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BY THE U.S. GENERAL ACCOUNTING OFFICE

Report To The Honorable Howard M. Metzenbaum United States Senate

Losses In The Department Of Agriculture's Tobacco Program

The Department of Agriculture (USDA) stands to lose money on loans made to support 1976-1981 flue-cured tobacco--the primary U.S. tobacco. On October 26, 1984, USDA offered substantial discounts on this tobacco. If all of the tobacco had been sold at the discount prices of that date, USDA's total losses would have been about $415 million. As of June 30, 1985, however, only about 11 percent was sold. The remaining tobacco continues to incur additional costs for storage and interest, and how much USDA will ultimately receive for the tobacco is unknown. Accordingly, the actual losses will not be known until all the tobacco is sold.

In addition, since the No Net Cost Tobacco Program Act of 1982 was enacted, USDA is to operate the tobacco program at no net cost to the federal government. However, as GAO reported in February 1985, USDA continues to lose money on its loans because it does not recover all of the interest costs it incurs. For example, as of June 1985, USDA charged about $16 million less in interest on the 1982 flue-cured crop loans than it paid to borrow the money.

UNITED STATES GENERAL ACCOUNTING OFFICE

GAO/RCED-85-167
SEPTEMBER 18, 1985

033341

UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

SEP 18 1985

RESOURCES, COMMUNITY, AND ECONOMIC DEVELOPMENT DIVISION

B-213761

The Honorable Howard M. Metzenbaum
United States Senate

Dear Senator Metzenbaum:

On February 15, 1985, you requested that we provide certain sales pricing and cost information on flue-cured tobacco under the Department of Agriculture's (USDA's) tobacco program. USDA stabilizes and supports the price of several different types of tobacco, including flue-cured, the major domestically produced tobacco, through price-support loans. As of June 30, 1985, USDA had about $3.1 billion in loans outstanding on all tobacco, of which about $1.8 billion was flue-cured.

As you requested, and as clarified in subsequent discussions with your office, this report provides

- --an estimate of the losses that USDA could incur on the 1976-1981 flue-cured tobacco crops and of the total inventory price reduction resulting from the USDA-approved discount sale terms of October 26, 1984;
- --an estimate of the total price reduction on actual sales of 1976-1981 flue-cured tobacco under the October 26, 1984, discount sale terms; and
- --an update on the interest costs USDA has incurred on the 1982 flue-cured tobacco crop, on which we reported in February 1985.[1]

USDA pays for any losses that occur on its price-support loans for crops grown prior to 1982. The loan process begins when eligible tobacco producers, who primarily sell through auction markets, do not receive a bid on their tobacco at least equal to USDA's price-support loan rate. They can then consign the tobacco

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[1] Department of Agriculture and Producer Costs To Operate the Tobacco Program (GAO/RCED-85-30, Feb. 8, 1985).

to producer-owned and -operated marketing associations that (1) provide them with cash advances for their tobacco at the price-support rates and (2) attempt to sell the tobacco. The associations in turn receive USDA loans, using the tobacco as collateral, to cover the cash advances and related marketing and handling costs. USDA makes additional loans to the associations to store the tobacco and charges interest on all the loans. Sales proceeds are used to reduce the loan balances. For crops grown prior to 1982, if the sales amounts are insufficient to cover the loans, USDA writes off the unpaid balance as a program loss.

Starting with the 1982 crop, however, USDA was to stop covering loan losses as a result of the No Net Cost Tobacco Program Act of 1982. Under this program, losses incurred by the marketing associations are to be covered by fees paid by the tobacco producers. As we stated in our February 1985 report, however, USDA is losing money on its No Net Cost Tobacco Program loans because it does not recover all of its interest costs. USDA pays compound interest on the money it borrows from the U.S. Treasury to provide the loans, but it does not charge compound interest on the money it lends to the marketing associations. To give an example of the interest losses that are occurring, we reported on the 1982 flue-cured crop. We estimated that as of June 1984 USDA paid about $6 million more to borrow the money it lent on that crop than it charged the Flue-Cured Tobacco Cooperative Stabilization Corporation, the marketing association that handles flue-cured tobacco. Interest losses are also occurring on subsequent crop years as well as on other kinds of tobacco.

