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BY THE COMPTROLLER GENERAL

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Report To The Congress

OF THE UNITED STATES

Questionable Payments And Loan Defaults In Sugar Programs

The Department of Agriculture's sugar price-support payment program on 1977 crop year sugar has resulted in questionable payments of millions of dollars.

Agriculture's loan program for 1977 crop year sugar is beset with problems of storage, underpayments to growers, and failure to verify or enforce minimum wage requirements.

Substantial defaults on Government loans are occurring as a result of low-cost sugar imports, but no final plans have been made to dispose of the sugar forfeited to the Government as loan collateral.

This report recommends that the Congress enact legislation to permit sugar agricultural workers to benefit from payment programs and that the Congress provide guidance on any future program implementation. This report also makes several recommendations to the Department of Agriculture to solve the problems of its two programs intended to help sugar producers.



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Report

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COMPTROLLER GENERAL OF THE UNITED STATES
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To the President of the Senate and the
Speaker of the House of Representatives

This report reviews the operation of both a sugar price-support payment program for 1977-crop sugar and a loan program for 1977-crop sugar operated by the Department of Agriculture. It raises questions about \$27 million in sugar price-support payments and identifies several other concerns involving both the payment and the loan programs.

We are sending copies of this report to the Secretary of Agriculture and the Director, Office of Management and Budget.

James P. Atchaf
Comptroller General
of the United States



D I G E S T

This report discusses the Department of Agriculture's ^{1/25} two programs intended to help sugar producers with price-support payments on 1977-crop year sugar and price-support loans for 1977- and 1978-crop year sugar.

The Department has made substantial questionable payments to sugar processors under the payment program.

The loan program will likely result in large Government expenditures because

--many loans are being defaulted and

--the Government will have to pay the cost of storing and marketing millions of pounds of sugar as the collateral (sugar) is forfeited.

QUESTIONABLE PAYMENTS

Some Department practices have led to questionable price-support payments to sugar processors. The Department paid about \$6.1 million 1/ for sugar which may be ineligible for participation in the payment program because

--the methods of determining eligibility and marketing in claims for payments to three integrated processor/refiners raises question,

--sugar was sold under contracts on which delivery periods had expired, and

1/The Department has made initial payments for 90 percent of the sugar reported as marketed, with 10 percent to be paid later. Dollar amounts in the GAO report relate to the full potential disbursement.

--payments were approved on sugar from the "1976 crop."

Under program regulations, all eligible participants receive a fixed payment per pound, determined by the amount the 1977 support level (13.5 cents) exceeds the average market price, regardless of the price at which any one sugar processor actually sold sugar. Consequently, certain program participants, whose market prices exceeded the average, received payments which, when added to those market prices, resulted in proceeds in excess of the support level totaling about \$20.8 million. (See pp. 18 to 21.)

In addition, GAO believes the method used to calculate the average market price for sugar produced in Hawaii distorts the national average market price and leads to higher support payments. (See pp. 9 to 11.)

In its review, GAO found three sugar processors that failed to comply with regulations in reporting some information needed to compute support payments. Errors made by these three processors resulted in all processors in the program being underpaid a total of about \$465,000. (See pp. 21 to 22.)

Because Department directions were not explicit on how producer payments were to be computed, some sugar processors could pay their producers about \$3.5 million less than they should have paid.

RECOMMENDATIONS TO THE SECRETARY OF AGRICULTURE

The Secretary of Agriculture should

- reconsider the method used to compute the average market price for Hawaiian sugar for any future payments;
- review the payments to the three raw sugar processor/refiners and if necessary adjust payments to them accordingly;

--review all contracts to identify those which do not comply with requirements for the cutoff date for payment eligibility and examine all future claims to insure that they are based on contracts which meet payment program eligibility requirements and, if appropriate, adjust payments; and

--provide adequate written instructions to processors on how benefits should be passed on to producers and require assurance that all producers receive equitable payments for their products.

RECOMMENDATIONS TO THE CONGRESS

Present law provides little guidance as to how the sugar payment program is to be implemented. GAO recommends the Congress consider providing more specific guidance on program implementation, particularly with respect to whether payments to any processor should be limited so that the sum of the Government payment and the market price received by any processor in any payment period does not exceed the support level.

Both the sugar loan program and the now defunct Sugar Act mandated minimum wages for sugar agricultural workers. However, the payment program contains no wage provisions because authorizing legislation does not provide authority to require minimum wages for sugar agricultural workers.

To assure more equitable treatment of sugar agricultural workers in any future sugar payment program, the Congress should specify that future sugar payment programs contain minimum wage provisions for agricultural workers.

LOAN PROGRAM PROBLEMS

Conferees on the Food and Agriculture Act of 1977 expected that needed loan support could

be provided to the sugar industry without any significant outlay of Federal funds. The conferees expected the executive branch would utilize existing authority of law to implement immediately, upon the act becoming law, an import fee or duty which when added to the current import duty would enable sugar to sell in the domestic market at not less than the effective support price. However, low-cost sugar imports have held down the price of domestic sugar and supplanted domestic sugar sales. Large Federal costs will probably be incurred as defaults occur. As of January 31, 1979, almost 374 million pounds of sugar valued at \$50.5 million were forfeited to the Agriculture Department as loans went into default. The Department has made no final plans to dispose of forfeited sugar, although it is considering the matter. The Department has noted that options for disposing of forfeited sugar are limited, but that it is exploring the most promising option--donations to domestic food assistance programs.

* Sugar being held by processors as collateral for price-support loans has created serious storage problems--problems which could ultimately be costly to the Government as substantial loans are defaulted.

GAO has noted in its report "Sugar and Other Sweeteners: An Industry Assessment" (CED-79-21) that the successful use of loans depends on the world price of sugar and the level of tariffs and fees.

Problems of minimum prices and wages also plague the loan program. The Department has not adequately enforced minimum wage rate requirements for agricultural fieldworkers. One sugarcane processor has not paid minimum prices to producers because of inadequate Department instructions on how growers should be paid.

RECOMMENDATIONS TO THE
SECRETARY OF AGRICULTURE

The Secretary of Agriculture should

- plan for the handling and disposition of sugar forfeited as a result of loan defaults,
- review wage payments made to fieldworkers to insure compliance with minimum wage requirements, and
- provide adequate written instructions to processors on how benefits should be passed on to producers.

AGENCY COMMENTS AND GAO'S EVALUATION

The Department of Agriculture agreed with GAO's recommendations to

- insure compliance with minimum wage requirements under the loan program for agricultural fieldworkers,
- adopt a plan for handling and disposing of sugar forfeited under the loan program,
- provide written instructions designed to assure that all payment and loan program participants receive payments, and
- reconsider the method used to calculate Hawaiian sugar prices in future payment programs.

The Department believes GAO's suggestion to limit support payments to any one processor such that the sum of Government payments and market prices does not exceed the support level would create a strong disincentive to individual processors to obtain a high market price. The Department also believes that there is ample precedent in other commodity programs for these payments.

GAO believes that it is to each firm's advantage to get the best possible price and that payments above the support level are not needed as an incentive. When GAO reviews other commodity programs, it will consider this matter further.

GAO's recommendations to (1) review payments to the three raw sugar processor/refiners and (2) review all contracts to identify those not complying with cutoff date requirements and examine all future claims to insure eligibility have been referred to USDA's Office of General Counsel. GAO understands that the issue of payments to the three processor/refiners is currently under investigation and a decision is expected in the near future. A recent USDA legal opinion has taken the position that delivery occurring after the delivery period specified in the agreement as of November 7, 1977, should not be considered eligible marketings. Also, the question of payments approved on "1976-crop" sugar has been referred by the Secretary of Agriculture to GAO for its legal opinion.

The Department's comments and GAO's views on them are discussed in more detail on pages 26, 27, and 34.

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I Letter dated February 5, 1979 from
the Department of Agriculture

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ABBREVIATIONS

ASCS Agricultural Stabilization and
Conservation Service

GAO General Accounting Office

USDA United States Department of
Agriculture

CHAPTER 1

INTRODUCTION

On December 31, 1974, the Sugar Act expired, ending 40 years of Government regulation of the U.S. sugar industry at a time of world sugar shortages and rising prices in both U.S. and world markets. A basic objective of the act had always been to provide U.S. consumers with an ample supply of sugar at prices which would maintain the domestic industry and be fair and reasonable to consumers. The act prescribed a pricing formula that established the price of sugar for the producer. The Secretary of Agriculture, to maintain this price, determined domestic requirements and allocated this quantity to domestic and foreign suppliers.

Since the Sugar Act expired world market conditions have changed. World sugar prices, which averaged a record 57 cents per pound raw value in November 1974, averaged 8.1 cents per pound in 1977 and 7.8 cents per pound in 1978. As a result, prices to sugar producers have declined dramatically and the U.S. sugar industry has encountered rising production costs, declining profits, declining employment, and increases in unsold inventories.

