



**United States
Department of
Agriculture**

Federal Crop
Insurance
Corporation

1400 Independence
Avenue, SW
Stop 0801
Washington, DC
20250-0801

DATE: June 5, 2007

TO: Board of Directors
Federal Crop Insurance Corporation

FROM: Eldon Gould /signed/
Manager

SUBJECT: Manager's Report
Exhibit No. 2899

This memorandum serves as the Manager's Report to the Board of Directors (Board), Federal Crop Insurance Corporation (FCIC), for the June 5, 2007 meeting. The report relates to program issues as outlined below:

Program Issues:

Pasture, Rangeland and Forage Pilot (PRF) Program Update – On May 21, 2007, the Risk Management Agency (RMA) released the results for the first Index Interval for the PRF Rainfall Index pilot area. RMA and the contractor Grazingland Management Systems (GMS) followed its Standard Operating Procedures for verifying and validating the data at the end of the Index Interval prior to release. Any potential anomalies were verified resulting in no modifications needed. There were 191 counties (out of 222 eligible for the pilot program) with participation in the first Index Interval. Out of those, 39 counties resulted in payable losses at the conclusion of the first Index Interval. These included counties in southern Texas, most of eastern Colorado, south-central Idaho, and parts of western South Carolina. The loss ratio for these 39 counties is expected to be approximately 0.42, while the overall loss ratio for the first Index Interval is expected to be approximately 0.09. The first Index Interval resulted in payable losses in several areas of the pilot program.

The PRF-RI Index Interval II period ended on May 31, 2007 and the first Index Interval for the PRF-Vegetation Index pilot will end on June 30, 2007.

As of May 21, 2007, there are 8,024 Rainfall Index policies sold covering 24,539,207 acres with \$328,224,658 in total liability. Each state in the pilot has a policy sold. The pilot area in Texas had the greatest number of polices sold with 5,928 policies and over 20.8 million acres covered. In the pilot, Texas has the largest area and South Carolina has the smallest number of potential acres. South Carolina had the lowest number of polices sold at 9 and just over 2,000 acres insured with \$159,995 in liability.

Vegetation Index pilot program sales are at 1,688 policies sold covering 3,963,141 acres with nearly \$61,791,260 in total liability. All states in the pilot sold policies with the

exception of Pennsylvania. The South Dakota pilot area contained the largest potential acres and has the highest number of policies with 886 policies sold. These policies insure 3,030,082 acres and a liability of \$41,987,230. The state with the lowest number of sales is South Carolina with two policies covering 318 acres with nearly \$20,289 in total liability.

Regulatory Update:

Combination Regulation Update – Currently, the final rule is with the Office of General Counsel (OGC) for review and approval. The final rule is to be effective for the 2009 crop year.

Mustard Crop Provisions – On November 16, 2006, the proposed rule published in the *Federal Register* converts the Mustard pilot crop insurance program to a permanent program. The final proposed rule comment period ended January 16, 2007. RMA's Product Administration and Standards Division (PASD) is in the process of responding to the public comments. The final rule is targeted for the 2008 crop year.

Cabbage Crop Provisions – On November 16, 2006, the proposed rule published in the *Federal Register* converts the Cabbage pilot crop insurance program to a permanent program. The proposed rule comment period ended January 16, 2007. PASD is in the final rule process of responding to the public comments. The final rule is targeted for the 2009 crop year.

Grape and Table Grape Crop Provisions – Currently, the proposed rule is in RMA's Product Management (PM) Office as part of the concurrence process. The rule is targeted for the 2009 crop year.

Fresh Market Sweet Corn – Currently, the final rule is with OGC for review and approval. The final rule is targeted for the 2008 crop year for counties with a November 30, 2007 contract change date.

Mint Crop Provisions – On April 17, 2007, the Final rule published in the *Federal Register* converts the mint program from a pilot program to a permanent program based upon the FCIC Board's action. The final rule is effective for the 2008 crop year.

Northern Potato Crop Provisions and the Central and Southern Potato Crop Provisions – Currently, the final rule is in PASD's concurrence process. The rule makes changes to the Storage Coverage Endorsement and the process for determining production to count for claim purposes intended to improve program integrity and address audit recommendations. The final rule is targeted for the 2008 crop year for the Northern Potato Crop Provisions and the 2009 crop year for the Central and Southern Potato Crop Provisions.