On October 26, 1984, the Stabilization Corporation announced a discount on all of its tobacco under loan. USDA approved the sale, according to a USDA official, to reduce the 800-million pound inventory and to be more competitive with foreign tobacco prices. Under the sale terms, tobacco from crop years[2] 1976-1981 is discounted from 90 to 50 percent, respectively, from the regular USDA-approved sales price if purchased with twice the amount of newer crop tobacco (1982 or later) at a 10-percent discount. For example, a purchaser could buy 100 pounds of 1976 crop tobacco at a 90-percent discount if the purchaser also bought 200 pounds of 1982 crop tobacco, which would be discounted 10 percent.

In summary,

--USDA stands to lose money on its 1976-1981 flue-cured crops under loan. If the entire inventory had been sold at the discount prices of October 26, 1984, USDA would have lost about $415 million on its loans. If it had been sold at the regular sales prices at that time, USDA would have lost about $89 million. The

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[2]A crop year is the year in which a crop is normally harvested.

price of the inventory was reduced a total of about $326 million from the regular sales price under the discount sale terms. USDA's actual losses will not be known until all the tobacco is sold. Storage costs as well as interest on the loans continue to be incurred on the unsold tobacco. In addition, how much USDA will ultimately receive for the tobacco is unknown.

--About 29 million pounds, or about 11 percent, of the 1976-1981 flue-cured tobacco inventory was actually sold at discount through June 30, 1985. It was sold for about $35 million below its regular sales price.

--As of June 30, 1985, USDA has lost about $16 million in estimated interest on loans made on the 1982 flue-cured crop under the No Net Cost Tobacco Program. This amount is about a $10 million increase since June 1984.

To respond to your request, we interviewed officials and obtained data from USDA and the Flue-Cured Tobacco Cooperative Stabilization Corporation in Raleigh, North Carolina. From their data, we calculated by crop year the amounts in inventory, prices, and loan amounts, as well as the interest losses. A more detailed discussion of our responses to your questions; objectives, scope, and methodology; and background follows in appendix I.

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We discussed the report's contents with the Acting Director, Tobacco and Peanuts Division, and the Director, Fiscal Division, both of USDA's Agricultural Stabilization and Conservation Service. They concurred with the factual information presented in the report and provided clarifying language, which was incorporated in the report as appropriate. They also noted that the cost estimates appeared reasonable, although they did not verify their accuracy. As requested by your office, we did not obtain official agency comments on this report.

As agreed with your office, unless you publicly announce its contents earlier, we plan no further distribution of this report until 7 days from its issue date. At that time we will send copies of this report to the Secretary of Agriculture, various Senate and House Committees, Members of Congress, and other interested parties.

Sincerely yours,

Ralph V. Carlone for

J. Dexter Peach
Director

Contents

ILLUSTRATIONS

ABBREVIATIONS

ASCS	Agricultural Stabilization and Conservation Service
CCC	Commodity Credit Corporation
GAO	General Accounting Office
USDA	Department of Agriculture

COST INFORMATION ON USDA'S PROGRAM FOR FLUE-CURED TOBACCO

BACKGROUND ON USDA's TOBACCO PROGRAM

The Department of Agriculture's (USDA's) tobacco program has several objectives, one of which is to support the price of domestic tobacco. The Agriculture Act of 1949, as amended (7 U.S.C. §1421 et seq.) authorizes USDA's Commodity Credit Corporation (CCC) to stabilize and support tobacco prices through price-support loans. Since the tobacco program's inception in 1933 through June 30, 1985, CCC has provided about $7.7 billion in loans to support tobacco prices, with $3.1 billion including interest still outstanding.

Nine separate kinds of tobacco are currently eligible for price supports. Flue-cured, which is the type of tobacco discussed in this report, comprises over one-half of all U.S. tobacco production and accounts for over one-half of all USDA tobacco loans.

The Agricultural Stabilization and Conservation Service (ASCS) administers CCC's operations because CCC is a government entity with no employees of its own. In this capacity, ASCS has overall responsibility for regulating the tobacco price-support program. ASCS' administrative expenses are funded through appropriations and its price-support operations through U.S. Treasury borrowings. To carry out the administrative responsibilities, ASCS contracts with 13 producer-owned and -controlled cooperative marketing associations. The Flue-Cured Tobacco Cooperative Stabilization Corporation handles flue-cured tobacco.

