

AGR-Lite: An Option for Montana Producers

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Adjusted Gross Revenue-Lite (AGR-Lite) is a whole farm revenue insurance product. The product is available in all Montana counties in 2009 and has a common sign-up date of March 15. AGR-Lite may be used as a stand-alone product or in conjunction with other federally subsidized crop-specific group or APH-based insurance products. When AGR-Lite is used in combination with other crop insurance products, a producer's AGR-Lite premium is reduced.

AGR-Lite is likely to be of more interest to producers who market all or most of their crops and forages than to producers who use a considerable portion of their crops and forages to feed their own livestock. The reason is that AGR-Lite insures a farm or ranch's gross revenues from market sales but does not provide coverage for production or quality losses associated with adverse growing conditions for forages and crops such as feed barley that are used by producers as feed in their own livestock operations.

Producer Eligibility

As its name suggests, AGR-Lite is not intended for farms with very large gross revenues.

To be eligible for AGR-Lite, a producer must satisfy the following criteria:

- Be a U.S. citizen or permanent resident;
- File a calendar year or fiscal year income tax return;
- Have a liability (maximum indemnity) of no more than \$1 million

- Have had the same tax entity for the previous 7 years (with 5 consecutive years of Schedule F or comparable tax forms, and a tax form for the insurance year) unless a change in the tax entity has been approved by the insurer;
- Have no more than 50percent of total revenue from commodities purchased for resale;
- Have no more than 83.35percent of total revenue from the sale of potatoes.

Seven consecutive years of tax forms for the same tax entity are required because producers are required to provide five consecutive years of information on Schedule F (or comparable tax form) revenues and expenditures to establish the gross revenue liability to be covered for their farm or ranch. The other two years are the earliest year, which is required to establish the insured entity's existence, and the tax form for the current year covered by the insurance contract.

AGR-Lite Basic Principles

A five year average gross revenue or ***total expected income*** for a producer's farm or ranch is established using information from a producer's IRS tax returns and an annual report for the insurance year on a farm or ranch's operations (acres planted to each crop, numbers of livestock, etc.). Farms and ranches with annual adjusted gross incomes that are increasing may be allowed to use indexing procedures to obtain ***total expected incomes*** that reflect that fact.¹ The producer selects a ***coverage level*** of 65 percent, 75 percent, or 80 percent. The operation's ***total expected income*** is multiplied by the

¹ Details of these indexing procedures are provided in the following publication by James Johnson, John Hewlett and Duane Griffith; *Adjusted Gross Revenue Lite: A Whole Farm Revenue Insurance Available in Wyoming*, Montana State University Agricultural Marketing Policy Paper No 24, February 2008.

coverage level to determine the **trigger revenue** level (or loss inception point) at which payments for losses will be triggered. If the operation's revenue in the current year falls below its **trigger revenue** then the farmer receives a payment for loss. The amount of the indemnity payment equals the **payment rate**, selected by the producer, multiplied by the amount of the insured loss (the difference between the operation's **trigger revenue** and its current year revenue). A producer may select either a 75 percent or a 90 percent payment rate. The **maximum indemnity** (the amount of the indemnity a producer receives if he no gross revenue), which is also the **liability** incurred by the insurer under the AGR-Lite contract, therefore equals the **trigger revenue x coverage level x payment rate**.

Constraints on Coverage Levels

Producers who select the 65 percent or 75 percent coverage levels are only required to have at least one commodity which makes a significant contribution to the operation's income. Producers who select the 80 percent coverage level must have a minimum of three commodities that make a significant contribution to the operation's **total expected income** for the insurance year. The definition of a significant contribution is as follows: the amount a commodity is expected to contribute to the operation's income must be at least equal to $(1/\text{number of commodities in the farm annual report for the insurance year}) \times 1/3 \times \text{total expected income}$. For example, suppose that a farm identifies four commodities in its annual farm report that contribute to a **total expected income** of \$600,000. For this farm, a significant contribution is therefore $1/4 \times 1/3 \times \$600,000 = \$50,000$. To be eligible for the 80 percent coverage level, this farm must have three commodities that are expected to contribute at least \$50,000 to total farm income.

A second constraint on coverage level choices derives from the requirement that a producer's maximum indemnity or liability cannot exceed \$1 million. Higher coverage level and payment rate combinations therefore reduce the maximum amount of *total expected income* that a farm can have and remain eligible for AGR-Lite insurance.

Table 1 shows the minimum numbers of commodities and maximum amounts of total expected income that are eligible for AGR-Lite insurance under each available combination of coverage levels and payment rates.

