

An Adjusted Gross Revenue (AGR-Lite) Insurance Case Study

**For
Grape Farm
Western New York
Prepared by G. White and
B. Shaffer
January 2005**

Description of farm

Mid-size grape farm

Increasing acreage from 60 bearing acres in 1998 to 87 bearing acres in 2006.

Growth from buying existing Concords and plantings of Niagara and hybrids.

Custom work has accounted for \$12,000 to \$33,000 over the last five years. (However this is not included in allowable income, which must be "income directly related to the production of agricultural commodities")

Marketing Plan

- ❑ Diversified cash market producer
- ❑ Increasing percentage of income coming from Niagara proceeds
- ❑ Weaning away from one cooperative that is experiencing financial difficulties. No coop distributions in 2003 or 2004. Now sells to four cash market processors.

Insurance history

- ❑ Yields per acre
 - 2004 7.1 t/ac
 - 2003 5.9 t/ac
 - 2002 6.4 t/ac
 - 2001 7.0 t/ac
 - 2000 5.6 t/ac
 - Average yield, '00-'04=6.4 t/ac
- ❑ He only had one MPCCI claim for 1998, receiving the payment in early 1999. Another claim in 2003, receiving payment in 2004.

Risk management practices

- ❑ He carried MPCl at varying levels depending on the year in the late '90's. He has been dissatisfied with MPCl, and is considering AGR-Lite so that he does not have to buy MPCl (as is required under regular AGR).
- ❑ He uses drip irrigation on much of his Niagara acreage for both increasing tonnage and reducing crop size variability.
- ❑ He has used mechanical crop thinning, especially on his machine-pruned blocks.

Revenue from the sale of ag commodities

Allowable income over the past five years:

- | | |
|--------|-----------|
| ❑ 2000 | \$95,288 |
| ❑ 2001 | \$106,940 |
| ❑ 2002 | \$141,456 |
| ❑ 2003 | \$83,573 |
| ❑ 2004 | \$116,826 |
- ❑ Allowable income was exceptionally low in 2003 due to a combination of low prices, lower brix, and lower yields than normal.
 - ❑ Yields recovered in 2004 (7.1 tns/ac.), although the price was low.

Eligibility

- To be eligible for AGR-Lite coverage, the farm must meet the following criteria:
- Have five consecutive years of Schedule F 1040 tax records, or equivalent tax forms
- Not more than 50 % of allowable income for ag commodities purchased for resale
- This farm meets all these criteria

Application

- To apply for coverage, the operator needs to prepare form USDA FCIC Actual Commodity Report for the insurance year 2006 (incl. commodity profiles for 2004 and 2005)
- He also needs to complete USDA FCIC AGR-Lite Histories for tax years 2000-2004
- Prior to Jan. 31 (March 15 for new policies), he needs to file his beginning inventory for insurance year 2006, including crops in storage and accounts payable and receivable

INTENDED COMMODITY REPORT FOR 2006

Crop or Commodity Name	Code	Amount (Acres, # head, area, etc)	Expected Yield or Quantity Produced		Value (Price Per Unit)	Total Value	
			#	Unit			
Juice grapes	891	83	8.0	tons	\$ 200.00	\$ 132,800	
Hybrid grapes	890	4	4.0	tons	\$ 600.00	\$ 9,600	
Total Number Commodities					2	Total Expected Income	\$142,400

Summary of AGR-Lite History - Income

- 5-Yr Total Adjusted AGR \$544,083
- AGR Index Factor 1.366
- Indexed preliminary AGR \$148,644
- Total expected income \$142,400
- The approved AGR becomes the smallest of the two; thus the approved AGR is \$142,400.
- The RMA Premium Calculator web-site will determine all this for you.

What income items do not count as allowable income?

- ❑ Market Loss Assistance payments
- ❑ Disaster payments
- ❑ Crop insurance proceeds
- ❑ Land or machinery rent, custom operations, storage rental, etc.
- ❑ Revenue from post production activities (packing, packaging, packaging materials, transportation to market (beyond local markets)) must be deducted from the value added gross income. Not usually applicable for grape farms unless they use direct marketing or have a winery

Summary of AGR-Lite History - Expenses

- ❑ Five year total expenses \$362,801
- ❑ Five year average expenses \$72,560
- ❑ Indexed allowable expenses \$110,219
- ❑ Why are expenses relevant to AGR-Lite?
- ❑ If your allowable expenses for the insurable year fall below 70 percent of your approved expenses, indemnity payments will be reduced. Must show that you are using "good agricultural practices" to bring in the crop.

What expenses are not allowable?

- Non-animal depreciation
 - Employee benefit programs other than line 25
 - Mortgage interest paid
 - Other Interest
 - Pension and profit share plans
 - Rent or Leases on vehicles machinery and equipment
 - Other rent (land, animal, etc.)
 - Taxes and other non-allowed expenses
- Thus, expenses not directly related to growing the crop are not allowable

Policy size limit: **max of \$1.0 M** liability coverage

Coverage level/pmt	Max. annual income
<input type="checkbox"/> 65/75	\$2,051,282
<input type="checkbox"/> 65/90	\$1,709,401
<input type="checkbox"/> 75/75	\$1,777,777
<input type="checkbox"/> 75/90	\$1,481,481
<input type="checkbox"/> 80/75	\$1,666,666
<input type="checkbox"/> 80/90	\$1,388,888

Since this farm falls below these income levels, it is not restricted, based on income, from higher levels of coverage. However, based on number of crops-----

Available coverage (illustrates the value of diversification)

Coverage level/pmt rate:	Number of commodities:
65/75	All eligible producers
65/90	All eligible producers
75/75	All eligible producers
75/90	All eligible producers
75/65	Discontinued
80/75	Three or more
80/90	Three or more

Coverage level for Grape Farms

- ❑ Could a grape farm have more than one commodity?
- ❑ Yes, in western New York, the commodity list includes FOUR types of grapes—grapes (hybrid), grapes (juice), grapes (Labrusca), grapes (vinifera).
- ❑ Thus a grape farm could theoretically qualify for four commodities—however each must be projected to generate 11.1 % of the gross revenue shown on the intended commodity report.
- ❑ For this farm, there are only two commodities listed (see next slide). Thus the case study farm cannot qualify for three commodities.