Price-support loans are made when eligible tobacco producers,[1] who primarily sell through auction markets, are unable to get bids for their tobacco equal to the price-support rates.[2] Producers can then consign the tobacco to producer-owned and -operated marketing associations. These associations act as

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[1]Only growers who approve and comply with marketing restrictions are eligible to receive price support.

[2]Price-support levels are based on the concept of parity. Parity is a general or overall standard which applies to the average of the various locations, grades, qualities, and classes of a commodity as sold by all farmers. Parity prices, the most commonly used parity standard, are those prices that will give farm commodities the same purchasing power they had in a selected base period when prices received and paid by farmers were considered to be in good balance. The formula for computing parity prices is set forth in the Agriculture Adjustment Act of 1938, as amended.

marketing agents for the tobacco producers and provide them with cash advances for their tobacco at the price-support rate. The associations in turn receive loans from CCC to cover the advances and other related costs they incur, such as storage, processing, and handling. The associations market the tobacco, which serves as collateral for the loans, at prices approved by CCC. For tobacco that is not sold, USDA makes additional loans to the associations for continued storage and handling expenses and charges interest on all the loans, generally on a monthly basis.

As the associations sell the tobacco, the proceeds are applied toward repayment of the loans. On crops prior to 1982, if the sales proceeds from the tobacco securing the loan are insufficient to repay the loan, CCC writes off the unpaid balance as a loss to the government. If sales proceeds exceed the loan, including interest, the net proceeds are distributed to the producers in proportion to the amount of tobacco each consigned. As of September 30, 1984, CCC had lost about $66 million in loan principal to support tobacco prices and had nearly 300 million pounds of pre-1982 tobacco remaining to be sold.

For 1982 and subsequent crops, however, under the No Net Cost Tobacco Program Act of 1982 (7 U.S.C. §1445-1, -2), losses cannot be written off. The act provides that, insofar as practicable, the program be carried out at no net loss to the government, other than for administrative expenses common to the operation of all USDA price-support programs. The act requires that each producer, as a condition of eligibility, pay an assessed fee to a fund or account to cover the program's cost. Any loss is to be offset by net gains realized on the sale of 1982 and subsequent crops or from the funds accrued from producer assessments.

Discount sale on flue-cured tobacco

On October 26, 1984, the Flue-Cured Tobacco Cooperative Stabilization Corporation announced a discount on the 1976-1984 flue-cured tobacco it held under loan from CCC. It did so, according to the Chief of ASCS' Tobacco Operations Branch, to reduce its 800-million pound inventory, totaling $1.8 billion in outstanding loans as of October 31, 1984, and to be more competitive with foreign tobacco prices. In addition, the tobacco inventory was continuing to incur storage and interest costs and to deteriorate with age. As with all tobacco prices, the discounts were proposed by the Stabilization Corporation and approved by CCC. To receive the discount, 2 pounds of the 1982-1984 crop year[3] tobacco must be purchased for every 1 pound of pre-1982 tobacco. The pre-1982 crops are discounted from 50 to 90 percent, as shown in the following table, and the 1982-1984 crops are discounted 10 percent. Effective October 29, 1984,

[3]A crop year is the year in which a crop is normally harvested.

these discounts have been taken from the established base prices[4] of that date.

Table I.1

1976-1981 Crop-Year Discounts

Crop	Percent reduction
1976	90
1977	85
1978	75
1979	70
1980	60
1981	50

About 265 million pounds of pre-1982 tobacco was offered for sale. As indicated earlier, any losses incurred on the pre-1982 crops will be absorbed by CCC. The sale remains in effect until such time as the Stabilization Corporation and ASCS agree to terminate it.

Interest computation practices

Although the tobacco program is to be carried out at no net cost to the government, except for administrative expenses, since the No Net Cost Tobacco Program Act, it does not operate at no net cost. We reported earlier[5] that CCC has incurred substantial unrecovered interest costs because of its interest computation practices. These costs occur because CCC pays compound interest on the money it borrows from the U.S. Treasury, but does not compound accrued interest on the money it lends to the tobacco associations.

Specifically, CCC borrows funds from the Treasury to meet its cash requirements, which include financing for the tobacco price-support program. The Treasury charges CCC interest on the outstanding balance owed, which includes unpaid interest on borrowings from prior periods. Interest on funds CCC borrows from the Treasury is set at the rate the Treasury charges during the month that the funds are disbursed and is compounded semiannually. In contrast, CCC charges the tobacco associations interest on the outstanding principal balances, which does not

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[4]Base prices are the regular sales prices buyers pay if they do not qualify for the discounts. They are generally proposed yearly by the associations and approved by CCC on the basis of the costs incurred on the crops and the current market conditions.

