United States Department of Agriculture

Federal Crop Insurance Corporation

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TO: Board of Directors

March 29, 2001

Minute Exhibit No. 2033
Board Meeting of 3/29/01

FROM: Phyllis W. Honor /s/ Phyllis W. Honor
Acting Manager

SUBJECT: Board Memorandum No. 605
Acting Manager's Report

1. Summary of Business 2000/2001 (as of 03/26/01)

Summary of Business, 2000: The 2000 book of business and program participation numbers are complete at this time with only late and corrected claims continuing to create minor changes in the crop year statistics. To date, nearly $34.3 billion dollars in liability have been reported on approximately 205 million acres of crop land representing 1,319,235 crop policies. Indemnities in the amount of nearly $2.442 billion have been paid out to date. Acreage insured under additional coverage policies increased by about 14 million acres between 1999 and 2000, while CAT acres decreased by about 4.8 million acres. The 2000 liability represents an increase of more than ten percent from 1999. Actual losses for the year ended up about $400 million higher than estimated by the Regional Offices (RO) from June to December. The Loss Ratio is .97. A copy of the National Summary of Business Report, as of March 26, 2001 is attached.

Preliminary Summary of Business, 2001: Although the bulk of spring acreage reports have yet to be filed, FCIC is expecting the new premium subsidies to assist producers in obtaining higher levels of coverage this year. To date premium volume is $434 million. The current Summary of Business Report for 2001 indicates that only 201,877 policies with premium have been reported covering 29 million net acres. Total liability is $7.1 billion and $24 million has been paid out for 2001 crop losses to date.

Current Loss Assessment: Risk Management Agency (RMA) is maintaining a strategy of monitoring loss situations closely as they develop to ensure uniformity between insurance providers and equal treatment of policyholders. This strategy includes a continuing emphasis to all parties to the crop insurance program of the need to assess requests for policy and procedural changes for their impact on the larger program issues including funding, actuarial soundness, simplification, and the contractual obligations between FCIC, insurance providers, and producers.

2. Program Issues:

2. Crop Revenue Coverage – Durum Wheat

Durum wheat is insurable under Crop Revenue Coverage (CRC) in fifteen North Dakota counties and by written agreement in adjoining counties. A key element in providing this coverage is the establishment of a base price. The CRC Commodity Exchange Endorsement - Wheat (CEEW) defines the base price for durum wheat as the February average daily settlement price for the harvest year's Minneapolis Grain Exchange (MGE) September durum wheat futures contract.

A minimum of 15 daily prices must be included in the average and each daily price must have a minimum of 25 open interest contracts. The CEEW also provides that if the minimum number of daily prices with the minimum level of open interest contracts are not found for the September contract during the month of February, prices may be taken for the contract immediately prior to the September contract, which is the July durum wheat futures contract.

For the 2001 crop year, there were insufficient numbers of open interest contracts to get the required fifteen daily prices for the MGE September durum wheat futures contract and the MGE July durum wheat futures contract. Since the minimum requirements were not met, no CRC base price for durum wheat could be determined for the 2001 crop year.

As a result, RMA issued Manager Bulletin MGR-01-011 (copy attached) advising reinsured companies of the non-availability of a CRC base price for durum wheat for the 2001 crop year. On March 9, 2001, RMA issued Manager Bulletin MGR-01-011.1 (copy attached) which advised reinsured companies, that unless they elected to accept all liability under the policy, all CRC wheat policies where durum wheat was reported on the acreage report for the 2000 crop year and the producer elected the separate durum wheat price must be canceled in writing for the 2001 crop year by the applicable cancellation/termination date of March 15, 2001.

On Thursday March 15, 2001, a group of North Dakota producers asked U.S. District Judge Rodney Webb to issue a temporary restraining order against the Department of Agriculture. The producers claimed the Department of Agriculture had no legal right to cancel a crop insurance program for durum wheat just days before their sign-up deadline.

Judge Webb denied the producers' request for a restraining order; saying he did not believe the RMA is mandated by Congress to provide the insurance program.

2. Program Issues:

Southern Minnesota Sugar Beets

On March 2, 2001, RMA issued Manager Bulletin MGR-01-010 (copy attached) to address damage to sugar beet crops affected by drought, freeze, and other natural perils. RMA was notified that a freeze occurred on October 6 - 10, 2000, in southern Minnesota which included the counties of Big Stone, Brown, Chippewa, Kandyohi, Lac Qui Parle, McLeod, Meeker, Nicollet, Pope, Redwood, Renville, Sibley, Stearns, Stevens, Swift, and Yellow Medicine. After the freeze, insured sugar beet producers did not remove the tops from the affected sugar beet crop and allowed the crop to heal.

After harvesting, the sugar beets were delivered to a farmer-owned cooperative for processing. Samples of each load of sugar beets were cut and tested to determine whether damage had occurred. At the time the sugar beets were delivered to the cooperative, there was no visible freeze damage. The sugar beets were placed in piles, as customary, after being weighed and tested to await processing.

