

GAO

Report to the Chairman, Committee on
Agriculture, House of Representatives

June 1989

FARMERS HOME
ADMINISTRATION

Implementation Issues
Concerning Four
Sections of the Food
Security Act



**Resources, Community, and
Economic Development Division**

B-232800

June 19, 1989

The Honorable E (Kika) de la Garza
Chairman, Committee on Agriculture
House of Representatives

Dear Mr. Chairman:

In a February 23, 1988, letter to us, the former Chairman, Subcommittee on Conservation, Credit, and Rural Development, House Committee on Agriculture, expressed concern about the Farmers Home Administration's (FmHA) apparent lack of progress in applying four provisions of the Food Security Act of 1985 designed to help financially distressed farmers with FmHA farm loans: (1) homestead protection, (2) disposition and leasing of farmland commonly referred to as "lease/buy-back," (3) conservation easement, and (4) softwood timber production. The former Chairman asked us to assess the extent to which these provisions are being applied, determine the reasons why they are not more widely used, and offer suggestions for modifying legislation and/or program regulations to help increase the opportunity for more financially stressed farmers to use the provisions. We have addressed this report to you because the former Chairman has retired and because of your continuing interest in FmHA issues.

We were limited in our ability to determine why some of the provisions were not more widely used because of the inadequacy of certain FmHA records. For example, FmHA did not maintain records on why borrowers are found to be ineligible for some of the provisions. Furthermore, we were unable to independently determine the volume of activity for the homestead protection and lease/buy-back provisions because of mis-coded activity reports. In February 1988 FmHA officials also cancelled the requirement that FmHA field offices report activity data on these two provisions until an automated reporting system, then being developed, became operational. Because of these data limitations, we cannot offer suggestions for increasing activity.

In August 1988 we briefed the former Chairman's office on the issues he raised as well as on other related issues that we identified during our review. This report summarizes and updates our briefing and presents matters for congressional consideration and recommendations to improve the implementation of the provisions.

Results in Brief

On the basis of the data available, we found that the four provisions have not been used extensively by distressed FmHA farm program borrowers. The homestead protection and lease/buy-back provisions have been used by several hundred former FmHA borrowers. An interim rule to implement various provisions of the Agricultural Credit Act of 1987, including conservation easement, was published on September 14, 1988, and only five borrowers—with 14 loans nationwide—have been approved for the softwood timber provision.

We identified several issues we believe the Congress and the Secretary of Agriculture should consider in assessing how the provisions are being implemented. For example, FmHA allows borrowers to use the same acreage to benefit from two U.S. Department of Agriculture (USDA) programs simultaneously. In this regard, we found two borrowers with approved softwood timber loans in consideration for planting trees on their land, and they will also receive an annual per-acre payment from USDA's Agricultural Stabilization and Conservation Service (ASCS) under its conservation reserve program involving the same trees on the same land. According to FmHA officials, they also intend to allow borrowers who receive debt forgiveness under FmHA's conservation easement provision to receive payments under ASCS' conservation reserve program. The law is silent on whether the Congress intended to provide benefits for the same land under these programs.

Our work also showed that FmHA charged interest rates for softwood timber loans, which were generally lower than the maximum permitted by the 1985 act, and calculated interest on softwood timber loans on a simple, rather than compound, interest basis. The use of lower interest and simple interest was contrary to the assumptions USDA used to conclude that the program was feasible. As a result, we calculated that at the end of the deferral period the government will receive about \$21.4 million less in interest revenues for the 14 approved softwood timber loans¹ than it would otherwise receive. To illustrate the significance of the potential reduction in interest revenues for the maximum number of acres that can be included in FmHA's softwood timber program, we calculated that the government—under certain assumptions—would receive over \$1 billion less in interest revenues than it would otherwise receive

¹At the conclusion of our audit work, three loans for one borrower had not yet been closed. Although FmHA intended to close these loans on January 19, 1989, it could not because of a problem with title to the land. The FmHA county supervisor assured us that the loans would be closed in the near future. As a result, for purposes of calculations shown in this report, we treat the loans as being closed as of January 19, 1989.

at the end of the deferral period if all allowable acreage (50,000 acres) was to be enrolled in the program.

Background

The Food Security Act of 1985, as amended by the Agricultural Credit Act of 1987, included two provisions—homestead protection and lease/buy-back—designed to assist qualified FmHA borrowers who lost their farms through foreclosure, voluntary conveyance, or bankruptcy proceedings, and two provisions—conservation easement and softwood timber—designed to assist FmHA borrowers who are at risk of losing their farms because of delinquent loans.

The homestead protection provision, which FmHA implemented in March 1986, authorized FmHA to permit former borrowers who had already lost their farms through foreclosure or voluntary conveyance to retain possession and occupancy of their principal residence, and a reasonable amount of land, through a lease with an option to purchase. To be eligible for the homestead protection provision, the borrowers must, among other things, have had gross annual farm revenue of at least \$40,000 in at least 2 calendar years during the 5-year period ending December 31, 1985. The Agricultural Credit Act of 1987 changed this revenue requirement to an amount reasonably commensurate with the size and location of the property for 2 of the last 6 years ending December 31, 1985.

The lease/buy-back provision, which FmHA implemented in April 1986, authorized FmHA to grant borrowers a lease with an option to purchase the farmland they had already lost through foreclosure or voluntary conveyance. The borrowers must demonstrate that they possess the financial resources, farm management skills, and experience to make a success of the farming operation. The Agricultural Credit Act modified this provision by giving previous land owners priority over current farm operators.

The conservation easement provision authorized FmHA to enter into agreements with borrowers who are delinquent on their farm loans to forgive the debt in exchange for an easement in real property. The easement, which would be for 50 years or more, would be for conservation, recreational, and wildlife purposes on farm property that is wetland, upland, or highly erodible land. The Agricultural Credit Act modified this provision by liberalizing the type of land that could qualify and the amount of debt that could be forgiven.

The softwood timber provision, which FmHA implemented in July 1987, allows borrowers who are delinquent on their farm loans to save their farms by replacing row crop or pasture land with softwood timber. Under the terms of this provision, borrowers must place not less than 50 acres of marginal land in softwood timber production. FmHA will then defer the principal and accrued interest owed on that land for up to 45 years. The Congress mandated that no more than 50,000 acres nationwide be placed in this program. To qualify for the softwood timber program, the land must secure a loan made or insured by FmHA and must have been previously used to produce an agricultural commodity or as a pasture. The total amount of debt secured by the land, including timber, may not exceed \$1,000 per acre. The Agricultural Credit Act made no changes to this provision.

FmHA published proposed regulations on May 23, 1988, to implement the Agricultural Credit Act's numerous provisions, including changes to the homestead protection, lease/buy-back, and conservation easement provisions. On the basis of the comments received, FmHA published on September 14, 1988, an interim rule, with an additional 60-day comment period. In effect, the interim rule allows FmHA to implement the Agricultural Credit Act's provisions, but it provides for other changes to be considered during the additional comment period. As of May 1, 1989, final regulations incorporating other changes resulting from the additional 60-day comment period had not been published.