Millet Crop Provisions – Currently, the final rule is in Product Management's concurrence process. The final rule removes the indemnity reductions for unharvested acreage that has caused producer concern for several years. The final rule is targeted for the 2008 crop year.

Florida Citrus Fruit – On November 27, 2006, the public comment period for the proposed rule for Florida Citrus Fruit ended. The proposed rule clarifies insurable citrus crops and provides coverage for

wind damage on fresh fruit when in conjunction with a hurricane or tornado. Due to issues raised by public comments to the proposed rule, RMA is conducting additional analysis before preparing the final rule. The final rule is targeted for the 2009 crop year.

Coverage Enhancement Option (CEO) – Previously, the proposed rule was approved by OGC and is now in USDA’s Office of Budget and Program Analysis (OBPA) for review and approval. The rule converts the pilot program to a permanent program option. The final rule is targeted for the 2009 crop year. On a side note, CEO is only offered in Texas for citrus trees.

Cultivated Wild Rice – Currently, the proposed rule is with OBPA for review and approval. The proposed rule converts the cultivated wild rice program from a pilot program to a permanent program. The final rule is targeted for the 2009 crop year.

Contracted Tobacco – On May 23, 2007, the proposed rule published in the *Federal Register* rewrites and renames the current Guaranteed Tobacco Crop Provisions to the Contracted Tobacco Crop Provisions reflecting the elimination of tobacco quotas. The proposed rule eliminates the Quota Tobacco Crop Provisions as well. The final rule is targeted for the 2009 crop year.

Program Highlights/Announcements:

Congressional Updates – The following are the latest on Congressional issues for the agency, which are divided by briefings and hearings:

Briefings

April 16 and 17 - RMA held crop insurance briefings for the Members and staffers of the US House Agriculture Committee.

April 24 - FCIC Board of Directors met with US Senate and House Agriculture Committee majority and minority staff to discuss issues related to the Federal crop insurance program.

April 26 - RMA Administrator Eldon Gould and staff met with Congressman Randy Neugebauer (R-TX) to discuss Group Risk Income Protection (GRIP) issues for dry land corn in West Texas.

May 7 - RMA staff met with US House Agriculture Committee staff regarding the reasoning why RMA does not provide sesame crop insurance.

May 8 - RMA staff met with US House Appropriations Subcommittee minority staffer David Gibbons to give him an overview of the crop insurance program.

May 15 - RMA staff met with US House Agriculture Committee staff regarding added land policy.

May 17 - RMA staff met with US Senate Agriculture Committee staff and staff from the office of Sen. John Thune (R-SD) regarding added land policy.

Hearings

April 17 - US Senate Homeland Security and Government Affairs Committee held a hearing to discuss a GAO report on Climate Change and its potential implications for federal and private insurers. RMA Administrator Eldon Gould testified.

May 1 - US House Agriculture Subcommittee on General Farm Commodities and Risk Management held a crop insurance oversight hearing. RMA Administrator Eldon Gould and FCIC Chairman of the Board Dr. Keith Collins testified on agency related issues.

May 3 - US House Oversight and Government Reform Committee held a crop insurance compliance and program integrity hearing. RMA Administrator Eldon Gould testified on agency related issues, and RMA Deputy Administrator for Compliance Michael Hand was present to assist with panel Questions & Answers.

June 7 - US House Agriculture Subcommittee on General Farm Commodities and Risk Management will hold a hearing on program integrity within the Federal crop insurance program. Administrator Gould and Chairman of the FCIC Board Dr. Keith Collins are scheduled to testify.

Reprieve Given for California Delta Pumps - The California Department of Water Resources (DWR) has temporarily stopped the 60-day clock shut down of the State Water Project's Delta Pumps due to filing an appeal. More than 23 million farmers rely on the Delta pumps for water. A memorandum of understanding was reached for DWR to withdraw their consistency determination by the State's Department of Fish and Game, and water users south of the Delta may receive reduced water supplies. At the same time, biological opinions on the smelt and salmon species that are impacted at the pumping station are pending completion in 2008. The consistency determination would ensure if the state were in line with the Endangered Species Act for the Chinook salmon and Delta smelt. It is not known how much time the appeal will grant. However, DWR must acquire a permit from the Department of Fish and Game.

