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# House Agriculture Subcommittee
# Crop Insurance Audit
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**Chairman Michael Conaway:** This hearing of the Subcommittee on General Farm Commodities and Risk Management entitled "Agricultural Program Audit: Examination of The Federal Crop Insurance Program" will come to order. We are pleased to have for us today administrator of the Risk Management Agency Bill Murphy.

It's appropriate that our first farm bill audit hearing focuses on federal crop insurance because crop insurance has evolved, over 73 years, to become a cornerstone of U.S. farm policy. It's as important now as ever. Farmers across the country are dealing with wildfires, droughts, and, I'm told, extra water in Minnesota, floods.

It's also important to observe why the federal government is involved in crop insurance. It's because without federal involvement, America's farmers, quite simply, would not have crop insurance, and without crop insurance, lenders would not likely make loans to producers. After all, producers are borrowing more money in a single year than many Americans borrow in a lifetime. So if there's ever a role for federal involvement in what would ordinarily be a private market activity, this is a prime example.

Still, as essential as federal crop insurance is to most producers, it has been a long road to get to where we are, and we have not yet reached our final destination. Three events helped farm crop insurance become what it is today. First, 100% private sector delivery through a strong agent workforce, second, the 2000 reform bill that increased producer access to higher levels of coverage at more affordable prices, and third, the approval of revenue products that help producers cope with production losses and better market their crops while dealing with price volatility. This last improvement was also a private sector innovation.

With these innovations, participation has more than doubled over the past 20 years, and total liabilities protected has increased over 600%, reaching an expected total of over 100 billion in 2011. We've witnessed an increase in risk management tools available to producers, most notably the revenue products now in the market.

Despite these successes, there are areas where federal crop insurance must move forward to meet the risk management needs of U.S. producers, and this is especially true in the current budget climate. Federal crop insurance must be built upon, or it will wither and die because it will fall behind producer needs. For example, it's great that we have producers covered at the 70 to 85% coverage levels, meaning deductibles ranging from 30 down to 15%. These high deductibles grow even larger when coupled with artificially low actual production histories, or APHs, that further shrink insurable yields. But for many producers, only low levels of coverage are cost effective. This is true despite the introduction of enterprise units in the farm bill that help producers buy up higher levels of coverage.

Unfortunately, a lot of time has already been lost. Over the last four years, the Risk Management Agency has taken its focus off of the task at hand in order to implement cuts to the federal crop insurance first made in the 2008 Farm Bill, roughly a $6 billion reduction, and then in the renegotiation of the standard reinsurance agreement, which reduced CBO baseline for ag spending about another $6 billion, all of which went to deficit reduction.

While I was comfortable with the farm bill, I was not sold on the wisdom behind the SRA. In any case, we do not yet know the full impact the farm bill and SRA will have on crop insurance. This has created great uncertainty and has preoccupied the time of RMA, and thus agents and companies, with issues that are not primarily the goal of federal crop insurance, which is to serve the producer risk management needs. RMA and the industry must pick up where they left off and focus on meeting the needs of farmers and ranchers.

In short, this public-private partnership, it is necessary. The farmer must pay to play. Risk management tools, under federal crop insurance, are tailored to producer price and production risks. Lenders require it, and the federal crop insurance has contributed to deficit reduction and fully complies with the WGO. This is a good deal for the farmer, the agents, the companies creating private sector jobs and economic activity, and good for the taxpayer. I look forward to hearing from Administrator Murphy on how we can make things better. First I'd like to yield to the Ranking Member of the subcommittee, Mr. Boswell, for any comments that may have.

**Ranking Member Leonard Boswell:** Well, thank you, Mr. Chairman, and appreciate you having this hearing, and I certainly concur with much of what you've just said. Pay to play, that's a pretty good little term, and I think it rings very true, and we'll probably talk about some of that. I also would like to thank everybody for joining us here today, as I look around the gallery and see who's here, and the interest level seems to remain high. And Mr. Murphy, welcome back. We've had a few conversations. It's been a little while, so maybe this is a chance for us to catch up.

But anyway, I come from a state where we've got, as you know, over 92,00 farms and more than 30 million acres in production.

**Male Voice:** House Democratic vote [now two bells.]

**Ranking Member Boswell:** It sounds like we're having an interruption, doesn't it? I understand the challenges that farmers and those in the agricultural business face today. It's high risk, as you well know. When I retired from the Army and returned home to farm, I quickly realized that farming had greatly changed over the 20 years that I was away, 20 plus. Back then I had always said that in order to farm, producers need to have access to a bank and a place to buy and sell product, inputs and where to go. And of course we've gotten much more sophisticated over the last years.

And I got caught right in the farm crisis of the late '70s, early '80s. After surviving it, which I did, and I also was chair of my local place to buy and sell, the cooperative, I realized how important is a good crop insurance agent to help me manage my risk. I worked with that agent and my agent was sure that I was never put in the position I was during the '80s farm crisis, because I had an opportunity to do it. I share that story because I understand the importance of the crop insurance industry, not only in the state of Iowa, but across the country.

In 2010, 255 million acres were enrolled in crop insurance. Signup and buy-up levels for crop insurance have proven that farmers appreciate having additional options to help them manage risk. However, certain regions and certain crops are underrepresented, we've found. Looking ahead, we need to see how we can make the program work for more producers. Additionally, I have to say that I am opposed to cutting funding of the program. Budgets are tight, but tight budgets do not mean we must jeopardize the risk management tools that we have today or put in question when improvements can be made in the future.

On that note, this committee has gone a long ways in previous years to address sound fiscal management, and the USDA has decreased costs through the renegotiation of the standard reinsurance, SRA. I have been concerned with these cuts and the effects this negotiation may have on the relationship between farmers and their agents. We must acknowledge that the crop insurance industry is a business, and both the companies and the agents need to make a reasonable profit in order to stay in the market.

Just yesterday I had a conversation, unexpected, with a senior agent in a small town surrounded by agriculture. I won't name the place, but I could if we have a conversation about it. And he is concerned. It's time to start thinking about passing the business on, and with all the questions, whether it's the family or somebody to keep it, it's a vital part. It's as important as having the bank and the place to buy and sell. That agency is important in that community, is my point.

So with that in mind, at this hearing I'll be submitting a question, when we get into the question time, to you, Mr. Murphy, with a request for a written response on this issue. The renegotiation of the SRA has left insurance agents in my state and many others perplexed, worried sick, I guess, by a direct cap on the SRA on the commissions private companies are allowed to provide. To me this is arbitrary and neglects the principal of a free market and the expertise and hard work of insurance agents our farmers rely on. So I look forward to the response and to working with you to further enhance the crop insurance industry so that it provides maximum benefits to producers and consumers alike.

Among the many farm programs we support, I highly value crop insurance, and believe it must be structured to ensure a free marketplace for insurance agents across the nation. We're making great strides to help the American farmer, and I look forward to hearing more about the crop insurance program today. And I thank you again for your testimony and what will be a central means for us to continue to move forward on the next farm bill. So thank you, Mr. Chairman. I yield back.

**Chairman Conaway:** Thank you, sir. I recognize the chairman of the full committee for comments he might have.

**Chairman Frank Lucas:** Thank you. And I'd like to thank the Chairman and the Ranking Member for holding this first in a series of audit hearings to examine programs authorized in the farm bill. My goal with these hearings is twofold. First, I want the department to present a spending snapshot of farm programs. Our subcommittees will examine spending trends and confirm whether the purposes and goals of the programs we authorize are being met successfully.

We'll look for duplication within issue areas to determine program overlap. We'll also examine program eligibility and whether those eligibility criteria meet the needs of our constituents. And we'll scrutinize waste, fraud and abuse and look for ways to build on the success the department has already achieved in this area of program integrity. In essence, this is what I mean by an audit of farm programs.