Closely associated with the four provisions is ASCS' conservation reserve program. It permits owners and operators of farms and ranches to convert highly erodible cropland normally devoted to the production of an agricultural commodity to a less intensive use, such as tree production, for 10 to 15 years. Harvesting and the commercial sale of trees are prohibited during the contract period, unless they are expressly permitted in the contract. These owners and operators, in consideration, receive an annual rental payment to compensate them for the conversion of their land to a less intensive use.

Homestead Protection Provision

The FmHA Administrator reported that 49 homesteads were rented to former farm owners nationwide in fiscal year 1987, but we were unable to independently determine the volume of activity because of FmHA data problems. FmHA officials attributed the low activity level to the eligibility requirements—primarily one that requires borrowers to have had gross annual farm sales of at least \$40,000 in 2 of 5 previous calendar years. FmHA officials expect an increase in the use of this provision

because of changes made by the Agricultural Credit Act. (App. I provides further information about this provision.)

Lease/Buy-Back Provision

In March 1988, the FmHA Administrator reported that in fiscal year 1987 FmHA had 276 leases in effect and that purchases under this program totaled 108. Again, we were unable to independently determine the volume of activity because of FmHA data problems. Under provisions established by the Agricultural Credit Act, FmHA will notify former owners of property in FmHA's inventory of their right to apply for the lease/buy-back provision. (App. II provides further information about this provision.)

Conservation Easement Provision

According to FmHA officials, final conservation easement regulations under the Food Security Act were approved by USDA's Office of General Counsel and were within a few days of being issued when the Agricultural Credit Act was signed into law on January 6, 1988. FmHA officials told us that they were not required to implement this provision since the law states that the Secretary "may" initiate such a program. FmHA officials added that some of the delay in implementing the conservation easement provision resulted from FmHA choosing not to implement it because of the administrative complexity and debt forgiveness features of the provision; however, conservation groups were aware of the provision and were pushing for its implementation.

FmHA's intent, under the conservation easement provision, is to allow borrowers to participate simultaneously in the program as well as in ASCS' conservation reserve program. According to FmHA officials, the prospect of receiving benefits for the same land—an annual per-acre payment from ASCS and debt deferral or forgiveness from FmHA—will provide an incentive for borrowers to apply for the conservation easement program. (App. III provides further information about this provision.)

Softwood Timber Provision

The softwood timber program began with the Agricultural Programs Adjustment Act of 1984, which required the Secretary of Agriculture to report to the Congress on the feasibility of such a program and to submit a plan for its implementation. USDA completed the feasibility study in March 1985 and concluded that a softwood timber program was feasible, given certain assumptions.

For example, the future revenue from tree crop production was discounted to obtain a present value per acre, which was then compared with the present value per acre of the debt. Alternative rates of 5 percent and 10 percent were used to discount the future revenue. For each rate, consideration was then given to the debt accumulating interest at the same rate. If the present value of the future revenue exceeded the current debt level, then tree crop production was determined to be a feasible strategy for amortizing debt with interest on these debts accumulating at the specified rate.

Section 1254 of the Food Security Act, which amended section 608 of the Agricultural Programs Adjustment Act of 1984, provided generally that the softwood timber program be implemented pursuant to the recommendations contained in the feasibility study. However, section 1254 also gave the Secretary discretion to set the rate on softwood timber loans, up to a maximum of

“the current average yield on outstanding marketable obligations of the United States with periods to maturity comparable to the average maturities of such loans, plus not to exceed 1 percent, as determined by the Secretary and adjusted to the nearest one-eighth of 1 percent.”

As of June 1988 five borrowers had been approved for the softwood timber program. These borrowers had a total of 14 loans involving about 869 acres. Two of the five borrowers approved for FmHA's softwood timber program are also receiving annual payments from ASCS for having the same land in the conservation reserve program.

The FmHA Deputy Assistant Administrator for Farmer Programs stated that interest rates on softwood timber loans have been treated in the same manner as any other loans that are deferred, consolidated, rescheduled, or reamortized under the Consolidated Farm and Rural Development Act of 1961, as amended. Under this act, the interest rate on such loans is the lower of (1) the rate of interest on the original loan or (2) the rate being charged for loans of the same type at the time of the deferral, consolidation, rescheduling, or reamortization. As a result, a borrower would be given the lowest interest rate possible and there would be no compounding of interest.

The Consolidated Farm and Rural Development Act does not, in our view, prevent FmHA from setting interest rates on softwood timber loans at a rate consistent with the feasibility study. The rate-setting provision in the Consolidated Act, by its terms, applies to programs in that act; the

softwood timber program is part of another statute, the Agricultural Programs Adjustment Act of 1984. In addition, the softwood timber program has its own rate-setting provision, which gives the Secretary specific authority to set rates at his discretion. The softwood timber authorizing statute also permits that program to be implemented pursuant to the feasibility study, “Notwithstanding any other provision of law”

FmHA charged interest rates on the 14 loans that were generally below the maximum rate permitted by the Food Security Act of 1985—a rate equal to the cost of money to the government—and used simple, not compound, interest in its calculations. In analyzing how much the government would have received if the loans had been made at the higher rate and had been calculated on the basis of compound interest, we calculated a reduction of about \$21.4 million in interest revenues than it would otherwise receive.

If all of the allowable acreage (50,000 acres) were to be enrolled in the program and under the terms described above, we calculated that the potential reduction in interest revenues for the government would be substantial—perhaps over \$1 billion—compared with what it would otherwise receive.

Matters for Congressional Consideration

The law is silent on whether the Congress intended to provide benefits for the same land under (1) the softwood timber provision and the conservation reserve program and (2) the conservation easement provision and the conservation reserve program. Neither the Food Security Act of 1985 nor the Agricultural Credit Act of 1987 specifically allows or prohibits borrowers from receiving benefits from two USDA programs with regard to the same land. Further, our review of Comptroller General decisions and court rulings disclosed no similar situations where such benefits were specifically allowed or prohibited. We believe the Congress may wish to consider whether both benefits for the same land should be allowed under these programs.

Recommendations to the Secretary of Agriculture

Softwood timber loans provide borrowers with significant financial benefits—deferral of debt for up to 45 years and revenue from tree crop production. The softwood timber program was determined to be feasible because the revenue generated during the deferral period would be sufficient to cover both the government’s long-term borrowing cost and the

compounding of interest on the deferred debt. To ensure that the interest rates charged and computed by FmHA on softwood timber loans are consistent with the conditions under which the program was determined to be feasible, we recommend that the Secretary of Agriculture require the Administrator of FmHA to (1) approve future softwood timber loans at an interest rate that equals the average yield on marketable U.S. obligations with periods to maturity comparable to the average maturities of the softwood timber loans and (2) modify previous FmHA instructions governing the softwood timber program to require that interest on future softwood timber loans be computed on a compound, rather than simple, interest basis.

