

**Testimony Before the U.S. House of Representatives Committee on Agriculture:
Subcommittee on General Farm Commodities and Risk Management
May 1, 2007**

Mr. Chairman, my name is Robert W. Parkerson. I serve as President of National Crop Insurance Services (NCIS), on whose behalf my testimony is presented today. I would like to thank the Subcommittee for the opportunity to present this testimony.

NATIONAL CROP INSURANCE SERVICES

NCIS is a not-for-profit trade association whose members include every crop insurance company that participates in the Federal crop insurance program. NCIS and its predecessor organizations have provided members support in their crop insurance businesses since 1915.

NCIS has worked actively with the Risk Management Agency (RMA) as an approved contractor and with the Board of the Federal Crop Insurance Corporation (FCIC) as an expert reviewer. We have received more than twenty risk management education grants or research awards over the last several years and have served as expert reviewers on fourteen projects.

NCIS is also a licensed advisory organization and statistical agent for private Crop-Hail insurance in forty-nine of the fifty states, and it assists the crop insurance industry in meeting the regulatory requirements of these states. This is accomplished by filing the appropriate policy forms and statistical information with state insurance departments. Further, NCIS serves as a liaison with individual state insurance departments through active participation with the National Association of Insurance Commissioners (NAIC).

In 2006, NCIS member companies wrote more than \$4.7 billion in Federal multiple peril crop insurance and related revenue products premium and over \$400 million in private Crop-Hail insurance products premium. The potential liability between both programs was approximately \$65 billion. NCIS member companies service policies that encompass all farmers participating in the federal and private programs, including limited resource and socially disadvantaged farmers. In partnership with the Federal government, our participating member companies comprise the safety net that equitably provides risk management to America's farmers.

Today, I want to emphasize three topics of great concern to private sector participants in the Federal crop insurance program – maintaining an economically sound program, enhancing program integrity, and funding RMA adequately. Discussion of these topics also will provide some private sector perspectives on the Administration's proposed 2007 Farm Bill.

MAINTAINING A SOUND PROGRAM

The Federal crop insurance program has reached a mature stage of development. Since 1980, when the public-private partnership for delivery of MPCCI coverage began, covered acreage has expanded dramatically, with twenty-one insurance plans now available covering approximately 80% of the acres for major program crops and equating to 70 – 85% of potential value of these crops.

Together, the private sector and FCIC have paid substantial indemnities to our agricultural producers when they have encountered bad years. In fact, the program's cumulative average loss

ratio for 1980 – 95 was 1.5, well in excess of the expected levels established in the Federal Crop Insurance Act. Substantial improvements in annual loss ratios over the last decade have had significant and positive financial and program integrity consequences, as discussed below.

Maintaining an economically viable crop insurance program requires that two objectives be achieved. First, when weather conditions are favorable, resulting in a lower than expected loss ratio, the private sector must be permitted to earn the profits that sustain its ability to make long-term commitments to the program. Second, there must be adequate and reasonably priced commercial reinsurance available in addition to the reinsurance provided through the FCIC's Standard Reinsurance Agreement (SRA).

Now that the program has achieved greater and improved actuarial soundness, an inevitable consequence of this improvement must be placed on the table and recognized as a positive development. Quite simply, the truth is that when actuarial soundness improves, the financial health of insurance providers and their reinsurers also improves.

Years with low national average loss ratios will produce significant profits. That is a very positive development for several reasons. Congress, the Administration, and the insurance companies should not be embarrassed by this reality. Program profitability enables existing program participants to build reserves to face the inevitable catastrophic losses that come with agriculture. We need to remember, for example, the widespread droughts of 1988 and 2002 and flooding of 1993, and have the resources to cope with such events. Although it is too early to predict what the losses will be in 2007, this year, unfortunately, is not starting out well – with

early season freeze damage in California, some Southern and Middle Atlantic areas, and parts of the Great Plains. If weather remains adverse, all of us will be grateful for reserves built in prior years.

Profitability also draws new entrants into the program. This, in turn, can benefit the program through different and broader perspectives and increasing the innovative drive of the recent past.

