



Weekly Farm Economics: Crop Insurance and Rental Arrangements: Lessons from the 2012 Drought

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The 2012 drought raised two issues related to crop insurance and rental arrangements. First, it appears that a significant number of share rent landlords did not take crop insurance, resulting in much lower returns for these share rent landlords. Second, variable cash rental arrangements typically have not included crop insurance proceeds in calculating rental payments, leading landlords to receive less of gross revenue than anticipated. Both of these issues are discussed below.

Share Rent Landlords and Crop Insurance

In Illinois in 2012, roughly 60% of corn and soybean acres were insured with products having relatively high coverage levels, 20% were insured with crop insurance products that would make modest payments, and 20% of the acres were not insured. Farm record data suggests that most commercial farmers insured with insurance policies having high coverage levels, leading to the inference that share rent landlords make up a good portion of the 20% of crop insurance policies with modest coverage and 20% of acres not insured.

Not taking crop insurance means that share rent landlords took larger losses than those who took crop insurance. While some share rent landlords may have had good reasons for not taking insurance, others likely did not adequately considered crop insurance choices. Share rent landlords likely are not prime targets for crop insurance sales, leading to share rent landlords receiving less crop insurance information than others. This could then result in less crop insurance sales to share rent landlords.

Share rent landlords are eligible for crop insurance. Farmers with share rent landlords may consider making their landlords aware of crop insurance alternatives. Purchase of crop insurance reduces could reduce downside revenue risk of landlords. Some of the incentive to switch to cash rent may be to avoid downside revenue risk. Reducing downside risk with crop insurance could reduce incentives for share rent landlords to shift to cash rent.

Variable Cash Rental Arrangements and Crop Insurance

Many variable cash rental arrangements have a minimum cash rent plus a bonus if crop revenue exceeds a specified level (see [here](#) for an example). The bonus generally is a percentage of crop revenue above the specified level, where crop revenue equals yield from the farm times a price. Typically, crop insurance

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proceeds are not considered in bonus calculations.

This year, crop insurance proceeds made up a large portion of gross revenue, particularly on farms with low yields. Because of crop insurance payments in low yields situations, farmers may have had less losses and, in some cases, have had revenue exceed the level resulting in bonus payments when crop insurance is included in the bonus calculation.

This has led to consideration of adding crop insurance proceeds to the revenue used to calculate bonus payments in variable cash rental arrangements. There are, however, issues in including crop insurance payments in bonus calculations. One of these is that many farmers buy crop insurance at an enterprise unit level, which covers all crops the farmer grows in a county. In these cases, the farmer's crop insurance payments are not based on a specific farm, but all farms in the county. Hence, a farmer's crop insurance proceeds could be higher or lower than indicated by the specific landlord's farm.

Requiring a farmer to buy specific crop insurance products to make bonus calculations for a farm does not seem prudent. There are cost advantages to farmers for buying crop insurance at a more aggregate level. Hence, the requirement to buy crop insurance at a more disaggregated level could greatly increase the costs to farmers.

If some recognition that crop insurance proceeds is needed in variable cash rent arrangements, I suggest an approach consisting of two steps. First, a crop insurance product could be simulated for inclusion in variable cash rent arrangements. Historical yields and projected prices could be used to set guarantees and actual yields and harvest prices could be used to establish revenue. The simulated crop insurance proceeds could then be used in calculating bonuses. Second, the minimum cash rents should be lowered in recognition that the farmer is now providing the landlord crop insurance, and the farmer should be compensated for providing this insurance.

Summary

Share rent landlords who have not purchased crop insurance in previous years should be made aware of crop insurance programs, so that they can make an informed decisions on whether to take crop insurance. Including actual crop insurance proceeds in rents from variable cash rental arrangements could be problematic. Use of alternative means through simulating crop insurance proceeds and reducing in minimum rents likely may be an appropriate alternative.