Unseasonably warm temperatures occurred in southern Minnesota after the sugar beets were placed in piles. According to sugar beet experts, freezing and thawing of drought-stressed sugar beets causes accelerated tissue cell damage and sugar loss. Damaged tissues became susceptible to microorganisms that greatly increased the decomposition of sucrose reducing sugar content levels.

Because the processor was telling producers that the sugar beets were fine upon delivery and that it could process the beets, producers had no reason to know that their beets had been damaged until notified by the processor in mid-December. Since producers were not aware of any damage until after the end of the insurance period, they could not have provided a timely notice of damage which is a pre-requisite condition for filing a claim for indemnity.

MGR-01-010 informs the insurance providers that a cause of loss that damages the production during the insurance period, but is not manifested until after the insurance period is a covered loss and if the producers did not know that their production was damaged within the time period to report losses, that time period would not be enforceable under the basic tenets of contract and insurance law. RMA informed the insurance providers that the payment of losses under these conditions would be reinsurable.

Private insurance providers through their trade association have expressed their disagreement with RMA's position and have requested that RMA withdraw Manager Bulletin MGR-01-010. RMA has met with the trade association and the insurance providers to discuss the information used to reach its' conclusions.

2. <u>Program Issues</u>:

<u>2000 Crop Year Dry Beans - Pink Eyed Beans</u>

As a result of numerous complaints from Texas and New Mexico, RMA issued an Informational Memorandum on December 15, 2000 (copy attached), regarding requirements for insuring "pinkeye" beans with written agreements. These complaints alleged that policies were issued for "pink-eyed" beans using standard county rates where Blackeye Beans were insurable. On consulting with the Grain Inspection Packers and Stockyards Administration (GIPSA), RMA was advised that "pinkeye" beans would be classified as Miscellaneous Beans under the standards referenced in the policy and county actuarial tables. Miscellaneous Beans were required to be insured with a written agreement unless listed on the county actuarial tables.

In February 2001, GIPSA advised RMA in writing that they had reviewed 2000 crop year samples and determined that the "pinkeye" beans they had examined would be classified as Blackeye Beans, thus making them insurable using standard rates in counties where Blackeye Beans were listed on the county actuarial tables. RMA issued Manager's Bulletin MGR-01-013 (copy attached) advising that "pinkeye" beans insured under standard Blackeye Bean rates or written agreement for 2000 were insurable and that for the 2001 crop year, "pinkeye" beans would be insurable using standard rates in any county with Blackeye Beans listed on the county actuarial table.

<u>Coverage for Organic Farming Practices</u>

Section 123 of the Agricultural Risk Protection Act of 2000 (ARPA) requires that organic farming practices be recognized as good farming practices. As a result, on January 17, 2001, RMA issued Manager's Bulletin, MGR-01-004 (copy attached), regarding Organic Farming Practices and the Implementation of the Section 123 of Agricultural Risk Protection Act of 2000 (ARPA). The 2001 Organic Crop Insurance Underwriting Guide was issued by on March 15, 2001 (copy attached).

3. Status Report on Implementation of ARPA

Risk Compliance Report on ARPA Section 121

RMA is charged with implementing section 121 of ARPA. RMA has been working closely with the Farm Service Agency (FSA) on five implementation teams. Each team is implementing a section of the legislation. The areas the teams are addressing are:

Consultation with FSA State Committees, Training of FSA Personnel, Claims Audit, Fraud Referrals and Data Reconciliation. The teams focused their work on developing internal communications and procedures for the two agencies to work together at the field level. The two agencies developed a Coordinated Plan for Implementation signed by Secretary Glickman on January 12, 2001, as required by ARPA. It was presented to the crop insurance industry on January 18, 2001. The ARPA teams were then expanded to include company participants. On March 1, 2001, the RMA and FSA team leaders met with the company participants to brief them in detail on the work done to date by the teams.

On March 28-29, 2001, the designated FSA State Office Points of Contact are being trained in Kansas City on the RMA compliance and oversight process. This will include the Consultation, Referrals and Claims Audit procedures developed by the teams. The procedures were incorporated into a handbook and will be distributed in early April. Also in April, training of the FSA county offices in loss adjustment begins. The reconciliation of RMA and FSA data from the 2000 FSA Disaster Assistance program is currently underway. Procedures to automate the process will be developed later in the year (copy is attached).

Contracting Skills-Research and Development

Research and Development has implemented a comprehensive training program to provide a series of classes on contracting skills to meet the new mandate of ARPA of accomplishing the mission of the agency through contractors. Since numerous R&D staff will be less hands-on and more contractor project managers, we are working to retool our workforce and equip them with the knowledge and skills necessary to be successful in the new culture and way of doing business. A number of classes have already been held this year: Introduction to Contracting, Cost Estimating, Task Order Contracting and Contract Administration. Four more classes are scheduled to be held before the end of the fiscal year: COR Training, Task Order Writing, Contract Law and Best Value Training. These training classes will give the staff the needed information and skills to move forward in developing contract vehicles to implement ARPA. The training that has been provided to date has already had significant impact on our ability to accomplish tasks via contract. For example, a contract to obtain a pool of contractors for developing new risk management programs has been awarded and several task orders under this contract are in the process of being competed for by the pool of contractors.

