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### **Rules Undefined for ACRE (Revenue Insurance) and SURE (Disaster Aid)<sup>1,2</sup>**

Congress provided the “outline” for the new Farm Bill (FB), but the “devil is in the details”. USDA civil servants will write these technical implementation rules for the Secretary, who will sign off on the final rules. In many cases those implementation rules will have greater impact on farmers’ bottom line than the Law written by Congress.

Congress has passed the “Food, Conservation, and Energy Act of 2008”, commonly referred to as the Farm Bill (FB). The FB has two new major programs for farmers that include **S**upplemental **R**evenue (SURE) and **A**verage **C**rop **R**evue **E**lection (ACRE), which effectively is a put option on expected state revenue. My current RAM workshops include a discussion on items to consider before switching to ACRE versus a 20% reduction in direct

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<sup>2</sup> Disclosure: The author has a “small” financial interest in the home ranch and includes pasture, bluestem hay and wheat. The author’s privately funded research work with people in the private sector, who are currently mostly with Agro National, was the basis for the development of CRC, the first revenue insurance contract that was release in 1996. RMA took over CRC in 2002 and completely changed the premium rating method. The author has had no input on CRC rates or underwriting rules since 2002.

payments. Currently ACRE is not built in to the workshop case study but the SURE program has been added to the case study.

The other major new FB program is SURE that has received less debate in Washington and as a result, less attention from the press. SURE is a standing disaster program that is directly tied to the level of crop insurance purchased. In the past insured growers' ad hoc disaster aid was based on 65% coverage irregardless of their crop insurance coverage, including CAT. Ad hoc disaster aid was also based on individual crops by county.

The SURE program is based the crop insurance coverage level selected by farmers. Those farmers who select CAT coverage will have their SURE coverage based on 50% coverage at 55% of the price. However, farmers insuring at the 75% level will also have their "free" SURE disaster aid based on 75% coverage at 100% of the price election.

SURE is a whole farm revenue guarantee and requires all acres to be covered with crop insurance and if no crop insurance is available farmers must obtain Noninsured Assistance Program (NAP) coverage from the Farm Service Agency (FSA). The SURE guarantee equals planted acres times percent crop insurance coverage times "adjusted aph"<sup>3</sup> yield times crop insurance price election times 115%. The revenue to count against the SURE guarantee includes indemnities, prevented planting payments, 15% of direct payments, counter cyclical payments, marketing loan gains, ACRE, and crop "revenue" (harvested acres times farm yield times Marketing Year Average price (MYA)). SURE payments equals the SURE revenue guarantee less the revenue to count times 60%.

There are two limits on SURE payments. The first limit is a per farm SURE cap equal to 90% of expected revenue. The whole farm revenue to count plus SURE payments can not exceed 90% times planted acres times "adjusted aph" yield times "insurance price guarantee". The other limit is a maximum SURE payment of \$100,000, otherwise the SURE the payments will be reduced by the amount over \$100,000.<sup>4</sup>

**The SURE program has a number of items that are not defined in the FB.** Therefore, the implementation rules developed by USDA will have major impacts on how the SURE program will work. As a result the "real Farm Bill" will effectively be written by USDA civil servants (Yes, the U.S. Secretary of Agriculture will sign for these implementation rules, but it will be civil servants who write these technical details). Items not defined include:

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<sup>3</sup> The lower case "aph" refers to the actual production history used to set crop insurance yields and SURE approved guaranteed yields. The upper case APH refers to the "yield" coverage crop insurance product that replaced MPCI.

<sup>4</sup> Most farmers will have a \$200,000 payment limit because a spouse also qualifies for a \$100,000 payment limit.

1. **Expected Price Definition.** The Law clearly states the SURE claims will be settled on the Marketing Year Average (MYA) price published by the National Agricultural Statistical Service (NASS-USDA). This feature will delay any SURE payments until a year after harvest unless Congress passes a technical correction to the Farm Bill.