Agency Comments and Our Evaluation

The Secretary of Agriculture was given an opportunity to comment on a draft of this report. USDA's Under Secretary for Small Community and Rural Development commented that FmHA recognized our concerns regarding the softwood timber program. In this regard, he stated that FmHA's analysis of the program indicated that (1) it does not have the potential for use on a broad basis nationwide; (2) its use in assisting financially distressed farmers with high debt loads, without additional income or debt relief, has little chance for success; and (3) it is difficult to estimate feasibility with any degree of accuracy when the program is based on 45-year future projections. USDA added that there had been limited participation in the program even with the lower interest rates and the opportunity to receive some income through the conservation reserve program.

USDA also stated that the debt write-down provisions of the Agricultural Credit Act of 1987 provide permanent debt relief and give borrowers a more viable solution than the softwood timber program to overcome their financial difficulties. USDA concluded that on the basis of the limited participation in the program to date and the enactment of the Agricultural Credit Act, it anticipates that the program will be used less in the future, and it is unlikely that the 50,000 acres authorized by the legislation will be converted to softwood timber. If these assertions prove accurate, our calculations of the potential reduction in interest revenues for the government, as discussed in greater detail in appendix IV of this report, would certainly be lower.

USDA stated that FmHA contended that if the program is to be workable at all for financially stressed farmers, it must be continued as implemented. USDA also stated that the legislation gave the Secretary latitude in how the program could be implemented.

We recognize that participation in the program is already low and that changing the interest rates as we recommend could hamper further participation. As pointed out in this report, however, the legislation also provided that the program be implemented pursuant to the recommendations contained in the feasibility study—interest rates should reflect the cost of money to the government and be computed on a compound basis. Although the Secretary was given discretion to determine the interest rates up to a specified maximum, we continue to believe that providing lower interest rates and simple, not compound, interest is too great a departure from the conditions under which the program was determined to be feasible. Therefore, we have not modified our recommendations.

We agree, however, with USDA's position that the Agricultural Credit Act provides "permanent debt relief and gives borrowers a more viable solution to overcome their financial difficulties" compared with the debt deferral alternative offered under the softwood timber program. We also agree that the softwood timber program, which has had very limited participation through June 1988, will probably be used less in the future because of the Agricultural Credit Act's debt restructuring provisions. USDA's comments do raise questions about whether a need remains for the softwood timber program given the more recent debt restructuring provisions authorized under the Agricultural Credit Act of 1987. (USDA comments are reprinted in app. V.)

To make our assessment we reviewed the Food Security Act of 1985 (P.L. 99-198, Dec. 23, 1985) and the applicable implementing regulations, policies, and procedures. We also reviewed the Agricultural Credit Act of 1987 (P.L. 100-233, Jan. 6, 1988), which amended three of the provisions, and both the proposed regulations to implement the act (published by FmHA on May 23, 1988) and the interim rule, with a 60-day comment period, that was published on September 14, 1988, to determine what changes were made. We discussed each of the four provisions with FmHA farmer program officials in Washington, D.C.; at the FmHA's state office in Athens, Georgia; and at the county offices in Hartwell, Georgia, and Collins, Mississippi. Further, using FmHA's internal reports, we attempted to determine the extent the four provisions were being used as of June 30, 1988.

We reviewed the FmHA loan documentation associated with the five borrowers approved for the softwood timber program as of June 30, 1988, to determine how softwood timber loans had been written or were to be

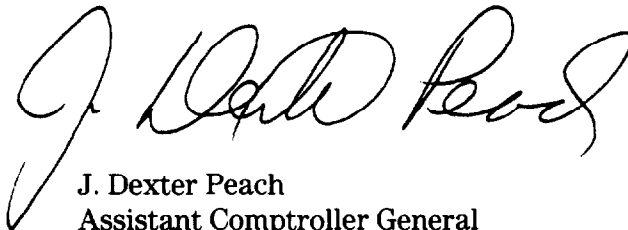
written. At FmHA's headquarters office we also determined whether borrowers participating in the softwood timber provision were also participating in ASCS' conservation reserve program. We searched Comptroller General decisions and court rulings for analogous situations in which such dual participation had been allowed or prohibited.

Our work was performed from March 1988 to January 1989 in accordance with generally accepted government auditing standards.

As arranged with your office, we are sending copies of this report to appropriate House and Senate committees; interested members of Congress; the Secretary of Agriculture; and the Director, Office of Management and Budget. Copies will also be made available to other interested parties who request them.

This work was done under the direction of John W. Harman, Director, Food and Agriculture Issues. Other major contributors to this report are listed in appendix VI.

Sincerely yours,



J. Dexter Peach
Assistant Comptroller General

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Abbreviations

ASCS	Agricultural Stabilization and Conservation Service
FmHA	Farmers Home Administration
GAO	General Accounting Office
SCS	Soil Conservation Service
USDA	U.S. Department of Agriculture

Homestead Protection Provision

Under the Food Security Act of 1985, the homestead protection provision authorized FmHA to permit former borrowers who have already lost their farms through foreclosure or voluntary conveyance to retain possession of their principal residence, and a reasonable amount of land, through a lease with an option to purchase. The act states that the period of occupancy of such homestead property is not to be less than 3 years or more than 5 years. FmHA grants the borrowers the right of first refusal to reacquire the homestead property at the end of occupancy on terms and conditions that FmHA determines. This provision was modified by the Agricultural Credit Act.

While occupying property, former borrowers must maintain it in good condition and pay rent substantially equivalent to rents charged for similar residential properties in the area. If borrowers do not pay the rent on time, they could lose their right to occupy the property. FmHA also requires applicants to occupy the dwelling as their residence and not own other suitable housing.

Eligibility Requirements

The act sets forth several eligibility requirements. To be eligible, FmHA borrowers were to apply for occupancy of the property by December 23, 1988, and were to have exhausted all other remedies for loan extension or restructuring. Borrowers were to have had gross annual farm sales of at least \$40,000 in at least 2 calendar years during the 5-year period between January 1, 1981, and December 31, 1985, and to have received at least 60 percent of their combined gross annual income from the farming operation during at least 2 years of this 5-year period. In addition to these financial requirements, borrowers must have occupied the homestead property and been engaged in a farming or ranching operation during the same 5-year period and must have been released from financial liability for all FmHA debts. The Agricultural Credit Act modified these requirements.

Modifications by the Agricultural Credit Act of 1987

The Agricultural Credit Act of 1987 modified the homestead protection provision in several ways. It redefined "homestead property" to include a reasonable number of farm outbuildings on the adjoining land and up to 10 acres of adjoining land used to maintain the family. In addition, for property acquired by FmHA, the act requires borrowers to apply for occupancy within 90 days. There is no longer a December 23, 1988, expiration date for applying.

The 1987 amendments also changed the farm revenue requirement from \$40,000 of gross annual sales for 2 of the last 5 years to revenue that is reasonably commensurate with the size and location of the property for 2 of the last 6 years. The act further stipulates that borrowers and their spouses must have received at least 60 percent of their combined annual income from farming in at least 2 of the last 6 years. The occupancy requirement was also changed from borrowers' occupying or controlling the property for 5 years to having continuously occupied the property for the last 6 years, with the provision that this requirement can be waived if borrowers left the property for 12 months or less.

