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PolicyPennings by Daryll E. Ray & Harwood D. Schaffer

FSA employees' association says: "Let us do the crop insurance"

The surest signal that almost everyone takes the need to save costs in writing the 2012 Farm Bill seriously is the number of groups proposing policies that would reduce government costs over the next ten years. The latest group to throw a cost-saving proposal into the legislative arena is the National Association of FSA County Office Employees (NASCOE).

In a press release announcing the results of an Informa Economics study they commissioned, NASCOE says they "[believe] that the Farm Service Agency [FSA] should be given additional responsibilities within the crop insurance program to achieve major budgetary savings, improve and streamline customer service, and improve program integrity" (http://nascoe.org/Legislative.aspx). An Executive Summary of the Informa study can be found at http://nascoe.org/Documents/NASCOE_Executive_Summary_insurance_Feb_2012.pdf.

In identifying the additional responsibilities that the FSA offices could take on, Informa analyzed four scenarios:

1. "FSA takes on the role of selling the crop insurance and functions currently performed by the insurance agent.
2. "FSA takes on the role of servicing the crop insurance and functions currently performed by the insurance company.
3. "FSA takes on both the sales and servicing role – redirecting functions currently performed by insurance companies and agents.
4. "Only FSA produced acreage and production reports, a task that is currently duplicated among FSA and RMA offices."

It is the third of the four options that saves the most money and has garnered the bulk of the headlines, offering savings in the range of $1.9 billion to $2.5 billion a year or as much as $25 billion over a 10-year period. In Informa's study, government costs for the current crop insurance program are calculated to be $4.8 billion a year (2006-2010 5-year average). Thus, turning the full crop insurance program over to the FSA would reduce the government cost of providing crop insurance to farmers by between 40 percent and 52 percent a year.

In looking at these numbers, several caveats are in order. First, Informa cautions readers "that the cost estimates presented within this section are intended to be used to establish perspective on the order of magnitude of each scenario." The savings they identify depend upon the assumptions they had to make in conducting the study. Second, these numbers are not computed using the 10-year baseline that the Congressional Budget Office (CBO) will use in providing the two ag committees with a cost savings for the NASCOE program. Third, Informa notes, "these cost savings estimates do not include costs associated with training and other expenses required in the short-term to transition the various functions from one entity to another." In addition, Informa's analysis "does not examine any changes to the premium subsidy and producer premium."

That being said, let's look at the changes that result in the potential cost savings that were announced. The cost savings come from two areas: underwriting gain/loss and A&O expense reimbursements.

An Informa footnote says, "underwriting gains/losses represent the portion of the total gain/loss (gross premiums minus indemnities/claims) insurance companies are able to retain." In the study, Informa calculates that to be $1.6 billion a year (5-year average). As Informa explains, "The profit of the private insurance companies may or may not be within reason relative to their risk—this is not the question analyzed within this study. Regardless, this is a profit that insurance companies are receiving in an industry that is subsidized by the government—the federal crop insurance program supports profits for farmers, private insurance companies and insurance agents."

"A&O expense reimbursements are paid to insurance companies to reimburse them for their expenses incurred in selling and servicing crop insurance," Informa writes. The recent agreement between the insurance companies and USDA caps this amount at $1.3 billion a year.

Thus, the total net costs for the insurance companies to run the crop insurance program, as calculated by Informa would be $2.9 billion. Depending on the crop insurance activities that would be shifted to the FSA, this amount represents the maximum potential savings.

In the sales and service scenario, which completely cuts out the insurance companies and their sales agents, Informa estimates that FSA would have to take on additional expenses of between $0.5 billion and $1.0 billion, resulting in the $1.9 to $2.5 (rounding error) in announced savings.

In the scenarios in which the FSA takes on either the sales or the servicing responsibilities for crop

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insurance the savings range from a $0.3 billion to $2.1 billion. In addition, "having FSA offices perform the sales function may improve service to underserved areas. This statement is based on: …the geographic locations of current agents versus county FSA offices…—insurance agents are highly concentrated in the Midwest and there are other geographies in which farmers must drive a substantial distance to reach their agent."

If the FSA were to be the only agency producing crop acreage reports (the fourth scenario) the savings would be an additional $197 million.

Needless to say, this proposal has generated a vigorous response from various insurance industry groups. Next week we will look at the arguments they present.

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