Livestock Risk Protection

What does “subsidy capture” mean under Livestock Risk Protection (LRP)?

Under LRP, “subsidy capture” means exploiting the difference between the producer paid LRP premium and the cost of a privately traded livestock contract (e.g., an option contract) to derive financial gain. Policyholders and any person with a substantial beneficial interest (SBI) are prohibited from offsetting LRP coverage for the purpose of subsidy capture. Administrative, civil, or criminal remedies may apply. This behavior is also called subsidy harvesting, or subsidy arbitrage, among other names.

Which actions are presumed to be subsidy capture?

Unless the producer can show a clear, inadvertent error, LRP presumes subsidy capture when any of the following occur:

- You buy an SCE and also sell a new put option on the relevant futures contract, provided that all the following conditions are met:
  - the option expires within 4 calendar days of the SCE end date;
  - the sale occurs from 2 trading days before through 5 trading days after the SCE effective date;
  - the option premium per cwt exceeds 80% of your SCE premium.
- You buy an SCE, sell a call option, and open a long futures position that together replicates a short put position, provided that all the following conditions are met:
  - The call option contract month is within 4 calendar days of the SCE end date;

    - the sale occurs from 2 trading days before through 5 trading days after the SCE effective date;
    - the option premium per cwt exceeds 80% of your SCE premium.
- You enter into a **private (off exchange) contract** that effectively swaps uncertain future LRP indemnities for a certain dollar amount.

Can I still hedge with CME options or futures while I carry LRP?

Yes—LRP does not ban hedging in general. LRP's prohibition targets arbitraging the premium subsidy, while Section 25 lists specific trades that are presumed subsidy capture. In practice, hedges aimed at bona fide risk management—and that do not trigger the Section 25 presumptions—are generally acceptable. The policy lists specific timing/size combinations that are presumed subsidy capture (see question "Which actions are presumed to be subsidy capture?"). Activities outside those combinations are not automatically presumed—but USDA may still determine subsidy capture if a compliance review shows the strategy's primary purpose was arbitraging the subsidy rather than managing risk.

What do I (and my agent) certify about subsidy capture when I buy an SCE?

The SCE includes two required signed certifications:

- Insured's certification that you will not offset LRP coverage through exchange traded livestock contracts or other means for the purpose of subsidy capture, acknowledging potential administrative, civil, or criminal remedies.
- Agent's certification that the agent has not advised or assisted with buying livestock contracts to offset LRP for the purpose of subsidy capture, with the same sanction acknowledgment.

Am I required to provide brokerage records?

Yes, but only if the USDA initiates a review of your policy. If requested for a USDA review, you or persons with an SBI in you, must provide brokerage records for those dates on which a potential violation may have occurred. Additional requirements can be found in Section 12(g) of the LRP Basic Provisions.

If you refuse to provide the requested information, your indemnities will be denied and you will still owe the premium.

Where can I learn more about subsidy capture?

Talk to your agent or AIP to ensure you are complying before purchasing LRP. Additionally, Dr. Marin Bozic, the submitter for Livestock Risk Protection, maintains a blog on livestock insurance programs at 508h.commoditymarkets.com/

The information provided on the submitter's blog is for general informational purposes only and must not be construed as representing official RMA opinions.