The second purpose of these audits is educational in nature. I think it's important for our committee to learn just how many programs we authorize in the farm bill, and the amount of money we dedicate in each area. And I want the members of our committee to have a holistic view of farm policy before we move forward. Too often in the past Congress has considered a piecemeal approach to farm programs, adding layer upon layer, while not looking at the overall picture to see how these programs interact. We are starting with comprehensive audits so we can examine each program within the broader context of farm policy.

These audits ensure that we are operating from the same base of knowledge. We represent states ranging from Alabama to Oregon, and the diverse constituencies that come with that, so we all have unique priorities for farm policy. But while our priorities may differ, our facts cannot, so these audits give all of us the same data to use in decision-making.

Having the best available data will help us better understand farm programs so we can navigate the tough, and I mean tough, road ahead. I hope that today we can start a dialogue on how to root out inefficiency so we can continue supporting our farmers and ranchers while spending, yes, fewer taxpayer dollars. It's also important for all of us to understand our priorities from the last two farm bills.

Before we move forward on new policies, we should understand how we got to where we are today. Some of the circumstances that shaped past farm bills are still relevant today. Others have changed. We all know that this farm bill will be developed under a very different fiscal climate than the '08 Farm Bill. The simple truth is we must make some difficult decisions. There are no sacred cows, so to speak, and during these tough fiscal times, every program, every title will be on the table.

This farm bill gives the committee an excellent opportunity to prioritize the programs that are working, fix the programs that are broken, eliminate the programs that are duplicative. We'll make these determinations with the help of these audits along with the input from our constituents. We'll start this process today by taking a serious look at crop insurance to ensure that our fund are used economically and the program delivery is efficient for farmers and ranchers.

As we begin the process of developing the 2012 Farm Bill, I know the challenge of doing more with less will be foremost in our minds. I believe that we can meet this challenge and develop thoughtful policies to keep American agriculture productive and competitive in the 21st century. Thank you, Mr. Chairman.

**Chairman Conaway:** Thank you, Chairman. We've got one vote, and I thought we'd just try to do a rolling deal, but it came quicker than I thought it was going to. Do you have any comments, Ranking Member? Okay. Why don't we take a quick break, run across the street, vote, and then come back, and then all of us will have access to hear you talk, and we won't be as disrupted that way. So the meeting will recess subject to the call of the chair.

[*Recess*.]

**Chairman Conaway:** Let me just add one piece of administrative… The gentleman from Indiana, Mr. Stutzman, is not a member of the subcommittee, but has joined us today, or will join us in a moment, and I've consulted with the Ranking Member, and I'm pleased to welcome him to join in questioning of the witnesses. So at this point in time, Mr. Murphy, you have the floor for your opening comments. Thank you for being here.

**Mr. William J. Murphy:** Chairman Conaway, Ranking Member Boswell, members of the subcommittee, as administrator of the Risk Management Agency, I am pleased to meet with you today to discuss the latest developments in RMA and the progress and challenges of the federal crop insurance program.

Along with Secretary Vilsack's leadership, I have the goal to administer the federal crop insurance program in a manner that provides effective risk management services to all farmers and ranchers, regardless of their location or the size of their operation. The Secretary and I are aware that in today's economy, it is important that the program be cost effective and give a fair value for taxpayers' dollars. I am proud that I can confidently say we are doing just that.

Crop insurance has become an integral part of the business life of the large majority of American farmers and ranchers. They would find it difficult, if not impossible, to continue without the protection provided by this part of the farm safety net. Many lenders now require crop insurance coverage in order to make operating loans to crop and livestock producers. Many producers use crop insurance as collateral for loans as well as to provide support for forward pricing their crop.

Today over 250 million acres of farms and ranches are covered by federal crop insurance, for an overall participation rate exceeding 80% for the major crops. The value of insured crops is at a record high. In 1994, program liability was less than $14 billion. This year it will exceed $100 billion. More producers buy higher levels of insurance now and more specialty crop producers participate in the program than every before.

Our unique and successful relationship with our private partners, 15 insurance companies, and the agents who deal directly with farmers and ranchers, is the foundation of this program. Producers purchase crop and livestock insurance from insurance agents operating and living in their communities. This relationship leverages the respective strengths of the public and private sectors.

The 2011 crop year, with widespread flooding in some areas and record drought in others, has been a true test of the crop insurance program. My staff and I are closely watching all developments to ensure that producers get all the protection provided by their policies. The preventive planning coverage available in most policies has been of extreme importance this year in areas where standing water and waterlogged soils have prevented producers from getting into their fields. In drought stricken areas the compensation provided for reduced yields will be extremely important in helping producers to survive till next year. In years like this one, the value of this critical safety net is made clear.

The $6 billion in savings created through the renegotiated standard reinsurance agreement in 2010 went toward reducing the federal deficit and supporting high priority risk management and conservation programs. By containing program costs, these changes also ensure the sustainability of the crop insurance program for American farmers and ranchers for years to come.

RMA's comprehensive information management system, CIMS, is of clear importance to producers. Working with the Farm Service Agency, RMA began, in 2007, to provide access to over 12,000 users of RMA, FSA and crop insurance companies as a single source of RMA and FSA program information for producers, crop acreage and production. The next stage of this information sharing is now underway in the department's efforts with cross-functional representation from RMA, FSA, NRCS and NASS. One-stop reporting for farmers and standardizing programs across the department is our goal.

As those of you acquainted with the dairy farmers may be aware, the livestock gross margin diary plan of insurance ran out of funding this year. Congress makes $20 million a year available for all livestock programs, and the popularity of a newly designed dairy program exhausted these funds in March, halfway through the fiscal year. We look forward to again funding LGM dairy in the new fiscal year.

RMA continues to make significant progress in preempting fraud, waste and abuse through the expanded use of data mining. RMA, FSA and the crop insurance companies have preempted tens of millions of dollars of improper payments through quality control, data mining and other measures. RMA is constantly identifying ways to balance competing needs to make our product less susceptible to fraud, while seeking to provide responsive, useful risk protection tools to farmers.

Again, thank you for the opportunity to participate in this important hearing. I look forward to discussing the crop insurance program with you and responding to any questions you may have.

**Chairman Conaway:** Well, thank you Bill. In under the wire on the five minute mark. Appreciate that. The chair would remind members they will recognized for questioning in order of seniority of members who were here at the time of the start of the hearing. After that, members will be recognized in order of arrival. I appreciate your understanding. I will now recognize myself for five minutes.

In my opening statement, in Leonard's and yours as well, you talked about the importance of the private-public partnership of delivery of crop insurance. From time to time we hear rumors that that partnership may need to go just totally public, and with a public delivery – I mean a private – excuse me, public delivery of the system. Are you and your stuff committed to this public-private partnership? Because it sure looks like it works to us.

**Mr. Murphy:** Yes, indeed. In fact, the Secretary reiterated that when meeting with one of the trades groups a couple weeks ago in his office. There's no doubt in my mind that we're enjoying these participation levels today due to that unique relationship with private agents and their companies.

**Chairman Conaway:** All right. You mentioned the importance of your information technology improvements. Will you be able to finish all of that under your existing budget authorities?

**Mr. Murphy:** We'll do the best we can, sir. It's moving along. We're having some very good success. I'm glad to see we had it up running and we're able to bring the combo product up this year. So it is functioning. I'm concerned for the out years. Next year we don't have the funding anymore that was provided in the farm bill. I'm sure I'll be up here asking for additional funding for that project. But that is of great concern to us.

**Chairman Conaway:** Well, I think that's going to be important, Bill, that you lay that out for us specifically because we have choices to make, and those need to be informed choices. And if one of those has an impact on that, then the committee needs to understand that.

**Mr. Murphy:** I'd like to add that also the more complex our programs become, we really need that IT capacity in order to deliver these programs to farmers.

**Chairman Conaway:** Well, also the impact on this budget, on FSA and their ability to deliver their side of the house is, in the same way, I think it's impacted by that. At one point in time, speaking of the data mining, there were some barriers between RMA and FSA data so that the folks in Charleston could not fully exploit everything available. Have those barriers been taken down? Is there anything left that we need to do?