[5]Department of Agriculture and Producer Costs To Operate the Tobacco Program (GAO/RCED-85-30, Feb. 8, 1985).

include unpaid interest on borrowings from prior periods. Thus, the amounts of interest recorded and collected on CCC tobacco loans are less than the corresponding interest that CCC pays the Treasury for borrowed funds. For example, in our February 8, 1985, report we estimated a $6 million interest loss on the 1982 flue-cured tobacco under loan as of June 30, 1984. Interest losses are also occurring on subsequent crop years as well as on other kinds of tobacco.

OBJECTIVES, SCOPE, AND METHODOLOGY

As requested in Senator Metzenbaum's February 15, 1985, letter and clarified in subsequent discussions with his office, our objectives were as follows:

(1) Compare the base prices and discount prices under the October 26, 1984, discount sale terms and the total value of loans outstanding for all 1976-1981 flue-cured tobacco under loan. This comparison shows the total losses CCC could incur on its loans for these years, assuming the crops were sold at the discount prices and the base prices at that time. It also shows the total potential price reduction from the base prices if the entire inventory were sold at the discount prices at that time.

(2) Compare the base and discount prices for the 1976-1981 flue-cured tobacco actually sold under the discount sale terms as of June 30, 1985. This comparison shows the total price reduction on the tobacco actually sold at discount.

(3) Update the effects of not charging compound interest on the 1982 flue-cured crop under loan, which we discussed in our February 8, 1985, report.

We obtained data from ASCS headquarters in Washington, D.C, and from officials of the Flue-Cured Tobacco Cooperative Stabilization Corporation located in Raleigh, North Carolina. Specifically, we met our first objective by interviewing officials of and obtaining documents from the Stabilization Corporation on the 1976-1981 flue-cured tobacco remaining under loan and the base prices and discount prices for the October 26, 1984, discount sale. We calculated the total pounds of 1976-1981 flue-cured tobacco in inventory by crop year and then priced the tobacco at the base prices and the discount prices. We also interviewed officials of and obtained documents from ASCS' Tobacco and Peanuts Division on the discount sale and on CCC's loan balance at October 26, 1984.

We met our second objective by interviewing and obtaining documentation from officials of the Stabilization Corporation on the amount of tobacco sold under the discount sale terms as of June 30, 1985, the most recent sales information available at the time of our review work. For all of these determinations, our cost estimates on the tobacco inventory and prices are as of October 26, 1984--the date of the discount offer.

We met our third objective by using the same formula from our previous report on costs under the No Net Cost Tobacco Program. (See p. 11.) We also interviewed ASCS' Fiscal Division officials for information on and verification of our computations.

Our work was performed in accordance with generally accepted government auditing standards. We discussed the contents of this report with the Acting Director, Tobacco and Peanuts Division, ASCS, and the Director, Fiscal Division, ASCS. They concurred with the factual information presented in the report and provided clarifying language, which was incorporated in the report as appropriate. The officials also noted that the cost estimates appeared reasonable, although they did not verify the accuracy of the estimates. As requested by your office, we did not obtain official agency comments. Additional specific information on the methodology we used for meeting these objectives is further explained as part of our detailed responses to each issue. We gathered our data from March through June 1985.

CCC POTENTIAL LOSSES AND REDUCTIONS ON 1976-1981 FLUE-CURED CROPS

Based on our comparison of the discount and base prices of October 26, 1984, with the balance of loans outstanding at that time, we determined that CCC stands to lose money on its 1976-1981 flue-cured crops. CCC could lose an estimated $414.5 million at the discount prices and $88.8 million at the base prices. The total price of the inventory was reduced by about $325.7 million under the discount sale terms.

From information provided by the Stabilization Corporation, we estimated the 1976-1981 flue-cured tobacco inventory under loan at October 26, 1984, to be approximately 264.7 million pounds. Based on ASCS data, we calculated the balance of loans outstanding on that inventory to be about $599.4 million, which includes interest and storage costs. We priced the inventory at the discount prices and at the base prices and found that neither would recoup enough to pay off the CCC loans. If the entire inventory had been sold at the discount prices of October 26, 1984, CCC would have received about $184.9 million, or about $414.5 million less than was owed on the loans. If the inventory had been sold at the base prices at that time, CCC would have received about $510.6 million, or about $88.8 million less than was owed on the loans. The total discount price of the inventory, therefore, was about $325.7 million less than the base price.