Finally, the act allows FmHA to enter into homestead protection agreements with owners who have (1) agreed to voluntarily liquidate or convey property to FmHA or (2) entered into bankruptcy resulting in property being conveyed to FmHA. The Food Security Act of 1985 required that applicants had to have been released from financial liability for all FmHA debts. Upon passage of the Agricultural Credit Act, FmHA notified all previous owners of farms in FmHA's inventory of their right to apply for the homestead protection option, according to USDA's Undersecretary for Small Community and Rural Development. The FmHA Deputy Assistant Administrator for Farmer Programs told us that FmHA was continuing to approve homestead protection agreements for former owners who can qualify under the guidelines established by the Food Security Act of 1985—the expiration date was December 23, 1988. For those borrowers who cannot qualify, he advised that they could reapply under the Agricultural Credit Act, since it liberalized the qualification requirements.

Status of the Provision

The Food Security Act of 1985 was enacted on December 23, 1985, and FmHA officials implemented the homestead protection provision in March 1986. According to FmHA's Assistant Administrator for Farmer Programs, since the homestead protection provision applies only to borrowers indebted during the 5-year period beginning January 1, 1981, and ending December 31, 1985, the provision had to be implemented as quickly as possible. In March 1988, the FmHA Administrator reported to the Subcommittee on Rural Development, Agriculture, and Related Agencies, House Committee on Appropriations, that during fiscal year 1987, 49 homesteads were rented to former owners of farms. FmHA data problems precluded us from independently determining the volume of activity.

The reason cited by FmHA officials for the low number of approvals was that most applicants did not meet the eligibility requirements of the Food Security Act of 1985. The one eligibility requirement cited most often as limiting the number of applicants was that the former borrower must have had a gross annual farm income of at least \$40,000 in at least 2 of the 5 years ending December 31, 1985. The Agricultural Credit Act modified this requirement, and FmHA's Chief, Direct Loans Branch, Loan Servicing and Property Management Division, expects an increase in homestead protection applications, resulting in more approvals, under the act's implementation.

Lease/Buy-Back Provision

Under the Food Security Act of 1985, the lease/buy-back provision authorized FmHA to grant leases to borrowers with an option to purchase farmland that had been taken into custody by FmHA after the borrowers abandoned it. The act required FmHA to sell, or lease with the option to purchase, such farmland to current operators of farms not larger than "family-size." In leasing such farmland, FmHA was to give special consideration to the previous owner or operator. FmHA is to offer farmland for sale at a price that reflects the average annual income that may be reasonably anticipated to be generated from farming such land. The lease/buy-back provision was modified by the Agricultural Credit Act.

The Food Security Act of 1985 requires that if two or more equally qualified operators desire to purchase or lease such land, the appropriate county committee is to select the operator to whom the land will be sold or leased.

Eligibility Requirements

Under the Food Security Act, FmHA required that the previous owners or operators of the property be given the first opportunity to lease it, with or without the option to purchase. The previous owners or operators had 30 days, after notification of the availability of the property for lease, to contact the FmHA county office. Further, they must have had the financial resources, farm management skills, and experience sufficient to ensure a reasonable prospect of success in the proposed farming operation.

Modifications by the Agricultural Credit Act of 1987

The Agricultural Credit Act of 1987 modified the Food Security Act by establishing a priority order for leasing or purchasing the farmland. It gave the previous land owners and their spouses or children a higher priority for leasing or purchasing the farmland than the current family-sized operator. The act requires other priorities and finally establishes farm operators of not larger than family-size farms as the last priority.

The Agricultural Credit Act also established a 180-day period, beginning on the date of acquisition of the real property by FmHA, to allow the former borrower to purchase or lease such property. Previously, FmHA's instructions required that, if interested, the previous owner or operator should contact FmHA within 30 days after notification of the availability of the property.

Status of the Provision

In April 1986 FmHA implemented the lease/buy-back provision of the Food Security Act of 1985. During April 1988 hearings before the Subcommittee on Conservation, Credit, and Rural Development, House Committee on Agriculture, Congressman Gunderson expressed concerns about giving owners the right of first refusal and stated that this provision has become controversial in his area. The Administrator of FmHA replied that FmHA has to give preference to the previous owner, stating that "it is in the law, you gave us no other choice."

Upon implementation of the Agricultural Credit Act, former owners of property in FmHA's inventory, who had not been previously considered for lease/buy-back, are to be notified of their right to such consideration. The final day for them to exercise their rights to lease or purchase the property is 180 days after FmHA acquires the property. FmHA will not renotify those former owners or operators who were previously considered and turned down for lease/buy-back under the terms of the Food Security Act of 1985.

The FmHA Administrator reported in March 1988 to the Subcommittee on Rural Development, Agriculture, and Related Agencies, House Committee on Appropriations, that as of the end of fiscal year 1987, FmHA had 276 leases in effect, and purchases totaled 108. We were unable to independently determine the volume of activity because of FmHA data problems. Furthermore, an FmHA Administrative Notice dated February 26, 1988, cancelled the requirement that field offices report on such activity in the future. FmHA is developing an automated reporting system that will become operational with the implementation of the Agricultural Credit Act, according to FmHA officials.

Conservation Easement Provision

Under the Food Security Act of 1985, the conservation easement provision authorized FmHA to acquire the right for public use of the property of a qualified borrower for not less than 50 years for conservation, recreational, and wildlife purposes on farm property that is wetland, upland, or highly erodible land. The easement acquired by FmHA is to be purchased from the borrower by cancelling that part of all outstanding FmHA loans of the borrower at the same ratio as the number of acres of easement property is to the total number of acres securing such loans. However, the amount so cancelled cannot exceed the value of the land on which the easement is acquired. This provision was modified by the Agricultural Credit Act.

FmHA must consult with the Director of the Fish and Wildlife Service in selecting the property to be acquired for easements, formulating the terms and conditions of such easements, and enforcing the easements. The terms and conditions of the easement will specify the purposes for which the farm property is to be used, identify the conservation measure(s) to be taken, and state the recreational and wildlife uses that are to be allowed. Some similarities exist between this provision's objectives and those of the ASCS' conservation reserve program, which was also created by the Food Security Act.

Eligibility Requirements

Under the Food Security Act, to be eligible for the conservation easement provision, the borrower must be unable to repay an FmHA loan on time and is required to permit FmHA and any person or governmental entity designated by FmHA access to the easement property for enforcing the easement and monitoring compliance. Except in the case of wetland, the land must have been row-cropped each year of the 3-year period ending December 23, 1985. The land must also be secured by an FmHA loan and be suitable for conservation, recreational, and wildlife purposes.

Modifications by the Agricultural Credit Act of 1987

The Agricultural Credit Act of 1987 modified the conservation easement provision in two ways. First, it exempted "other wildlife habitat" from the 3-year row-cropping requirement. In addition, the restriction on the maximum dollar amount to be cancelled for an easement was to be the higher of the value of the easement land or the difference between the amount of the outstanding loan secured by the land and the current value of the easement land.