However, the “expected price” used to set the SURE guarantee is not defined. One would also expect the same “expected price” will be used to determine the 90% cap on payments by farm that applies to all farms irregardless of size. The Law uses the term “insurance price guarantee” for “expected” price. Will the Secretary “define” this “expected price” as 100% of the APH price election for all farmers or will revenue insurance buyers receive the planting price set by new crop futures? Will Farmers who purchased Crop Revenue Coverage (CRC), Revenue Assurance with Harvest Price Option (RA-HPO), or Group Risk Income Protection with the Harvest Revenue Option (GRIP-HRO) be allowed to use the higher of the planting price or the harvest price? Clearly these insured growers crop insurance price guarantees are the higher of the planting price or harvest price but will the Secretary define price the same as a farmer’s selected crop insurance price. **The “expected price” is a critical definition and will determine the optimal level and type of crop insurance to purchase.** The Law states;

*(5) EXPECTED REVENUE.—The expected revenue for each crop on a farm shall equal the sum obtained by adding— (A) the product obtained by multiplying—  
the greatest of—  
the adjusted actual production history  
yield of the eligible producer on a farm; and  
the countercyclical program payment yield;  
the acreage planted or prevented from being planted for each crop; and  
100 percent of the **insurance price guarantee**.*

If the farmer has purchased APH crop insurance then this section of the Law clearly states the “insurance price guarantee” is 100% of the price election. However, a large number of farmers have purchased RA-HPO, CRC and GRIP-HRO. The price insurance guarantee in RA without HPO is the planting price based on new crop futures. The price guarantee in CRC, RA with HPO, and GRIP with HRO is the higher of the planting price or harvest price.

If the USDA does not define **insurance price guarantee** as the higher of the planting price or harvest price then the USDA’s SURE implementation rules will penalize farmers who buy the harvest price option or CRC. When farmers have a short crop and the price increases, then CRC, RA-HPO and GRIP-HRO will pay higher indemnity payments and reduce their SURE payments when compared to farmers who purchase RA without the HPO. However, CRC, RA-HPO and GRIP-HRO insured growers paid higher premium costs for those contracts only to have their “free” SURE payments lowed.

Logic would say the *insurance price guarantee* is the price guarantee in the farmer's selected crop insurance contract. If the same price definition is not used for SURE the incentive will be to reduce crop insurance coverage by eliminating the HPO and the HRO.

However, a large number of farmers don't have the option to purchase RA without the harvest price option. There is no RA offer on grain sorghum. CRC is the only choice for grain sorghum producers who prefer an aph based revenue insurance contract. CRC has the harvest price built in with no alternative to delete it. There are also a large number of States that only have the CRC offer including Texas wheat, Wisconsin corn and soybeans, Delaware corn and soybeans, etc. (Table 1 below lists States with no RA offer).

2. **Expected Yield Definition.** What adjustment to the aph will USDA make for SURE? The Law states;

*(2) ADJUSTED ACTUAL PRODUCTION HISTORY YIELD.—The term ‘adjusted actual production history yield’ means—*

*(A) in the case of an eligible producer on a farm that has at least 4 years of actual production history yields for an insurable commodity that are established other than pursuant to section 508(g) (4) (B) , the actual production history for the eligible producer without regard to any yields established under that section;*

*(B) in the case of an eligible producer on a farm that has less than 4 years of actual production history yields for an insurable commodity, of which 1 or more were established pursuant to section 508(g) (4) (B), the actual production history for the eligible producer as calculated without including the lowest of the yields established pursuant to section 508(g) (4) (B)*

This part of the Law apparently allows farmers with less than 4 years of history to drop one “plugged” yield and average the remaining years. Farmers with more than 4 years of yield records apparently will be allowed to drop all “plugged” yields and then average the remaining yield records. Apparently farmers will not be allowed to drop their “low yields” unless they are plugged yields.

Needless to say farmers that have had crop failures and replaced those yields with 60% of T-yield (yield plug) in their aph will have a substantially higher adjusted aph for SURE than they do for their crop insurance aph. In addition the SURE guarantee is multiplied by 115% so effectively the SURE adjusted aph could be 20-25% higher than their crop insurance aph.

3. **County Yields or Farm Level Yields.** The FB says nothing about GRIP/Group Risk Plan (GRP) but one would assume GRIP/GRP insured farmers will qualify for SURE. While the Law is silent on GRIP/GRP, it does refer to “nonyield based” insurance contracts. However GRIP/GRP are based on yields, it is just they are based on county

yields and not farm level yields. So will the Secretary interpret “equitable treatment” as setting SURE guarantees based on county yields rather than aph yields for GRIP/GRP buyers? The Law states;

*D) EQUITABLE TREATMENT FOR NONYIELD BASED POLICIES.—The Secretary shall establish equitable treatment for nonyield based policies and plans of insurance, such as the Adjusted Gross Revenue Lite insurance program.*

The Law states the dollar based contract buyers will get the equivalent of aph yield based crop insurance buyers and specifically mentions Adjust Gross Revenue (AGR and AGR Lite) but says nothing about GRIP/GRP. Because GRIP/GRP contracts are yield based contracts does that imply the “equivalent” coverage for GRIP/GRP buyers will have their SURE guarantees based on county yields?

