



# **Tobacco-Related Programs and Activities of the U.S. Department of Agriculture: Operation and Cost**

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## Summary

The U.S. Department of Agriculture (USDA) has long operated programs that directly assist farmers and others with the production and marketing of numerous crops, including tobacco. In most cases, the crops themselves have not been controversial. However, where tobacco is involved, the use of federal funds has been called into question. Taken together, all of the directly tobacco-related activities of the USDA generated net expenditures of an estimated \$30.8 million in FY2006, and the budget anticipates net expenditures of \$29.5 million for FY2007. Over 90% of this spending is related to crop insurance.

The federally financed tobacco price support program, once the major form of tobacco farmer assistance and in some years a costly program, was terminated at the end of crop year 2004. The USDA is prohibited by language in the annual appropriations law from spending funds to help promote tobacco exports and to conduct research relating to production, processing, or marketing of tobacco and tobacco products. Other tobacco-related activities have been subjected to congressional scrutiny. The USDA does operate numerous programs that are not tobacco-specific, but are available to farmers that produce tobacco and other crops. These are not examined in this report.

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## Price Support Program

From the late 1930s through the 2004 crop, the USDA operated the tobacco price support program. It was designed to raise and stabilize farm tobacco prices at higher levels than they otherwise would have reached. This was accomplished through a combination of farm marketing quotas and federal nonrecourse commodity loans. Administration was done through the county offices of the Farm Service Agency (FSA),<sup>1</sup> and loan program funding was provided through the Commodity Credit Corporation (CCC). In 1982, legislation was adopted that applied an assessment on all tobacco marketings to be used to offset price support losses and make the loan operations function at no net cost to taxpayers. On two occasions legislation relieved the program of its obligations on large inventories. These actions cost about \$1 billion. In addition, Congress made so-called tobacco loss payments of \$852 million during FY2000-FY2003 to offset a sharp decline in farm sales to domestic and foreign buyers. Overall, from FY1982 through FY2005, tobacco support net expenditures totaled about \$1.57 billion, for an annual average cost of \$71 million.

After Congress enacted the Fair and Equitable Tobacco Reform Act of 2004 (P.L. 108-357), the tobacco support program came to an end. Tobacco quota owners and farm operators were compensated for the diminished value of their farms and the loss of future support with a payment of \$9.6 billion over 10 years, funded by an assessment on tobacco manufacturers and importers. Because of this tobacco buyout, CCC support program expenditures have been eliminated, and it is not anticipated there will be any future *ad hoc* assistance to tobacco farmers. FSA administrative expenditures associated with the buyout are estimated to be \$1.827 million in FY2006, and the budget for FY2007 is zero.

(For additional information, see CRS Report RS20802, *Tobacco Farmer Assistance*, and CRS Report RS22046, *Tobacco Quota Buyout*.)

## Federal Crop Insurance

The federal crop insurance program, administered by USDA's Risk Management Agency,<sup>2</sup> provides farmers with subsidized multi-peril insurance on tobacco and other crops. The insurance covers unavoidable production losses due to adverse weather, insect infestations, plant diseases, and other natural calamities. It does not cover avoidable losses caused by neglect or poor farming practices. Sales and servicing of policies are done by private companies with some federal reimbursement, and most of the net indemnity losses fall upon the government. Additionally, the premiums have been subsidized since 1980 in order to encourage participation and avoid enactment of *ad hoc* disaster assistance programs. Experimental Crop Revenue Coverage, available for wheat, corn, and soybeans, is not available for tobacco.

Total net federal expenditures for tobacco crop insurance coverage include outlays for crop loss indemnity payments, plus the premium subsidies, plus sales administrative expenses, less the farmer-paid premiums. Net federal outlays are estimated to be \$27.9 million in FY2006, and are budgeted at \$28.7 million for FY2007.

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<sup>1</sup> <http://www.fsa.usda.gov/FSA/webapp?area=home&subject=toba&topic=landing>.

<sup>2</sup> <http://www.rma.usda.gov/>.