To obtain the loan balance on the October 26, 1984, inventory of 1976-1981 flue-cured tobacco under loan, we had to adjust CCC data to account for differences in the dates of CCC's and the Stabilization Corporation's inventory and transactions in process. For example, CCC loan data was as of October 31, 1984, whereas the Stabilization Corporation inventory was as of October 26, 1984. In addition, CCC data included tobacco in inventory for which payment and/or paperwork had not yet been received, but which the Stabilization Corporation had already deleted from its inventory because it had been purchased. Therefore, CCC's inventory was about 3 percent larger than the Stabilization Corporation's inventory. Based on discussions with the Chief and an agricultural marketing specialist of ASCS' Tobacco Operations Branch, we adjusted CCC's figures to coincide with the Stabilization Corporation's inventory of October 26, 1984.

Table I.2 shows by crop year the total potential losses on the outstanding tobacco loans as of October 26, 1984, and the total price reduction as a result of the discount sale.

Table I.2

Comparison of Base Price, Discount Price,
and Loan Balance on 1976-1981 Flue-Cured Tobacco under Loan
as of October 26, 1984

Crop year	Inventory (lbs.)	Loans outstanding	Base price	Discount price	Loss/gain (+) at base price	Loss at discount price	Price reduction
1976	10,138,800	$ 21,246,130	$ 11,072,978	$ 1,107,298	$10,173,152	$ 20,138,832	$ 9,965,680
1977	85,741,550	163,007,040	117,651,408	17,647,711	45,355,632	145,359,329	100,003,697
1978	14,979,600	23,669,102	23,985,591	5,996,398	+ 316,489	17,672,704	17,989,193
1979	16,209,500	31,481,680	31,129,529	9,338,859	352,151	22,142,821	21,790,670
1980	57,134,500	135,430,058	125,866,937	50,346,775	9,563,121	85,083,283	75,520,162
1981	80,461,200	224,602,831	200,943,525	100,471,763	23,659,306	124,131,068	100,471,762
Total	264,665,150	$599,436,841	$510,649,968	$184,908,804	$88,786,873	$414,528,037	$325,741,164

APPENDIX I

Although CCC could lose $414.5 million at the discount price, compared to $88.8 million at the base price, this does not necessarily mean that the discount price is not in the best interest of the government. Sales at either price could be limited. It is possible that CCC could receive no more for the tobacco than the $184.9 million it would receive if it were sold at the discount price. In addition, as the tobacco is held in storage awaiting sale, storage and interest costs on the loan increase, and the tobacco deteriorates. According to an agricultural marketing analyst in ASCS' Tobacco Operations Branch, the tobacco begins to deteriorate after about 2-1/2 years and at about 10 years has reached its maximum storage life. Therefore, it could be more expensive in the long run to try to get higher prices for the tobacco if it does not sell within a reasonable time than to sell it more quickly at the discount prices. Because of these factors and because how much CCC will ultimately receive for the crops is unknown, the final losses cannot be computed until all of the 1976-1981 flue-cured crops are sold.

DISCOUNT PRICE REDUCTION ON ACTUAL SALES

Our comparison of the base and discount prices for the actual amount of tobacco sold at discount through June 30, 1985, showed that the tobacco was sold for about $34.5 million below its base price. As agreed with your office, we reviewed the sales under the special offer of 1976-1981 flue-cured tobacco through June 30, 1985. About 28.9 million pounds, or 11 percent of the inventory, was sold. Had the tobacco been sold at the base prices in effect at that time, CCC would have received about $42 million rather than the discount price of about $7.4 million.[6]

These figures are based on sales in which the buyer has committed to purchase the tobacco but can have up to 2 years to actually pay for it. The committed sales figure will not provide the exact purchase cost, however, since some of the tobacco has not yet been paid for and interest and storage costs will be added to the price each month until it is paid for. According to the Stabilization Corporation's Accounting Department Manager, most of the discount sales were paid for quickly, so our cost estimates should be reasonably close to the actual purchase cost.