**Mr. Murphy:** No. Actually, we're making a lot of progress. There continue to be problems between the data between RMA's data and FSA's. We're actually working through the SURE program. We're fixing a lot of that data. I think as CIMS comes up and running, it'll be extremely helpful in identifying where we have differences between the two programs.

**Chairman Conaway:** But in terms of legal—

**Mr. Murphy:** Oh, no, we're working through that. In fact, FSA is just about prepared to publish their new [sworn] which will provide us the flexibility we need.

**Chairman Conaway:** Okay, so if there's something in that regard to fully exploit that, it benefits all of us.

**Mr. Murphy:** Right.

**Chairman Conaway:** Can you walk us through a little bit about how the 508H program is working and maybe some examples that are currently in the pipeline?

**Mr. Murphy:** Okay. Actually, we have three different ways that we can develop programs. One of them is that we can go out and contracts ourselves for the development. The other way is where the private sector actually comes into the board of directors and presents a program. They can go the 508H route, which is that they bring a fully developed program to the board of directors for approval.

Another route with the last farm bill was the concept proposals, where actually folks can come into the board of directors, explain what they'd like to develop, and then we can get partial funding for that development, and then it follows the 508 procedure after that. It seems we're getting new programs out on the street. That seems to be working well to that effect. There are some issues or some concerns being raised about some other maybe programs that are higher priority that should be done first. But that's just the way the system is established. But we are working along it.

**Chairman Conaway:** All right. The members know that there's a questionnaire that we've asked each of the major proponents. You sent yours in. I'd like a question on Page 5, or No. 10, it says "utilization participation data." If you could walk us through that. The number of policies stayed exactly the same for ten years. Can you just walk across those columns and help us understand what each one of them means?

**Mr. Murphy:** Okay. Actually, I think the next chart is much better if we're looking at the changes over years.

**Chairman Conaway:** Well, just tell us what that means. We talked about $100 billion in coverage out there, but that bottom line for 2010 just says 71.

**Mr. Murphy:** Okay. Yeah, well, that's actually in 2010 it was in the $70 billion range -- $78 billion, I think, is what it's at right now. But with the increase in commodity prices between 2010 and 2011 is where we expect to see the increase to over $100 billion.

**Chairman Conaway:** Well, we've talked about participation, but the number of policies have stayed dramatically the same.

**Mr. Murphy:** No, it's, actually – well, there hasn't been a lot of variation since 2001.

**Chairman Conaway:** Okay. And then the loss ratio and the loss cost columns, can you explain those to us real quick?

**Mr. Murphy:** Okay, the loss ratio is just the experience of the program. That's the ratio of premiums to indemnities paid. The good story here is that you can see the ten year average. We're at .837. That means for every dollar in premium in, we pay out .83 cents. So the program is actually performing very solidly at this time. In fact, if you go back 20 years, you're still under a dollar loss ratio. So we've very proud of the changes in that. Loss cost ratio is just a measure of how much of the liability is being used by the indemnity. We actually use both of these ratios in order to come up with the rates for the program.

**Chairman Conaway:** All right. Thank you, and I'll yield back. Leonard, five minutes.

**Ranking Member Boswell:** Thank you. Well, again, going to our, continuing our running conversation, Bill, I continue to be…we've found at our hearings across the country, months ago, what we need out there to our producers is available, affordable, and viable in the sense it works, crop insurance, and I think you're trying very hard to do that, so I'm not… But I just say this is extremely important.

Think of the high cost inputs. And I don't know about cotton country and so on, wheat country, but they like to talk about the price per bushel, or corn, when it's doing well. You never hear any conversation about the cost of input. I think it's incumbent on all of us on this committee that we ought to make an issue of that, because the public out there don't really get the idea of what it costs to put that crop in. And it's capital intensive, and this crop insurance is terribly important.

So anyway, I want to ask you this question, which we've referred to, and then I'll leave it with you. The Risk Management Agency has redefined the definition of agent compensation relative to the release of the 2011 standard reinsurance agreement. The restrictions outlined in the agency acquisition section of the manager's bulletin on agent compensation are very troubling because they restrict an agent's ability to sell his agency or her agency at the full market value. In many instances the sales of these family owned crop insurance agencies are relied upon for retirement income and for future financial planning. In addition, such restrictions will also hinder a company's ability to grow.

The only option for company expansion will be through the acquisition process, which favors large companies over small companies, and will lead to less choice for consumers. So how does the agency acquisition provision in the 2011 SRA improve the federal crop insurance program and strengthen the safety net for farmers, and is the RMA willing to revisit this provision to address these concerns? And I'll give you this in writing as well after this is over with, but I'd like for you to comment on it.

**Mr. Murphy:** Actually, that provision is not in the SRA itself. That provision is actually in follow-up procedures that we provided after the—

**Ranking Member Boswell:** Well, let's address the point.

**Mr. Murphy:** Right. There's nothing in there that restricts the sale of an agency. What they're talking about there, and where this becomes an issue, if a company buys an agency and then employs the principal of that agency and continues to pay the agents, all we're saying there is that that sale, if the principal stays in, involved in that agency as it becomes part of the company, is that that counts towards compensation. There is a great concern that that particular scheme was being utilized to evade the caps on agent commissions. So, you know, I want to make clear that there is nothing that restricts it.

**Ranking Member Boswell:** Well, at least…

**Mr. Murphy:** Okay, now—

**Ranking Member Boswell:** It [toughens] the possibility, we can—

**Mr. Murphy:** Yeah, well, limits…it limits potential sales. You could say that.

**Ranking Member Boswell:** Okay.

**Mr. Murphy:** Yeah, you could say that. Now, this is in a procedure that we actually got…we just finished getting comments from the agents. We sent it out to the agents groups to get their comments as well. We're incorporating all that now and we have not issued it yet as a final procedure.

**Ranking Member Boswell:** I hope we could have some conversation on that. I would look forward to that. And seriously, when I shared with you the person that I talked to, I didn't call him, he called me. I talked to him for…at any other time in during this whole process, we have not had conversation.

**Mr. Murphy:** I'm sure it's because the procedure went out—

**Ranking Member Boswell:** Anyway, he comes in with this concern. And coming from this individual, as I'm sure many others, it's a genuine concern, and we need to talk to him about it, so I would trust we'd do that. And if you might give us a few points on what you might have to say about the pilot program concerning livestock.

**Mr. Murphy:** The livestock programs?

**Ranking Member Boswell:** Yeah.

**Mr. Murphy:** Actually, well, the big news has been the dairy gross margin coverage. Historically we get $20 million for the livestock program since ARPA, since 2000. We have been actually only spending about, of that $20 million, about three or four a year. What changed this year is that the dairy industry requested, through the developer of that program, to make two changes, one of them to provide a subsidy, which was not in there before, and is not really in any livestock programs.

We do have a small one in some of the others, but that's just to offset some additional cost. So there's no true subsidy like we see in the crop programs. They requested a subsidy and they also requested that the premium payment be changed from the beginning of the insurance period to the end, like the rest of our crop insurance program. The developers agreed to that and we put it out, I think it was four months ago, and growers were extremely interested in the program. Like I said, they used up all the funding that we had available for dairy, which was about 75% of that 20 million.

**Ranking Member Boswell:** Well, thank you. I'll do a follow-up later. I yield back.

**Chairman Conaway:** Thank you, Leonard. Mr. Neugebauer, five minutes.

**Rep. Randy Neugebauer:** Thank you, Mr. Chairman. Mr. Murphy, this will come as no surprise to you. I want to talk about something that has been a big concern of mine for a number of years, and that's shallow losses. For some of my colleagues that are new to the committee, basically a lot of producers can purchase an APH policy and get 65, 70% coverage, but in many cases if they want to buy up that coverage, when you get above that level, the premium becomes extremely expensive. In fact, it's almost a one-to-one, a dollar of premium for a dollar of benefit, and obviously that makes the economics...