On March 17, 1977, the U.S. International Trade Commission reported to the President that sugar was being imported in such increased quantities as to be a substantial cause of the threat of serious injury to the domestic industry. The Commission recommended that quotas be imposed on imported sugar. On May 4, 1977, the President rejected the recommendation because he felt such action would raise domestic prices and would not be in the overall national economic interest. Instead, he instructed the Secretary of Agriculture to institute an interim income-support program pending negotiation and implementation of a new international sugar agreement, designed to stabilize prices at a level profitable to sugar producers.

PRICE-SUPPORT PAYMENT PROGRAM IMPLEMENTED BEFORE LOAN PROGRAM

The interim program, announced by the U.S. Department of Agriculture (USDA) on June 14, 1977, was to provide compensation of up to 2 cents per pound to producers of sugarcane and sugar beets when the market price for domestic raw sugar fell below 13.5 cents per pound. However, on July 19, 1977, we ruled that this proposal for sugar payments was illegal because a program of direct payments to producers not designed to support or increase the market price of sugar was not authorized under section 301 of the

Agricultural Act of 1949, as amended. On August 19, 1977, the Justice Department concurred with this ruling.

On October 7, 1977, USDA issued regulations on a new payment program under section 301 of the Agricultural Act of 1949, modified to meet legal objections to the previous payment plan. Section 301 authorizes the Secretary of Agriculture to make available through loans, purchases, or other operations price support to producers for any "non-basic agricultural commodity." Sugar beets and sugarcane are nonbasic agricultural commodities under the act. The act provides little guidance as to how the program is to be implemented. The program regulations authorized payments to sugar processors for all 1977-crop sugar marketed from September 15, 1977, forward until all 1977-crop sugar had been marketed and set forth the operation of the program. Payments were to be the amount by which 13.5 cents, the price USDA deemed necessary to support the efficient producer, exceeded the average market price. The program was to remain in effect until all 1977-crop sugar had been marketed or until superceded by another price support program. Modifications were later made to include all 1977-crop sugar marketed before September 15, 1977.

Through May 31, 1978, sugarcane and sugar beet processors had reported as marketed more than 6.2 billion pounds of sugar for price-support payments in excess of \$199 million. All sugar beet and sugarcane processors have received payments under the price-support payment program, except one sugarcane processor in Texas whose sugar was not committed for sale as of November 7, 1977, the cutoff date for payment eligibility. Payment detail is shown below.

<u>Area</u>	<u>Number of processors</u>	<u>Pounds marketed</u> (millions)	<u>Percent of 1977 total production</u>	<u>Support payments received</u> (note a) (millions)
Sugar beet States (note b)	12	2,795.9	47.7	\$ 88.1
Florida	6	524.2	29.5	13.4
Louisiana	29	952.0	71.3	28.2
Texas	1	0.0	0.0	0.0
Hawaii	15	1,740.2	84.2	63.2
Puerto Rico	<u>11</u>	<u>236.2</u>	<u>44.1</u>	<u>6.2</u>
Total	<u>74</u>	<u>6,248.5</u>	<u>53.2</u>	<u>\$199.1</u>

a/Represents potential full payments to producers which will be adjusted when all eligible sugar has been reported as marketed and final weights are known. (See pp. 7 and 8.)

b/Twelve processors operate sugar beet plants in 17 States.

PRICE-SUPPORT LOAN PROGRAM ENACTED IN 1977

Public Law 95-113, the Food and Agriculture Act of 1977, was passed by the Congress on September 16, 1977, and signed into law by the President on September 29, 1977. The act amended section 201 of the Agricultural Act of 1949 to provide for a price-support loan program for the 1977 and 1978 crops of sugar beets and sugarcane, and on November 8, 1977, the Department of Agriculture implemented a loan program for the 1977 crop.

Through May 12, 1978, loans were outstanding on more than 2.2 billion pounds of 1977-crop sugar for over \$317 million. By September 1, 1978, loans had fallen to \$176 million for 1.2 billion pounds due to loan redemptions. Loans are made at 13.5 cents per pound, raw value, for 1977-crop raw cane sugar and 15.57 cents per pound for refined beet sugar. Participation in the program by area is exhibited in the following table.

<u>Area</u>	<u>Processors</u>	<u>Parti- cipating pro- cessors</u>	<u>Pounds of sugar</u> (millions)	<u>Percent of 1977 crop total pro- duction</u>	<u>Unre- deemed amount on loans</u> (millions)
Sugar beet States	12	7	466.1	8.0	\$ 72.6
Florida	6	4	665.5	37.5	89.8
Louisiana	29	1	1.0	0.1	0.1
Texas	1	1	100.5	58.3	13.6
Hawaii	15	0	0.0	0.0	0.0
Puerto Rico	<u>11</u>	<u>0</u>	<u>0.0</u>	<u>0.0</u>	<u>0.0</u>
Total	<u>74</u>	<u>13</u>	<u>1,233.1</u>	<u>10.5</u>	<u>\$176.1</u>

A staff of five professionals and three support personnel from the Agricultural Stabilization and Conservation Service (ASCS) administer the two programs. In addition, ASCS field offices assist with the loan program administration.

SCOPE OF REVIEW

We reviewed the operation of both the sugar price-support payment and loan programs. In compiling information and data we interviewed and obtained data from

- USDA officials in Washington, D.C.;
- State and county ASCS officials in the cane-producing States of Florida and Louisiana and in selected beet-producing States;
- officials of sugarcane and sugar beet trade associations in Washington, D.C., Florida, and Louisiana;
- sugarcane producers, processors, and refiners in Florida, Louisiana, California, and Hawaii; and
- sugar beet producers and processors in selected beet-producing States.

We did not review the adequacy of the 13.5 cent support price to support the efficient producer.

Because of time constraints, we did not visit the cane-producing areas of Texas and Puerto Rico but did contact officials in these areas by telephone.

We reviewed the legislative history of domestic sugar programs, authorizing legislation, and other materials pertaining to U.S. sugar policies and programs. We also examined USDA program records in Washington, D.C., and selected State and county ASCS records in States we visited that produce sugarcane and sugar beets. We also reviewed records of sugarcane processors and sugar beet producers in the States visited.

Our analysis in this report concentrates on the operation of the 1977-crop year sugar programs. Our report entitled "Sugar and Other Sweeteners: An Industry Assessment" (CED-79-21, Feb. 26, 1979), describes the principal elements of the U.S. sugar industry and discusses some of the issues involved in developing sugar legislation.

We met with officials of USDA's Office of Inspector General who also were conducting an internal audit of selected aspects of the sugar payment program. To coordinate our work, we kept each other advised of respective audit activities. To avoid duplication of work, we limited our activity in individual firms in light of the Office of Inspector General's detailed examination of individual firms' records. The Office of Inspector General's findings are included in appropriate parts of our report.

CHAPTER 2

PRICE-SUPPORT PAYMENT PROGRAM

Although the price-support payment program provided substantial benefits of approximately \$200 million to program participants through May 31, 1978, we believe it has a number of administrative problems and weaknesses. These weaknesses can be avoided in any future sugar payment program. In addition, some of the problems can be remedied for the 1977 program by reviewing actual payments against eligibility criteria.

- The method used to calculate the average market price for sugar produced in Hawaii distorted the average market price for sugar which was used in computing price-support payments.
- USDA paid about \$6.1 million in price support payments for sugar that we believe may be ineligible for participation in the payment program.
- Some participants in the program received about \$20.8 million in payments by USDA above the support price for sugar.
- Processors were underpaid about \$465,000 because three sugar processors failed to comply with USDA reporting regulations.
- Some sugar processors paid about \$3.5 million less than would otherwise have been paid to their producers because USDA did not provide sufficiently explicit directions on how producer payments were to be computed.

Agricultural workers do not share program benefits since the authorizing legislation does not require minimum wages for sugar agricultural workers.

PAYMENT PROGRAM OPERATION

The payment program supported prices for sugarcane and sugar beets at average levels estimated to be 52.5 percent of the parity prices for these commodities as of July 1977. The rate of payment to processors who manufacture sugar from sugarcane and sugar beets was the amount by which 13.5 cents exceeded the average market price. The 13.5 cents per pound for unrefined (raw) sugar is the amount considered necessary to provide the percentage of parity prices

established for producers. In turn, processors were required to pay producers the established support prices for their products which varied for different locations. There were no requirements under the payment program concerning wages paid agricultural workers.

USDA computed average market prices based on the quantity of sugar marketed and the corresponding gross proceeds as reported by processors. Data provided for refined beet sugar was converted to a raw sugar price equivalent basis under a formula detailed in the regulations. When the average market price was equal to or greater than 13.5 cents, there would be no payments.