Apple Moth Quarantine Update - California Senator Patricia Wiggins has proposed funding for a task force after apple moths have been found in Napa County, which is a county that is prominently known for its premium wine grapes. The pest has not been found in other North Coast counties, but the pest has been found in these nine other counties: Alameda, Contra Costa, Marin, Monterey, Napa, San Francisco, San Mateo, and Santa Cruz). Most of the 2,019 moths have been found in Santa Cruz County. On May 2, 2007, the USDA added a federal quarantine. The moth is native to Australia and can cause harm to 250 plants, trees, and fruits. Because of the frequency of quarantines in the state and the need to protect, the agricultural production quarantine coverage is a high interest to California agriculture producers.

Severe Drought in the Southeast - Drought conditions continue to affect much of the southeast. South Georgia and Florida have not had any appreciable rain in the last three months. RMA issued Bulletin MGR-07-005 to answer questions from Approved Insurance Providers concerning nursery insurance in areas of South Florida that are under irrigation restrictions. As the Final Planting Date for peanuts and cotton in Georgia and Florida approaches, there is no rainfall in sight even in the extended

weather forecasts. RMA's Valdosta Regional Office (RO) continues to field numerous questions on prevented planting and first crop/second crop issues. The RO has worked with the University of Georgia Cooperative Extension Service and Southern Cotton Growers Association to outline the options available to insured producers.

Mid-South Freeze Update – Currently, RMA's Jackson, MS Regional Office (RO) is working with the National Crop Insurance Services' (NCIS) Loss Committee in the region to resolve loss adjustment issues relating to crop damage caused by the Easter freeze. Of particular concern, is damage to nursery in east Tennessee and early release of wheat acreage in western Kentucky. On a side note, the Jackson RO participated in a teleconference of the Kentucky-Tennessee Loss Committee on May 24 to discuss these issues.

Payments by Cooperatives and Trade Associations - Section 508(b)(5)(B) of the Federal Crop Insurance Act authorizes benefits to be provided to producers through cooperatives and trade associations as an exception to the Standard Reinsurance Agreement's (SRA) anti-rebating provisions. The crop insurance industry has shown increasing interest in providing such benefits. Earlier this year, RMA sent a draft Manager's Bulletin and procedures to all AIP's for review and comment. RMA has reviewed all comments and made a number of changes, and a revised draft is currently circulating within USDA for clearance. These procedures, when finalized, would be used by RMA to administer benefits provided to producers under the authority of section 508(b) (5) (B).

Application of Federal Information Security Rules to AIPs – RMA's Chief Information Officer met with Approved Insurance Provider (AIP) program officials and with AIP IT leaders to discuss the implementation and monitoring of Federal rules governing the protection of personal identifiable information of crop insurance customers. This process will continue over the next several months as RMA works with the AIPs individually to discuss what steps, if any, the AIPs must implement in addition to the safeguards that they already apply.

Group Risk Plan Rangeland Final Payment Yields - RMA published its final payment yields on May 1, 2007 for the 2006 crop year on the Group Risk Plan (GRP) Rangeland Pilot. The pilot is currently offered in 39 Montana counties and 10 Wyoming counties. For 2006 in Montana, the pilot had \$111,108,706 in liability, \$12,777,103 in premium, \$18,036,146 in indemnities, and a loss ratio of 1.41. In Wyoming, the pilot had \$22,968,218 in liability, \$2,700,739 in premium, \$12,388,981 in indemnities, and a loss ratio of 4.59. The GRP Rangeland pilot is an indexed insurance product that uses the total non-irrigated hay production in a county to determine the indemnity on rangeland acres. The RMA Billings Regional Office has received a significant number of producer and agent calls and visits to the office since the release of the final payment yields. There seems to be a general dissatisfaction across many of the counties that either did not trigger an indemnity or did not feel their indemnity payment was in line with neighboring counties. There are large fluctuations in the National Agriculture Statistical Service (NASS) data from county to county, which caused some counties to trigger payments and others not triggering or some counties not triggering payments to the extent that their neighboring counties triggered. This apparent inconsistency appears to be driving this dissatisfaction with the pilot and process NASS follows in gathering (surveys) and interpolating the producer data it publishes.

