?

A: LGM covers the difference between the gross margin guarantee and the actual gross margin. LGM does not insure against dairy cattle death loss, unexpected decreases in milk production, or unexpected increases in feed use.

15. Q: Where can I purchase LGM coverage?

A: LGM is available for sale at your authorized crop insurance agent's office. Crop insurance agents must be certified by an insurance company to sell LGM and that agent's identification number must be on file with the Federal Crop Insurance Corporation.

16. Q: What months make up the Insurance Period?

A: The insurance period contains the eleven months following sales closing. For example, the insurance period for the January 29 sales closing date contains the months of February through December. However, coverage begins in the second month of the insurance period, so the coverage period for this example is the months of March through December.

17. Q: What are the Producer's Target Marketings and Target Feed?

A: A determination made by the insured as to the quantity of milk to be sold and the quantity of feed to be fed for each month during the insurance period. Target marketings must be less than or equal to that producer's applicable approved target marketings as certified by the producer. Target feed must be within the bounds that are specified in the underwriting rules.

18. Q: What are the Producer's Approved Target Marketings?

A: The producer's approved target marketings are the maximum amount of milk that may be stated as target marketings on the application. Approved target marketings are certified by the producer and are subject to inspection by the insurance company. A producer's approved target marketings will be the lesser of the capacity of the producer's dairy operation for the eleven-month insurance period as determined by the insurance provider and the underwriting capacity limit as stated in the special provisions.

19. Q: What is the Expected Corn Price?

A: For months in which a CBOT corn contract expires, the simple average of the settlement prices for the CBOT corn futures contract for the month during the expected price measurement period plus the state-specific corn basis for the month. For other months, the state-specific corn basis for the month plus the weighted average of the immediately surrounding months' simple average of the daily settlement prices during the expected price measurement period. The expected price measurement period is the three days prior to the second to last trading day of the month. (See the Commodity Exchange Endorsement for more information.) Prices will be released by RMA after the markets close on the last day of the price discovery period.

20. Q: What is the Expected Soybean Meal Price?

A: For months in which a Chicago Board of Trade (CBOT) soybean meal contract expires, the expected soybean meal price is the simple average of the daily settlement prices of the CBOT soybean meal futures contract for the month during the expected price measurement period. For other months, the expected soybean meal price is the weighted average of the immediately surrounding months' simple average of the daily settlement prices during the expected price measurement period. No basis adjustment is made to soybean meal prices. The expected price measurement period is the three days prior to the second to last trading day of the month. (See the Commodity Exchange Endorsement for additional information on the calculation of the expected soybean meal price.) Prices will be released by RMA after the markets close on the last day of the price discovery period.

21. Q: What is the Expected Cost of Feed?

A: The expected cost of feed for each month equals the target corn (or corn equivalent) to be fed times 2000/56 (to convert tons to bushels) times the expected corn price for that month, plus the target protein meal (or protein meal equivalent) to be fed times the expected soybean meal price for that month. Prices will be released by RMA after the markets close on the last day of the price discovery period.

Expected Cost of Feed for an operation that produces 1,560 cwt. of milk in a month with target feed levels of 20.5 tons of corn and 6 tons of soybean meal:

20.5 tons x (2,000/56) x Expected Corn Price$_t$ + 6 x Expected Soybean Meal Price$_t$

If the Expected Corn Price is $2.10 per bushel and the Expected Soybean Meal Price is $150 per ton, expected feed costs would be $2,437.50 [20.5 x (2,000/56) x $2.10 + 6 x $150 = $2,437.50].

22. Q: What is the Expected Milk Price?

A: The expected milk price is the simple average of the daily settlement prices of the CME Class III milk futures contract for the month during the expected price measurement period plus the state-specific milk basis for the month. The expected price measurement period is the three days prior to the second to last trading day of the month. Prices will be released by RMA after the markets close on the last day of the price discovery period.

23. Q: What is the Expected Gross Margin per Month?

A: The expected gross margin per month is the approved target marketings times the expected milk price for that month less the expected feed costs for that month. Extending the above example, if approved target marketings are 1,560 cwt. of milk for a month, the expected milk price is $12 per hundredweight, and the expected feed cost is $2,437.50, then the Expected Gross Margin is equal to $16,282.50 [(1,560 x $12.00) – $2,437.50 = $16,282.50].

24. Q: How is the expected total gross margin calculated for each insurance period?

A: The expected total gross margin is the sum of the expected gross margins for each month of an insurance period.

25. Q: How is the gross margin guarantee calculated for each insurance period?

A: The gross margin guarantee for each coverage period is calculated by subtracting a deductible amount from the expected total gross margin for the applicable insurance period.

If our example producer wants a $0.10 deductible on each of 1,560 hundredweight of milk, then the gross margin guarantee would be $16,126.50 [$16,282.50 – ($0.10 x 1,560) = $16,126.50].

The deductible is the portion of the expected gross margin that you elect not to insure. Allowable deductible amounts range from zero to $1.50 per hundredweight of milk in $0.10 per hundredweight increments.

26. Q: What is the Actual Corn Price?

A: For months in which a CBOT corn contract expires, the actual corn price is the simple average of the daily settlement prices for the CBOT corn futures contract for the month during the actual price measurement period plus the state-specific corn basis for the month. For other months, the state-specific corn basis for the month plus the weighted average of the immediately surrounding months' simple average of the daily settlement prices during the actual price measurement period. The actual price measurement period is the last three trading days prior to contract expiration. (See the Commodity Exchange Endorsement for more information.)