Profitability is also good for the government's fiscal interests. Profitability means that the burden on the taxpayer is reduced when America's farmers have fewer losses than expected. Improved actuarial soundness also is evidenced by the private sector's willingness to share greater risk under the SRAs negotiated in 1997 and 2004, and it also is manifested by their increased designation of policies to the Commercial Fund, where the private sector has a risk at least equal to, if not greater than, the government's risk.

I now want to turn to the importance of commercial reinsurance to the Federal crop insurance program. Although FCIC provides substantial support to the program through reinsurance available under the SRA, companies still remain exposed to substantial risks. Depending on the resources of individual companies, the availability of commercial reinsurance at adequate levels and reasonably priced rates is essential. Even our strongest members cannot individually sustain their multi-billion dollar portions of widespread losses. Thus, for them to survive, to remain profitable, and to be energetic participants in the Federal crop insurance program, they must be able to transfer a portion of their risks to commercial reinsurers. Commercial reinsurers will not accept these risks if profit margins are too thin. Quite simply, they have other alternatives for

investing their capital. We should not, we cannot, drive commercial reinsurers from the program.

Having noted the importance of commercial reinsurance, I now must offer some concerns about the Administration's proposed Farm Bill. The proposal drastically would reduce the potential profitability of the program. For instance, there is now a 5% premium paid to FCIC under the SRA for quota share reinsurance. The Administration proposes increasing this to 22%. That type of profit erosion, quite frankly, is draconian and will result in driving commercial reinsurers from the crop insurance market. The Administration also proposes a two percentage point reduction in administrative and operating subsidy. As it is now, the A&O subsidy has been steadily declining over the last decade. Reducing the subsidy, while simultaneously increasing quota share costs by 440%, invites serious and adverse consequences.

ENHANCING PROGRAM INTEGRITY

When discussing improved actuarial soundness, I noted that there are resulting program integrity consequences. First, the profits associated with lower loss ratios provide resources which permit improving internal controls as part of promoting program integrity. Second, reduced loss ratios also are a positive sign that RMA has improved its program management. To illustrate, we have not witnessed since 2000 any broad-based criticism by USDA's Office of Inspector General of RMA's development of costly and inappropriate coverages.

Comments on loss ratios bring me to a beneficial proposal in the Administration's 2007 Farm Bill. It proposes reducing the expected loss ratio from 1.075 to 1.0. That may seem like a minor

change, but it could have major significance for improving program integrity as well as actuarial soundness. Tightening down the expected loss ratio sends a significant signal that we do not want to invite losses through inadequately developed coverages.

We believe that the Federal crop insurance program operates with a high degree of integrity. Yet, with taxpayers' dollars and the private sector's resources at risk, vigilance is required. To this end, NCIS last year held its first annual Program Integrity Conference. That conference centered on the crop insurance industry's ability to reduce fraud, waste, and abuse and how best to handle these issues in a growing and complex program. Senator Pat Roberts, RMA Administrator Eldon Gould, and Bert Little of Tarleton State University were key speakers at this conference. Over 100 people from the crop insurance industry attended this day and a half event. Representatives from the RMA, NAIC, OIG, FBI, International Center for Ethics in Business, NCIS, and crop insurance companies spoke on various issues dealing with fraud, waste, and abuse.

Our second annual Program Integrity Conference will be held on May 21 – 22, 2007, in Overland Park, Kansas. Like last year's program, this conference will focus on reducing fraud, waste, and abuse. Many of the same organizations who contributed to last year's program will be participants this year. Key speakers will be Congressman Jerry Moran from this Committee, as well RMA Administrator Eldon Gould.

For those of us working in the crop insurance industry, our livelihoods depend on the integrity of this program. Without it farmers would not have the safety net they so richly deserve. Without it

the crop insurance industry would be smaller and fewer in number. We have all worked too hard and achieved too much to allow the slightest erosion of integrity to cause the downfall of this program.