Status of the Provision

As of September 1, 1988, the conservation easement provision had not yet been implemented. An FmHA Environmental Protection Specialist told us that the final easement regulations were approved by USDA's Office of General Counsel and were within 3 days of being issued when the Agricultural Credit Act was signed into law on January 6, 1988. FmHA had to return to the regulation writing stage because this act modified the conservation easement provision. According to FmHA officials, the conservation easement was an optional program, as the law stated that the Secretary "may" initiate such a program. FmHA officials added that FmHA initially chose not to implement this provision because of the administrative complexity and debt forgiveness feature of the program; however, conservation groups were aware of the program and were pushing for its implementation.

FmHA held several meetings with the Agricultural Conservation Coalition, which includes the American Farmland Trust and the Sierra Club, to discuss the implementation of the conservation easement program, and FmHA drafted the implementing regulations with the coalition's help. FmHA invited members of the coalition to participate in a model easement review program in Mississippi and Ohio that used farmland previously acquired by FmHA.

On September 14, 1988, FmHA published an interim rule, with a 60-day comment period, to implement various provisions of the Agricultural Credit Act, including conservation easement.

Use of Private Conservation Groups

The regulations for implementing the conservation easement provision allow such entities as nonprofit conservation organizations to be used by FmHA as easement enforcement authorities, but only if a federal, state, or county agency is unwilling, or unable, to do so for selected easements. As such, they would be responsible for monitoring compliance with the easement's terms, conditions, and management plan. The enforcement authority must also agree, among other things, to ensure that the easement property is safely maintained and accept all liabilities associated with implementing and carrying out its management responsibilities. In addition, the enforcement authority must agree to submit periodic reports on the status of the compliance with the easement's terms and conditions.

The order of priority by which FmHA is to select enforcement authorities will be federal agencies, state agencies, local agencies, and then nonprofit organizations. Should more than one federal agency be interested,

the one whose mission most closely matches the type of easement will be chosen. According to FmHA officials, nonprofit organizations would receive the lowest priority partly because they are more risky—they can have a short lifetime and they may not be around in 50 years.

FmHA selects the enforcement authority, whether a private nonprofit organization or a governmental unit, after studying fully a proposed conservation easement. After an FmHA borrower and the FmHA county supervisor agree that a conservation agreement is the best solution to the borrower's financial problems, the county supervisor will establish an easement review team composed of officials of the Soil Conservation Service (SCS), U.S. Fish and Wildlife Service, state Fish and Wildlife agencies, National Park Service, Forest Service, and any other entities, including nonprofit organizations, that may be interested in serving as an enforcement authority for an easement. Other groups, such as the local rod and gun club, will have to inform FmHA of their interest to be included on the list for a particular area.

The review team will have up to 45 days to perform its easement study and submit a report of its findings to the county supervisor. The items addressed in the review team's report include the amount of land, if any, that is wetland, wildlife habitat, upland, or highly erodible, and the approximate boundaries of each type of land. The report will also contain a finding of whether the land is suitable for conservation, recreation, and/or wildlife habitat purposes and a priority ranking of purposes, if the land can be so classified and ranked. If appropriate, any special terms or conditions that would need to be placed on the easement will be addressed in the report. The report will also contain a proposed management plan consistent with the purpose(s) for which the easement would be established, recommend the time limitation of the easement, and include the name of the qualified entity that is willing to be assigned as the enforcement authority for the easement.

Simultaneous Participation in FmHA's Conservation Easement and ASCS' Conservation Reserve Program

FmHA's regulations do not prohibit land being considered for FmHA's conservation easement program from participating in ASCS' conservation reserve program, or vice versa. An FmHA official told us that borrowers in the conservation reserve program do not automatically qualify for FmHA's conservation easement provision, but that a borrower can participate in both programs at the same time. Such participation may provide an incentive for borrowers to get into the easement program, according to FmHA officials.

FmHA did not publish the interim rule to implement the various provisions of the Agricultural Credit Act, including conservation easement, until September 14, 1988. Because the conservation easement rules were not in effect at the time we completed our field work, we found no examples of participation in both programs that had actually occurred.

Softwood Timber Provision

Under the Food Security Act of 1985, the softwood timber provision authorized FmHA to reamortize a distressed farmer program loan with the use of future revenues produced from planting softwood timber crops. All, or a portion, of the payments on the reamortized loan will be deferred until the softwood timber crop produces revenue, or for a term of up to 45 years, whichever comes first. However, repayment of such reamortized loan shall be made not later than 50 years after the date of reamortization. This provision was not modified by the Agricultural Credit Act.

FmHA and other USDA sources may further assist borrowers by making loans to them for tree planting on land placed in the program. These loans must be secured by the land, including timber, on which the trees are planted. The basic objectives of this provision are to assist eligible FmHA borrowers to develop a positive cash flow and to improve their financial conditions, so they can repay their outstanding FmHA debts in an orderly manner, carry on feasible farming operations, and take marginal land, including highly erodible land, out of the production of other agricultural commodities.

Eligibility Requirements

To qualify for the softwood timber program, the land must have been previously used to produce an agricultural commodity or as a pasture and must have been used to secure a loan made or insured by FmHA. The total amount of debt secured by the land, including timber, may not exceed \$1,000 per acre, and the minimum amount of land that can be placed in softwood timber can be no less than 50 acres of marginal land that SCS determines to be suitable for growing trees. The land, including timber, may not have any lien against it other than a lien for a loan made or insured by FmHA. The Congress mandated that no more than 50,000 acres nationwide may be placed in this program.

Borrowers must be reliable, industrious, and have necessary debt repayment and managerial abilities to carry out the proposed operation. They must also have sufficient training or farming experience to ensure reasonable prospects of success in the proposed operation. Any other FmHA loans must be made current through servicing actions such as rescheduling, reamortizing, consolidating, or deferring before the softwood timber notes are signed. Borrowers must also be able to obtain sufficient money through FmHA or other sources for planting, caring for, and harvesting of the softwood timber trees.

Status of the Provision

The softwood timber program began with the Agricultural Programs Adjustment Act of 1984 which required the Secretary of Agriculture to report to the Congress on the feasibility of such a program and to submit a plan for its implementation. USDA completed the feasibility study in March 1985 and concluded that a softwood timber program was feasible, given certain assumptions.

For example, the future revenue from tree crop production was discounted to obtain a present value per acre, which was then compared with the present value per acre of the debt. Alternative rates of 5 percent and 10 percent were used to discount the future revenue. For each rate, consideration was then given to the debt accumulating interest at the same rate. If the present value of the future revenue exceeded the current debt level, tree crop production was determined to be a feasible strategy for amortizing debt with interest on these debts accumulating at the specified rate.

Section 1254 of the Food Security Act, which amended section 608 of the Agricultural Programs Adjustment Act of 1984, provided generally that the softwood timber program be implemented pursuant to the recommendations contained in the feasibility study. However, it also gave the Secretary authority to determine the interest rate on loans, up to a specified maximum, as we mention later in this appendix.

Final regulations implementing the softwood timber provision were issued July 13, 1987. Regarding the feasibility of the softwood timber program, the final regulations stated that

“... under the assumption of high prices, 5% inflation rate and final harvest at 45 years, the future revenue discounted at 10% has a present value of \$882 per acre. This is interpreted to mean that up to \$882 of debt could be amortized at a compound interest rate of 10%. The results do not include any appreciation in land value.”

