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**Forest Service Needs to Improve Efforts to
Reduce Below-Cost Timber Sales**

Statement of
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Before the
Subcommittee on Forests, Family Farms, and
Energy
Committee on Agriculture
House of Representatives



Mr. Chairman and Members of the Subcommittee:

We are pleased to be here today to discuss our review of below-cost timber sales. Our work was aimed at identifying the current extent of below-cost timber sales, assessing actions undertaken by the Forest Service to reduce the number of below-cost sales, and recommending any additional steps the Forest Service should take.

In summary, we found the following:

- In fiscal year 1990, under our most conservative definition of costs, the Forest Service had timber sale preparation and administration expenses of \$35.6 million that went unrecovered as a result of below-cost timber sales. These expenses range as high as \$112.2 million when all costs are considered. Timber sale preparation and administration costs varied greatly from forest to forest, with costs per thousand board feet of timber harvested on the highest-cost forest being 23 times greater than those on the lowest-cost forest.

- The Forest Service has issued a draft policy to reduce losses from below-cost timber sales. While the draft policy is a step in the right direction, we believe that it leaves gaps in a comprehensive approach to below-cost

sales because (1) many below-cost sales will not be subject to review, (2) Forest Service costs are not considered when advertised prices are set for timber sales, and (3) the Forest Service does not evaluate, before incurring most preparation costs, whether the benefits of a below-cost sale justify the unrecovered costs.

Background

When the Forest Service sells timber from national forests, it incurs costs for a variety of activities, such as conducting environmental reviews, preparing the timber contract, appraising the value of the timber, and building access roads. In fiscal year 1990, the Forest Service reported that it had sold 9.3 billion board feet of timber and received about \$1.4 billion in revenues.

The issue of below-cost timber sales is long-standing. In 1976, the National Forest Management Act directed the Forest Service to provide information on sales below estimated expenditures. This information covered only a representative sample of timber sales. In its fiscal year 1985 appropriation, the Congress directed the Forest Service to develop an accounting system with the capacity to compare the cost of selling timber with the estimated value to be received from the sales. The

system that was subsequently created with our assistance--called the Timber Sale Program Information Reporting System, or TSPIRS--became operational in fiscal year 1989.

Forest Service Reports on Timber Sales Costs and Revenues

Using TSPIRS, the Forest Service reports on timber sale costs and revenues for the nation, individual states, and each forest. For fiscal year 1990, the Forest Service reported that revenues from timber sales exceeded costs (before payments to states which under federal law receive 25 percent of all timber revenues) by about \$629 million. However, for individual forests, revenues often did not exceed costs. In all, according to TSPIRS data, timber sale costs exceeded revenues for 65, or more than half, of the 122 national forests.

The Forest Service does not report costs and revenues for each sale. At your direction, we used average forest costs to compare costs and revenues on a sale-by-sale basis. In doing so, we used three different cost categories: the costs to prepare and administer the sale; second, a more inclusive set of all operating costs (such as investment costs for fertilizing, thinning, and taking other actions as the timber is growing); and third, all operating costs plus payments to states. Attachment I describes our methodology in greater detail.

Analysis of Fiscal Year 1990 Sales

Using these three categories we compared timber sale costs to actual sale prices for 3,731 "large" timber sales, which we defined as sales greater than \$2,000 in value and/or 2 million board feet in size, and about 258,000 "small" timber sales, which we defined as sales \$2,000 or less in value. (See Table 1.) More detailed results on large sales are included in attachments II through IV.

Table 1: Unrecovered Costs on Sales Using the Three Different Cost Categories

Dollars in Millions	<u>Large sales</u>	<u>Small sales</u>	<u>Total</u>
Preparation and administration	\$ 14.9	\$ 20.7	\$ 35.6
All operating costs	46.9	41.0	87.9
Operating costs plus payments to states	68.4	43.8	112.2

Unrecovered costs for large sales ranged from \$14.9 million when only costs to prepare and administer the sale are considered, to \$68.4 million when all operating costs plus payments to states are included. For small timber sales unrecovered costs ranged from \$20.7 million when only costs to prepare and administer the sales are considered to \$43.8 million when all operating costs plus payments to states are included.

We also compared sale preparation and administration costs for the 122 national forests. We found that these costs ranged

from a low of about \$15 per thousand board feet of harvested timber to a high of about \$348 per thousand board feet. Although the scope of our review did not permit us to fully analyze these differences, we believe that they could occur for a variety of reasons. For example, some forests could operate more efficiently than others, differences in timber sales practices could affect costs, and costs might not be uniformly captured from forest to forest. A review of these wide disparities could result in discovering ways to reduce costs. In this regard the Congress has directed the Forest Service to reduce timber sale costs by 5 percent each year for the next 3 years.