Regulations governing the program were amended twice. On October 7, 1977, USDA issued the initial regulations authorizing payments for all 1977-crop sugar marketed from September 15, 1977, forward. The payment program was amended once on November 3, 1977, and again on December 27, 1977. The first amendment removed the September 15 beginning eligibility date to include all 1977-crop sugar marketed before September 15 and, to prevent possible program abuses, required a written contract fixing both the quantity and price of sugar committed for delivery within a period not to exceed 30 days following the end of the marketing period (the period that will end when all 1977-crop sugar has been marketed).

The second amendment fixed the end of the marketing period as November 7, 1977, 1 day before the November 8, 1977, effective date of the price-support loan program discussed in chapter 3, which was to replace the payment program. The 1977-crop sugar contracted for future delivery as of that date, however, was considered as having been marketed by November 7. USDA stated that it included this provision in the regulations because processors who had commitments as of November 7, 1977, for future delivery of sugar could not participate in the loan program and before this amendment had been ineligible to receive direct payments.

Primarily because final weights are not known for some time after sugar is reported as marketed, USDA decided to make initial payments to processors for 90 percent of

the pounds reported as marketed. ^{1/} The 10-percent payment which is held back will serve as a buffer against adjustments made by processors for various reasons and for changes in the national average market price. When all eligible sugar has been reported as marketed and final weights are known, a national average market price will be computed for the entire 1977 crop and the final 10-percent disbursement, adjusted to reflect changes in selling prices, will be made. USDA officials told us on March 13, 1979, that final disbursements had not yet been made to processors for the 1977 crop.

Legal questions explored

We explored the following questions.

- Was the price-support payment program announced September 15, 1977, legal?
- Was USDA's implementation of the price-support program consistent with the conferees' intent as manifested in the conference report's consideration of section 902 of the Food and Agriculture Act of 1977, Public Law 95-113, 91 Stat. 949?
- Could the price-support payment program cover sugarcane and sugar beets marketed before program institution?

As to the first question, we sustained the legality of the price support payment program announced September 15, 1977, in a letter (B-118622, Oct. 3, 1977) to Senator Hubert H. Humphrey. With respect to the second question, we decided that the operation of the price-support payment program is consistent with the conferees' intent that price support be extended to that portion of the 1977 crop marketed before the loan or purchase program could be put into effect. The conferees intended to save the Secretary's existing authority under section 301 of the Agricultural Act of 1949 and this was apparently done to permit him to make payments to sugar processors for that portion of the

^{1/}Because our report contains the full amount of the potential disbursement and USDA has made only 90-percent disbursements, all amounts appearing in this report relating to price-support payments to processors or producers may be overstated by as much as 10-percent, pending the final 10-percent disbursement by USDA.

1977 sugar crop already marketed before the new loan or purchase program could be put into effect. Notwithstanding this, the conferees also intended that USDA implement "as soon as possible--even before the Act is signed into law" a loan or purchase program covering the 1977 and 1978 sugar crops. Concerning the third question, we stated in a letter (B-118622, June 28, 1978) to Congressmen Edward R. Madigan and Paul Findley that the price-support payment program could make payments to cover sugarcane and sugar beets marketed before program institution as long as the regulatory program is otherwise consistent with the statute.

HAWAIIAN RAW SUGAR PRICES DISTORTED AVERAGE MARKET PRICES

Raw sugar produced in Hawaii is generally shipped to a mainland refinery cooperatively owned by the Hawaiian sugarcane producers. There the raw sugar is refined and then marketed. Title to the raw sugar passes to the mainland refinery upon shipment, but the Hawaiian producers are paid primarily on the basis of the price received by the refiner for the refined sugar. There is consequently no arms-length transaction between the Hawaiian producers and the refiner which would establish a selling price for Hawaiian raw sugar that could be used in computing the average market price for the payment program.

A similar situation exists in Louisiana. The regulations exclude those Louisiana processors who also are refiners of raw cane sugar or specialty sugar from the average market price computation. USDA officials told us that the Louisiana processors were excluded from the average market price computations because valid sales prices could not be determined since there was no arms-length sale of raw sugar. We believe the situation of the Louisiana processors is similar to that in Hawaii. The Hawaiian sugar, however, is treated in the opposite fashion and not excluded from average market price computations. USDA officials told us that it is included on the premise that Hawaii produces a very large amount of sugar.

We believe the average selling price calculated for Hawaiian raw sugar is unreasonably low and distorts the national average market price.

The regulations allow a facility which refines raw cane sugar and is cooperatively owned by its raw cane sugar processors to deduct up to 8 percent from gross proceeds to the cooperative member-processors to reflect that portion of returns which can be attributed to their

investment in the refinery facility. The only facility that fits this description is the one cooperatively owned by the Hawaiian sugarcane processors and/or producers. In calculating gross proceeds to the cooperative-member processors, USDA permitted the refiner of Hawaiian sugar to subtract the total refining costs; transportation costs including ocean freight; and all other costs incurred, such as overhead, from refined sugar sales revenues. The proceeds were further reduced by the maximum 8 percent of the refined sugar proceeds allowed by the regulations to reflect a return on the producers' investment in the refinery.

The proceeds remaining after these deductions were merged with gross proceeds for all other sugar, as adjusted under the regulations. They were then divided by the total quantity of sugar, raw value, marketed to obtain the national average price. Table 1 illustrates the large disparity between Hawaii's raw cane sugar selling prices and those of other cane-producing areas.

Table 1

Raw Cane Sugar Selling Prices By Area

<u>Marketing periods</u>	<u>Average selling prices</u>			
	<u>Florida</u>	<u>Louisiana</u>	<u>Puerto Rico</u>	<u>Hawaii</u>
	------(cents per pound)-----			
Prior to 11/8/77	11.18	10.16	(a)	9.41
11/8/77 -12/31/77	11.41	11.17	10.89	9.96
1/1/78 - 1/31/78	12.18	12.46	(a)	10.94
2/1/78 - 2/28/78	13.50	13.19	(a)	9.59
3/1/78 - 3/31/78	13.28	13.39	(a)	9.75
4/1/78 - 4/30/78	13.57	13.09	(a)	9.87
5/1/78 - 5/31/78	<u>13.42</u>	<u>13.27</u>	<u>11.00</u>	<u>9.35</u>
Total	<u>12.36</u>	<u>11.79</u>	<u>10.90</u>	<u>9.57</u>

a/No sugar reported as marketed in these periods.

The method of calculation permitted by USDA results in a residual figure--the amount left after deducting all costs from refined sugar revenues--rather than a bona fide sales price of raw sugar. In our opinion, to include a residual figure as the average selling price for Hawaiian sugar in calculating the average market price for the payment program results in a distorted average market price because it does not represent a true selling price that would be established between unrelated buyers and sellers of raw sugar.

USDA's Office of Inspector General, in its review of the 8-percent deduction for return on investment, stated that:

"Excessive support payments estimated at over \$9 million were made on sugar marketed through December 31, 1977, because program regulations permit an excessive deduction from reported gross proceeds.

"Program regulations permit cooperatively owned cane sugar refiners to deduct up to 8 percent from the gross proceeds on refined cane sugar marketed. The intended effect of this deduction is to subtract from the gross proceeds on refined sugar sales that portion attributable to investments in the refinery. During the 1977 program this provision applied exclusively to one program participant * * * but resulted in increased program payments to all participants. Furthermore, the 8 percent deduction was equal to a 30 percent annual return on the investment (equity) of processor owner-members."

The report went on to state that because the processor marketed over 38 percent of all sugar reported in the first two program periods, the excessive deduction substantially understated the national average market price.

QUESTIONABLE PRICE-SUPPORT PAYMENTS MADE
FOR SUGAR REPORTED AS MARKETED

USDA paid about \$6.1 million in price-support payments for sugar we believe may have been ineligible for participation in the payment program. The specific elements of these payments are as follows.

- Three integrated raw sugar processor/refiners received increased price-support payments of about \$4.8 million because of the methods of determining eligibility and marketing USDA permitted in claiming payments.
- At least three beet sugar processors received price-support payments in excess of \$800,000 for sugar sold under contracts that may not qualify according to program marketing requirements.
- A beet processor may be paid about \$500,000, with USDA's approval, for sugar produced from the "1976

crop," although program regulations limit payments to sugar produced from the "1977 crop."

Payments to processor/refiners based on both claiming sugar that may not be eligible for payments and on short marketing periods

There are three integrated raw sugar processor/refiners in Louisiana. They produce raw cane sugar which, in turn, is processed into refined sugar at their own plants. All of this sugar, which is derived from cane grown in Louisiana and ground by the processor/refiners, is eligible for price-support payments, assuming all requirements in the program regulations are met.

Raw sugar is also purchased from other processors, both domestic and foreign, since none of the processor/refiners produce enough raw sugar to meet their orders for refined sugar. The raw cane sugar which these firms purchase from other processors for processing into refined sugar would not be eligible for price-support payments made to the processor/refiners because they purchased the raw sugar rather than selling it to others. Approximately 39, 52, and 55 percent, respectively, of each firm's refined production is accounted for by the raw sugar it produces and the balance by purchases of raw sugar from others.