As part of improving program integrity, we want to urge Congress to adopt the Administration's proposal in its version of the 2007 Farm Bill giving companies direct access to the data mining efforts that have been underway since passage of the Agricultural Risk Protection Act of 2000. It is fine to gather data and to analyze it. That does not complete the process, however, as the results of data mining efforts need to be provided directly to each company participating in the program. Doing so will permit each company to work proactively on improving compliance by its agents and loss adjusters. In short, for data mining to have real utility in reducing losses, the private sector needs direct and faster access to data mining results. We are pleased that the proposed Farm Bill addresses this issue.

ENHANCING RMA RESOURCES

The private sector can only do so much through its own efforts to improve the integrity of the Federal crop insurance program. Please let me outline several steps which Congress can take to enhance RMA's resources beyond those proposed in the 2007 Farm Bill.

First, Congress should provide RMA with an adequate budget to match the data processing systems utilized by the private sector. RMA needs its own thoroughly modern data processing system that interfaces with the private sector's state of the art systems. This goes beyond data mining and relates to fundamental day-to-day business operations. We absolutely never should

encounter a situation where farmers who have suffered legitimate losses covered by their MPCI policies cannot be paid promptly because of inadequacies in the data processing system of RMA. We have come to the brink on this issue in the past, but fortunately not encountered any disaster. RMA should have a state of the art data processing system to match the companies' systems so that policyholders' claims are processed and paid promptly.

Second, Congress needs to provide RMA with ample funding to participate as an equal partner in the risk management training and education programs that the private sector sponsors. For example, we at NCIS sponsor annually various national conferences on program issues, and we also sponsor schools to train loss adjusters. We average conducting twenty to twenty-five such schools and conferences annually. Our national conferences are well attended by both company representatives and RMA personnel, who often make major presentations. Loss adjustment schools are well attended by company personnel, and they are taught by our industry's most experienced adjusters. Over the past few years, we routinely have had insightful RMA participation. An adequate operating budget for RMA to send its experts in different crops to our conferences and schools is essential. When actively participating in our industry sponsored programs, RMA offers valuable contributions.

The private sector firmly believes that educational efforts can be key deterrents to fraud, waste, and abuse. The Federal crop insurance program is complex, and improving understanding of its terms and operation should help limit fraud, waste, and abuse. Everyone involved—our policyholders, agents, adjusters, RMA personnel, and company employees—all need to understand the program and recognize that their individual actions affect the integrity of the

entire crop insurance program. On a whole, agents who sell crop insurance and loss adjusters who determine the amount of indemnities payable are honest and dedicated professionals. As a result of their dedication, America's farmers can be assured that program options will be accurately explained to them at time of purchase, and that losses will be adjusted fairly and accurately in the event of damage. Moreover, through proper education, company employees, agents, and adjusters are becoming better equipped to recognize behavior outside the bounds of program compliance. Knowing this encourages policyholders to behave in an ethical manner. The benefits of effective training are that errors can be avoided, that uniformity in adjusting losses can be increased, thus leading to higher confidence in the program, and that there will be appropriate discipline in those rare instances of intentional wrongdoing. Achieving these benefits can be improved by greater RMA participation in our loss adjustment schools. It simply is "penny wise, but pound foolish" to deny RMA the economic resources to participate at a greater level than it now can.

CONCLUDING POINTS

NCIS is in regular contact with Mr. Gould and his staff and we have worked diligently together to resolve issues as they arise in the program. Some of these have dealt directly with program vulnerabilities that, if not corrected, could lead to program abuse. Even though this process has been successful, there are still some issues to be resolved. Certain review processes still take a random approach towards discovering program vulnerabilities. We want to sit down with RMA and follow up on discussions of processes and methods that would allow us all to all "work smarter."

Crop insurance is an effective risk management tool for growers to protect themselves. Growers must have confidence in the stability of the program and purchase adequate coverage. As an industry we take seriously our responsibility to deliver the federal crop insurance program with integrity and fairness, and we have a long history of being proactive in addressing issues of fraud, waste, and abuse. We shall continue to be proactive. We realize the 2007 Farm Bill is a work in process. We remain available to answer questions and to provide comments as your work continues.