Product Management Partnership Request for Applications (RFA) – On May 17, 2007, the 2007 RFA for Non-Insurance Risk Management Program Partnerships closed. Thirty (30) applications were received and will be evaluated from June 18 to June 20, 2007. The objective of the RFA is to develop non-insurance risk management tools that will increase knowledge of and participation in existing insurance programs, especially insurance products related to Adjusted Gross Revenue / Adjusted Gross Revenue (AGR/AGR-Lite), Livestock products & Pasture, Rangeland, and Forage.

Requests for Applications – On April 23, 2007, applications for the Risk Management Education funding opportunities closed. One hundred and eighty-six (186) applications were received. The Risk Management Education (RMED) staff conducted the first level review. Of those applications, 165 were approved to be sent to the review panel for further consideration. The following is the breakdown by the program with additional information provided:

- ***Commodity Partnerships Program (84 applications)***
RMA Regional Office listed project Objectives. Many of those objectives did not receive any applications. This will result in additional projects in the unrestricted or general topics grouping.
- ***Targeted States Program (22 applications)***
RMED did not receive any complete and valid application packages for the State of Maine under the original Request for Application Notice published in the Federal Register on March 14, 2007. RMED has re-announced this funding opportunity under the Targeted States Program for the State of Maine, which was published in the *Federal Register* on May 18, 2007. Applications were due June 4, 2007
- ***Small Sessions Program (59 applications)***
One June 5 to June 8, 2007, the review panels will meet in Raleigh, North Carolina to determine the applications who will be recommended for funding.

Conflict of Interest Update - RMA's Reinsurance Services Division (RSD) circulated a third draft Manager's Bulletin on May 14, 2007 to provide guidance to AIP's regarding *Conflict of Interest* disclosures by company employees, agents, and loss adjusters. The draft incorporated changes from comments submitted by the crop insurance industry from an earlier draft. Companies provided comments to the latest draft at a Program Integrity conference sponsored by National Crop Insurance Services held on May 22, 2007 in Overland Park, Kansas.

Evaluation of Plans of Operation – Currently, RSD is evaluating Plans of Operation submitted by companies according to Appendix II of the Standard Reinsurance Agreement. Plans must be approved by RMA before companies are authorized to write business for the 2008 reinsurance year, which begins July 1, 2007.

Coordination with NAIC – Currently, RSD is coordinating several program issues with the National Association of Insurance Commissioners and these issues include rebating by cooperatives and loss adjuster licensing. On June 1 to June 5, those issues were discussed at a meeting of the Crop Insurance Working Group at the NAIC Spring Meetings in San Francisco, CA.

Electronic Written Agreements (eWA) Project - The eWA Investment project is an initiative to replace the current RMA automated systems and methodologies. The initiative consists of the development of an enterprise architecture and platform necessary to support the RMA processes and store current and historical data. The project continues to be on schedule for implementation beginning in the winter of 2007-2008 to support the introduction of the COMBO product for Crop Year 2009.

Compliance:

Update GAO Report on Fraud, Waste, and Abuse – This audit provided recommendations to RMA as to how we could improve compliance efforts. RMA agreed in principle with most of the GAO recommendations and agreed to proceed on the following items:

- Adjusting the producer spot-check list procedures to permit FSA to review fall seeded crops for the following year as opposed to the current year, which was ineffective. RMA discussed the possibility of separating the data mining algorithms for the fall and spring, but determined that essential data would be excluded in the process. Farm Service Agency has stated that without additional resources, it will be unable to perform 100 percent of the designated growing season inspections.

Status - Complete.

- Distributing to each AIP the listing of its policyholders whose tax identification numbers or shareholders with substantial beneficial interests did not reconcile with FSA’s permitted entity file. RMA will formally require the AIPs to review the discrepancies under Appendix IV and report the results at some point in time.

Status – The Farm Service Agency did not add “Taxpayer Identification Number Data Mining by RMA” to its routine use listing under the Privacy Act as expected. Subsequently, until FSA completes this task, RMA cannot use FSA entity information to implement the GAO recommendation.