The three processor/refiners have claimed that all the raw sugar they processed from sugarcane they produced or purchased from independent Louisiana growers is eligible for payments since it was committed to their respective refineries. USDA has concurred and made payments on this sugar. The program regulations, however, do not address treatment of these firms except to omit them from the calculation of the national average market price. The payment program regulations state that

"Refined beet sugar or raw cane sugar shall be deemed to have been marketed during the marketing period when (i) delivered to the purchaser, or (ii) delivered to a carrier for delivery to the purchaser, or (iii) title otherwise passes to the purchaser, * * * but * * * only to the extent that gross proceeds are accounted to the seller; Provided, that where raw cane sugar processors market their sugar through a cooperatively-owned refiner, marketing shall not be deemed to have occurred until the raw sugar or refined

sugar produced therefrom is marketed by the cooperative."

Each of the processor/refiners is a single corporate entity which produces both raw and refined cane sugar. It is not divided into separate entities, one of which processes raw sugar and the other refined sugar. Consequently, it is arguable that the simple act of moving this raw sugar to the refining stage would not constitute marketing of the product. On this basis the test of eligibility should have been whether the refined sugar produced by these firms was marketed or committed as of November 7, 1977. This is the same test USDA used in the payment program regulations to determine payment program eligibility for both refined Hawaiian and beet sugar.

In addition, two of the processor/refiners reported all of their raw sugar production as marketed in the first two and three payment periods, respectively, when the national average market prices were at their lowest and subsidy payments at their highest. These two processor/refiners considered their sugar marketed as it was processed into refined sugar. The third processor/refiner had allocated the amount of sugar placed under the payment program based on the period over which it expected to sell sugar from the 1977 crop. We believe that the third processor/refiner's method of allocating production to marketing periods was more reasonable and appropriate than assuming that the sugar was marketed when processed into refined sugar.

USDA's Office of Inspector General, in its review of the payment program, stated that two claims were based on agreements to transfer raw sugar to refineries owned by the processors. Its review further stated that:

"The two program claims were for the quantity of sugar transferred to the refinery, not for the quantity of sugar marketed. The regulations require that claims for support payments be based on the quantity of sugar marketed."

In the Office of Inspector General's discussion on this matter with ASCS, ASCS requested that the Department's Office of General Counsel be requested to determine the legality of allowing processors to report sugar as marketed when the raw sugar is delivered to the integrated refinery. The Office of Inspector General agreed to request an opinion from the Department's Office of General Counsel on this matter. We have been informally advised that a decision on this matter is expected in the near future.

The three processor/refiners gave us information on sugar marketed and committed for future delivery as of November 7, 1977. Two of the processor/refiners would not permit us to examine their refined sugar production and commitment records, and the third said approval would be needed from the firm's attorneys before permission could be granted for us to examine such records. The processor/refiners apparently adopted this position because they believed that all raw sugar they produced from sugarcane they either grew or purchased from independent Louisiana growers was eligible for price-support payments without considering refined sugar marketed or committed.

We used the unverified data provided by the processor/refiners to estimate the effect of allowing them to report all raw sugar produced as eligible for support payments rather than only refined sugar marketed or committed by November 7, 1977, and allowing them to claim that sugar was marketed as produced rather than over reasonable or actual marketing periods. Concerning the latter point, however, we accepted one processor/refiner's claim that all refined sugar reported to us as committed by November 7, 1977, was eligible for price-support payments because it was processed from sugarcane produced by the firm or purchased from independent Louisiana growers and had been priced with gross proceeds accounted for to the seller by the commitment date. Based on these statements, we would consider the sugar as eligible for price-support payments and as marketed by November 7, 1977.

In the absence of more accurate marketing information, we apportioned the other processor/refiners total refined sugar commitments at November 7, 1977, over the same marketing period used by the processor/refiner who allocated the amount of sugar placed under the payment program based on the period over which it expected to sell sugar from the 1977 crop. We apportioned the refined sugar marketed between eligible and ineligible sugar for these two processor/refiners based on the portion of their total refined sugar production accounted for by raw sugar they actually produced from sugarcane they either grew or purchased from independent Louisiana growers.

If only eligible sugar as opposed to all sugar produced was sold and it was sold over reasonable or actual marketing periods rather than in periods claimed by the processor/refiners, we estimate, based on the information provided, that one of the processor/refiners would have received

about \$3.2 million less than it did and the other about \$1.6 million less for a total price-support overpayment of \$4.8 million. The third processor/refiner claimed sugar as marketed over a reasonable period but also would have received about \$43,500 less for ineligible sugar. This processor/refiner said the quantity of sugar committed as of November 7, 1977, which was provided to us, was understated, but it would not permit us to examine records to identify additional commitments.

Processor/refiner officials said that USDA was aware of and approved the method they followed in reporting sugar for price-support payments. The officials also said that their marketing decisions may have been different if USDA had not permitted them to receive price-support payments for all raw sugar produced. One possible marketing option cited was obtaining sugar price-support loans. In regard to this option, the sugar not marketed or committed for sale by November 7, 1977, would have been eligible for price-support loans, assuming minimum wages required for eligibility had been paid to agricultural field workers.

The processor/refiner officials also expressed concern that lower price-support payments would have reduced their payments to Louisiana growers for their sugarcane.

Payments may have been made
on expired commitments

USDA paid at least three beet sugar processors more than \$800,000 in price-support payments for sugar sold under contracts that may not have met program marketing requirements. Moreover, additional payments of this kind, which were not identified during our review, are possible if sales under contracts which are not eligible for price-support payments are claimed and approved as eligible for the payment program. The contracts were entered into by November 7, 1977, the date by which sugar had to be committed to be eligible for the price-support payment program. Sales claimed under these contracts after the delivery periods had expired may have been commitments made after the cutoff date for payment eligibility and so were ineligible for the payment program, depending on the specific circumstances of each contract.

Sugar beet processors often reported sugar as committed by November 7, 1977, based on contracts to sell to purchasers a specified amount of sugar by a certain date. In many cases, however, the purchasers did not request delivery of the sugar by the date specified. For example,

in August a buyer sent a purchase order to a processor for 500,000 pounds of sugar to be delivered by December 31, 1977. At the end of December, only about 173,000 pounds had been requested by the purchaser. In March 1978 the processor delivered and received a price-support payment for another 42,000 pounds of sugar and on May 30, 1978, was still holding open the balance of 285,000 pounds for future requests from the buyer.

We explored whether deliveries of sugar under a contract whose specified delivery period had expired was a valid contract qualifying for USDA price-support payments. We concluded that no clear-cut answer can be given. Generally, under such contracts sugar processors are not contractually committed to deliver the sugar after the contract delivery period has expired. They are only obligated under the contracts to deliver sugar during the period agreed upon. However, if the parties have modified or waived the delivery terms of the contracts, the contracts remain in effect. The deliveries would then be made pursuant to a contractual commitment entered into before November 8, 1977. In such cases, support payments could be allowed. Consequently, the specific circumstances surrounding each contract must be examined to determine payment program eligibility.

USDA has taken the position that support payments should not be allowed in such a situation. It maintains that sellers were under no contractual obligation to make deliveries after expiration of the agreed delivery period. Thus, these deliveries should not be considered "eligible marketings." In the Department's opinion:

"To the extent that deliveries were made under an agreement in accordance with the terms of the agreement as entered into and/or modified prior to November 8, 1977, such deliveries should be treated as eligible marketings of 1977 crop sugar under the payment program. Those deliveries which occurred after the delivery period specified in the agreement as of November 7, 1977, should not be considered eligible marketings, since the seller was under no contractual obligation (i.e. an obligation entered into prior to November 8, 1977) to make such sales."

In USDA's view, this sugar was available to be placed under the loan program.

At least three beet sugar processors may have received price-support payments in excess of \$800,000 on deliveries claimed after contracted delivery periods ended.

Payments for "1976-crop" sugar

USDA approved paying a beet processor about \$500,000 for sugar produced from the "1976 crop," even though program regulations limit sugar eligible for payments to that produced from the "1977 crop." The original payment program documentation filed by this company with USDA showed 1977-crop sugar sales beginning September 3, 1977. The company had started to process sugar from its 1977 sugar beet crop on September 3, which consequently is the earliest date on which it could have filled orders with sugar from its 1977 crop. The company subsequently filed revised documentation indicating August 1977 sugar sales which had to be filled with sugar produced from the "1976 crop," since it told us it did not begin producing sugar from its "1977 crop" until September 3.

Although an ASCS official told us that the company could not have had 1977-crop sugar available in August 1977 with which to fill orders, USDA apparently administratively approved the payment because it was sold during the processor's 1977 marketing year. Stated differently, the ASCS interpretation treats as "1977 crop" that sugar which the processors and growers have contractually agreed to treat as 1977-crop sugar for the purpose of sharing proceeds. The regulations, however, specify that price support is for 1977-crop sugar beets and sugarcane. Hence, it is unclear whether the regulations are susceptible to the administrative interpretation given them by ASCS. The regulations, however, specify that price support is for 1977-crop sugar beets and sugarcane. Sugar produced from the "1976 crop" would by definition be ineligible.