So what in many cases can happen for producers, they can have anywhere from a 25 to 30, 35% loss and not receive any coverage from their policy. And obviously there's very few businesses I know that can sustain a 30, 35% loss in their margin and be profitable. So there's a lot of potential solutions to that out there, and some have said additional premium support for APH to make it more cost effective to buy up. Others have, as you know, I have a plan that would provide a supplemental opportunity based on area yield or county yield. So what are your thoughts? Do we stick with the APH or do we look at some of these supplemental opportunities?

**Mr. Murphy:** Well, I know the SURE program, which was instituted with the last farm bill, was actually supposed to address that, basically utilizing the crop insurance indemnity for an additional payment under, as a disaster payment. I have not gotten too involved in SURE. Anecdotally I understand there's concerns in different parts of the country whether it's achieving what it was intended to do. How it's actually working day-to-day, I really am not the best person to talk to, but I would be very happy to work with you towards the farm bill and look for some…

**Rep. Neugebauer:** Yeah, I think part of the SURE program is it's triggered on a statewide basis.

**Mr. Murphy:** Right.

**Rep. Neugebauer:** And, you know, Texas is a pretty big state, and so you can have one condition in one area of our state and others. But I think that's going to be an important part of that because I think as we begin to look at the basket of safety net for producers, price, you know, it doesn't do you any good to have any price safety net if you don't produce a crop.

**Mr. Murphy:** Right. I think also it requires a disaster declaration in the county, in the adjacent counties, and so if only a small percentage of farmers get his with the problem, it's not going to trigger the county as a potential.

**Rep. Neugebauer:** Absolutely. And I want to go on to another area. I know that plains cotton growers initiated an effort on cotton seed, a pilot program, and I guess this was the first year of that program. Can you kind of give us a little thumbnail of how that program has worked and the results of that?

**Mr. Murphy:** Okay. We haven't gotten the acreage information in yet. That's probably going to be another couple months away, but I can tell you anecdotally, from our offices down there and the companies there, it's extremely popular. This is something that those growers are very interested in. That seed is becoming, especially when the prices drop, that seed becomes a bigger part of the revenue for the year, so it's critical that you not only have the [lint], but the seed as well to get the offset for the seed. So from what I understand, the growers are very happy with it. We worked with the developers and we actually made it extremely simply administered, the program, so I think agents are happy with it. So overall I think it's been a success.

**Rep. Neugebauer:** You know, recently, when they renegotiated the SRA, I think RMA kind of divided the country into, I think, three groupings. Group 1 was Illinois, Indiana, then Group 2 was Alabama, [assume] to be some of the southern states, and

Group 3 was kind of a hodgepodge, all the way from Alaska to Nevada to Vermont. Can you kind of give me some perspective of how those were grouped?

**Mr. Murphy:** Okay. The reason we had done that, and that was something new we introduced for the first time with this SRA. In the past, with the underwriting, the ability to make underwriting gains or loss were equal across the country. What we tried to do this time, as an effort to try to get that same high level of service we see in the Midwest and other parts of the country, we reduced the company's ability to make underwriting gains in the five, what normally are referred to as the "I states" in the Midwest.

And actually, we increased the opportunity to make underwriting gains in other parts of the country. So we were just, for the first year, in 2011, going through it. I think, from the modeling we've gotten so far, it seems to be working. We've talked to agents who are saying that actually, in some of the parts that have historically had low commissions, that this is actually making it more – more companies are becoming interested in getting into these other parts of the country, and that's what we wanted to do, so we wanted to spread that competition as well.

**Rep. Neugebauer:** Were the premiums different in the groupings?

**Mr. Murphy:** Pardon?

**Rep. Neugebauer:** Were the premiums different in those?

**Mr. Murphy:** Only by nature of whatever the experience was for those crops, yeah.

**Rep. Neugebauer:** But nothing to do with the group?

**Mr. Murphy:** No. Not from – from the grower's standpoint, no, no difference at all.

**Rep. Neugebauer:** Thank you, Mr. Chairman.

**Chairman Conaway:** Thank you, gentlemen. Joe Courtney, Connecticut.

**Rep. Joe Courtney:** Thank you, Mr. Chairman. Thank you for holding this hearing. Mr. Murphy, I want to go back to the dairy pilot program that you were talking about earlier. Obviously the high demand is an interesting signal that the interest is there. One of the farms in my district, one of the subscribers to the insurance was sharing with me his experience with it, which, you know, he's got a, I'd say, moderate sized herd, farm, and he signed up for it kind of like as a test run because I think looking out on the horizon, it's pretty clear that risk insurance is going to be part of the world of that industry. His concern, obviously, was cost a little bit, which I think a lot of the smaller farms are nervous about.

But the other issue was the complexity of the product. I mean, he was describing to me the system for calculating the monthly premiums, and we're pretty comfortable in Connecticut with insurance products, as you can imagine, but this one was pretty sophisticated. And I was…I mean, the message was that they've got to run a farm. You know, trying to sort of calculate what their payments are, it was…it took some fairly difficult and time consuming effort. So I wonder if you could walk through about whether that's a complaint that you're hearing and whether there's ways to address it. Simplicity is always a good thing.

**Mr. Murphy:** Yes. Yes, indeed. You know, I haven't heard too many complaints about that, but it does not surprise me because it is a great deal more complex than our normal crop insurance program for corn or soybeans or something like that, because what you're actually doing, you're looking forward into the next 11 months and you're comparing the prices of the feed versus the price of the milk itself using the futures contract. And that is what makes the margin, and so you're insuring that margin month to month in the out years. So instead of looking at, if I was a corn grower, I'm looking at one insurance period, when you're actually a dairy farmer, you're looking at potentially 11 that you have to go out there, so a great deal of complexity.

The program has not been evaluated yet. That will probably occur within the next couple of years. And what I'd encourage is they can either send comments in to us and we can share them with the developer or we can get the address of the developer and the grower can go directly to them. But like I said, they instituted a major change just this year, so I believe they'll be open to looking at comments the growers might have. But I think the very nature of that type of a program is going to be more complex than something like the corn the guy probably insures already.

**Rep. Courtney:** Is it too soon to say whether people have been actually filing claims?

**Mr. Murphy:** Yes, it is. Yeah, it's too soon now, definitely. But I think it certainly shows their concern with the volatility that they've been seeing in pricing for the product. And I understand that the industry has put forward something very similar, something that they would like to see potentially in the farm bill. I have not seen what they're suggesting, but I know they've been working on a product.

**Rep. Courtney:** Right. All right, thank you, Mr. Chairman. I yield back.

**Chairman Conaway:** Thank the gentleman. Before we move to our side, the Ranking Member slipped in. Comments for five minutes?

**Ranking Member Collin Peterson:** Yeah, thank you, Mr. Chairman. I guess what I'd like to know, you know, we made these significant changes in the farm bill and the SRA. When are you going to have solid information about how this actually sorted out? You probably don't have that yet, I would assume.

**Mr. Murphy:** No, no. We're already seeing some of the effects, Congressman, especially in the area of agency compensation. This has been a bit tricky for the companies to try to get through. We're doing it new for the first time, the cap and how it's implemented. We are exceeding the cap, as is no surprise, for 2011, with the way the commodity prices. We're seeing areas like California where commissions had dropped a good deal more than we thought they would.

The industry, the companies themselves have expressed some concern here, so we're going to take a look at that to try to even out the pain of reducing the A&O overall in the program. Some of the companies are interested in having that discussion. On the underwriting gain side, all I've seen is some studies that have been done on the new underwriting gain potential, underwriting loss potential, and they have not been bad at all, especially with the prices we're seeing this year. Now we're getting off to a bad start, and so I guess, I imagine it has the companies nervous. But it's probably going to be, I'd say, November, December before we have a good handle on what the impacts would be on underwriting gains or losses.

