Supplemental Coverage Option (SCO) and Crop Insurance Changes in the 2018 Farm Bill

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Crop insurance in the 2018 Farm Bill

- Policy makers protected crop insurance
  - While discussed, no income limits or payment limits were applied to crop insurance
  - Retained the Harvest Price Option (HPO) that provides yield replacement coverage

- Enterprise units are now allowed across county lines

- May increase the use of cover crops in some areas due to how cover crops are counted

- Requires RMA to consider expanding availability of limited irrigation crop insurance but doesn’t require it

- Dual-use option: can insure both grazing and grain on small grains in some areas
Where does SCO fit in?

Elect a Program

- **PRICE LOSS COVERAGE (PLC)**
- **AGRICULTURAL RISK COVERAGE - County Level - (ARC-CO)**
- **AGRICULTURAL RISK COVERAGE - Individual Level - (ARC-IC)**
- **Supplemental Coverage Option (SCO)**

Purchased on Planted Acres

<table>
<thead>
<tr>
<th>Commodity</th>
<th>Share of KS crop base acres enrolled in PLC under 2014 Farm Bill</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wheat</td>
<td>26%</td>
</tr>
<tr>
<td>Grain sorghum</td>
<td>56%</td>
</tr>
<tr>
<td>Corn</td>
<td>14%</td>
</tr>
<tr>
<td>Soybeans</td>
<td>12%</td>
</tr>
</tbody>
</table>

What is SCO?

- **A relatively new risk management tool**
  - Created under the Agricultural Act of 2014
  - Provides higher coverage level with a county-based trigger
  - Not available if you enrolled in ARC

- **A crop insurance product**
  - Charges a premium, rates reflect expected payouts
  - Indemnities paid when loss criteria satisfied (county-based revenue or yield loss)
  - Sold through local crop insurance agents
  - Backed by USDA’s Risk Management Agency
  - Must sign up prior to planting
What is SCO’s purpose?

- To provide *additional protection* on top of your individual crop insurance policy

- Intended to provide *similar coverage to ARC* (86% to 76% band) for producers enrolled in PLC

- *SCO range*: brings coverage up to 86% of average revenue/yield

SCO brings the guarantee level up to 86%
SCO combines with your regular crop insurance

- Must have an “underlying” crop insurance policy; **SCO is an endorsement to your underlying policy**

- Underlying policy can be Revenue Protection, RP with harvest price exclusion, or Yield Protection (no area plans)

- SCO policy will use **same coverage criteria** (yield or revenue) as your underlying policy

Types of SCO coverage

- **Revenue version**: based on county revenue
  - Expected county revenue = expected county average yield \( \times \) crop insurance price*
  - **Payment trigger**: actual county revenue \(<\) 86% of expected county revenue

- **Yield version**: based on county yield
  - Payment triggered when actual county yield falls below 86% of expected average county yield

- **Crop insurance price**
  - For underlying RP policies, the SCO crop insurance price will be the **higher of** the **Projected Price** (price at insurance sign-up, prior to planting) and the **Harvest Price**
  - For underlying YP and RP-HPE policies, the SCO crop insurance price will be the **Projected Price**
Calculating dollar coverage under SCO (revenue version)

**SCO $ liability** = \( \text{Expected farm revenue} \times \text{SCO range of coverage} \)

- **Expected farm revenue** = \( \text{farm APH yield} \times \text{crop insurance price} \)
- **SCO range** = 86% - coverage level of underlying policy

Example: 75% RP policy, 140 bu corn APH yield, $4.00 corn price

\[
\text{SCO $ liability} = (140 \times 4.00) \times (86\% - 75\%) \\
= 560 \times 11\% = 61.60
\]

Calculating losses under SCO

Loss occurs if actual county revenue < 86% of expected county revenue*
*revenue example

Expected county revenue = \( \text{Expected county yield} \times \text{Crop insurance price} \)

Corn example:

\[
\$520.00 = 130 \text{ bu/a} \times 4.00/\text{bu}
\]

Revenue trigger = ECR \( \times \) 86%

\[
\$447.20 = 520 \times 86\%
\]

Actual county revenue = \( \text{Actual county average yield} \times \text{Crop insurance price} \)

\[
\$410.80 = 102.7 \text{ bu/a} \times 4.00/\text{bu}
\]

Actual Revenue Percent = \( \frac{\text{Actual county revenue}}{\text{Expected county revenue}} \)

\[
\frac{410.80}{520} = 79\%
\]
Calculating losses under SCO

Calculate the **County Payment Factor**

CPF = the share of the SCO range that is considered a loss

**CPF example:**
- Underlying coverage: 75%
- **SCO range**: 86% - 75% = 11%

Actual revenue/Expected revenue = 79%

**Loss range** = 86 - 79% = 7%

CPF = 7 / 11 = 0.636

Calculating losses under SCO

**Indemnity payment** = **SCO $ liability** x **CPF**

Corn example:

75% RP, 140 bu APH, $4.00/bu insurance price

SCO $ liability = 140 bu x $4.00 x 11% = $61.60

Actual county revenue / Expected county revenue = 79%

CPF = 7 / 11 = 0.636

Indemnity = $61.60 x 0.636 = $39.18
2019 SCO availability: WHEAT

SCO availability: GRAIN SORGHUM
2019 SCO availability:  CORN

2019 SCO availability:  SOYBEANS (non-irrigated)
2019 SCO availability: SOYBEANS (irrigated)

Should you buy SCO?

- Depends on ARC/PLC decision: only available if not in ARC:

- Does SCO affect the ARC/PLC decision?
  - SCO applies to \textit{planted acres}, ARC paid on \textit{85\% of base} acres
  - SCO could be more attractive when \textit{base acres} $\ll$ \textit{planted acres}

- When would SCO be preferred to individual coverage?
  1. Is APH yield far less than expected yield?
     New farm with little/no yield history: APH history full of T-yields
     Understated APH yield means individual coverage providing less effective protection
  2. Could county have a loss \textit{before} the farm has a loss?
Should you buy SCO?

• Even with PLC, producer still has a crop insurance portfolio decision:
  1. Add SCO to underlying farm policy
     SCO has cheaper premium rates and 65% premium subsidy...
     But SCO uses county trigger...
  2. Or just buy higher coverage on underlying farm policy
  3. Or don’t add any additional insurance coverage

• Effectiveness of SCO: consider relationship of farm and county yields
  • Will county-based loss closely reflect the farm loss?
  • Will county-based coverage pay when there is a small farm loss?

Premium costs, 2019 crop year

• Wheat, Saline County: 45 bu APH, $5.74 price, RP, non-irrigated

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<thead>
<tr>
<th>Farm covg %</th>
<th>Farm policy</th>
<th>Farm + SCO = Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>85%</td>
<td>$21.53</td>
<td>$21.53 + 0.46 = $21.99</td>
</tr>
<tr>
<td>80%</td>
<td>$14.82</td>
<td>$14.82 + 2.49 = $17.31</td>
</tr>
<tr>
<td>75%</td>
<td>$9.71</td>
<td>$9.71 + 4.09 = $13.80</td>
</tr>
<tr>
<td>70%</td>
<td>$6.19</td>
<td>$6.19 + 5.33 = $12.25</td>
</tr>
<tr>
<td>65%</td>
<td>$5.41</td>
<td>$5.41 + 6.19 = $11.60</td>
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Source: Univ. of Illinois FAST Tools
Consult a crop insurance agent for actual premiums in your case
Premium costs, 2019 crop year

- Corn, Saline County: 92 bu APH, $4.00 price, RP, non-irrigated

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</tr>
<tr>
<td>75%</td>
<td>$24.63</td>
<td>$31.44</td>
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<tr>
<td>70%</td>
<td>$19.30</td>
<td>$28.70</td>
</tr>
<tr>
<td>65%</td>
<td>$16.81</td>
<td>$28.44</td>
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Source: Univ. of Illinois FAST Tools
Consult a crop insurance agent for actual premiums in your case

Acres covered by SCO in KS, 2015-18
2018 KS: SCO acres a small share of PLC acres

Comparing farm and SCO coverage

- Illinois FAST tools
  - [http://farmdoc.illinois.edu/fasttools/](http://farmdoc.illinois.edu/fasttools/)
  - Plug in own APH yields, compare premiums for different plans and coverage levels
  - Excel spreadsheet format
  - Be careful with updates

- Check with your crop insurance agent for *actual premium quotes*
SCO sign-up and commodity programs

• Problem: sign-up periods didn’t coincide
  • Must sign up for SCO along with underlying crop insurance policy prior to planting
  • Can cancel SCO coverage later if ARC is selected

• Special case for 2019 crops:
  • Only eligible for SCO if signed up before planting (March 15 for spring-planted crops)
  • July 15 Acreage Reporting Date: indicate which FSA farms will be in ARC and PLC; can drop the SCO coverage for farms enrolled in ARC
  • July 15 indication to RMA does not lock in the ARC/PLC decision with FSA
  • Old rule: can drop SCO later if they elect ARC, but must pay penalty of 20% of SCO premium
  • “The existing penalties for misreporting eligible acreage on the SCO endorsement will not apply in 2019.”

Questions?
Comments?
Thank you!

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