- Finalizing a quality control program for the AIPs intended to help RMA assess the effectiveness of the quality controls used by the AIPs. In addition, RMA Compliance will continue to test AIP quality control programs during scheduled national operations reviews.

Status – RMA continues to work on this recommendation. On April 30, 2007, companies were required to have all their quality control inspections electronically submitted to RMA on “Type 57” records. In the initial review of the data, Compliance identified processing errors that appear to have corrupted some of the data. RMA is working to correct the problem and will ask the companies to resubmit their 2006 crop year review information when complete.

- Finalizing the ARPA-implemented sanctions regulations as soon as OGC has completed its review of the current draft. RMA informed GAO that the lack of these regulations had not

hindered RMA from using the statutory authority to sanction some producers. However, getting the regulations in place should help improve the overall sanctions process.

Status – The proposed rule to amend the *General Administrative Regulations, Administrative Remedies for Non-Compliance* provisions published in the Federal Register on May 18, 2007, with the comment period ending on June 18, 2007.

NCIS Program Integrity Conference – On May 21, 2007, the RMA Administrator, Deputy Administrator for Product Management, and Deputy Administrator for Compliance addressed the NCIS Program Integrity Conference. At the conference, they provided an update on the crop insurance program, discussed the use of data mining in compliance activities and provided updates on program compliance issues generated from various data mining projects.

Hurricane Indemnity Program (HIP) Review – The Office of Inspector General for Audit (OIG) is continuing their review of the Farm Service Agency (FSA) administered HIP program. RMA provided loss data to FSA to assist with the determination of the disaster payments. RMA had initiated an inquiry into changes in the cause of loss data subsequent to the HIP announcement that made producers eligible for payments. RMA has shared the Cause of Loss Report with OIG and has further requested that CAE run a similar report to show policies where the “date of damage” was altered after the HIP program was announced. RMA sent the 2005 Cause of Loss list to the companies requesting their review of the changes and has received the initial group of responses back from the companies. RMA will be issuing the suspect “date of damage” changes for 2005 and 2006 as well as the 2006 “cause of loss” change reports to the companies asking them to review the changes with a similar request for the companies to explain why the information was altered.

National Program Operations Reviews (NPOR) – Compliance completed issuing final determinations for policies with errors selected for the 2005 crop year NPOR reviews. The policy reviews help assess the insurance providers’ adherence to the Standard Reinsurance Agreement (SRA), quality control guidelines and approved policies and procedures. RMA conducts random policy reviews during the NOR to report an error rate to OMB under the requirements of the Improper Payments Information Act of 2002. On May 25, 2007 RMA reported a 2-year program error rate of 2.68 percentage based upon the 600 randomly policy reviews conducted to date.

Compliance offices will conduct the following Operations Reviews for 2007:

- Dallas – *John Deere*
- Davis – *Farmers Mutual Hail of Iowa*
- Indianapolis – *Agriserve*
- Kansas City – *Heartland*
- Raleigh – *Agro National*
- St. Paul – *Farm Bureau Mutual*

Ongoing Investigations/Sanctions Update –

- Reported Plea Agreement – On May 30, 2007, a Sioux Falls South Dakota newspaper reported:

“A Faulkton farmland owner will plead guilty this week to federal charges that he lied to the government to receive \$373,500 in crop insurance and other benefits. Plea agreement documents were filed last week in which Roger Melius, 64, admitted conspiring with family members and making false statements regarding the operation of M&M Farms in Faulk County.

The indictment alleges that over three years, M&M Farms received \$111,500 in Farm Service Agency payments, \$102,800 in Multi-Peril Crop Insurance payments and \$159,200 in farm storage loans. A change of plea hearing is Thursday.”

RMA previously provided language regarding program voluntary disqualification to OIG on this case.

- RMA recently completed two significant sanction actions for program violations. In the first action, RMA suspended two Georgia producers following a lengthy investigation and a monetary plea agreement in which they admitted to significant program violations.

The second action involved suspending a North Carolina agent and adjuster for program violations.

RMA intends to pursue program debarments for these individuals as soon as possible.

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