27. Q: What is the Actual Soybean Meal Price?

A: For months in which a CBOT soybean meal contract expires, the actual soybean meal price is the simple average of the daily settlement prices for the CBOT soybean meal contract for the month during the actual price measurement period. For other months, the actual soybean meal price is the weighted average of actual soybean meal prices in the immediately surrounding months. The actual price measurement period is the last three trading days prior to contract expiration. (See the Commodity Exchange Endorsement for more information.)

28. Q: What is the Actual Cost of Feed?

A: The actual cost of feed for each month equals the target corn to be fed times 2,000/56 (to convert tons to bushels) times the actual corn price for that month, plus the target soybean meal to be fed times the actual soybean meal price for that month. Calculation of the actual cost of feed uses the same target corn and soybean meal to be fed as the expected cost of feed. Changes in feed rations from these target amounts are not covered under the LGM for Dairy Cattle policy.

The actual cost of feed for an operation that produces 1,560 cwt. of milk in a month with target feed levels of 20.5 tons of corn and 6 tons of soybean meal:

20.5 tons x (2,000/56) x Actual Corn Price_t + 6 x Actual Soybean Meal Price_t

If the Actual Corn Price is $2.00 per bushel and the Actual Soybean Meal Price is $175 per ton, actual feed costs would be $2,514.29
[20.5 x (2,000/56) x $2.00 + (6 x $175) = $2,514.29].

29. Q: What is the Actual Milk Price?

A: The actual milk price is the simple average of the daily settlement prices of the CME Class III milk futures contract for the month during the actual price measurement period plus the state-specific milk basis for the month.

The actual price measurement period is the last three trading days prior to contract expiration. (See the Commodity Exchange Endorsement for more information.)

30. Q: What is the Actual Gross Margin per Month?

A: The actual gross margin per month is the actual marketings times the actual milk price for that month less the actual feed costs for that month. Extending the above example, if actual marketings are 1,560 cwt. of milk for a month, the actual milk price is $10 per hundredweight, and the actual feed cost is $2,514.29, then the actual gross margin is equal to $13,085.71 [(1,560 x $10.00) – $2,514.29 = $13,085.71].

31. Q: How is the actual total gross margin calculated?

A: The actual total gross margin is the sum of the actual gross margins for each month of an insurance period.

32. Q: How are indemnities determined?

A: Indemnities to be paid will equal the difference between the gross margin guarantee and the actual total gross margin for the insurance period.

The producer in our example would receive an indemnity of $3,040.79 ($16,126.50 - $13,085.71 = $3,040.79).

33. Q: Is a marketing report required and when should the company receive it?

A: Yes, in the event of a loss the producer must submit a marketing report and sales receipts showing evidence of actual marketings for each month. The producer must submit the marketing report within 15 days of receipt of notice of probable loss.

34. Q: Is this a continuous policy?

A: This is a continuous policy with twelve overlapping insurance periods per year. Target marketings must be submitted for each insurance period. If a target marketing report is not submitted by the sales closing date for the applicable insurance period, target marketings for that insurance period will be zero.

35. Q: When must the application for insurance be turned into the company?

A: The sales closing dates for the policy are the third to last business day of the month for each of the twelve calendar months. The application must be completed and filed not later than the sales closing date of the initial insurance period for which coverage is requested. Coverage for the milk described in the application will not be provided unless the insurance company receives and accepts a completed application and a target marketing report, premium is paid in full, and the insurance company sends the producer a written summary of insurance.

36. Q: When does coverage begin?

A: Coverage begins one month after the sales closing date. For example, for the January 29 sales closing date, coverage begins on March 1.

37. Q: When are the contract change dates for the policy?

A: The contract change date is April 30. Any changes to the Livestock Gross Margin policy will be made prior to this contract change date.

38. Q: When are the cancellation dates for the policy?

A: The cancellation date is June 30 for all insurance periods.

39. Q: When is the end of insurance for the policy?

A: The end of insurance for the policy is eleven months after the sales closing date. For example for the January 29 sales closing date, coverage ends on December 31.

40. Q: What deductible levels are available for the policy?

A: The producer may select deductible levels between $0 and $1.50 per hundredweight of milk in $0.10 increments.

41. Q: How is the producer's premium calculated?

A: The producer's premium is calculated by a premium calculator program that determines the premium based on target marketings and expected gross margins for each period and deductibles.

42. Q: When is the premium for the policy due?

A: The premium for the initial insurance period is due with the application for Livestock Gross Margin insurance coverage. The premium for all subsequent insurance periods is due with the target marketings report, which is due no later than the sales closing date.

43. Q: What portion of a producer's milk will be insured under the policy?

A: 100 percent of a dairy farmer's milk can be insured under the policy.

44. Q: What information is required for acceptance of an application for the Livestock Gross Margin for Dairy Cattle Insurance Policy?

A: The application for the Livestock Gross Margin for Dairy Cattle Insurance Policy must contain all the information required by us to insure the gross margin for the livestock or livestock products. Applications that do not contain all social security numbers and employer identification numbers, as applicable (except as stated in the policy), deductibles, a target marketings report, and any other material information required to insure the gross margin for the livestock or livestock products, will not be acceptable.

45. Q: Can the manager of RMA suspend LGM sales?

A: Yes. Sales of LGM may be suspended for the next sales period if unforeseen and extraordinary events occur that interfere with the effective functioning of the corn, soybean meal, or milk commodity markets.

46. Q: What if the expected milk and feed prices are not posted on the RMA website on the sales closing date for the month?

A: LGM will not be available for sale for that insurance period.