A total of five applications for the softwood timber program had been approved as of June 30, 1988. Applications were approved for two farmers in Mississippi and a farmer each in Alabama, Wisconsin, and Vermont. In total, 869 acres have been used for the softwood timber provision out of a total of 50,000 allowable acres. Of the five approved applications, only three borrowers had their loans closed prior to

June 30, 1988—one closed in July 1988, and the other one had not closed as of January 31, 1989.¹

Simultaneous Participation in FmHA's Softwood Timber and ASCS' Conservation Reserve Program

Two of the five borrowers approved for FmHA's softwood timber program are also receiving annual payments from ASCS for having the same land under the conservation reserve program. ASCS' conservation reserve program permits owners and operators of farms and ranches to convert highly erodible cropland, normally devoted to the production of an agricultural commodity, to a less intensive use, such as trees, for 10 to 15 years. These owners and operators, in consideration, receive an annual rental payment to compensate for the conversion of their land to a less intensive use. Harvesting and the commercial sale of trees are prohibited during the contract period, unless expressly permitted in the contract.

The Food Security Act of 1985 does not specifically allow or prohibit a distressed borrower from simultaneously participating in FmHA's softwood timber program and ASCS' conservation reserve program. A May 2, 1988, FmHA Administrative Notice states that borrowers should be encouraged to use existing ASCS cost-sharing programs for forestry purposes such as for planting, caring for, and harvesting of softwood timber trees and that borrowers can use the conservation reserve program and FmHA's softwood timber loan program on the same land, if they meet the requirements of both programs. The stated purpose of this notice was to clarify that softwood timber can be produced on the same land that is both in ASCS' conservation reserve program and FmHA's softwood timber program.

FmHA's Deputy Assistant Administrator for Farmer Programs told us that the same marginal farmland can be used for both programs at the same time allowing the distressed borrower to receive an annual income from ASCS while having distressed loans deferred up to 45 years by FmHA. For example, one of the five FmHA borrowers approved for the softwood timber program will receive \$7,304 per year for 10 years, or a total of \$73,040, from ASCS' conservation reserve program. This same borrower will also receive an FmHA deferral on softwood timber loans totaling about \$182,000 for the same farmland.

¹At the conclusion of our audit work, three loans for one borrower had not yet been closed. Although FmHA intended to close these loans on January 19, 1989, it could not because of a problem with the title. The FmHA county supervisor assured us that the loans will be closed in the near future. As a result, for purposes of calculations shown in this report, we treat the loans as being closed as of January 19, 1989.

Questionable Interest Charged on Softwood Timber Loans

FmHA's Deputy Assistant Administrator for Farmer Programs stated that interest rates on softwood timber loans have been treated in the same manner as any other loans that are deferred, consolidated, rescheduled, or reamortized under the Consolidated Farm and Rural Development Act of 1961, as amended. Under this act, the interest rate on such loans is the lower of (1) the rate of interest on the original loan or (2) the rate being charged for loans of the same type at the time of the deferral, consolidation, rescheduling, or reamortization.

The Consolidated Farm and Rural Development Act does not, in our view, prevent FmHA from setting interest rates on softwood timber loans at a rate consistent with the feasibility study. The rate-setting provision in the Consolidated Act, by its terms, applies to programs in that act; the softwood timber program is part of another statute, the Agricultural Programs Adjustment Act of 1984. In addition, the softwood timber program has its own rate-setting provision, which gives the Secretary specific authority to set rates at his discretion.

Section 608(a)(1) of the Agricultural Programs Adjustment Act also states

“Notwithstanding any other provision of law, the Secretary of Agriculture . . . may implement a program, pursuant to the recommendations contained in the study mandated by section 608 of the Agricultural Programs Adjustment Act of 1984 (7 U.S.C. 1421 note), under which a distressed loan (as determined by the Secretary) made or insured under the Consolidated Farm and Rural Development Act (7 U.S.C. 1921 *et seq.*), or a portion thereof, may be reamortized with the use of future revenue produced from the planting of softwood timber crops on marginal land”

FmHA charged interest rates on the limited number of softwood timber loans that were generally lower than the cost of money to the government and has computed interest on the simple, rather than the compound, basis. As a result, we calculated that the government will receive at the end of the deferral period about \$21.4 million less in interest revenues for the 14 softwood timber loans than it would otherwise receive. To illustrate the significance of the potential reduction in interest revenues for the maximum number of acres that can be included in FmHA's softwood timber program, we calculated that the government—under certain assumptions—would receive at the end of the 45-year deferral period over \$1 billion less in interest revenues than it would otherwise receive if all allowable acreage (50,000 acres) were to be enrolled in the program. In its comments on a draft of this report (see app. V), however, USDA (1) anticipated that the program will be used less in the future and

(2) indicated that it is unlikely the 50,000 acres authorized will be converted to softwood timber. If these assertions prove accurate, our calculations would certainly be lower.

Interest Rates Lower Than Those Permitted by the Food Security Act

FmHA has charged interest rates on the 14 softwood timber loans that are generally below the rate that the feasibility study assumed would be charged and that the law permits. USDA's March 1985 feasibility study recommended that the interest rates on reamortized softwood timber loans be equal to the Treasury's long-term cost of borrowing. The Food Security Act of 1985 states that the softwood timber provision be implemented pursuant to the feasibility study. However, the act further states that the Secretary of Agriculture may determine the interest rate on reamortized softwood timber loans but that the rate will not exceed the current average yield on marketable U.S. obligations with periods to maturity comparable to the average maturities of the softwood timber loans, plus not to exceed 1 percent, adjusted to the nearest one-eighth of 1 percent.

In March 1987 FmHA instructed its field offices to charge an interest rate of 8.25 percent on the softwood timber loans they approved. According to FmHA officials, this interest rate represented the average yield on marketable obligations at the time FmHA's instruction was circulated. But the instruction further required the field offices to charge the rate of interest of the original reamortized loan, if lower than 8.25 percent. As a result, 9 of the 14 softwood timber loans approved as of January 1989 were written at interest rates lower than 8.25 percent. Two loans were correctly made at the 8.25-percent rate, two loans were erroneously made at a 10-percent rate (because the county supervisor misread the instruction), and one loan that we assumed was closed in January 1989 would be written at 9.50 percent—the rate permitted at that time.

The 14 softwood timber loans cover about 869 acres. As shown in table IV.1, the interest rate FmHA charged on these loans ranged from 3 percent to 10 percent, for an average rate of about 6.3 percent. Given those rates, and assuming (1) a 45-year deferral period with no interim payments—because 4 of the 14 loans were written with only a 19-year deferral period, our calculations for these 4 loans are based on the 19-year deferral period—and (2) interest computed on a simple basis—as has been the practice of FmHA—the government will collect \$1,814,397 in interest revenues at the end of the deferral period. If FmHA had charged the rate permitted that was in effect at the time the loans were

**Appendix IV
Softwood Timber Provision**

closed, which it had established as the average yield on the government's marketable obligations, we calculated that the government would collect \$2,432,539 in interest revenues, or about \$618,000 more.