**Ranking Member Peterson:** Okay. And then how about on the agent situation, the same time frame?

**Mr. Murphy:** Yeah. We're already hearing the concerns from the agents on it, and we're already talking to some agents. They're coming up with some ideas. We're getting questions, is there – can anything be done, since it's sort of locked in place. Basically, as long as we don't increase the cost, we do have some flexibility, all right? But it would require all the companies to agree to make the change. And so those discussions will probably just get started within the next couple months.

**Ranking Member Peterson:** So depending on when we actually write the farm bill, but say it's next year, we'd probably have pretty good information?

**Mr. Murphy:** Certainly on the A&O side, yes, the administrative and operating expense side that we provide to companies, and we'll have some preliminary information on the underwriting gain potential, underwriting loss potential as well.

**Ranking Member Peterson:** Okay, all right. Thank you, Mr. Chairman.

**Chairman Conaway:** Thank you, Mr. Chairman – Mr. Peterson. Austin for five minutes.

**Rep. Austin Scott:** Thank you, Mr. Chairman. And Administrator Murphy, thank you for joining us today. And thinking back to when I was a child, I can remember quite vividly my grandfather, who was a producer, telling me that he thought that the insurance program was the most important thing that the federal government did for the farmer, and was, quite honestly, maybe the only thing that we would have to do for the farmer if we had it right. I also majored in risk management and insurance at the University of Georgia, which is the best school on the face of the earth, I might add.

**Mr. Murphy:** For the record.

**Rep. Scott:** And my question gets back to this, one is, I would say, and you can check these numbers, while the average loss ratio is 83.7%, the total loss ratio over ten years is even a little better, and closer to 77%. Is that right?

**Mr. Murphy:** Yeah.

**Rep. Scott:** So our total loss ratio is even a little better than our average loss ratio because of the years where we got hit so hard. I also remember my grandfather talking about people who had learned to game the insurance system, if you will. And so as we work forward with this insurance program, I want to make sure that we have the best program possible for the good farmer. And it gets back to something you've talked about a little bit before I'd like you to expand on. Somebody's whose claims ration – and I know you've talked about it more from the standpoint of a discount for a consistently good producer—

**Mr. Murphy:** Right.

**Rep. Scott:** —but virtually every insurance product out there in America is risk adjusted based on the conduct of the individual, and so as we go forward with that, would you talk with us about your ideas for having somebody who makes multiple claims versus somebody who is not making those claims, someone whose loss ratios are out of line, if you will, consistently, how do you intend to handle them paying more into the system, the risk adjustment there?

**Mr. Murphy:** Okay. Overall, first I'll just say that from a standpoint of integrity, it's actually embedded in every function of the program. It's critical that we continue to try to do the best we can to combat fraud, waste and abuse. We've got some very advanced tools – data mining, which has been very successful. That has helped us identify schemes going on. We have some very large cases occurring right now in tobacco in North Carolina as a result of the findings of data mining. That's an important tool, so that will help us.

But you're absolutely right. When you get down to the county level of this program, if somebody's abusing the program, that county is paying for it, the neighbors are paying for it. We rate on a crop county basis in this program, and so as a result, next to data mining, probably the most important tool that we have in identifying and fighting fraud are neighbors who do not want to see their premiums go up because of something somebody is doing.

We keep working more and more. We work very closely with FSA on a spot checklist and we identify anomalies through data mining. FSA spot checks those through the year. That has been extremely effective. And so I think as long as we try to keep up with new schemes, because as you tighten things up, a certain group of people will always look for ways to get money for doing little, we'll keep addressing that going forward.

**Rep. Scott:** I think you're right with what you've said. I think my FSA agents could probably predict for you who was going to file the claims.

**Mr. Murphy:** Who you need to watch.

**Rep. Scott:** And so could the majority of the farmers in the community. And so I guess I hope that we will work towards and adjustment in that and make sure that we are creating the program that works for the good producer. And I understand that a good producer's going to have some losses. That's just the facts of life. But I just hope that you'll keep moving down that path and keep us informed. And I do, again, want to point out the importance, I believe in the private-public partnership here where we are the insurer, but we have private agents out there actually handling the insurance product. Thank you. I yield back the rest of my time.

**Chairman Conaway:** Thanks, Austin. Ms. Roby for five minutes.

**Rep. Martha Roby:** Thank you, Mr. Chairman, and thank you, Mr. Murphy, for being with us today. And just to build upon what Mr. Scott was talking about, in preparation for this hearing we heard from our folks back home who shared similar concerns, that we should be rewarding farmers for good performance history with crop insurance, either through lower premiums or increased coverage levels, because more consideration needs to be given to the individual experiences that would not disadvantage good producers in a bad county experience situation.

I'm going to ask you a specific question about the group risk insurance program. It was very, very popular throughout the South and was used pretty heavily in Alabama. And the RMA stopped the program in many counties due to insufficient data. So I want to know is RMA currently exploring any avenues that would allow reintroduction of this program or a similar program in areas that previously lost access to those products?

**Mr. Murphy:** I think there's a two part answer, and one of them is I think NAS is working harder with farm groups, realizing the importance of getting this data into NAS, so I think there's an emphasis on growers and making sure that everybody in the county reports to NAS the correct numbers. The second thins we're doing is we're looking at our group risk plan as well as a few other changes to the actual production history basis of the program.

One of the things we'll be looking at is maybe perhaps having area group plan participants provide their yields every year. That way we'd be able to use our own data instead of having to rely on NAS's program alone. So we're looking at that as a way to address that. Another thing we could do is look at combining districts. That gets a little tricky if you have a lot of changes in geography of the area. But that's another thing we can take a look at. But we're very aware of that, and we're looking at ways that we can bring the program back into those counties as well as expand into other counties.

**Rep. Roby:** Good. Thank you for that. And I just want to make this as a comment, and you can respond if you want, but right now, under the current rules, in some situations a farmer is required to carry a failed crop to harvest, and this comes from our groups back home, and so they spend more money to actually harvest the crop than the crop's going to bring. And I just want to point that out, that that needs to be addressed. It's detrimental, in some situations.

But I want to go back, since I've got a little bit more time. You mentioned in your testimony that lenders now require crop insurance coverage in order to make operating loans, and many producers use collateral for loans. Can you tell us why crop insurance has become so important to the producers in securing financing?

**Mr. Murphy:** I think it is because a grower knows up front what his protection is going to be, and the banker knows up front what the protection is there. It's not only their knowledge of the crop insurance. Bankers have become extremely, actually, the mechanics of the programs, and so they'll suggest certain types of products that they want the grower to purchase. Another thing that they can do is that they could have the indemnity send to the bank or make the indemnity payable to both the bank and the grower.

Now, the growers don't always like that, but if it helps secure a loan, I think it's a good thing. So it's just become something that banking depends on. Now with the advance of revenue coverage as well as yield coverage, for a grower to be able to go into a banker and say I'm guaranteed to make this much money per acre, that's a pretty powerful source of collateral for that bank. So I believe that's why it's become – we don't need Congress to take any action during the year, we don't need the Secretary to take action, the program just works, and if a grower has a loss, he gets paid.

**Rep. Roby:** Thank you so much. Mr. Chairman, I yield back.

**Chairman Conaway:** Thank the lady. Mr. Schilling for five minutes.

**Rep. Robert T. Schilling:** Thank you, Chairman. What I wanted to just address – thank you for coming out – duplication and overlapping of services, basically. One of the concerns is about the duplication of the acreage reporting, including the cost of administering and the frustration that it causes our producers. And given that many of the producers have multiple farms with different acres and crop rotations on each farm, it seems the process drastically increases the margin of error, and increases twice as many opportunities for the mistakes. Why can't we just avoid – I think you know where I'm going with that.

**Mr. Murphy:** Yeah, I understand your point exactly, sir, and I'm very pleased to tell you we are making progress in this area. Through the Comprehensive Information Management System, the CIMS program, we are pulling together the acreage report dates for both FSA and RMA. I think next year spring crops, 2012, we'll see the first dates of that, and that will be in the northern country. That has always been a source of angst to growers out there.