4. **Setting SURE Coverage Level under GRIP/GRP?** If GRIP/GRP buyers receive an aph based SURE contract then at what coverage level? For example will a 90% GRIP insured grower receive a 90% SURE? Currently the subsidy for 90% GRIP is the same as 80% aph so one might assume 90% GRIP insured farmers would get an 80% SURE guarantees, if aph yields are used to set SURE guarantees.

However, 90% GRP insured farmers receive the higher 75% aph subsidy rate. But one would assume a GRP insured grower would get the same SURE coverage level as the GRIP buyers. Under GRIP/GRP the coverage levels are typically 85% or 90% while it is 70% or 75% on aph products, so will USDA set the SURE coverage at 75% for GRIP/GRP at the 90% coverage level?

5. **SURE Loss Adjusting under GRIP/GRP.** If a GRIP/GRP buyer receives SURE coverage based on farm level aph yields rather than county yields, then will FSA also tract farm yields. Will FSA provide a loss adjuster to adjust individual farm yield losses for SURE on farms insured under GRIP/GRP? Currently yield records and individual farm level loss adjustment is provided by the **Risk Management Agency (RMA)** but only if the grower purchased an individual aph based contract rather than a county yield based GRIP/GRP contract that does not adjust individual farm losses.
6. **Net or gross indemnity?** The Law states crop insurance indemnity payments will count against the SURE guarantee, but is it net or gross indemnity? The Law states;

*(vi) the amount of crop insurance indemnities received by an eligible producer on a farm for each crop on a farm;*

The author was told by phone the intent of Congress was gross indemnity payments but past ad hoc disaster programs used net crop insurance payments. If net payments are not used then this will be to the disadvantage of farmers who buy higher crop insurance coverage levels that require higher farmer paid premiums.

7. **Prevented & Late Planting.** Under prevented planting the crop insurance coverage is reduced to 60% of the guarantee. There is also a 1% reduction in the insurance guarantee for each day insured farmers plant after the final planting date. So is the SURE coverage also reduced or do farmers maintain the same SURE coverage level but there are fewer indemnity dollars to count against the guarantee?
8. **Uninsurable acres.** There are cases when neither crop insurance nor NAP is available. For example if one's crop is hailed out and the claim is settle but the farmer decides to re-plant those failed crop acres after the final planting date, then those acres will not be covered by crop insurance. The question is will those uninsured acres violate the SURE requirement that all acres must be insured? If no, then will the revenue from those uninsurable acres count against the SURE guarantee?
9. **Major Administrative change to Crop Insurance.** Starting with winter wheat the price limit in CRC and GRIP-HRO was changed from \$2 to 200% times planting price.<sup>5</sup> If this rule had been change last year the limit on Texas, Oklahoma, Colorado, and Kansas wheat would have been increased from a maximum price of \$7.88 to \$11.72 (\$5.88 X 200%). RMA also eliminated the downside price limit.

In addition, RMA put the same 200% times planting price limit on RA-HPO, so that RA-HPO has the same price limit as CRC. The harvest price measurement periods are different on wheat and the author believes, but can not prove, there is still a slight advantage for RA-HPO. So one would think Great Plains winter farmers would still select RA-HPO but only if the premiums are nearly identical. Otherwise, farmers will likely select the coverage with the lowest premium costs.

10. **Winter wheat Crop Insurance signup.** Winter wheat growers will likely not have all of these SURE parameters defined before they signup for crop insurance on September 30, 2008. If one is buying the harvest price option, it is very likely they will want to retain that option, even if the SURE rules end up working against the RA-HPO, CRC and GRIP-HRO insured farmer. Because SURE is a whole farm guarantee and it is possible that USDA will define SURE's "expected price" the same as it is in CRC/RA, it is probably not a good idea to drop the harvest price option until more SURE details are made available.

Even if the FSA "expected price" definition does not favor the harvest price option, farmers may still want to retain the coverage because they have forward priced a significant amount of production or they are highly diversified, which will reduce the effectiveness of SURE. One suggestion is 85% insured farmers will likely want to reduce their coverage to 80% because the higher coverage will likely reduce their SURE

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<sup>5</sup> The CRC and GRIP-HRO price limit for corn was \$1.50, \$3 for soybeans, \$1.50 for grain sorghum, and 70 cents for cotton. All price limits have been changed to 200% times planting price and the new price limits will also apply to RA contracts.

payments. It is unlikely there will be any benefit from 85% coverage unless the farm is highly diversified. Remember diversification is not just based on the number of crops but also distance because the whole farm revenue definition crosses county and state lines. Some farms may have their crop acres separated by more than 100 miles, which is a form of diversification.