USDA has already amended program regulations two times to redefine eligible sugar and had made an administrative decision to further extend the eligibility, pending a legal opinion, to permit the practice described above. In this regard, USDA has requested our advice on this issue and our response is currently under development.

USDA's Office of Inspector General, in its broader review of the payment program, stated that

"ASCS made an administrative decision which permitted program participants to claim support payments of \$8.9 million on prior years' sugar. This decision was not documented in any written

format but had been communicated to program participants verbally. Some participants were not aware of the ASCS decision, and implementation was not uniform among those who were. Program legislation and regulations extend eligibility only to 1977 crop sugar. We reported these conditions to ASCS in an interim report, dated May 28, 1978. We have also referred this matter to the Office of General Counsel for its opinion on the legality of the ASCS decision."

PRICE-SUPPORT PAYMENTS PAID ABOVE
THE ESTABLISHED SUPPORT LEVEL

Under the applicable regulations the amount by which the 13.5-cent support level exceeded the average market price was paid to all processors who qualified for the payment program regardless of whether any one processor sold sugar at a price such that the selling price plus the Government payment exceeded the support level. As a result, moneys received by some processors, including support payments, exceeded the support level.

Through May 31, 1978, 38 of 73 processors participating in the program have received payments in excess of the support price totaling about \$20.8 million. Table 2, based on our review of the sugar processor forms filed with USDA, provides greater detail and shows an analysis of the price received per pound and the total Government moneys paid to the 38 processors receiving payments in excess of the support level. As shown in table 2, payments above the support level resulted in a price per pound of up to 15 to 15.5 cents. The number of processors receiving prices above the support level, including Government payments, ranged from six getting 13.5 to 14 cents per pound, with payments of \$1.4 million in excess of the support level, to five receiving 15.01 to 15.5 cents per pound, with payments in excess of the support level of \$11.1 million.

While there is no prohibition on payments which, when added to the selling price received by a processor, would result in proceeds above the support level, we believe the Government payments should have been restricted so that the sum of payments and selling price do not exceed the 13.5 cent per pound support level for any processor, as the price-support program should support the price up to some predetermined level (in this case 13.5 cents per pound) and not above that level. We believe that the payment regulations implicitly recognize this because they state that when the average market price was equal to or greater than 13.5 cents, there would be no payments.

Table 2

Analysis of Payments in Excess of the Support level

<u>Area</u>	<u>Number of processors and price per pound including Government payments</u>					<u>Payments in excess of the support level in each price category</u>				
	<u>13.5</u>	<u>14.01</u>	<u>14.51</u>	<u>15.01</u>	<u>Total</u>	<u>13.5</u>	<u>14.01</u>	<u>14.51</u>	<u>15.01</u>	<u>Total</u>
	<u>to</u>	<u>to</u>	<u>to</u>	<u>to</u>		<u>to</u>	<u>to</u>	<u>to</u>	<u>to</u>	
	<u>14¢</u>	<u>14.5¢</u>	<u>15¢</u>	<u>15.5¢</u>		<u>14¢</u>	<u>14.5¢</u>	<u>15¢</u>	<u>15.5¢</u>	
	----- (million) -----									
Sugar beet States (note a)	5	0	0	0	5	\$1.3	\$ 0.0	\$0.0	\$ 0.0	\$ 1.3
Sugarcane States:										
Florida	0	1	3	1	5	0.0	0.5	2.1	4.7	7.3
Louisiana	<u>1</u>	<u>5</u>	<u>18</u>	<u>4</u>	<u>28</u>	<u>0.1</u>	<u>1.2</u>	<u>4.5</u>	<u>6.4</u>	<u>12.2</u>
Total	<u>6</u>	<u>6</u>	<u>21</u>	<u>5</u>	<u>38</u>	<u>\$1.4</u>	<u>\$1.7</u>	<u>\$6.6</u>	<u>\$11.1</u>	<u>\$20.8</u>

a/Sugar beets were produced in 17 States in 1977.

We discussed this subject with USDA officials, who expressed the strong belief that to limit payments such that the sum of Government payments and selling price do not exceed the support level would cut the effectiveness of the incentive to sell sugar at a higher price. According to USDA officials, this is the principal reason the program is operated in a fashion that leads to payments above the support level. Without this incentive USDA officials believe that firms would be willing to cut prices, knowing that the Government would be making more payments to them.

We do not believe that an incentive of Federal payments which, when added to the selling price received by a processor, results in proceeds above the support level is necessary, as firms would seek the highest price they could obtain regardless of whether they received direct payments. If firms were to sell their sugar for more than the support level, they would profit. In 10 specific instances through May 31, 1978, firms reported a selling price of more than the 13.5-cent support level, which yielded them proceeds that totaled almost half a million dollars above the support price. In addition to these moneys, which resulted from the firms' marketing efforts, these firms received more than \$3.6 million in Federal payments, all of it above the support level cited earlier. Since these firms already received more than the support level from their marketing efforts, we do not believe that if they received no payments above the support level they would slacken their marketing efforts; if anything they might increase them since by selling above the support level they could increase their gross proceeds.

Moreover, USDA officials advised us that processors do not know where they stand in getting support payments until after their sales are made; consequently, they can not depend on a specific Government payment if they relax their marketing effort. This is because the price support payment is based on the average market price and no one firm knows where its selling price will stand in relation to the average. We believe that if payments are limited such that the sum of Government payments and selling price do not exceed the support level, firms would still not know where they stand in getting support payments; they still could not depend on a certain Government payment; and therefore we see no reason why they would relax their marketing efforts. Since the program is not permanent, we further believe that firms would maintain a vigorous marketing effort to remain competitive when there is no payment program and that vigorous marketing cannot simply be turned on and off.

A secondary reason offered by USDA for operating the program in the current fashion is the precedent of a number of support programs for other commodities which also make payments based on averages. We are not in a position to comment on the operation of these programs at this time, but when we review those programs we will give further consideration to this matter.

Since payments are based on the average market price, firms that sold sugar for less than the average receive a total price, including the support payment, which is below the 13.5-cent support level. It might be argued that firms selling for less than the average should receive the full difference between their actual selling price and the support level. USDA officials told us that if they were to do this, processors would sell sugar for whatever price they could get and would also undercut competitor prices, knowing that the Federal Government would make up the difference to achieve the support level. USDA told us that this approach was considered but that it was discarded after very brief consideration. We agree with USDA that such payments would be a disincentive for companies to market sugar vigorously. However, as discussed on page 20, we do not believe that Federal payments above the support level are needed as an incentive to sell sugar at a higher price.

PRICE-SUPPORT PAYMENTS BASED ON INCORRECT
DATA RESULTED IN UNDERPAYMENTS TO PROCESSORS

The failure of three processors to comply with USDA regulations on the calculation of gross proceeds and quantity of sugar marketed resulted in underpayments to processors of \$465,000.

In response to USDA regulations, processors submitted reports showing the quantity of sugar marketed and gross proceeds to USDA for a base year ending June 30, 1977, and for each marketing period established for the price-support payment program. USDA made price-support payments based on this data. According to program regulations, support payments were to be based on the adjusted raw value weight of sugar, a weight which differed from actual weight.

Payment program regulations defined gross proceeds as total receipts from the sale of refined beet and raw cane sugar at the factory less all allowances and discounts and before any insurance or freight adjustments. The regulations also required beet processors to include in gross proceeds price differentials for sugar in other than bulk form.

Because three sugar processors included in our review erroneously reported to USDA the quantity of sugar marketed and/or the related gross proceeds, all processors were underpaid about \$465,000 for the first seven marketing periods established for the price-support payment program. The underpayments occurred primarily because a beet processor should have deducted about \$294,000 in price discounts from gross proceeds received for sugar marketed, as required by program regulations. Because the discounts were not deducted, the processor overstated gross proceeds which resulted in overstated average market prices used by USDA to compute price-support payment amounts for each marketing period. USDA officials said that they were not aware of this and would follow up on it.

PRICE-SUPPORT UNDERPAYMENTS TO SUGARCANE PRODUCERS

Although the price-support payment program regulations dictate that sugar beet and sugarcane processors will pay producers a specified minimum price for their unprocessed commodities, we found that some of the processors we visited in Louisiana will underpay producers by about \$3.5 million based on their plans for making final payments to them. In the beet-producing States, five processors will underpay producers under the operation of their traditional contracts, which is permitted by USDA regulations.

Underpayments to Louisiana sugarcane producers

The price-support payment regulations specify that producers of sugarcane in Louisiana will be paid the general support price of \$15.90 per net ton of sugarcane of average quality by processors who participate in Louisiana. USDA payment program regulations also require processors to pay producers any amount over and above the support price which results from contractual agreement or from normal and traditional methods of settlement between producers and processors. We found that six processors, including two processor/refiners, could underpay their growers by more than \$3.5 million.

