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More Cuts to Crop Insurance? The Proposed AFFIRM Act

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In a previous policy brief, I discussed legislation in the Bipartisan Budget Act of 2015 that cuts government support to the US crop insurance through a reduction in the rate of return to insurance companies from 14.5% to 8.9% (Rejesus, 2015). This piece of legislation created a lot of "buzz" in the agricultural sector because of the lack of consultation and discussion among lawmakers prior to it being included in the Act. One important update to this issue though is the repeal of this cut, which was included by legislators in Section 32205 of the Fixing America's Surface Transportation (FAST) Act (effective Dec. 1, 2015).

This recent repeal is welcome news to the agricultural sector, specifically the crop insurance companies. However, even with this positive development, there has been new legislation introduced that proposes to make more comprehensive cuts to the US crop insurance program. This legislation is known as the "Assisting Family Farmers through Insurance Reform AFFIRM) Act." The House version of this bill was introduced by Representatives Ron Kind (Democrat-WI) and Jim Sensenbrenner (Republican-WI), while the Senate version was introduced by Senator Jeff Flake (Republican-AZ) and co-signed by Senator Jeanne Shaheen (Democrat-NH).

The AFFIRM Act proposes several cuts to crop insurance, which includes a section that reduces the rate of return of insurance companies from 14.5% to 8.9%. Hence, this piece of legislation also has a section that is the same as the one introduced in the Bipartisan Budget Act (and consequently repealed in the FAST Act). As before, this reduction in the rate of return is estimated to save $3 billion over 10 years (as estimated by the Congressional Budget office (CBO)).

In addition, the AFFIRM Act proposes a number of other cuts to the US crop insurance program. First, it considers limiting the total Federal crop insurance subsidies that an individual farmer receive to only $40,000 per year. Second, the AFFIRM Act proposes to stop individuals with Adjusted Gross Income (AGI) of $250,000 or more to receive any form of crop insurance subsidy. Third, the bill also includes a provision that caps government reimbursement of crop insurance companies' administrative & operating (A&O) costs to $900 billion per year. Currently, the government pays 100% of insurance companies' A&O expenses. Fourth, the AFFIRM Act aims to eliminate subsidies given to producers who buy revenue protection (RP) insurance with the Harvest Price Option (HPO). Farmers who want the HPO coverage (i.e., ability to recalculate revenue insurance guarantee when the harvest price becomes larger than the "base" planting time price) would have to pay for the full insurance premium of the plan. Lastly, there is language in the AFFIRM Act that promotes transparency, as well as using savings from new Standard Reinsurance Agreements (SRAs) to be used for Federal deficit reduction.

Overall, the CBO estimates that the AFFIRM Act will save about $24 billion in crop insurance program expenses over 10 years, with the majority of savings coming from taking away the premium subsides for the RP insurance that includes HPO.

Clearly, the AFFIRM Act proposes more dramatic cuts to the US crop insurance program as compared to the piece of legislation included in the Bipartisan Budget Act of 2015. Unlike the previous legislation, the AFFIRM Act will

directly affect individual producers' ability to cost-effectively access crop insurance as a risk management tool. Farmers that hit the AGI limits and subsidy caps will definitely have to pay more for crop insurance. Farms that want RP with the HPO will have to pay more for this coverage. And if they cannot afford it they have to simply buy the RP without the option to recalculate guarantees to harvest time prices. This may be problematic in "high price, low yield" scenarios because it is likely that the higher prices would eliminate payments from commodity programs and at the same time the RP insurance without HPO may not pay (since there is no adjustment in the value of the crop lost). Hence, farmers would not have any payments even if they suffer yield losses in this case.

The AFFIRM Act's proposed cuts to the subsidies given to crop insurance companies is also more "painful" as compared to the legislation in the Bipartisan Budget Act. The additional cut to A&O reimbursement would further erode these companies' ability to effectively deliver crop insurance to our growers. The reduction in A&O, together with the rate of return reduction, may cause more firm exits from the industry. At the extreme, it could happen that all private companies might exit and crop insurance delivery may have to fall under the purview of the government. Would the Farm Service Agency (FSA) or Risk Management Agency (RMA) have the necessary resources and ability to deliver the program?

At this point, the good news for the agricultural sector is that the AFFIRM Act is still a proposal. It is not yet legislation that passed both chambers of Congress. And it is looking like there is not enough support for this bill (outside of the bill sponsors) to actually become law (Clayton, 2015, Barnaby, 2015a & 2015b).

But there is always the possibility that the AFFIRM Act (or parts of it) may be added at the last minute in a separate piece of legislation (i.e., as in the Bipartisan Budget Act). Therefore, it is important for the agricultural sector to be always on the lookout for these types of actions. New proposals to cut crop insurance will also likely come up in the future. Individual growers, commodity groups, and other farm organizations should be vigilant about this and should constantly communicate with their legislators about their views on these issues.

FOR MORE INFORMATION:

Barnaby, A. 2015a. "Will the Proposed Crop Insurance Budget Cuts Ever end?" Kansas State University Ag. Manager Fact Sheet (See: http://www.agmanager.info/crops/insurance/risk_mgt/rm_pdf15/AB_CropInsWorkshop.pdf)

Barnaby, A. 2015b. "Crop Insurance Critics Who Make Up or Omit Facts to Support their Advocate Position" Kansas State University Ag. Manager Fact Sheet (See: http://www.agmanager.info/crops/insurance/risk_mgt/rm_pdf15/AB_Critics.pdf)

Clayton, C. 2015. "Plans to Cut Crop Insurance Got You Down? Let's Talk." DTN Progressive Farmer Magazine (11/06/2015)

Rejesus, R.M. 2015. "Crop Insurance Cuts in the Bipartisan Budget Act of 2015." Agricultural Policy and Risk Management Brief (11/02/2015)

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