Farmers, who reduce their crop insurance coverage to fit under the SURE 90% cap limit, may want to consider replacing the coverage with private crop insurance coverage. That is because private crop insurance indemnity payments do not count against the SURE guarantee.

The other suggestion is the CAT contract will set the SURE coverage based on 50% coverage and 55% of the price election. So CAT insured growers may want to consider increasing their coverage to at least 65% because that will also set their SURE coverage at 65%.

Over time one would expect the SURE program to cause farmers to be less diversified. For example, Corn Belt growers will likely eliminate wheat from their crop rotation of corn and soybeans. At one of my recent seminar presentations in Illinois, I was surprised at the number of farmers in Illinois that were planting continuous crop corn and SURE will provide those farmers the same unit structure as an enterprise crop insurance unit, assuming their entire farm is in one county. In Kansas, will SURE cause more farmers to drop grain sorghum out of their rotation and plant wheat and corn or in the East, corn and soybeans? SURE would reduce the risk of planting dryland corn west of Salina because it is "free" coverage and the aph is adjusted by dropping all of the plug yields and multiplying by 115%.

Also there is a \$100,000 payment limit on SURE. There, is no indemnity payment limit on farmer paid crop insurance coverage. Therefore for large farms there will be less of a reason to change crop insurance coverage levels because if there is a loss they will likely exceed the \$100,000 SURE payment limit anyway.

11. **RAM workshops.** I am currently booking risk management workshops for 2008-09. I have built the SURE program in the case study to help workshop participants better understand how their crop insurance and marketing decisions will affect the level of "free" SURE coverage. Currently the simulation of SURE payments is based on assumptions of how FSA may write the implementation rules. Therefore the case problem will need to be continuously updated to reflect the most current rules, so the case problem will likely change over the winter months.

I also discuss the ACRE program but it is currently not built in to the case problem. However, that may change in the near future.

**Table 1. List of Crops and States with No RA offer**

State	Feed Barley	Malting Barley	Canola/ Rape-seed	Corn	Cotton	Rice	Soy-beans	Sun-flowers	Spring Wheat	Winter Wheat	Grain Sorghum
Alabama	<b>No RA Available</b>										
Alaska	<b>No RA Available</b>										
Arizona					x						No RA
Arkansas				x	x	x	x			x	No RA
California	<b>No RA Available</b>										
Colorado	x	x		x			x	x	x	x	No RA
Connecticut	<b>No RA Available</b>										
Delaware	<b>No RA Available</b>										
Florida	<b>No RA Available</b>										
Georgia	<b>No RA Available</b>										
Hawaii	<b>No RA Available</b>										
Idaho	x	x	x						x	x	No RA
Illinois				x			x				No RA
Indiana				x			x			x	No RA
Iowa				x			x		x	x	No RA
Kansas				x			x	x		x	No RA
Kentucky				x			x			x	No RA
Louisiana				x	x	x	x				No RA
Maine	<b>No RA Available</b>										
Maryland	<b>No RA Available</b>										
Massachusetts	<b>No RA Available</b>										
Michigan				x			x			x	No RA
Minnesota	x	x	x	x			x	x	x		No RA
Mississippi	<b>No RA Available</b>										
Missouri				x			x			x	No RA
Montana	x	x						x	x	x	No RA
Nebraska				x			x			x	No RA
Nevada	<b>No RA Available</b>										
New Hampshire	<b>No RA Available</b>										
New Jersey	<b>No RA Available</b>										
New Mexico					x						No RA
New York	<b>No RA Available</b>										
North Carolina				x			x				No RA
North Dakota	x		x	x			x	x	x		No RA
Ohio				x			x			x	No RA
Oklahoma				x	x		x			x	No RA
Oregon	<b>No RA Available</b>										
Pennsylvania	<b>No RA Available</b>										
Rhode Island	<b>No RA Available</b>										
South Carolina	<b>No RA Available</b>										
South Dakota	x	x		x			x	x	x	x	No RA
Tennessee				x			x			x	No RA
Texas	<b>No RA Available</b>										
Utah	<b>No RA Available</b>										
Vermont	<b>No RA Available</b>										
Virginia				x			x				No RA
Washington	<b>No RA Available</b>										
West Virginia	<b>No RA Available</b>										
Wisconsin	<b>No RA Available</b>										
Wyoming	<b>No RA Available</b>										