USDA officials told us that in computing the payments due producers, processors should deduct the applicable freight allowance for their area from their sales proceeds (inclusive of subsidy payments) and then multiply this result by a 1.06-percent pricing factor used in Louisiana. The wide variety of methods we found Louisiana processors using in paying producers indicates that USDA did not provide adequate instructions on the proper method for computing

grower payments. Essentially, the underpayments could occur because processors did not include all subsidy payments received in determining amounts growers should be paid. Although one of the six processors and the two processor/refiners were paying producers more than the \$15.90 per net ton minimum payment required, they were not basing the payments on total payments received for their sugar including subsidy benefits. Traditional payment practices and customs in Louisiana, however, require that producers share in all proceeds derived from the sale of sugar. On this basis, the three firms would be required to pay producers substantially more than the minimum support price.

The two processor/refiners who sell only refined sugar had traditionally paid producers based on a season's average price determined from quoted prices for raw sugar, but quoted prices were not available for the 1977 crop. Accordingly, our underpayment-to-producer estimates for these firms presume that payment to their producers should be based on average prices received by other Louisiana processors who participate in the payment program, increased by subsidy payments received by the processor/refiners.

AGRICULTURAL WORKERS DO NOT SHARE BENEFITS

The payment program does not contain any wage provision, and so growers are not required to share payment benefits with agricultural workers. USDA officials informed us that the Agricultural Act of 1949, the legislative authority for the program, does not provide authority to require minimum wages for the price-support payment program. In contrast, the Congress mandated that in carrying out the sugar loan program under section 201 of the Agricultural Act of 1949, as amended by section 902 of the Food and Agriculture Act of 1977, the Secretary of Agriculture establish minimum wage rates for agricultural employees engaged in sugar production. The rates set were above the Federal minimum wage. The now defunct Sugar Act also mandated minimum wages for sugar agricultural workers.

CONCLUSIONS

The administration of the sugar price-support payment program has resulted in what we believe to be questionable payments of about \$26.9 million to processors. These payments resulted from a variety of decisions made by USDA in the promulgation and administration of the payment program regulations. In addition, we believe that the method used to calculate the average market price for sugar produced in Hawaii results in a residual that may be one method

for sharing proceeds from refined sugar sales but does not represent a true selling price that would be established between unrelated buyers and sellers of raw sugar. The USDA method, in our opinion, distorts the national average market price.

Payments of about \$6.1 million have been made for sugar which we believe may not be eligible for participation in the payment program. In one instance we question the methods of determining eligibility and marketing which USDA permitted the three processor/refiners in Louisiana in claiming payments. In a second instance sugar sold under contracts whose delivery periods had expired were administratively ruled eligible, while we believe that these contracts may not have met program marketing requirements, depending on the specific circumstances surrounding the contracts. However, in a recent legal opinion, USDA has taken the position that deliveries occurring after the delivery period specified in the agreement as of November 7, 1977, should not be considered eligible marketings. In a third instance, it is unclear whether administratively approved payments on "1976 crop" sugar comport with program regulations.

The program regulations permit payments that, when added to the selling price received by some processors, result in proceeds above the support level since all eligible participants receive the same payment per pound regardless of the price at which they actually sell their sugar. We believe that the sugar price-support program should support the price up to some predetermined level and not above that level. Through May 31, 1978, this practice has resulted in payments in excess of the support level totaling about \$20.8 million.

Because three sugar processors included in our review failed to comply with USDA regulations in reporting some of the information needed to compute payments, all processors in the payment program were underpaid a total of about \$465,000.

Some sugar processors could pay about \$3.5 million less than would otherwise have been paid to their producers. In these cases, USDA did not provide sufficiently explicit directions on how producer payments were to be computed.

The Congress mandated in the amendment of the Agricultural Act of 1949 that in carrying out the sugar loan program the Secretary of Agriculture establish minimum wage rates for agricultural employees engaged in sugar production. The now defunct Sugar Act also mandated minimum wages for

sugar agricultural workers. The Agricultural Act of 1949, which also provides the authority for the price-support payment program, does not provide authority to require minimum wages under the program. Consequently, sugar agricultural workers do not share in the payment benefits accruing to growers.

RECOMMENDATIONS TO THE
SECRETARY OF AGRICULTURE

To improve the operation of the payment program, with respect to 1977 crop sugar as well as any future payment program, we recommend that the Secretary of Agriculture

- review all contracts to identify those which do not comply with requirements for the cutoff date for payment eligibility and examine all future claims to insure that they are based on contracts which meet payment program eligibility requirements and, if appropriate, adjust payments;
- provide adequate written instructions to processors on how benefits should be passed on to producers and require assurance that all producers receive equitable payments for their products; and
- review the payments to the three raw sugar processor/refiners in Louisiana and if necessary adjust payments to them accordingly.

To improve the operation of any future payment program, we also recommend that the Secretary of Agriculture

- reconsider the method used to compute the average market price for Hawaiian sugar for any future price-support payments.

RECOMMENDATIONS TO THE CONGRESS

Present law provides little guidance as to how the sugar payment program is to be implemented. In the event the Secretary of Agriculture operates a payment program as part of overall sugar policy in the future, the Congress should consider providing more specific guidance on program implementation. In particular, the Congress should consider whether payments to any processor should be limited such that the sum of the Government payment and the selling price received by any processor in any payment period does not exceed the support level.

Also, to assure more equitable treatment of sugar agricultural workers in any future sugar payment program, we recommend that the Congress specify that future sugar payment programs contain minimum wage provisions for agricultural workers to allow them to share in program benefits.

AGENCY COMMENTS AND OUR EVALUATION

The Department of Agriculture agrees with our recommendation to provide adequate written instructions to processors on how to share benefits with producers and assure that all receive adequate payments. USDA also agrees with our recommendation that it reconsider the method used to compute the Hawaiian average market price for sugar in any future payment program. However, USDA believes that we did not consider that replacing the payment program with the loan program gave Hawaiian sugar relatively more importance in the payment program as compared to its proportion of total U.S. sugar production. We recognize that the change in programs gave greater weight to Hawaiian sugar's impact on the payments, but our concern is with the method used to compute the average market price for Hawaiian sugar.

We suggested that payments to any processor be limited to no more than the support level. USDA believes that if payments were limited to the support level there would be a strong disincentive to individual processors to obtain a high market price. We do not believe an incentive involving payments above the support level is needed to encourage getting the best price possible. As we noted, some firms actually sold sugar for more than the support level, and we do not believe they would slacken their marketing efforts. If anything these firms might increase them, since by selling above the support level they increase their gross proceeds.

We also noted that USDA advised us that processors do not know where they stand in getting support payments until after sales are made because they do not know how their selling price compares with the average. We believe if payments were limited such that the sum of Government payments and selling prices did not exceed the support level they still would not know where they stand in getting support payments, since the average is based on all individual sales of program participants. Consequently, they would not be able to relax their marketing efforts since they could not depend on a certain Government payment. USDA also notes that there is ample precedent for this payment method in other commodity programs. We are not in a

position to comment on these programs now, but when we review those programs we will consider this matter further.

Our recommendations to (1) review payments to the three raw sugar processor/refiners in Louisiana and (2) review all contracts to identify those not complying with cutoff date requirements and examine all future claims to insure eligibility have been referred to USDA's Office of General Counsel. We understand that the issue of payments to the three processor/refiners in Louisiana is currently under investigation and a decision is expected in the near future. As noted earlier, a recent USDA legal opinion has taken the position that delivery occurring after the delivery period specified in the agreement as of November 7, 1977, should not be considered eligible marketings. Also, the question of payments approved on "1976 crop" sugar has been referred by the Secretary of Agriculture to us for our legal opinion.

CHAPTER 3

PRICE-SUPPORT LOAN PROGRAM

The conference report on the Food and Agriculture Act of 1977 stated that the loan program would provide needed support to the industry without any significant outlay of Federal funds. The conferees expected that the executive branch would utilize existing authority of law to implement immediately, upon the act becoming law, an import fee or duty, which, when added to the current import duty, would enable sugar to sell in the domestic market at not less than the effective support price. However, it seems evident that significant Federal expenditures will be made as a result of forfeiture of much of the sugar serving as collateral for \$176.1 million of price-support loans which were outstanding as of September 1, 1978. We believe these expenditures will be necessary primarily because imports of low-cost sugar have materially interfered with the operation of the loan program both by holding down the price of sugar and supplanting sales of domestic sugar.

USDA assigned responsibility for administering loans, from receipt of applications through issuance of sight drafts, to certain designated ASCS State and county committees. In Florida and Louisiana, all loans were administered by a specially designated ASCS County Executive Director. In the beet-producing States we visited, loans were administered by the various State ASCS offices, with one exception which was handled at the county ASCS office.