We're working toward, through that same project, a single report reporting. If the farmer wants to go to his FSA county office and report, why can't the agent download that information and use it himself, and vice versa? If it's a rainy Thursday afternoon, why can't a grower sit and certify at home and have it sent to both programs? That's the end goal of the CIMS project. Under Secretary [Skews] is a primary proponent of in the department, and I'm happy to say that we are moving very quickly toward that.

**Rep. Schilling:** Very good. Have there been any issues in reconciling the crop production? Well, we've talked a little bit about that. I'm going to pass on that. One of the things I'm a big proponent, like Mr. Scott had indicated, is the public-private partnerships. I think those are huge. And one of the things in the Illinois 17th District, where I'm from, that's the one thing I continue to hear from the farmers, you know, leave our insurance alone. But with that, I appreciate your time, sir.

**Mr. Murphy:** All right, thank you.

**Chairman Conaway:** Thank the gentleman. Mr. Crawford, from Arkansas, for five minutes.

**Rep. Rick Crawford:** Thank you, Mr. Chairman, and thank you, Mr. Murphy, for being here. Can you provide any insight into the differences in participation rates between crops and/or regions? For example, in 2010, according to RMA data, about 68% of rice, and particularly in Arkansas, acres were insured. By contrast, nearly all of Texas cotton acres were insured. Are there unique concerns with certain crops or regions?

**Mr. Murphy:** Actually, there is, indeed. I'm happy to report that we are seeing increases. One of the concerns we often get is between major program crops and specialty crops. We're at 83% participation on the major program crops. We've come up to 75% for specialty crops, so we're seeing progress there.

I think the introduction of the additional subsidy for enterprise units has also been extremely helpful, especially in your area, for both rice and cotton down there. It reduces the premium tremendously. Growers have flocked to those programs, and we're seeing increases there. That alone is not going to solve it. We're seeing probably Arkansas, Mississippi, Alabama, that area is where we're seeing lower participation than other parts of the country.

We are actively working with commodity groups down there to try to improve the programs. We're looking at the dates in the program to make sure that they're the correct dates we should be using and that they're not such as planning dates, rate reporting dates, end of insurance dates. We're taking a look at that. We're even getting into the policies themselves. We've been having great meetings with the rice growers and working at some additional coverage the growers would like to see for downed rice, which results – hurricanes come through the area and they have to deal with the additional costs of harvest. Hopefully that is going to see some progress in the next couple years.

It's been very successful work between us and the group down there. So we're using multiple ways to do it. I think it's slowly coming along. I just think we have to keep working with it. Program integrity is another big issue. There have been issues with program integrity in the past. They have to be convinced that their premium dollars that they're paying out is going only to legitimate losses. Compliance, our compliance office is putting extra effort into that area to show that. So we're doing a number of things going forward, and as we get into the farm bill, I'd be more than happy to work with you and your staff at additional ways we could look at increasing participation.

**Rep. Crawford:** Excellent. I've just got half my time left here, so let me ask you this. Is the flooding that has resulted from the Army Corps of Engineers breaching the levees along the Mississippi and Missouri Rivers an insurable cause of loss under the federal crop insurance program?

**Mr. Murphy:** Yes, it was. And there was some consternation at the beginning when the Corps first had decided to intentionally breach some of those levees. We worked with the Corps. They've provided us with information of what would happen if they did not breach the levees where they did. Additional damage would occur to corps downstream, uncontrolled damage where they couldn't tell us what additional damage would occur, especially in the northern part, the Missouri levee. The water was actually toping the plugs at the point that they blew them. If a levee is topped, the integrity of that structure is compromised severely and would probably fail anyway.

As we move further along the Mississippi, the Corps was able to show that, actually, if they did not breach those levees where they did, the potential for the levees alongside with more intensive cropping, higher value cropping, would be compromised. We were able to make the determination up and down the Mississippi River that they were insurable events. The companies have been informed. They tell me that they are moving loss adjusters in now to start working with the growers there. So yeah, we were able to address all those concerns.

**Rep. Crawford:** Okay, excellent. Real quick, I want to move back to rice. You covered that pretty well, but I just want to ask what's the current participation rate of rice and buy-up coverage levels of protection, and how does this participation rate compare to other major crops like corn, soybeans, wheat and cotton?

**Mr. Murphy:** I don't have that information right with me. I can tell you it's lower than you see in the major crops. I will get that to you, though.

**Rep. Crawford:** Any ideas of what we can do to increase that?

**Mr. Murphy:** Again, I think it's working with the growers and seeing how we can improve that program. I mean, it was the development of revenue coverage that brought in the corn and soybean growers to the levels we've seen, so program improvements will bring in growers once they believe their risks are being addressed by our programs. So I think it's just a matter of continuing working until we get it right.

**Rep. Crawford:** Excellent. Thank you, Mr. Murphy. Appreciate it. Yield back.

**Chairman Conaway:** Thank the gentleman. Tim, five minutes.

**Rep. Tim Huelskamp:** Thank you, Mr. Chairman. Appreciate your appearance here today, Mr. Murphy. And I come from a fairly large district, and doing town halls across the district, you learn not to complain about certain things, or you complain about water in my area, it's a drought, in the other end of the district it's flooding, and so we have both of those. But what I hear consistently is the importance of the product you produce, and we'll be watching that very closely.

And as one proponent noted, that given the situation, this is really going to test the program, and we're going to have to really perform like we never have before. With that in mind, particularly with not only the higher, but much more volatile commodity prices, how does that impact, in your mind, and how do you adjust for that and maintain the solvency of a program with the type of changes we've seen and are likely to see in the next six months?

**Mr. Murphy:** Actually, there's a lot of data available for us to go back and stress test our rates against historic results of the futures market, which we do. In 2008 I think we saw the biggest drop ever for the major commodities on the futures market from the beginning of the year to the end of the year. We actually ended up with a positive loss ratio nationwide, even though the companies probably did a claim on just about every corn or soybean policy out there that had revenue, and so we ended up with a positive price.

We continue to work with, have others review our actual rating methods, so we have outsiders look at what we're doing and validate or suggest changes, which is done, and we incorporate the changes. It's a constant work in progress, and I'm very happy that it has been successful to date. With the commodity prices we're seeing today, if a farmer goes ahead and forward contracts his price, he has a massive risk, and crop insurance is just necessary to protect that grower in the event that the price is to drop or goes considerably higher if you have a loss.

**Rep. Huelskamp:** Appreciate that. And how much room for margin of error do you have? I mean, there are suggestions out there, with the current economic environment, with items happening, whether it's in this building or at the Federal Reserve, that impact on volatility. How much margin of error? I mean, 2008 was a year, 2011 might be one for the books as well.

**Mr. Murphy:** Yeah, indeed. We take volatility into account when doing the rating of the program. In 2008, that's what led to such large premium bills for farmers. It wasn't the yield portion of the risk, it was the volatility factor associated with the revenue portion of the risk that they saw. So I think we have it well addressed. The margin of error, only experience will let us know. But like I said, we have a lot of data we can go back and take a look at, and again, stress test the program, which we do.

**Rep. Huelskamp:** I appreciate that. And 2008 is a good year to—

**Mr. Murphy:** Yes.

**Rep. Huelskamp:** An appropriate year to talk about, and I think 2011 might be one we talk about for many years as well.

**Mr. Murphy:** Yes.

**Rep. Huelskamp:** The second question would be – and I had looked through the materials closely and didn't see this – but as far as taxpayer cost of the programs, how does that vary across the crops, and is that in information you've provided us?

**Mr. Murphy:** We can provide more information on that. The taxpayer cost of the program changes dramatically on the experience that we have for that year. For the last 10 to 20 years, except for a little blip in 2002, we've had positive loss ratios, so I think the program is well worth the money. The subsidy, the premiums are subsidized an average between 60 and 65%. So if we have $10 billion in premium this year, well, the subsidy is going to be up about $6 billion in the program, so the cost goes along with the commodity prices as well. There's a lot of variables in the program. The loss ratio, how much of the losses that the companies pick up versus the government.