Table IV.1: GAO Calculation of Reduced Government Interest Revenues Resulting From FmHA Using Interest Rates Lower Than Those Permitted by the Food Security Act of 1985 on Softwood Timber Loans Approved as of January 1989

Figures in percent

Borrower	Reamortized loan			Deferred loan			Total GAO-calculated interest revenue	Reduced interest revenues to the government
	Outstanding principal and capitalized interest	Original interest rate	Rate charged by FmHA	Total FmHA interest revenue	Rate permitted by the act	Total FmHA interest revenue		
A	\$28,776	3	3	\$38,856	8.25	\$106,855	\$67,999	
	67,900	5	5	152,810	8.25	252,136	99,326	
B	73,476	5.25	10	338,000	8.25	278,850	(59,150)	
	6,524	5.25	10	30,011	8.25	24,759	(5,252)	
C ^a	41,351	5	5	39,053	8.25	64,437	25,384	
	36,800	3	3	20,853	8.25	57,345	36,492	
	29,501	3	3	16,717	8.25	45,971	29,254	
	133,887	5	5	126,446	8.25	208,636	82,190	
D	81,602	5	5	181,368	8.25	299,256	117,888	
	54,497	8.50	8.25	199,855	8.25	199,855	0	
	32,000	8.50	8.25	117,353	8.25	117,353	0	
E ^b	81,823	8	8	294,200	9.50	349,362	55,162	
	11,780	11.25	9.50	50,297	9.50	50,297	0	
	88,396	5.25	5.25	208,578	9.50	377,427	168,849	
Total	\$768,313			\$1,814,397		\$2,432,539	\$618,142	
Average FmHA interest rate			6.30 percent					

Note: Dollar amounts are rounded to the nearest whole dollar.

^aBorrower C's loans were deferred for only 19 years since after that time he will be able to make periodic payments.

^bBorrower E's loans, although approved, had not been closed as of January 31, 1989. Because the rate permitted had increased to 9.50 percent at that time, our calculations assume that this rate was applicable for the three loans and that they were closed in January 1989.

The potential impact for reduced interest revenue becomes much greater when—using certain assumptions—it is projected to the total volume of possible softwood timber loans that could be made by FmHA. Using the following assumptions, which are derived from our analysis of the 14 loans in table IV.1, the government would receive about \$38.8 million less in interest revenues than it would otherwise receive at the end of the 45-year period, if all allowable acreage (50,000 acres) were to be enrolled in the program. The assumptions are

-
- \$884 per acre of outstanding principal and capitalized interest (the total outstanding principal and capitalized interest of \$768,313 for the 5 borrowers divided by the 869 acres covered by the 14 loans);
 - interest rates of 6.30 percent (the average rate charged the five approved borrowers) versus the 8.25 percent rate (even though 9.50 percent was the rate permitted for the the three loans that we assumed were closed in January 1989, for ease of presentation we used only the 8.25 percent interest rate in our calculations for the 50,000 acres);
 - a 45-year deferral period with no interim payments (although 4 of the 14 loans had a 19-year deferral period, our assumptions are based on the 45-year maximum deferral period); and
 - interest computed on a simple basis.

The high interest calculation is $\$884 \times 50,000 \text{ acres} \times 8.25 \text{ percent} \times 45 \text{ years} = \$164,092,500$. On the other hand, the low interest calculation is $\$884 \times 50,000 \text{ acres} \times 6.30 \text{ percent} \times 45 \text{ years} = \$125,307,000$. At the end of 45 years, the difference between the two interest rates is \$38,785,500.

Compound Versus Simple Interest

FmHA calculated simple interest on the approved softwood timber loans over the deferral periods, rather than compounding the interest as contemplated by the feasibility study. The Food Security Act of 1985 gives the Secretary of Agriculture authority to prescribe terms and conditions for loans under the softwood timber program but also provides that the program be implemented pursuant to the recommendations contained in the March 1985 feasibility study. The study concluded that the softwood timber program would be feasible using compound interest computations and recommended that the program be limited to debt levels that could be amortized without a federal subsidy.

In commenting on FmHA's normal practice of subsidizing its borrowers for up to 5 years during periods of delinquency or deferral, and the propriety of applying this practice to long-term softwood timber loan deferrals, the feasibility study states that

"No interest is charged on interest during these periods, which provides a subsidy to the extent of the Government's cost of borrowing to finance the delinquency or deferral of interest payments."

The study further states that

“The subsidy feature of these policies, however, is relatively short-term in nature. To apply them to the long-term deferral of all interest and principal payments, as would be required in a program to amortize debts from tree crop production, would be considerably more costly to the Government. At current interest rates, the cost of borrowing to cover the deferral of interest for 45 years would be several times larger than the amount of principal involved. Further, such a policy would be highly inequitable because of the limited number of borrowers who might be able to participate in such a program.”

Notwithstanding the recommendations of the feasibility study, and the provision in the law that the softwood timber program be implemented pursuant to those recommendations, an FmHA instruction to its field offices provides for interest to be calculated on the simple, rather than compound, basis. The FmHA Deputy Assistant Administrator for Farmer Programs confirmed that all of the softwood timber loans closed for the five borrowers complied with these instructions and were written using simple interest.

We calculated that the government will receive at the end of the deferral period about \$12.9 million less in interest revenue from the five borrowers than it otherwise would have. In addition, if this situation is left unchanged and if all 50,000 acres were to be included in the program, the potential exists—under certain assumptions—for the government to receive at the end of the deferral period over \$500 million less in interest revenues than it otherwise would have received. This compound interest calculation is $\$884 \times 50,000 \text{ acres} \times 6.30 \text{ percent compounded for 45 years} = \$690,906,330$. On the other hand, the simple interest calculation is $\$884 \times 50,000 \text{ acres} \times 6.30 \text{ percent} \times 45 \text{ years} = \$125,307,000$. At the end of the 45 years, the difference between simple and compound interest is \$565,599,330.

Combined Effects of Low Interest and Simple Interest

The two previous sections disclosed the effects of FmHA's using interest rates lower than the government's cost of borrowing and of using simple, rather than compound, interest during the deferral period for softwood timber loans. When these effects are combined, we calculate that there is about a \$21.4 million difference in interest revenue the government would collect at the end of the deferral period from the 14 loans.

By using the same assumptions mentioned in the previous sections, the government would, in 45 years, receive about \$1.4 billion less in interest revenue than it would otherwise receive, if all allowable acreage (50,000 acres) were to be enrolled in the program, because of the combined

effect of lower interest and simple interest compared with higher interest and compound interest. Because all of our calculations are sensitive to changes in the variables used, such as the per-acre value of outstanding principal and capitalized interest and the interest rate applied, we have provided, in table IV.2, a sensitivity analysis showing the potential amount of reduced interest revenues at the end of the 45-year deferral period if loans were closed at various simple interest rates rather than at the compounded 8.25 percent interest rate.