LOAN PROGRAM OPERATION

The implementing regulations for the loan program stipulate that price support, in the form of nonrecourse, 6-percent loans, will be provided to sugar beet and sugar-cane processors for 1977-crop sugar at a level of at least 52.5 percent of parity, but not less than 13.5 cents per pound, raw sugar equivalent.

The price-support loans mature 11 months after the last day of the month in which they are made, at which time the processor must redeem the loan or forfeit the sugar used as collateral. The sugar used as collateral must (1) have been produced from the 1977 crop, (2) be owned by the eligible processor or producer, (3) be maintained in the processor's storage, and (4) not have been reported as marketed under the price-support payment program.

To be eligible for participation in the loan program, processors must have paid their producers the same minimum

support prices as required under the price-support payment program, and minimum wages were required to be paid to agricultural employees engaged in the production of sugar.

SUGAR IMPORTS THREATEN LOAN PROGRAM SUCCESS

On April 17, 1978, the U.S. International Trade Commission reported to the President that imports of sugar are materially interfering with domestic sugar price support programs administered by USDA and recommended that import fees on such sugar be increased and quantitative limitations be imposed if certain conditions are met. The Commission's determination and recommendation were the culmination of a 5-month investigation under section 22 of the Agricultural Adjustment Act, as amended, which was conducted at the request of the President.

The Commission found that the price at which foreign sugar is available for export to the United States by potential foreign suppliers, coupled with the duty fee and cost of insurance and freight from greater Caribbean ports as of April 17, 1978, was only slightly above the support price and was below the redemption level of sugar if placed under price-support loan and not redeemed until the end of the marketing year.

The domestic sugar problem was found to be further complicated by the inordinate volume of sugar imported in late 1977 in anticipation of higher fees and duties. After the announcement of the price-support program and before the effective date of the increased duties and fees, approximately 1.5 million tons of raw sugar were imported into the United States. Because of the presence of these large stocks of lower priced imported sugar, domestically produced raw sugar was being placed under the loan program. With world production in excess of world consumption, the Commission concluded it is practically certain that, given unrestricted access to the U.S. market, foreign producers will undersell domestically produced sugar and force it into the loan program, thereby burdening and interfering with the price-support program.

The conditions affecting refined sugar were also found to threaten the U.S. sugar industry. Currently, 1/ refined sugar is available in world markets at prices almost as low as that of the world price of raw sugar. After paying the duties and fees currently in effect, refined sugar can be

1/The Commission report was issued Apr. 17, 1978.

imported at prices well below those which will reflect the minimum levels required by the legislation mandating the price-support loan program.

STORAGE AND DISPOSAL PROBLEMS
FOR SUGAR USED AS COLLATERAL
FOR PRICE-SUPPORT LOANS

USDA is considering but has made no final plans for disposing of sugar used as collateral under the price-support loan program in the event that processors choose not to redeem the loans. A final rule, effective November 24, 1978, was issued by USDA on November 29, 1978, to extend the maturity dates on loans to discourage defaults. Despite this, on December 1, 1978, USDA became the owner of more than 192 million pounds of sugar as the result of loan defaults in Florida and Texas.

Only one Louisiana processor has obtained a loan. However, four of the six processors in Florida as of September 1, 1978, had more than 665 million pounds of sugar stored in their warehouses as loan collateral, and there is little likelihood that prices will rise sufficiently to enable these processors to sell this sugar before their loans mature in 1978. All of these processors stated that loans probably will not be paid unless sugar prices are at least high enough to cover the loan and interest costs, and they do not foresee that prices will go that high in the near future. More than 273 million pounds of Florida raw sugar has been forfeited as of January 31, 1979, and USDA officials believe that another 30 million pounds will be forfeited by May 31, 1979.

The sugar warehouses of those Florida processors receiving loans were full as of May 1978, and some processors have rented warehouse space from other firms. One converted a vehicle storage shed for storage, and another stored raw sugar under a circus tent until suitable space could be rented from another processor.

Faced with the prospect of being unable to sell their sugar because of low prices, Florida processors expressed grave concern in May 1978 that USDA has been indifferent to their plight and that, as a result, they will have no space for their 1978 crop when harvesting begins in October or November. They feel that they may have no alternative but to build additional warehouse space, at very high cost, which may sit idle in the future. USDA officials told us that the Florida storage problem has been largely corrected through securing additional storage space, including some several hundred miles away.

Substantial amounts of sugar under price-support loans are being forfeited primarily because of the low market price for sugar and interest charges which the processors have incurred on the loans which must also be repaid if the loans are redeemed. Through January 31, 1979, almost 374 million pounds of sugar valued at \$50.5 million were forfeited to USDA--more than 100 million pounds valued at \$13.6 million in Texas and more than 273 million pounds valued at \$36.9 million in Florida.

As USDA takes possession of forfeited sugar, it is faced with the problem and cost of storing this perishable commodity. Storage costs alone are expected to be significant. USDA would pay storage costs.

USDA would also be responsible for marketing the forfeited sugar and any deterioration in the stored sugar would probably raise handling costs and reduce its commercial value. The storage life of sugar depends on how it is stored, but under proper conditions it could be stored for extended periods. A Florida processor was concerned that USDA will unload all of this sugar on the market, further depressing prices and inhibiting the sale of its future production.

INEXPLICIT DIRECTIONS BY USDA LED TO UNDERPAYMENTS TO SUGARCANE PRODUCERS

Loan program regulations require that sugar beet and sugarcane processors pay producers the same minimum prices for their products as those required under the price-support payment program. One sugarcane processor participating in the loan program had not paid the minimum amounts required and, accordingly, could pay growers about \$25,000 less than called for in the regulations judging from its plans for making final payments to its growers. This processor did not make minimum payments because USDA did not provide sufficiently explicit directions on how payments to producers were to be computed. The State and county ASCS officials responsible for administering the loan program were not required to either verify or enforce compliance with the minimum payment provisions, and none did.

MINIMUM WAGE REQUIREMENTS NOT VERIFIED OR ENFORCED

The loan regulations stipulated that a producer was eligible for participation in the loan program only when he certified to his processor that minimum wages were paid to agricultural workers engaged in the production of sugar.

The processor could apply for price-support loans merely by obtaining these certifications from producers, and ASCS officials who administered loans were not required to verify before July 1978, in any way, that the required minimum wages were paid. USDA officials said instructions were issued in July 1978 which require ASCS field personnel to make spot checks to determine that producers comply with the wage rate requirements. We found that the required wages had not been paid in several cases. We did not review enough wage payments to assess whether the failure to pay minimum wages was widespread, but the fact that our spot check in Florida revealed several cases where required wages had not been paid indicates that it could be a significant problem.

The Food and Agriculture Act of 1977 contains no provisions for punitive action for noncompliance with the wage rates established. Minimum wage rate regulations issued by USDA, however, state that "* * * we can only provide an incentive for compliance by limiting sugar price support benefits to those producers who pay at least the minimum rates established * * *." We found no evidence that support benefits were limited because of noncompliance with the minimum wage rate regulations.

All Florida and Louisiana processors secured the required minimum wage rate certifications from their producers. The responsible ASCS County Executive Directors did not examine the validity of the certifications.

Our limited verification of wage payments disclosed that some processors had complied with wage payment requirements and that others had not. One processor received a loan on sugar purchased from a large growers' cooperative that had not paid minimum wages but planned to pay them. A large, independent grower we visited started paying minimum wages in January 1978 but had not paid the wages retroactively to November 8, 1977, as required. The independent grower said checks were being prepared at another location to pay the retroactive wages.

A Florida processor had not obtained a loan at the time of our visit but had obtained certifications from growers that minimum wages had been or would be paid. A processor official, however, said he knew the growers had not paid the minimum wages. USDA records show that this processor later received price-support loans.

The one Louisiana processor who had received assistance under the price-support loan program had paid the required minimum wages to its own agricultural employees and had

obtained wage certifications from its independent producers. We attempted to locate three of these producers but were unable to do so. However, we determined that they are only part-time farmers, employing only family labor, and that the wage rate certifications were meaningless, since they employed no outside help.

In some beet-producing States, most of the harvest was completed before minimum wages became effective. Of six ASCS offices visited, three did not require processors to obtain the wage certifications, two reviewed the processor certifications, and the remaining office did not receive a loan application. None of these ASCS offices reviewed grower records to determine the validity of the certifications.

CONCLUSIONS

Although the conference report on the Food and Agriculture Act of 1977 stated that it expected that needed support would be provided without any significant outlay of Federal funds, it seems evident that significant expenditures will be made under the loan program because substantial loan defaults are occurring.

The conferees expected that the executive branch would utilize existing authority of law to implement immediately, upon the act becoming law, an import fee or duty, which, when added to the current import duty, would enable sugar to sell in the domestic market at not less than the effective support price. However, low-cost sugar imports have held down the price of domestic sugar and supplanted domestic sugar sales. As noted in our report entitled "Sugar and Other Sweeteners: An Industry Assessment" (CED-79-21, Feb. 26, 1979), the successful use of loans depends on the world price of sugar and the level of tariffs and fees.