**Rep. Huelskamp:** And the high cost over the last decade would have been how much, in what year?

**Mr. Murphy:** As far as the total cost of the program? I would have to pull that together for you. I can do that the last ten years.

**Rep. Huelskamp:** Okay. I'd appreciate that. All right, thank you, Mr. Chairman. I yield back my time.

**Chairman Conaway:** Thanks, Tim. Chris, five minutes.

**Rep. Christopher Gibson:** Thanks, Mr. Chairman, and appreciate, Mr. Murphy, you being here today. I represent a district in Update New York, and your agency enjoys a good reputation up there for how quickly you process claims. So given the current climate, the natural disasters that have hit all across the country, including in my district – we've had flooding along the Hudson River – I'm interested in your assessment of whether or not you'll be able to keep up with the timeliness of the payouts, and is there something about that program that I should carry back? I'm about ready to meet with all my farmers, have a quarterly panel, so if you want to give me some assessment as to how you think that's going to go and if there's any best practices that you think I should carry back, I would welcome them.

**Mr. Murphy:** I have been, because of the nature of the losses we're seeing this year, just about every part of the country is dealing with something this year. I don't think I've ever seen anything like it, and I've been with the program for 30 years. A lot depends how the rest of the year goes, the total amount of claims that will have to occur. I've talked to the companies. They feel very confident that they have an adequately trained work force. They're moving people around the country, which they routinely do, to be able to address situations like this. I do believe we'll be able to make the 30 day turnaround required once the insurance signs the claim to payment of the claim. The companies have told me that they feel good about it, so I'm confident going through we'll be able to – the companies will be able to provide that same level of service the growers have become accustomed to.

**Rep. Gibson:** That's encouraging. Is there anything that in this period would be helpful for me to convey to the farmers in terms of best practices?

**Mr. Murphy:** If they have a loss is to notify their company immediately. That's probably the most important thing you could bring back. You don't want to get into a situation where the company is notified late in the year and they don't have the ability to look at that crop. That becomes extremely problematic. So I would say stay in touch with your company, stay in touch with your agent.

**Rep. Gibson:** Thanks very much. And the second area I'd like to cover is, like everyplace else around the country, our dairy farmers, beef farmers, the beef industry in the 20$^{th}$, we're having issues with input costs. And I'm curious to get your assessment as the ongoing activities in the Senate with regard to ethanol, your assessment how significant that would impact input costs.

**Mr. Murphy:** Okay, that's getting a little bit out of my area of expertise. I usually look toward economists for their advice on it, and I will continue to do so. I'm happy to report that we do have programs for livestock that are gross margin. Basically you're insuring that margin between the price of the finished product and the input costs. It has been a slower uptake in cattle than we have seen in dairy, but it's an excellent program for times like these, so I'd encourage growers to take a look at that if they're concerned about both input and future price for their commodity.

**Rep. Gibson:** Thanks very much, Mr. Murphy. I appreciate your being here. I yield back.

**Chairman Conaway:** Thank the gentleman. Vicky for five minutes.

**Rep. Vicky Hartzler:** Thank you, Mr. Chairman, thank you Mr. Murphy, and I'd like to echo the comments that have already been said here. But among my farmers, your part of the farm bill is probably the most popular part, and everyone, all of us – I'm a farmer, too – appreciate what you do. I wanted to ask, regarding the costs, of course we're looking at budget issues now, and Fiscal Year 2010 it says the crop insurance costs were $4.7 billion. I just wondered, can you give me kind of a rough breakdown of how much of that went to claims and how much went to administrative costs and operating costs?

**Mr. Murphy:** Actually, we're a very small agency. We have about 500 employees overall. So when you're talking discretionary costs of the program, we're only talking 78 to 80 being the overall cost of the program of discretionary. The major costs that we see in the program are the producer subsidy that they get paid, the potential underwriting gains that the companies can make on a good year, and then the administrative and operating expense that we provide to the companies in order to deliver the program.

Crop insurance, unlike private property and casualty insurance, the farmers don't pay that in their premium bill. We provide a separate payment to the companies to deliver the program for it. The negotiation of the standard reinsurance agreement, we actually reduced both the potential underwriting gains for the companies as well as the administrative and operating costs provided to the companies, so we're certainly going to see a reduction. Probably the wild card in the whole thing is the premium subsidy going forward. Like I said, as we've seen these record commodity prices, that brings up the producer premium subsidy payment.

**Rep. Hartzler:** But in Fiscal Year 2010 how much money for those various things? Or maybe you could get that to me later.

**Mr. Murphy:** I can provide that to you on a year basis. I'll break it out for 2010 and get it up to your office.

**Rep. Hartzler:** Yeah, that would be fine. Another question. We have about an 80% crop insurance participation, right, on your major crops. In Fiscal Year 2009, about \$79 billion worth of crops were insured, but yet the overall value of crops in the U.S. that year was \$169 billion, so in other words, about 53% of the value of crop production was actually insured. So how does that reconcile with an 80% participation rate? And given the price volatility and extreme weather, does that concern you?

**Mr. Murphy:** Yes, sure, it always concerns me. There are quite a few crops we haven't reached yet. That's a major – that's a priority with the agency, is figure out how we can expand coverage to the remaining crops out there. Another thing to keep in mind is that our yield guarantees are based on a ten year average, so that basically makes the APH guarantee lower than expectations, if you've seen some of the modeling on how yields have been increasing, especially over the last ten years.

**Rep. Hartzler:** Sure.

**Mr. Murphy:** So you're going to see a lag with the guarantee compared to what expectations of the crops are today. I think that adds a lot to it.

**Rep. Hartzler:** Definitely, that's true. Your testimony states there's only \$20 million available annually to cover administrative and operating costs and premium subsidy costs for the pilot livestock insurance plans. So can you tell me a little bit about that? Are there pilot livestock insurance plans generally available, or are they limited geographically now? Given the finite resources, are they based on a first come, first served principle to sign up? And how much would livestock insurance plans cost the government if it was widely available, given its popularity, so three questions here.

**Mr. Murphy:** Well, I think there's a couple different issues available here. I wouldn't look at livestock programs that we have, such as the revenue programs and the dairy program being the only – we have a pasture rangeland program out there now, forage program that's widely available. We're expanding it as we have the funding to do so. That's something I think livestock folks generally participate in. A lot of livestock growers also grow corn, alfalfa, soybeans. They can insure those. We only got the authority to actually start insuring livestock in the ARPA act in 2000, so it's been a slow ramp-up.

I think Congress wanted to limit how much we wrote until they could see the experience of the programs. I think that impacts it. That's why they limited it to $20 million. That's something I think I'd be very interested in discussing with the committee as we get into the farm bill, taking a look at that and see if that's realistic anymore. I think cattle guys have been slow to come into the program overall. Cattle folks are very independent, as I'm sure you're aware, if you work with cattle guys out there. It's a different breed. So I think that's maybe a barrier as well.

**Rep. Hartzler:** Okay. All right, thank you very much. Thank you, Mr. Chairman.

**Chairman Conaway:** Thanks, Vicky. Ms. Schmidt, five minutes.

**Rep. Jean Schmidt:** Thank you, Mr. Chairman, and thank you, Mr. Murphy, for coming today. In the last few years of higher commodity prices, and given the flooding and drought across this country this year, including the flooding in my own district, how do you insure that farmers' claims are adjusted, processed and reviewed in a timely manner, and are there ways to speed up that process?

**Mr. Murphy:** Well, the companies themselves, who we enter into the reinsurance agreement, they're responsible for that part of the program. They keep a core of well trained individuals in claims adjusting on board. When we have a year like this, they bring others in the community that have worked in the past on loss adjustment or have been farmers themselves, or farm managers. They bring them on to help to bring their numbers up and they get it done. Rarely do I hear, even 2008, do I hear concerns that it has taken too long to get a claim paid.