Table 1: Coverage levels, Payment Rates, Minimum Numbers of Commodities and Maximum Total Expected Income

Coverage level (percent)	Payment Rate (percent)	Minimum Number of Commodities	Maximum Total Expected Income
65	75	1	\$2,051,282
65	90	1	\$1,709,401
75	75	1	\$1,777,777
75	90	1	\$1,481,481
80	75	3	\$1,666,666
80	90	3	\$1,388,888

Premiums and Premium Subsidies

Premium rates for AGR-Lite are established by RMA and differ by coverage level, payment rate, diversification factors based on the number of commodities contributing to a producer's approved *expected total revenue*, and by RMA rating region. As with other RMA products, a *total premium* amount, a *subsidy* amount, and a *producer premium* amount are identified for each insurance contract. A producer pays the *producer premium* for the coverage liability obtained for the operation. The *subsidy* amount is paid by the federal government and is based on a *subsidy rate* that depends on the producer's choice of coverage level. The *total premium*, *subsidy* amount, and *producer*

premium are determined by the producer's *liability* (or *maximum indemnity*), the *premium rate*, and the *subsidy rate* as follows;

$$\begin{aligned} \text{total premium} &= \text{liability} \times \text{premium rate} \\ \text{subsidy} &= \text{total premium} \times \text{subsidy rate} \\ \text{producer premium} &= \text{total premium} - \text{subsidy} \end{aligned}$$

Premium subsidy rates vary by coverage level as follows:

Coverage level	Subsidy Rate
65%	59%
75%	55%
80%	48%

For example, suppose a farm with an *expected total revenue* of \$600,000 selects a 75 percent coverage level and a 90 percent payment rate. The farm's maximum indemnity or *liability* is therefore $0.75 \times 0.90 \times \$600,000 = \$405,000$. In addition, suppose that the applicable *premium rate* is 4 percent. The farm is eligible for a 55 percent premium *subsidy rate* because the producer has selected a 75 percent *coverage level*. Then, for this farm,

$$\begin{aligned} \text{total premium} &= \text{liability} \times \text{premium rate} &= \$405,000 \times 0.04 &= \$16,200 \\ \text{subsidy} &= \text{total premium} \times \text{subsidy rate} &= \$16,200 \times 0.55 &= \$8,910 \\ \text{producer premium} &= \text{total premium} - \text{subsidy} &= \$16,200 - \$8,910 &= \$7,290 \end{aligned}$$

Losses and Indemnities

Indemnity payments are made when losses occur because of insured causes. Insured causes include any unavoidable natural occurrences during the current or previous insurance year and/or market fluctuations that cause a loss of revenue in the current insurance year. No payments will be made for losses due to negligence, mismanagement or wrong-doing by the producer, the producer's family, members of the household,

tenants, employees, or contractors; crop abandonment; bypassing of acreage; or other uninsurable causes listed in the insurance policy.

Indemnities are paid when a farm's **revenue to count** as adjusted gross income for the insurance period is less than the farm's **trigger revenue**. The indemnity is equal to the difference between the farm's **trigger revenue** and its **revenue to count** multiplied by the **payment rate** selected by the producer. For example, suppose the above example farm with a **trigger revenue** of \$405,000 and a payment rate of 90 percent has a **revenue to count** of \$305,000. The farm will receive an indemnity because its revenue to count is less than its trigger revenue. The amount of the indemnity payment is:

$$\begin{aligned}\text{indemnity payment} &= (\text{trigger revenue} - \text{revenue to count}) \times \text{payment rate} \\ &= (\$405,000 - \$305,000) \times 0.9 = \$90,000\end{aligned}$$

A farm's **revenue to count** includes income from the sale of covered commodities (as reported on its IRS Schedule F or comparable tax form for the insurance period), crop insurance indemnities, non-insured crop disaster assistance program payments, income lost due to non-insured causes, net gains from hedging, and changes in balances of accounts receivable and inventories of agricultural commodities held for sale. It does not include payments received by a farm or ranch in the form of federal Counter-Cyclical Program Payments, Direct Program Payments, or ACRE Program Payments.

Summary

AGR-Lite is a whole farm insurance program available in all Montana counties for 2009. It can be used as a stand-alone insurance product or in conjunction with other federally

subsidized insurance products. One feature of AGR-Lite is that farms that use this product satisfy the Farm Service Agency requirements for participation in the new Supplemental Revenue Assistance (SURE) program in 2009. The SURE program is a standing disaster relief program established under the provisions of the recent 2008 Farm Bill. AGR-Lite is likely to be of most interest for operations that market all or most of the commodities they produce. Production or quality losses associated with commodities used on the farm such as forage and feed grains are not covered by this product.