Table I.3 shows by crop year the tobacco actually sold under the discount sale from October 30, 1984, to June 30, 1985, and the resulting price reduction.

[6]Figures do not add due to rounding.

Table I.3

Comparison of Base Price and Discount Price on 1976-1981 Flue-Cured Tobacco Sold at Discount through June 30, 1985

Crop year	Discount (percent)	No. of lbs. sold	Base price	Discount price	Price reduction
1976	90	4,047,800	$ 4,655,107	$ 465,511	$ 4,189,596
1977	85	20,293,800	28,706,888	4,306,033	24,400,855
1978	75	1,272,450	2,063,517	515,879	1,547,638
1979	70	2,747,600	5,228,726	1,568,618	3,660,108
1980	60	296,600	598,846	239,538	359,308
1981	50	268,400	708,557	354,279	354,278
Total		28,926,650	$41,961,641	$7,449,858	$34,511,783

LOSSES UNDER THE NO NET COST TOBACCO PROGRAM

Because of CCC's practices in computing interest on its tobacco loans, it is losing money. On just one crop, the 1982 flue-cured crop, it has lost about $16 million as of June 1985. The losses occur because CCC is required to pay compound interest on the money it borrows from the Treasury but charges simple interest on the money it lends to the tobacco associations. We have discussed CCC interest computation practices in several previous reports;[7] however, USDA has not yet chosen to change its procedures.

The No Net Cost Tobacco Program Act of 1982 describes its purpose as implementing congressional intent that the tobacco program be carried out at no net cost to the government. The act requires that a fund or account be established by or for each tobacco association to be used to insure, insofar as practicable, that CCC will suffer no net losses under its loan agreements with

[7] Collection and Accounting for Accrued Interest on Commodity Credit Corporation Producer Loans (AFMD-82-40, Jan. 11, 1982); Tobacco Program's Production Rights and Effects on Competition (CED-82-70, Apr. 23, 1982); Information on Commodity Credit Corporation Loan Repayment Practices (CED-82-106, June 16, 1982); Cost Information on USDA's Tobacco Program (GAO/RCED-84-33, Dec. 12, 1983); and Department of Agriculture and Producer Costs To Operate the Tobacco Program (GAO/RCED-85-30, Feb. 8, 1985).

producer associations. The act does not, however, require CCC to charge interest on loans to producer associations in an amount sufficient to cover the interest costs it incurs on funds borrowed from the Treasury. The act also does not require that fees assessed by the tobacco associations be used to fully reimburse CCC for losses incurred because of CCC's interest computation practices.

To illustrate the effects of compounding, we developed an example using the 1982 flue-cured crop. We estimated that during the first year (July 1982 - June 1983) the 1982 flue-cured tobacco crop was under loan, CCC charged the Stabilization Corporation's no net cost tobacco fund about $815,000 less in interest costs on that crop than it had to pay the Treasury. Furthermore, because of the effects of compounding, these interest costs will escalate rapidly. Our previous report, for example, covered the period through June 1984 and estimated that CCC would collect about $6 million less than it had to pay. We estimated about $10 million in additional losses during the next year. As table I.4 shows, we estimated that during the first 3 years (July 1982 - June 1985) the 1982 flue-cured tobacco crop is under loan, CCC will charge the Stabilization Corporation about $16 million less than it will pay the Treasury for the borrowed funds, increasing over 2-1/2 fold in the last year.

Table I.4

Interest Costs on the 1982 Flue-Cured Crop

Interest period	Interest computation date	Simple interest due at end of period	GAO computed additional interest due at end of period because of compounding	Cumulative additional interest due because of compounding	Total interest due at end of period[a]
July-Dec. 1982	Dec. 1982	$ 18,275,011	$ 0[b]	$ 0[b]	$ 18,275,011
Jan.-June 1983	June 1983	39,918,796	815,615[c]	815,615	40,734,411
July-Dec. 1983	Dec. 1983	63,077,376	1,950,780[c]	2,766,395	65,843,771
Jan.-June 1984	June 1984	76,743,711	3,283,161[c]	6,049,556	82,793,267
July-Dec. 1984	Dec. 1984	92,361,585	5,008,424[c]	11,057,980	103,419,565
Jan.-June 1985	June 1985	101,674,969	4,872,035[c]	15,930,015	117,604,984

[a]Column 3 plus column 5.

