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Disaster Assistance and Crop Insurance: Time for a New Approach?

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Congress has once again passed a disaster assistance program for farmers. This time the drought of 2001 and 2002 was the rationale for the legislation. (For a review of the build-up to the current disaster aid package, see “Disaster Assistance: How Best to Pay When Nature Has Her Way,” in the Fall 2002 Iowa Ag Review, available at www.card.iastate.edu/iowa_ag_review/fall_02/article4.html.) In 1998, 1999, 2000, and 2001, the rationale was low market prices. The current disaster assistance program pays crop farmers if their harvested yield was less than 65 percent of the average yield. The cost of the crop assistance package is estimated at about $2.1 billion. While this might seem relatively modest, it is important to recognize that the crop insurance program will pay out more than $4 billion in 2002, and it paid out almost $3 billion in 2001.

What is it about the crop insurance program that makes it an inadequate assistance tool? After all, Congress passed the Agricultural Risk Protection Act (ARPA) in 2000 to better enable farmers to withstand financial downturns. Did ARPA have its intended effects?

Crop insurance works by making up the difference between harvested yield (for traditional Multiple Peril Crop Insurance) or harvested yield times market price (for revenue insurance) and a farmer’s chosen in-
The combination of a federal disaster program and privatized crop insurance is workable. The federal disaster program would cover widespread agricultural disasters. These disasters are what prevent privatized crop insurance from working today. A single agricultural disaster would wipe out most private companies. With a federal disaster program in place, private crop insurance would provide coverage that would pay any losses that exceed the federal payment. Farmers would decide if the federal protection was adequate for their needs or whether the additional private coverage was worth the cost, which they would pay in full.

The current crop insurance program costs roughly $3 billion per year. A federal disaster program could pay farmers when county revenue falls below a certain percentage of average county revenue for a crop within a year. We estimate that the cost of this program at a 95 percent payment trigger level would average $2.65 billion per year. The federal program could be designed to cover losses at the state or crop-reporting district level, which would lower costs, or it could provide coverage for yield losses. With a stable federal program in place, private insurers could determine adequate insurance rates, and producers would have plenty of opportunities to address their risk management needs.