Forest Service Actions

On April 11, 1991, the Forest Service issued a draft policy and guidelines to address below-cost timber sales programs on individual national forests. The draft policy calls for evaluating below-cost sales for forests as a whole rather than for individual sales. Work on this policy started with the August 1989 issuance of an action plan by the Below-Cost Timber Program Guidelines Task Force, a working group within the Forest Service. The Forest Service also used this continuing effort to respond to the congressional directive to reduce timber sale costs. To implement this policy, the Forest Service plans to concentrate its efforts on below-cost forests but is also asking all forests to look for ways to reduce costs.

Delays in completing this policy is affecting action on two recommendations we made in our May 1990 report to this Subcommittee.¹ In our report we recommended that

-- all timber sale costs be considered in establishing advertised prices for timber sales. The Forest Service assembled a study team, but the team's proposal for redefining minimum rates has been set aside until the below-cost policy is developed. In the meantime, advertised prices continue to be set without consideration of Forest Service costs.

-- a formal decision-making process be adopted as part of any procedures for offering below-cost sales. Our recommendation called for a decision to (1) raise the price to cover costs, (2) terminate the sale, or (3) proceed with the sale on a below-cost basis but explain the reasons for doing so, such as needing to remove diseased timber that could affect other resources.

In addition, TSPIRS continues to undergo change. Because TSPIRS has been in operation for only 2 years, it continues to change to fit its users' needs. Major changes have been made to TSPIRS in 1991, that will affect the way in which timber program

¹Federal Timber Sales: Process for Appraising Timber Offered for Sale Needs to Be Improved (GAO/RCED-90-135, May 2, 1990).

costs are collected and reported. Some of these changes could affect average operating costs on some forests. In April 1991, the Forest Service also began using TSPIRS to track separately the costs of large and small sales, which were tracked together. This change will provide a clearer picture of revenues and expenses associated with large and small sales.

Conclusions

In our opinion, the Forest Service's proposals for addressing below-cost timber sales do not go far enough. We think additional actions are warranted in three areas.

First, we believe that the Forest Service should extend consideration of below-cost sales to the individual sales level rather than for forests as a whole as presently proposed. In fiscal year 1990, nearly every forest had below-cost sales, and more than half of the total unrecovered preparation and administration costs on large sales occurred on above-cost forests. However, the proposed policy calls for potentially adjusting the timber sale level only in below-cost forests.

Second, the Forest Service should consider its costs when setting minimum rates for a timber sale. When the Forest Service first established minimum rates in the early 1900s, it defined its minimum rate as the cost to make the sale. Over time, however,

this definition fell from use. As a result, the minimum rates often do not reflect the preparation and administration costs currently captured in TSPIRS. With TSPIRS, it is now possible to return to this original basis for setting minimum rates.

Third, the Forest Service is not evaluating, before incurring most preparation costs, whether the benefits of a below-cost sale justify the unrecovered costs. However, the current timber sale planning process provides the information needed to make a below-cost determination at the first decision point in the preparation process. If the sale were to be classified as marginal or below-cost at this time, we believe that the Forest Service should stop further work, avoiding the cost for such work as environmental reviews and contract and appraisal preparation. If the Forest Service had made these determinations for large sales conducted in fiscal year 1990 and concluded that the sales should not be made, almost all of the \$35.9 million in preparation and administration costs could have been avoided. And if the Forest Service had determined that some or all of these below-cost sales should still be prepared, it would have had an opportunity to raise prices or document its reasons for selling below cost.

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Recommendations

In our testimony of April 24, 1991 before the Subcommittee on Interior and Related Agencies, House Committee on Appropriations, we recommended that the Secretary of Agriculture direct the Chief of the Forest Service to take the following actions:

- Expand the below-cost sales policy beyond forests as a whole, as presently proposed, to individual sales.

- Define the minimum rate for timber sale bids as the cost of timber sale preparation and administration, and ensure that the sale price recovers these costs.

- Amend the timber sale process to include a below-cost determination at the first decision point in the sale preparation process, so that, if the sale is not conducted, unnecessary preparation costs can be avoided. If a below-cost sale proceeds, the reasons should be documented.

Mr. Chairman, this concludes my prepared statement. I would be pleased to answer any questions you or members of the subcommittee might have.

OBJECTIVES, SCOPE, AND METHODOLOGY

In a letter dated August 27, 1990, the Chairman and Ranking Minority Member, Subcommittee on Interior and Related Agencies, House Committee on Appropriations, expressed concern about the Forest Service's procedures for selling and administering of federal timber assets. We were asked to (1) identify Forest Service timber sales that did not recover their associated costs and (2) determine what actions the Forest Service has taken or plans to take to reduce the occurrence of such below-cost timber sales.

To identify below-cost timber sales and calculate unrecovered costs, we used the Forest Service's 2400-17 Report of Timber Sale data base and data from its Timber Sale Program Information Reporting System (TSPIRS) for fiscal year 1990. We concentrated our review on sales greater than \$2,000 in value or 2 million board feet in size. The Forest Service Report of Timber Sale data base contained 3,731 sales that met these criteria for fiscal year 1990.