ARPA Contracting Expenditures for FY2001:

Sec 131 Reimbursements: $10,000,000-This requires a regulation describing the process and requirements for reimbursement of costs. The draft regulation is in OGC for review. Once the regulation is final, reimbursements will be contingent upon submitting companies making successful requests for reimbursement.

Sec 131 R&D Contracting and Partnerships: $20,000,000 -$2,000,000 of this was assigned to RME for educational activities. The remainder is for R&D product development. Two task orders have been released for competition within this pool of contractors. Several more task orders are in process within R&D. Plans are being developed to expand the pool of contractors so that all projects for which funds are available can be awarded.

Sec 121 Program Compliance: $9,000,000-$5,000,000 has been spent on a cooperative agreement with Tarleton State University, Texas and the remainder is being spent on data reconciliation between RMA and FSA data, and for training of FSA personnel for risk compliance assistance.

Sec 133 Risk Management Education: $10,000,000 -$5,000,000 for risk management education has been transferred to CSREES. The remaining $5,000,000 is being used by RME for crop insurance education. Two projects are proceeding through FEDSIM, with other cooperative agreements, grants, and contracts in process.

Sec 142 Board Reviews: $3,500,000-This money is available for Expert Reviews and certain implementation costs. One Board review, (Income Barley) is in process with FSA contracting, and is awaiting signature of an AD-700. However, if the Board decides to rescind its previous decision that expert review of these program changes are required, no reviews will be pending.

Sec 225 Livestock and Poultry Waste: $5,000,000 -Insurance Services is working on a proposal.

Section 133-Education and Risk Management

ARPA directs RMA to "establish a program under which crop insurance education is provided to producers in under served states." Secretary Glickman identified the 15 under served states which are: Maine, Vermont, New Hampshire, Massachusetts, Rhode Island, Connecticut, New York, New Jersey, Pennsylvania, Maryland, Delaware, West Virginia, Nevada, Utah and Wyoming. The Act provides $5 million in funding for FY 2001-2005. The Raleigh Regional Office will host kick-off conferences in May and June to implement Section 133. A five year strategic and 1 year action plan outlining the direction and focus of risk management education plans and activities for these 15 under-served states was approved with implementation currently underway. As a result, several ideas for potential projects have been received from the private sector which are currently being reviewed.

Section 225-Improved Storage and Management of Livestock and Poultry Waste

Section 225 directs the Secretary to review and assess the actual or potential failure of waste storage and handling systems used in the livestock or poultry production and the environmental damages associated with the failure of the systems and to study and demonstrate appropriate market oriented mechanisms to assist livestock producers and poultry producers to prevent the failure of the systems and rectify environmental damages associated with the failure of the systems. This section is to be carried out through grants, contracts and cooperative agreements.

On October 13, 2000, RMA received an unsolicited proposal. The proposal was reviewed and later revised to focus more attention on mechanisms that may be used to assist producers to better manage handling and storage of animal waste and mitigate environmental damages caused by system failures. A decision is pending on the proposal.

4. Upcoming Issues- 2001 Crop Year

Cooperative Selling

On June 30, 2000, the Standard Reinsurance Agreement was amended to incorporate section 1508(b)(5)(B) of the Federal Crop Insurance Act, as amended by the Agriculture Risk Protection Act of 2000 ("Act"). Under section 1508(b)(5)(B) of the Act, if permitted by state law, a cooperative or trade association that receives a licensing fee or other payment from an insurance provider, may return all or part of the fee or payment to policyholders who purchase catastrophic risk protection insurance (CAT) or additional coverage in those states where the practice is permitted by state law. Under these arrangements, CAT fees may also be paid on the behalf of policyholders in the

states in which rebating practices are permitted as well as in adjoining states.
A Manager's Bulletin, recently drafted to address compliance with the Act, is undergoing legal sufficiency clearance.

<u>Energy Issues-Irrigation Water and Power Shortages</u>:

RMA has been working with the Regional Offices and producer groups to identify the issues associated with irrigation water and power shortages for the coming crop year. RMA has drafted a bulletin to address insuring and indemnifying producers who are impacted by these potential shortages.

RMA is also closely watching the impact of increased costs, particularly fertilizer, as they relate to acceptable farming practices. There is concern that with input costs on the rise, some farmers may cede production risks on to their crop insurance policies through reduced application of fertilizer, reduced tillage to save fuel, etc. RMA will continue to monitor this issue throughout the growing season and will remind producers and their representatives of the policy requirement to carry out good farming practices as needed.

Attachments