United States Department of Agriculture

Risk Management Agency

1400 Independence Avenue, SW
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BULLETIN NO: MGR-05-011

TO: All Reinsured Companies
All Risk Management Field Offices
All Other Interested Parties

FROM: Ross J. Davidson, Jr. /s/ Ross J. Davidson, Jr.
Administrator

SUBJECT: Calculations of Premium Reductions under 7 CFR §400.720(b)(2)

BACKGROUND:

On July 20, 2005, RMA published an interim final rule in the Federal Register outlining procedures that pertain to premium reduction plans authorized by section 508(e)(3) of the Federal Crop Insurance Act (the Act). As stated in 7 CFR §400.720(b)(2), the Risk Management Agency (RMA) is to establish procedures on how expense information submitted by insurance providers (company) will be used to calculate premium reductions.

ACTION:

The procedures use information from the following three exhibits prepared by the company in accordance with Appendix II of the Standard Reinsurance Agreement:

- *Exhibit 10.m. Commission Template*. (Agent compensation information on a state basis)
- *Exhibit 10.n. Loss Adjustment Expense Template*. (Loss adjustment expense information on a state basis)
- *Exhibit 10.o. Expenses Template*. (Total expenses in the delivery of Federal crop insurance)

Companies must prepare these exhibits for the "Baseline Year" (currently the 2005 reinsurance year) and the "PRP Year" (the year for which the company is requesting approval to pay a premium reduction). 7 CFR §400.720(a)(1) requires that these exhibits be audited and certified by an independent certified public accountant before submitting to RMA.

The Risk Management Agency Administers
And Oversees All Programs Authorized Under
The Federal Crop Insurance Corporation

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Initially, RMA will establish that a company may be approved to provide a premium reduction by determining whether the company's Administrative and Operating (A&O) cost is below the company's A&O subsidy for the PRP Year. RMA will then determine state-by-state efficiencies due to operational changes by comparing the company's state-level costs as a percentage of buy-up premiums for the PRP Year with those of the Baseline Year. In certain instances, a company's total efficiency may be greater than the total for all state-level efficiencies due to operational changes, leaving a residual efficiency. RMA will allocate this residual efficiency by determining the difference between total efficiencies and those due to state-by-state operational changes, then pro rating this amount across all states according to a state's buy-up premium. The total state-level amounts will then be adjusted to determine a maximum premium reduction and maximum premium discount to ensure that the total premium reduction for all states does not exceed the total efficiency for the company and that the amount for each state does not exceed the maximum percentage specified in 7 CFR §400.715(a) (currently 4 percent). Finally, RMA will examine the state-level premium reduction amounts and percentages requested by the company according to 7 CFR §400.720(a)(3) to ensure that the amount to be paid to producers does not exceed the state-level maximum premium reduction amounts and percentages calculated above.

Attached are a spreadsheet and a description of the data and calculations used to determine state-level cost efficiencies and maximum premium reductions and percentages that can be paid to producers.

As stated in 7 CFR §400.720(b)(2), these procedures are in effect for the 2006 reinsurance year and will remain in effect for subsequent reinsurance years unless revised. If such approved procedures will be revised, these approved procedures will be issued not later than January 1 before the start of the applicable reinsurance year.

<u>DISPOSAL DATE</u>:

This Managers Bulletin is for the purpose of transmitting information and will remain in effect until rescinded, revised according to the provisions of 7 CFR §400.720(b)(2)(ii), or upon publication of procedures in the Code of Federal Regulations.