[b]Treasury compounds interest on January 1 and July 1 of each year. Because no loans were outstanding for crop year 1982 flue-cured tobacco on July 1, 1982, no compounding was computed at December 30, 1982.

[c]Formula for compounding is amount of interest due at the beginning of the period (A) times the prevailing interest rate (R) divided by the number of days in a year (X) times the number of days in the semiannual period (Y) equals the additional interest due because of semiannual compounding (I), or A(R/X)Y = I. Thus:

$$\$18{,}275{,}011 \times (.09/365) \times 181 = \$\ 815{,}615$$
$$\$40{,}734{,}411 \times (.095/365) \times 184 = \$1{,}950{,}780$$
$$\$65{,}843{,}771 \times (.10/365) \times 182 = \$3{,}283{,}161$$
$$\$82{,}793{,}267 \times (.12/365) \times 184 = \$5{,}008{,}424$$
$$\$103{,}419{,}565 \times (.095/365) \times 181 = \$4{,}872{,}035$$

Source: Developed by GAO on the basis of information obtained from USDA.

APPENDIX I

Additional uncollected interest will accrue as long as any part of the 1982 flue-cured tobacco crop remains under loan. We have not estimated this additional amount because any such estimate would have to be based on assumptions about several hard-to-predict factors, including interest rates and the length of time that the crop would remain under loan. In general, the shorter the time the crop is assumed to remain under loan and the lower the assumed interest rate, the lower the estimate of additional interest costs. For example, ASCS' Tobacco and Peanuts Division assumed that none of the 1982 flue-cured crop would remain under loan beyond 5 years and estimated a total of about $50 million in additional interest costs. USDA's Office of Inspector General assumed that portions of the 1982 flue-cured crop would be under loan for 8-1/2 years and that the interest rate charged would be 10 percent a year for the entire period. In a March 23, 1984, report,[8] the Office of Inspector General estimated that CCC would lose about $164 million in uncollected interest on the 1982 crop. Neither of these figures is directly comparable to our estimate of $16 million because our estimate is for interest costs occurring over only 3 years.

The Secretary of Agriculture, who is also CCC's Chairman, has the discretion, as authorized under the Agricultural Act of 1949, as amended (7 U.S.C. §1421 et seq.) and the Commodity Credit Corporation Charter Act (15 U.S.C. §714 et seq.), to adjust CCC interest computation procedures to collect the necessary funds to insure that the program is carried out at no net cost to the government. The Charter Act authorizes CCC to support the price of agricultural commodities through loans, purchases, payments, and other operations. The act allows CCC to determine the character of and the necessity for its obligations and expenditures and the manner in which they shall be incurred, allowed, and paid.

In a December 1, 1983, letter to Senator Thomas F. Eagleton, the Administrator, ASCS (who is also the Executive Vice President of CCC), provided the agency's position on the interest issue. He said that:

> ". . . We do not believe that the no net cost provisions of the 1982 Act require any change in the procedures which are utilized by the Corporation with respect to the charging of and crediting interest under the tobacco price support program. In our view, a substantive change in these procedures would fundamentally alter the structure of the tobacco price support program in a manner which is not contemplated by the provisions of the Act."

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[8] No Net Cost Tobacco Program, USDA Office of Inspector General Report No. 03099-67-At, Mar. 23, 1984.

Unless CCC changes its interest computation practices to include compound interest charges, program costs will continue to increase because CCC's procedures apply to all tobacco under loan, and similar interest costs will occur each crop year beginning in 1982 on each kind of tobacco under loan.

However, obtaining full recovery of interest costs by CCC might be a factor in producers' deciding not to participate in the program. Under the No Net Cost Tobacco Program, producers vote on continuance of the tobacco program in a referendum generally held every 3 years. According to the Deputy Director of ASCS' Tobacco and Peanuts Division, if the producers do not approve continuation of the program, the government would pay losses on any tobacco brought under loan in prior crop years unless producers vote in a subsequent referendum to reinstate the program.

In our February 1985 report on this issue, we recommended that, if the Congress wants to ensure no net costs, it should amend the No Net Cost Tobacco Program Act of 1982. The amendment should require that the amount of payments on principal and interest that tobacco producer associations pay to CCC on price-support loans equals the amount of payments on principal and interest that CCC pays the Treasury for borrowed funds. The Congress has not yet acted on this recommendation.

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