There is some concern that the audits that have to go on on some of these claims, that has been voiced in the past. What I do to address that is I do what I can to inform farmers that this whole program is predicated on you having records to support your yields; please make sure you have those together, and that way the audit will go quicker in the event that the grower is chosen. So I think overall the industry is well geared up to address these across the nation. I think things will go smoothly, as they have in the past.

**Rep. Schmidt:** Thank you. And along the same lines, I understand that risk sharing between the USDA and the private insurance companies is spelled out in the standard reinsurance agreement. However, can you please give a general explanation of the risks borne by the government and those borne by the insurance companies? And do you think the current arrangement is an appropriate balance of risk sharing?

**Mr. Murphy:** Yeah, I can do my best. We take a look at, of course with the lower the loss ratio the year, the lower the claims, the more the companies assume the risk. The higher it gets, the more the government assumes the risk. That's why the government is involved in this program. If there wasn't a need, we would not be here; the industry would be able to handle the problem. They're concerned such a systemic loss would occur in the Midwest and the High Plains that they would not be able to address it. That's why we're here.

So that's where we put the majority of our protection on, is the higher levels, once you get above a dollar twenty loss ratio, where we're paying out a dollar twenty for every dollar we get in. What we've seen over the last ten years, the companies have been picking up most of those losses because it's been very good loss ratios nationwide. It's a very complex formula in the program, but I think generally, the higher the loss ratio is, the more the government assumes, the more risk the government assumes.

I think it's also important that the private reinsurance market worldwide participates in this program by taking some of that residual risk after it passes through the SRA, so we actually have some of that being sent off into the worldwide international market.

**Rep. Schmidt:** Thank you. And for several crops, while a larger percentage of planted acres are insured, they're insured at a minimum [cad] or buy-up coverage levels. Cotton and rice are good examples of this. What can be done to increase coverage for these crops?

**Mr. Murphy:** I think especially if you look at geographical areas, that's where you see the lower amount of coverage. Rice growers, especially in the Central South, they have wells to get their water, so they're always going to be able to get water, so it's a perception of risk. Their big concern is hurricane or diseases that comes through, and how often does that occur. It's all on perception of risk.

I think it's just continuing working with the growers, what we can do. We've not always had high participation in corn, soybeans and what. It's only by making changes to the program, insuring that the program addresses their risks that they have to deal with that we've seen the participation increase. I think it's the same with these other crops, it's just constantly working with them.

**Rep. Schmidt:** Thank you, and one final, and this is more personal view. Some of the critics back home that are fiscal hawks think that all of this is nonsense and it is not needed. How would you address that?

**Mr. Murphy:** I think this year is an excellent example of how important the farm safety net is to farmers out there. Food security is a priority with this country. I would say all these programs are extremely important. Now, I agree the cost of government has gotten high; I think everybody does. And we're looking for ways to become efficient and ways to reduce the costs to taxpayers. But the farm safety net is critical, and I'd hate to be put in a position where we do not have these programs available and there would be widespread losses across the country.

**Rep. Schmidt:** Excellent answer. Thank you.

**Chairman Conaway:** Thank the gentle lady. Bill, on the statutory loss ratio is one, I guess, which would mean we'd lose a dollar for every dollar of premium we put in. Right now ten year average 83 cents on every dollar. If we pushed that 83 cents up to a dollar, do you think that would increase by…would that have an impact on participation, get other people into the program by lowering the costs, or how do we…?

**Mr. Murphy:** You mean if you get into, like, a subsidy itself?

**Chairman Conaway:** I guess [lower] the premium down to that 83 cent number.

**Mr. Murphy:** Yeah, I think once you get under…our target loss ratio now, over time, is a dollar. Once you start getting below that as your target, it starts getting very complex.

**Chairman Conaway:** How do you push it, up, how do you get to that dollar and increase participation?

**Mr. Murphy:** There's a number of different ways. Participation, working with the rate itself. Now, we also have a reserve in there, okay, because the law requires we keep a reserve. So even though the 83 cents is there, that means we have a 20 cent reserve for future years.

**Chairman Conaway:** Well, let me ask if the – yeah, I get that, because you're going to have a year like two years ago when it was a buck forty. If your loss ratio was closer to the dollar, would you have greater participation in the program because the premiums would be lower?

**Mr. Murphy:** Yeah, I think generally you can say that. But again, you have to look at the length of time you're looking at to do that analysis. When we do rate-making, we actually use about 30, 35 years of data.

**Chairman Conaway:** Okay. And the reserve is pegged at what?

**Mr. Murphy:** The reserve is just required by statute that we have so much money held—

**Chairman Conaway:** How much? How much, is that per…?

**Mr. Murphy:** It doesn't actually say in the law. We try to stay around 10 to 20%.

**Chairman Conaway:** Of premium?

**Mr. Murphy:** Of reserve in there, yeah. That means you want to be around 90 cent loss ratio. Once you start getting up above 90, then we'd be concerned that we had the correct.

**Chairman Conaway:** All right. You never, ever hardly hear about actual production histories, I bet.

**Mr. Murphy:** [*Laughs.*]

**Chairman Conaway:** What are you doing to try to…given how long it takes those to move and the impact that it has, and the continued droughts in our part of the world pushing those down, what's on the table?

**Mr. Murphy:** Okay, we're doing a number of different things. We're taking a look at the rating itself and how we weight the years. Like I said, we use 30 years of data to rate the program. There's been a big issue we've had, especially with soybean and corn growers, is how you rate those individual years. I think we all are now on the same page. That's probably the most recent years need to be weighted more than the earlier years.

We're working in that direction. We're to adjust the yield drag on individual yields. If I'm a corner grower in Illinois, ten years ago my yield and my APH, is that really relative to what my expectations are this year? We have movement going on in that, and hopefully growers will see some of that progress in 2012. So we're doing things like that to try to address it.

We're also working with growers, manufacturers, how we can incorporate some of this GPS technology to improve some of the efficiencies in the program. For instance, as a farmer is planting, why can that information not be sent directly to the agent and start populating the acreage reporting day? As I'm harvesting and I have a loss, why can't that data start populating a claims form for me? So it's looking at efficiencies like that in the program to make it a better product to farmers out there.

**Chairman Conaway:** Yeah, and this may sound a little self-serving. Earlier Mr. Scott made some unfounded, specious comments about some small university in Georgia. [Charleston State] has the data mining program. Do you know off the top of your head what value is pushed back to the taxpayer as a result of that work?

**Mr. Murphy:** Sure. We're looking at cost avoidance now, since the inception, of about $840 million.

**Chairman Conaway:** Versus a cost of?

**Mr. Murphy:** Probably $4 million a year, probably $40 at the most.

**Chairman Conaway:** I guess the point being that as we move into these austerity programs, I'm hopeful that programs that actually, you don't want to say money. You could say cost avoidance.

**Mr. Murphy:** Exactly.

**Chairman Conaway:** Exactly. Most the folks out there want to do it right, but there's a few that don't. And so as we trim your budget, so to speak, I'm hopeful that the data mining issue is one that we see value in. It won't score that way, necessarily, because of the way our complex rules work, but that data mining program, wherever it is, is fully exploited, not only in this part of the farm bill, but I suspect there's some applications in food stamps or SNAP and other programs in which that data mining concept could be used and exploited.

**Mr. Murphy:** Yes again.

**Chairman Conaway:** Mr. Boswell, you have any further questions?

**Ranking Member Boswell:** No further questions.

**Chairman Conaway:** Bill, thank you. This is one of those rare circumstances where we actually got the entire hearing done in a reasonable point of time, in spite of a vote. I've got some official words to read here somewhere. All right. We've already gone and asked the Ranking Member if he wanted to say anything. Under the rules of the committee, the record of today's hearing will remain open for ten calendar days to receive additional material and supplementary written responses. A couple of questions you answered that were asked from the witness to the question posed by a member. This hearing of the Subcommittee on General Farm Commodities and Risk Management is adjourned.

[*End of recording.*]