There are no final plans to dispose of forfeited sugar, although USDA is considering the matter. In addition, there has been a serious storage problem for sugar held by processors as collateral for price-support loans. This is a problem which could ultimately be costly to the Government as substantial loans are defaulted.

One sugarcane processor has not paid minimum prices to producers because of inadequate instructions from USDA on how growers should be paid. With respect to minimum wages mandated for the loan program, USDA has not adequately enforced minimum wage rate requirements for agricultural field workers.

RECOMMENDATIONS TO THE SECRETARY
OF AGRICULTURE

To rectify the problems found in the loan program for 1977-crop sugar, we recommend that the Secretary of Agriculture

- adopt a plan to allow for the handling and disposition of any sugar forfeited as a result of loan defaults,
- provide adequate written instructions to processors on how benefits should be passed on to producers, and
- insure compliance with the minimum wage requirements for agricultural field workers by reviewing wage payments made to these workers.

AGENCY COMMENTS AND OUR EVALUATION

USDA agrees with our recommendation to provide written instructions to processors on how benefits should be passed on to producers. Concerning the 1977 crop, USDA intends to request its Office of Inspector General to spot check processor compliance for both the loan and payment programs. For the 1978 crop, USDA states that processors must certify in their loan applications that they will pay producers in accordance with the regulations. USDA will include instructions to loan-making offices on conducting compliance checks.

With respect to our recommendation to insure compliance with minimum wage requirements for agricultural fieldworkers, USDA intends to vigorously pursue this matter. In one instance where noncompliance was discovered USDA has required payment of wages due, verified that such wages have been paid, and instructed loan-making offices to expand the check to 100 percent of all producers involved.

USDA notes that plans for the safe storage of sugar forfeited to the Commodity Credit Corporation have been completed and are being implemented. With respect to the disposition of forfeited sugar, USDA notes that options are limited, but that it is actively exploring the best, albeit limited, prospect, which is donations to domestic food assistance programs.



UNITED STATES DEPARTMENT OF AGRICULTURE
AGRICULTURAL STABILIZATION AND CONSERVATION SERVICE
P. O. BOX 2415 . . . WASHINGTON, D. C. 20013

FEB 5 1979

Mr. Henry Eschwege
Director
Community and Economic
Development Division
U.S. General Accounting Office
441 G Street, N.W.
Washington, D.C. 20548

Dear Mr. Eschwege:

This is in response to your letter of December 7, 1978, enclosing the draft of your audit of the sugar payment and loan programs.

We have reviewed your draft report as requested. In your report you make four major recommendations regarding the payment program and three regarding the loan program based on your findings. We will discuss each in turn:

The payment program:

1. Reconsider the method used to compute the average market price for Hawaiian sugar for any future payments.

When the regulations for the payment program were being drafted we recognized that calculation of market returns for Hawaiian sugar presented a special problem. Hawaiian processors market their raw sugar through the California and Hawaiian Sugar Company (C&H), an agricultural cooperative owned by the Hawaiian processors. C&H refines and markets sugar on their behalf, and proceeds are divided up among the member processors according to (a) the amount of raw sugar each delivers to C&H, and (b) the market proceeds obtained by C&H from the sale of refined sugar. Therefore, net income to C&H is actually gross returns to the member processors. We reasoned that unless the price received by the Hawaiian processors for their raw sugar was adjusted by some amount to offset the return properly attributable to sales of the sugar as a refined product, then the returns to Hawaiian processors would be distorted. Further, the distorted Hawaiian returns would have affected the calculation of national average market proceeds to the detriment of all program participants, both sugarcane and sugarbeet. After considering various alternatives and consulting with the Office of General Counsel, we decided that a deduction of up to 8 percent of C&H's net sales proceeds (gross proceeds to the member processors) from the marketing of refined sugar would be appropriate.

We believe that the effects of this decision have been distorted by the fact that the payment program was replaced by the loan program before the entire domestic beet and cane crop had been marketed. Because of this the Hawaiian crop, normally about one-sixth of the total domestic crop, accounted for upwards of 40 percent of sugar marketed under the payment program. We do not believe this factor was considered in your recommendation. Nevertheless, if a decision should be made to institute another payment program at some point in the future, we will reconsider this matter and carefully evaluate all the alternatives.

2. Review the eligibility of sugar claimed under the payment program and adjust payments on any sugar found to be ineligible. Your report states that such ineligibility arose in three different situations: (1) the method for determining eligibility is "questionable," (2) sugar was sold and delivered under contracts whose delivery periods had expired, and (3) payments were approved on 1976 crop sugar.

All three of these situations are the subject of requests to our General Counsel for legal opinions, and one of them (situation number 3 above) has been referred by the Secretary of Agriculture to the Comptroller General for his views.

We are, therefore, reserving comment on these situations until we receive the legal opinions involved.

3. Provide adequate written instructions to processors on how benefits should be passed on to producers, and require assurance that all receive adequate payments for their products.

Final payments have not been made to producers since CCC has not made final program payments to processors (10 percent was withheld). However, most processors have made pro forma final payments to producers based on estimates. Final government payments will be made once the issues raised by our own audit and your report are resolved, some of which depend on formal opinions of Counsel. Detailed instructions with respect to how payments are to be shared with producers will be issued with the final government payment. We understand that the Office of Audit, USDA, intends to reexamine the payment program, including payments to producers, when final government payments have been made to processors. We believe these steps will assure receipt by producers of full program benefits.

4. Amend the payments program regulations to limit payments to any processor to no more than the support level.

We feel that adoption of this recommendation would invite and/or encourage collusion and fraud between sellers and buyers of sugar. We now provide that all sellers report to us the proceeds received for sugar marketed

together with the associated quantity. A weighted average is then calculated. If the average for all processors falls short of the support level, a payment is made to all processors equal to the difference between the average market price and the support price. Processors are thus motivated to do the best possible job in marketing their sugar. If your recommendation were to be adopted, there would be a strong disincentive to individual processors to obtain a high market price, inasmuch as the processor would know that even if he sells for a lower price the government payment will make him whole.

We also feel strongly that adoption of this recommendation would not be in the best interest of the government. There is ample precedent for the method of payment adopted in the regulations, e.g., the deficiency payment programs for wheat, feedgrains and cotton, and the incentive programs for wool and mohair. We hold that this system has surely reduced Treasury outlays associated with all of these programs as well as the sugar program.

The loan program:

1. Adopt a plan for the handling and disposition of any sugar forfeited as a result of loan defaults.

Plans for the safe storage of sugar forfeited to CCC have been completed and are being implemented. With respect to disposition of CCC stocks, our options are limited to (a) resale in the domestic or foreign markets, (b) donation to domestic or foreign feeding programs, or (c) non-food uses, e.g. production of alcohol, use in livestock feeds, etc. Resale in the domestic market is limited by law to not less than 105 percent of the current support price, plus normal carrying charges, if sugar is determined to be a storable commodity. Under present conditions, no sales are likely. Terms of the International Sugar Agreement will prevent export sales, since the U.S. is an importing member and thus has no export quota. Donation to foreign sources is not a viable alternative, since most of the prospective recipients are themselves sugar exporters. Therefore, donations to domestic food assistance programs may offer a prospect, albeit a limited one, for disposal of CCC stocks. We are actively exploring this alternative.

2. Provide adequate written instructions to processors on how benefits should be passed on to producers.

We will issue such instructions for 1977 crop loans along with the final instructions on how to share the benefits of the payment program. Since it will be necessary to look at total 1977 crop benefits received by producers under both the loan and payment program, we will request

the USDA Office of Audit to spot check processor compliance for the 1977 crop as a whole. With regard to the 1978 crop loan program, the regulations provide that processors are to pay producers a minimum price per ton of average quality beets or cane with adjustments in that price for non-average quality beets or cane as agreed upon between the producer and processor. Processors must certify in their application for loan that they will pay producers in accordance with the regulations. Instructions to loan making offices on conducting compliance checks will be included in ASCS Handbook 10-SU--Sugar Loans.

3. Insure compliance with the minimum wage requirements for agricultural fieldworkers by reviewing wage payments made to these workers.

We have issued instructions to State and county office personnel regarding verification of producer compliance with wage certifications submitted to processors. We have since supplemented those instructions in considerable substance and detail. In cases where spot checks reveal noncompliance, we instruct loan making offices to expand the check if considered necessary. It is our intent to pursue this matter vigorously. In that instance where you discovered noncompliance (believed by us to be in Florida), we have required payment of wages due, have verified that such wages have been paid, and have instructed loan making offices to expand the check to 100 percent of all producers involved.

Finally, we found your report in general to be carefully researched, and well written. We appreciate the assistance you have provided in the administration of this complex and controversial program.

Sincerely,


Stewart N. Smith
Administrator

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