INTENDED COMMODITY REPORT FOR 2006

Crop or Commodity Name	Code	Amount (Acres, # head, area, etc)	Expected Yield	Value	Total Value
			or Quantity Produced # <u>Unit</u>	(Price Per Unit)	
Juice grapes	891	83	8.0 tons	\$ 200.00	\$ 132,800
Hybrid grapes	890	4	4.0 tons	\$ 600.00	\$ 9,600
Total Number Commodities		2	Total Expected Income		\$142,400

Coverage level for Grape Farms

This farm can choose from four policies:

- 65% Coverage level/75 % payment rate for a producer premium of \$1,025;
- 65% Coverage level/90% payment rate for a producer premium of \$1,230
- 75% coverage level/75% payment rate for a producer premium of \$2,019;
- 75% coverage level/90% payment rate for a producer premium of \$2,422

Let's assume he chooses the highest level of Coverage available to him, 75%/90%.

Differences between AGR and AGR-Lite

- ❑ Copies of tax forms are not required at time of application for AGR-Lite (producers can gather numbers and certify their accuracy). For AGR, tax forms are required up front.
- ❑ No limitation on the percentage amount of receipts from animals or animal products for AGR-Lite (maximum of 35% for AGR).
- ✓ The purchase of individual crop insurance policies is the producers' option for AGR-Lite (mandatory for AGR if 50 % of your allowable income for the insurance year is derived from a combination of the production of crops for which individual insurance policies are offered)
- ❑ Historical by commodity information 2 years for AGR-Lite (5 years for AGR)

Differences (con't)

- ❑ Maximum policy liability is \$1.0 Million (up to \$2.05 Million of gross revenue @ 65/75% and \$1.39 Million @ 80/90% coverage) for AGR-Lite (\$6.5 Million for AGR).
- ❑ Commodities with small revenues can be grouped to determine diversification credits for AGR-Lite (not allowed for AGR).
- ❑ Additional clarification on organic farming practices for AGR-Lite (not clarified in AGR policy).

Loss Scenario

- ❑ Grape Farm's yields in '06 fell to 5 tons per acre for juice grapes, and 2 tons per acre for hybrid grapes due to frost damage.
- ❑ Washington State had a large grape crop in '06, and national inventories were high coming into the harvest season. The Price for juice grapes fell to \$175 per ton.
- ❑ Grape Farm's "revenue to count" for '05 was \$76,225.

Inventories, accounts payable, accounts receivable , and prepaid expenses as of Jan. 1, 2006 and Dec. 31, 2006

- | | |
|-----------------------|-------------------|
| ❑ Fruit in inventory | \$0 / \$0 |
| ❑ Accounts Receivable | \$35,000/\$30,000 |
| ❑ Accounts Payable | \$12,000/\$14,000 |
- ❑ Inventories (as of January 1, 2006) must be provided by 31 January 2006 (March 15 for new policies)
 - ❑ A written notice is required to be filed in your agent's office within 72 hours of discovery that your allowable income may be less than the revenue guarantee of the policy.
 - ❑ In the event of a claim, the producer should have detailed lists of fruit in inventory and accounts receivable (listed by buyers—including those from 2 years ago, if they are still outstanding) for January 1, 2006 and December 31, 2006.

Information needed to determine possible claim situation (about March 2007):

- 1) 2006 Schedule F or related Tax Form
- 2) 2006 Beginning and Ending Inventory
- 3) 2006 Beginning and Ending Accounts Receivables
- 4) Determine the amount of added value to deduct from the 2006 Tax Forms
- 5) Need Schedule of Insurance to determine your guaranteed gross revenue
- 6) Need to compare 2006 allowable expenses with 5-year history (70% rule)
- 7) Determine if the grower received any NAP payments or Crop Insurance indemnities that were due to the insured year

Premium

<input type="checkbox"/> Total premium	\$5,383
<input type="checkbox"/> Subsidy	\$2,961
<input type="checkbox"/> Total cost to producer	\$2,422
<input type="checkbox"/> Coverage	\$96,120

for:

Coverage level @ 75 %/ Pmt. rate @ 90 %
and an approved AGR of \$142,400

Determining Loss and Indemnity

- ❑ Approved AGR of \$142,400 X 75% coverage level=\$106,800
- ❑ => "loss trigger"
- ❑ \$106,800 (-) \$76,225 revenue to count=\$30,575
- ❑ Factoring the decreases in account receivable (\$5,000) and decreases in fruit in inventory (\$0), the adjusted loss becomes \$35,575
- ❑ \$35,575 X the 90 % payment rate=\$32,018
- ❑ Accrual adjusted income was \$76,225-\$5,000 decrease in accounts receivable, or \$71,225

Summary of income scenario

❑ Approved AGR	\$142,400
❑ '05 Income without insurance	\$71,225
(Accrual basis-adjusted for decr. in accts receivable)	
❑ Indemnity payment	\$32,018
❑ Income with 75/90 policy	\$103,243
❑ Producer premium	\$2,422
❑ Producer benefit/cost ratio	\$13.22
(Indemnity payment/producer prem.)	