Table IV.2: GAO Calculation of Reduced Government Interest Revenues, for Selected Scenarios, Resulting From the Combined Effect of Low Interest and Simple Interest Compared With Higher Interest and Compound Interest

Per-acre value of outstanding principal and capitalized interest	Maximum total loan amount based on 50,000 acres	Simple interest rate		
		Dollars in billions		
		6.30 percent ^a	7 percent ^a	8.25 percent ^a
\$1,000	\$50,000,000	\$1.580	\$1.564	\$1.535
884	44,200,000	1.396	1.382	1.356
750	37,500,000	1.184	1.173	1.152
620	31,000,000	.979	.969	.952

^aThe numbers in these columns represent the amounts by which interest revenues would be reduced as compared with a scenario involving an 8.25 percent interest rate that was compounded over 45 years.

As pointed out in table IV.2, if the \$884 per acre value is used with the 6.30-percent interest rate, the combined effect in 45 years is about \$1.4 billion. However, the combined effect could be nearly \$1.6 billion if the \$1,000 per acre value is used with a 6.30-percent interest rate or \$952 million if the \$620 per acre value is used with an 8.25-percent interest rate. Regardless of the assumptions used, the potential impacts are substantial.

Comments From the Under Secretary for Small Community and Rural Development, USDA



United States
Department of
Agriculture

Farmers
Home
Administration

Washington
D.C.
20250

APR 24 1989

SUBJECT: GAO Proposed Report Entitled "FmHA Implementation Problems with Certain Provisions of the Food Security Act of 1985"

TO: John W. Harman
Director
Food and Agriculture Issues
General Accounting Office

ATTN: John Hunt

THROUGH: Roland R. Vautour
Under Secretary
Small Community and Rural Development

Neal Sox Johnson
Acting Administrator
Farmers Home Administration

Attached is a copy of the response from the Deputy Administrator for Program Operations referencing the subject draft report.

If we can be of further assistance, please contact Doris Morgan of my staff at FTS: 475-5318.

LEONARD HARDY JR.
Director
Planning and Analysis Staff

Attachment



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**Appendix V
Comments From the Under Secretary for
Small Community and Rural
Development, USDA**



United States
Department of
Agriculture

Farmers
Home
Administration

Washington
D.C.
20250

APR 24 1989

■
SUBJECT: GAO Proposed Report Entitled "FmHA Implementation Problems with Certain Provisions of the Food Security Act of 1985"

TO: Leonard Hardy, Jr.
Director
Planning and Analysis Staff

This is in response to your memorandum dated March 12, 1989, concerning the General Accounting Office (GAO) draft report on the above subject.

REASON FOR THE REPORT

The GAO report is the result of a request from the former Chairman, Subcommittee of Conservation, Credit and Rural Development, House Committee on Agriculture, to determine the reasons why certain provisions of the Act are not more widely used, and/or programs regulations to help increase an opportunity for more financially stressed farmers to use the provisions.

The programs reviewed were as follows:

- (1) Homestead protection.
- (2) Disposition and leasing of farmland commonly referred to as leaseback/buyback.
- (3) Conservation easement.
- (4) Softwood timber production.

GAO made no recommendations on the homestead protection, leaseback/buyback, or conservation easement programs. The report raised an issue for Congressional consideration of the regulatory permitted practice of simultaneous participation by a FmHA borrower in softwood timber (ST) and the Agricultural Stabilization and Conservation Service, conservation reserve program. In addition, a recommendation was made by GAO concerning the interest rate changed by FmHA and the compounding of interest on (ST) loans. The following responds to the issue for congressional consideration and the GAO recommendation to the Secretary.



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**Appendix V
Comments From the Under Secretary for
Small Community and Rural
Development, USDA**

GAO RECOMMENDATION FOR CONGRESSIONAL CONSIDERATION

The law is silent on whether the Congress intended to provide benefits for the same land under (1) the softwood timber provision and the conservation reserve program and (2) the conservation easement provision and the conservation reserve program. Neither the Food Security Act of 1985 nor the Agricultural Credit Act of 1987 specifically allows or prohibits borrowers from receiving benefits from the two USDA programs with regard to the same land. Further, our review of the Comptroller General decisions and court rulings disclosed no similar situations where such benefits were specifically allowed or prohibited. We believe the Congress may wish to consider whether both benefits, for the same land, should be allowed under these programs.

GAO RECOMMENDATIONS TO THE SECRETARY OF AGRICULTURE

Softwood timber loans provide borrowers with significant financial benefits--deferral of debt for up to 45 years and revenue from tree crop production. The softwood timber program was determined to be feasible because of the revenue generated during the deferred debt. To ensure that the interest rates charged and completed by FmHA on softwood timber loans are consistent with the conditions under which the program was determined to be feasible, we recommend that the Secretary of Agriculture require the Administrator of FmHA to (1) approve all future softwood timber loans at an interest rate that equals the average yield on marketable U.S. obligations with periods to maturity comparable to the average maturities of softwood timber loans and (2) modify previous FmHA instructions governing the softwood timber program to require that interest on all future softwood timber loans be completed on a compound, rather than simple, interest basis.

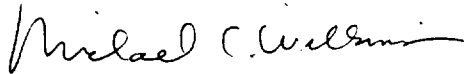
FmHA COMMENT

The Farmers Home Administration (FmHA) recognizes the concerns of GAO in regard to the Softwood Timber Program. The legislation authorized the program to provide relief to financially distressed farmers, to take marginal land out of production, and use softwood timber as a soil conserving crop. FmHA's analysis of the legislation indicated: (1) The program did not have the potential for utilization on a broad basis nationwide, (2) Utilization by financially distressed farmers with high-debt loads without additional income or debt relief, had little chance for success. (3) Feasibility based on 45-year future projections are difficult to estimate with any degree of accuracy.

**Appendix V
Comments From the Under Secretary for
Small Community and Rural
Development, USDA**

Our review of the legislation indicated the Secretary had latitude in how the program could be implemented. In implementing the program, FmHA considered the following and the potential outcome for a financially distressed farmer: (1) Capitalization of market interest over a 45-year period causes a high debt to accumulate, (2) No or limited income from the land over a 45-year period, while expenses and taxes continue to accrue, would contribute little relief to a financially stressed farmer. Based on this information, FmHA implemented the program to provide relief to farmers in difficult financial situations, utilizing discretion as authorized by the legislation, to encourage borrower participation. There has been limited participation in the program even with the lower interest rates and the opportunity to receive some income through the ASCS conservation reserve program. On January 6, 1988, the Agricultural Credit Act of 1987 (ACA87) was enacted which provides a more viable solution to debt relief to financially distressed farmers. The debt write-down provision of the (ACA87) provides permanent debt relief and gives borrowers a more viable solution to overcome their financial difficulties. FmHA contends if the ST program is to be workable and provide a feasibility program for financially stressed farmers, it must be continued as implemented.

Based on the limited participation in the Softwood Timber Program to date, and the enactment of the (ACA87), it is anticipated that the program will be utilized less in the future and is unlikely that the 50,000 acres authorized by the legislation will be converted to softwood timber.



MICHAEL C. WILKINSON
Deputy Administrator
Program Operations

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