Since we had assessed the reliability of selected data elements from the 1988 data base in connection with our 1990 report of Federal Timber Sales Appraisals (GAO/RCED-90-135), we did not do another reliability test.

We used the Forest Service's Timber Sale Program Information Reporting System annual reports for fiscal year 1990 to obtain the costs associated with the timber sales. We calculated three different categories of cost for each national forest:² (1) the costs to prepare and administer the sale, (2) all operating costs, and (3) all operating costs plus payments to states. For the latter two categories of costs, we allocated operating expenses for the Forest Service's Washington office and regional offices to the 122 national forests on the basis of the volume of timber harvested. The payment to states was calculated individually for each sale as 25 percent of gross revenues. We then calculated average costs per thousand board feet³ (MBF) for each of the three categories which is the method generally used by the Forest Service and accepted by GAO. We did not verify the cost figures drawn from the published TSPIRS reports.

For all large sales, individual sale volumes were converted to MBF, multiplied by the average cost per MBF under each cost category for the associated forest, and then compared with the total selling price. The sales highlighted in this testimony are

²Although there are 156 national forests, the TSPIRS cost information we used in our cost analyses was based upon 122 administrative units.

³A board foot is a unit of quantity for wood equal to the volume of a board 12 inches by 12 inches by 1 inch.

those that failed to recover costs under any one of the alternatives. If cost data was available on a sales basis then the number and dollar amount of below-cost sales could be more or less than our analysis calculates on an average forest basis.

Unrecovered costs on the small timber sale program were calculated using figures supplied by the Forest Service for fiscal year 1990 and the timber sales program annual report for the same year.⁴ Total national volumes for sales \$2,000 or less was multiplied by national TSPIRS unit cost figures using the same three cost definitions used for the large sales. The 25- percent payment to states was based on the value of the small sales. These cost figures were then compared with the total sales amount of the small sales. We did not perform this analysis on an individual sale basis because there were so many sales in this size class--258,336 in fiscal year 1990 and the limited time available to respond to this request.

To determine what actions the Forest Service has taken or plans to take to reduce below-cost timber sales, we interviewed Forest Service headquarters officials and reviewed pertinent documents.

⁴The small timber sale program is generally referred to as "personal use" sales and includes such things as firewood, fence poles, and Christmas trees.

ATTACHMENT I

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Our review was performed between September 1990 and April 1991 in accordance with generally accepted government auditing standards.

ACTUAL UNRECOVERED SALES PREPARATION AND ADMINISTRATION COSTS
ON LARGE FISCAL YEAR 1990 TIMBER SALES

<u>Region</u>	<u>Total number of sales</u>	<u>Sold below sales preparation and administration costs</u>	
		<u>Number of sales</u>	<u>Unrecovered Costs^a</u>
1	263	38	\$ 773,019
2	122	48	1,235,989
3	54	24	1,421,335
4	186	24	563,226
5	430	83	3,491,334
6	1,128	52	3,364,469
8	1,026	168	2,306,317
9	518	109	1,784,351
10	4	0	0
Total	3,731	546	\$14,940,040

^aCalculated as the difference between the total high bid price on each sale and the corresponding forest's average sales preparation and administration cost per MBF multiplied by the total volume for each sale.

ACTUAL UNRECOVERED TOTAL OPERATING COSTS
ON LARGE FISCAL YEAR 1990 TIMBER SALES

<u>Region</u>	<u>Total number of sales</u>	<u>Sold below total operating costs</u>	
		<u>Number of sales</u>	<u>Unrecovered Costs^a</u>
1	263	64	\$2,298,007
2	122	71	3,232,279
3	54	37	4,028,574
4	186	65	2,547,748
5	430	146	7,781,615
6	1,128	99	9,369,541
8	1,026	391	9,190,357
9	518	292	8,493,140
10	4	0	0
Total	3,731	1,165	\$46,941,261

^aCalculated as the difference between the total high bid price on each sale and the corresponding forest's average total operating cost per MBF multiplied by the total volume for each sale.

ACTUAL UNRECOVERED TOTAL OPERATING COSTS PLUS PAYMENTS
TO STATES ON LARGE FISCAL YEAR 1990 TIMBER SALES

<u>Region</u>	<u>Total number of sales</u>	<u>Sold below total operating costs plus payments to states</u>	
		<u>Number of sales</u>	<u>Unrecovered costs^a</u>
1	263	106	\$ 3,739,452
2	122	90	4,539,442
3	54	43	5,811,407
4	186	99	3,984,554
5	430	200	10,184,130
6	1,128	154	14,250,783
8	1,026	588	14,113,060
9	518	372	11,823,419
10	4	0	0
Total	3,731	1652	\$68,446,247

^aCalculated as the difference between the total high bid price on each sale and the corresponding forest's average total operating cost (including allocation of Washington office and regional office operating costs) per MBF multiplied by the total volume for each sale, plus the 25-percent payment to states.