RMA Offers Tool to Avoid Risk

by **MARY LOU PETER**

Livestock owners have a new tool to manage price risk. It comes in the form of subsidized Livestock Risk Protection (LRP) contracts now available through the U.S. Department of Agriculture (USDA) Risk Management Agency (RMA).

The agency, best known for its crop insurance instruments, made LRP contracts available on feeder cattle in Colorado, Iowa, Kansas, Nebraska, Nevada, Oklahoma, South Dakota, Texas, Utah and Wyoming, says Art Barnaby, ag economist with Kansas State University (K-State) Research and Extension.

Fed-cattle contracts are available only in Iowa, Illinois and Nebraska.

"Because eligibility is determined by the location where the cattle are being fed, it is possible for Kansas producers to buy a fed-cattle contract if they are feeding the cattle in a Nebraska feedlot," he says.

Barnaby, whose research was the basis for the privately-developed Crop Revenue Coverage (CRC), explains that the new livestock contract does not guarantee the producer a cash price. Rather it's a single-peril risk contract — effectively an off-board price derivative, but for legal reasons it is referred to as an insurance product.

"This contract may be very attractive to certain producers over a CME (Chicago Mercantile Exchange) feeder-cattle put contract," he says. "Producers may buy LRP only on the number of head they actually own, and that may be fewer than would be required for a CME contract."

He believes cattle owners should be aware of LRP contract details:

- Producers must submit an application for an LRP contract. Once the application has been accepted, the producer must submit a specific coverage endorsement (SCE).
- The LRP contract receives a 13% premium subsidy. The administrative and commission expenses are also paid by a separate subsidy.

"In a private insurance market, one would not receive any premium subsidy, and the purchaser would have to pay the administrative and operating costs of the contract," Barnaby says.

- Producers must identify the number of feeder steers that are expected to be ready for market at 650 pounds (lb.) to 900 lb. (As of this writing, the LRP was not available on heifers or breeds containing significant amounts of Brahman or dairy genetics.) The producer then chooses the appropriate insurance period, ranging from 21 to 30 weeks, to reach the target weight.
- The producer selects a coverage price for the period of the policy. The insured value will equal the number of head multiplied by the target weight multiplied by the coverage price multiplied by the ownership share. The total premium will equal the insured value multiplied by the rate. The 13% subsidy is then subtracted.
- The feeder cattle LRP contract is limited to 2,000 head per crop year (July 1-June 30) and 1,000 head per SCE. For those in states where fed-cattle contracts can be written,

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that contract is limited to 2,000 head per SCE, although one may purchase an SCE with fewer head and a maximum of 4,000 head per crop year, the economist says.

- The length of the LRP for SCE feeder cattle coverage has been approved for 30-day increments from 13 to 52 weeks, but only a limited number of weeks are currently being offered.

"But I've checked the RMA (Risk Management Agency) Web site and the current offer is a maximum of 30 weeks," he said.

For more information about livestock or crop insurance, visit K-State Research and Extension's new ag economics Web site at *www.agmanager.info*.

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Livestock risk protection may appeal to certain producers

The new Livestock Risk Protection (LRP) insurance available on feeder cattle in Kansas and several other states may be particularly attractive to some producers over a feeder-cattle put contract on the futures market, says Art Barnaby, professor of ag economics at Kansas State University (K-State).

"Producers may buy LRP only on the number of head they actually own, and that may be fewer than would be required for a CME (Chicago Mercantile Exchange) contract," he adds.

A full CME feeder contract represents about 67 head. If the producer only has 50 steers, then he or she would be able to purchase LRP on just the 50 steers, Barnaby explains. Also, this is an insurance contract because once it's purchased, it cannot be cancelled. Since it is an insurance contract with a specified length, it will be attractive for lending institutions that are lending money on cattle serving as collateral.

"Because it is an insurance contract, there is no question that it is a tax-deductible expense and would be included as a farm expense item. Options also are tax-deductible although some trading strategies sometimes are not considered deductible expenses," Barnaby says.

The contract also has potential to provide additional interest simply because producers may insure the cattle for months further out, he says.

Barnaby says the LRP has a 13% premium subsidy, and producers do not pay a commission — two more reasons the contract may be attractive to some producers.