Myth vs Fact

Myth	Fact
Myth: The new SRA will affect producers' premium subsidy.	**Fact:** The premium subsidy can only be changed by Congress and will not be affected by the SRA.
Myth: Lower reimbursement rates would most likely be passed along to producers in the form of higher premiums.	**Fact:** The SRA has no effect on premium rates. These rates are required by law to be actuarially sound and are based on long-term program performance.
Myth: RMA has proposed "reckless" and "excessive" cuts in the new SRA.	**Fact:** Government expenditures to insurance providers have more than doubled in recent years – from $1.8 billion in 2006 to $3.8 billion in 2009 – while the number of policies has been essentially unchanged over this period and has actually declined since 2000. Some are trying to suggest there are "cuts" in the SRA by comparing it to record gains in 2008 or 2009. This windfall was primarily due to a record spike in commodity prices, and was not due to an increase in policies or corresponding workload. American taxpayers should not be responsible for continuing to pay these windfall gains to the insurance industry; the program needs to be restructured. The new agreement seeks to eliminate this windfall in the future while ensuring that companies will receive a stable and reasonable amount to deliver the program. RMA also contracted for two studies by Milliman, Inc. (Milliman), a private consulting firm. The Milliman studies, recently updated for 2009, indicate that, over the last 21 years, the "reasonable rate of return" for crop insurance companies averaged 12.7 percent, while the companies actually received an average rate of return of 17.0 percent. The second draft of the SRA will give the companies a rate of return of about 14%, more than a reasonable rate of return according to Milliman. Also of note, the updated Milliman report goes on to show that in 2009 the companies earned a rate of return of 26.4%, the second highest in the past 21 years.
Myth: The cap on agent commissions is unnecessary and harmful.	**Fact:** This provision responds to calls from Members of Congress, academia, government accountability organizations, and the insurance companies themselves to moderate the unsustainable growth in agent commissions. The 2002 failure of the then largest company in the program illustrates these concerns. A primary cause of this company's failure was that it was paying agents significantly more than it received in A&O, under the assumption that it would make enough on underwriting gains to this obligation. However, a year in which large underwriting gains are not realized can easily pressure a company's financial position ultimately leading to a company going out of business, as happened with the largest company in 2002. This provision will help minimize the potential for a company to go bankrupt because it is making unsustainable commitments to its agents. The companies' own data, through its Grant-Thornton study, show that agent commissions are growing at an unsustainable rate (See Chart 1 below). Company expenditures for loss adjustment, training, overhead, information technology and other expenses have shown only modest increases over the past few years, but agent commissions have increased from $600 per policy to almost $1,450 per policy. Even as the amount of A&O paid to the companies more than doubled between 2006 and 2008, the companies still managed to run an expense deficit because of runaway agent commissions.
Myth: The new SRA will jeopardize rural jobs	**Fact:** The new agreement seeks to provide more protection to companies in bad years, thus increasing the financial viability of companies for the long haul. In addi tion, the changes are designed to provide more stability for companies should commodity prices drop. While we are in difficult economic times, the new SRA seeks to provide reasonable compensation for delivery services that is neither excessive nor insufficient. The levels of projected funding are consistent with, or even slightly higher than that of the mid-2000s, which provided many good jobs within rural America supporting the crop insurance program.

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Myth: The new SRA will put crop insurance companies out of business	**Fact:** Under the new SRA, insurance companies can expect to earn a reasonable rate of return and have greater protection in bad years. In March, RMA welcomed Occidental Fire and Casualty Company of North Carolina as the newest participating company to sign the current SRA. This company was well aware of the details of the new SRA when petitioning for approval as a new company. As the signing of Occidental shows, this new agreement is still a very attractive business proposition.
Myth: The new SRA will lead to consolidation in the crop insurance industry.	**Fact:** Although some consolidation has occurred in the Property and Casualty insurance industry generally, crop insurance companies have fared proportionately better – a trend that is expected to continue under the new SRA. Moreover, there is no direct correlation between consolidation and decreased government expenditures (or profitability). In fact, the last insurance company contracted through the SRA that consolidated did so after one of the most profitable years on record. As with any industry, there will always be some level of potential consolidation or Corporate mergers for purposes of efficiency.
Myth: Crop insurance sustained a cut of $6.4 billion over ten years in the 2008 Farm Bill.	**Fact:** The reduction of outlays in the Crop Insurance Title of the Farm Bill were $5.6 billion over 10 years, using the March 2007 Congressional Budget Office Baseline, which was used by Congress in scoring the 2008 Farm Bill. However, of this, only approximately $1.4 billion can be directly attributed to a reduction in payments to insurance companies for the delivery of crop insurance. The remaining "reductions" involved timing shifts that did not result in dollar for dollar reductions in payments; instead it delayed when those payments are made.
Myth: The A&O payment rate has fallen by nearly 50% over the last 15 years, from 33% to the 17.9% in the last farm bill.	**Fact:** In 1994, A&O payments for the industry were $282 million. In 2009, A&O payments were $1.6 billion. This is a 470 percent increase in A&O dollars paid to the companies over the last 15 years. While some argue that Administrative and Operating (A&O) payments should be considered in terms of a percentage of premium, the government and taxpayers are far more concerned about the total dollars being provided to deliver the program. Additionally, A&O payment data in recent years shows the windfall the companies have received. In 2006, A&O payments for the industry were under $1 billion (about $835 per policy) and this amount of money was more than adequate to provide for effective delivery of the program. In 2009, A&O payments increased to over $1.6 billion (over $1,373 per policy), due almost entirely to commodity price spikes. The new agreement would provide payments of about $1.2 billion per year ($1000 per policy), which is still about 25 percent higher than 2006.
Myth: The new SRA will force companies to pull out of less profitable states.	**Fact:** The new SRA provides better risk sharing terms to all states outside of the Corn Belt (the Corn Belt states have been the most profitable states). Therefore, opportunity for underwriting gains in these states will increase in all states outside of the Corn Belt. The new SRA also provides for 5% higher reference prices for all states outside of the Corn Belt, which will provide the companies with a higher A&O in these states that are currently less profitable. Additionally, the new agreement will provide companies with additional financial incentives to service the 17 underserved/less-served States.
Myth: RMA cannot determine an adequate amount of A&O payments until it completes its study of costs associated with selling and servicing crop insurance policies as recommended by the Government Accountability Office (GAO).	**Fact:** In recommending that RMA conduct a study on delivery costs, GAO did not recommend or expect that RMA should place the restructuring of the A&O subsidy on hold until the study is completed. On the contrary, GAO recommended that RMA take quick and decisive action in the current SRA negotiations to significantly restructure the A&O subsidy. GAO found that actual delivery expenses could be reasonably approximated to be less than the A&O subsidy levels provided prior to 2006, in terms of dollars per policy. The A&O structure developed by RMA for the SRA negotiations draws on reasonable economic inferences that are similar to, but in reality more generous to the industry, than those used by GAO in its analysis. The restructuring is limited to rolling back the windfall revenues to companies and their agents arising from high crop prices since 2006. When the detailed expense study recommended by GAO is completed, RMA can use its findings to fine tune the A&O subsidy structure when the SRA is again negotiated in five years. Meanwhile, RMA is confident that its restructuring of the A&O subsidy protects program delivery, is economically sound, and is entirely consistent with GAO's findings.