## **Tobacco Inspection and Grading**

The USDA's Agricultural Marketing Service (AMS)<sup>3</sup> carries out voluntary inspection and grading services at tobacco auction markets and import terminals. The establishment of uniform standards of quality, with grading by unbiased experts, helps assure that auction markets perform efficiently and fairly. Historically, federal grading provided an assurance of quality for tobacco held as collateral for CCC price support loans. Additionally, imported and domestic tobacco is inspected voluntarily to guard against illegal pesticide residues. Since 1981, the grading and inspection services have been financed through user fees (now set at \$0.62 per 100 pounds for grading and \$0.85 per 100 pounds for pesticide testing). These fees are sufficient to fully cover the costs of inspection activities as well as the cost of developing and maintaining the standards applied by the inspectors. This has dramatically reduced the use of AMS inspectors. AMS inspection work now is done on imported tobacco, as nearly all of the domestic crop is contracted for sale rather than auctioned.

## **Market News Services**

The Agricultural Marketing Service<sup>4</sup> provides a market news service for sellers and buyers of tobacco. Daily reports of grades, prices, and sales volume at the auction markets are distributed throughout the tobacco industry. The cost of the tobacco news service in FY2006 is an estimated \$190,000, and the budget for FY2007 is \$194,000. Similar market news services are provided for all major agricultural commodities. Market news services are designed to provide farmers, and others in the marketing chain, with timely, accurate, and unbiased information on market conditions, to help them make better decisions on where and when to sell and buy commodities. According to economists, such information is necessary for a market economy to function efficiently and effectively. In the absence of a taxpayer-funded market news service, the information might be collected and sold by commercial enterprises, but questions of bias could arise.

## **Tobacco Research**

In the past, USDA-funded research related to tobacco production, processing, and marketing. Some of the research was carried out by Agriculture Research Service (ARS)<sup>5</sup> scientists and some was done by university scientists funded through the Cooperative State Research, Education, and Extension Service (CSREES).<sup>6</sup> Annual research spending by the USDA averaged about \$6.6 million until it was terminated under the FY1995 agricultural appropriations law and subsequent laws. The restriction does not apply to research on medical, biotechnological, food, and industrial uses of tobacco. A special research grant of \$329,000 was approved for FY2006 to investigate alternative uses of tobacco plant material. No similar spending is anticipated in FY2007.

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<sup>3</sup> <http://www.ams.usda.gov/tob/>.

<sup>4</sup> <http://www.ams.usda.gov/tob/>.

<sup>5</sup> <http://www.ars.usda.gov/main/main.htm>.

<sup>6</sup> <http://www.csrees.usda.gov/>.

## **Extension Education**

The jointly funded federal-state-county extension education and technical assistance program is designed to serve as a link between the nation's agricultural research institutions and farmers. The term extension conveys the concept of extending the work of researchers into the community. At the county level, extension agents distribute information and expert advice to farmers and others through published materials, seminars, and direct consultation. The state extension staff, given their close proximity to researchers, continuously trains the county agents and designs and prepares materials for use by the county agents. In FY1997, CSREES spent \$680,000 on tobacco-related extension activities. Federal funding was eliminated in FY1998 by the Administration and remains at zero. All state and county extension activity related to tobacco is funded by the states.

## **Economic Analysis**

The Economic Research Service (ERS)<sup>7</sup> is responsible for assembling and analyzing economic data and forecasting market data within the USDA. As with the other major commodities, ERS assembles and analyzes supply and demand data on tobacco. ERS periodically publishes analytical findings in a Tobacco Situation and Outlook Report. Economists also conduct studies on related topics, such as the structural characteristics of tobacco farming, the role of tobacco in local economies, and the likely impact of program changes and policy options. ERS spending on tobacco analysis during FY2006 is estimated at \$123,000, and the budget for FY2007 is \$125,000.

## **International Data Collection and Analysis**

The Foreign Agriculture Service (FAS),<sup>8</sup> through its network of agricultural counselors and attaches, collects economic intelligence throughout the world. This intelligence is used by trade negotiators, economists, policymakers, and the business community. Tobacco is one in a long list of commodities on which the FAS staff collects information. The USDA estimates that the cost of this effort for tobacco will be \$200,000 in FY2006, and the budget for FY2007 is \$205,000.

## **Domestic Crop Data Collection**

The National Agricultural Statistics Service (NASS)<sup>9</sup> collects field-level data on planting intentions, crop conditions, harvesting progress, yield, and production. This information helps the business community, including farmers develop marketing plans. Also, it serves to alert policy officials of likely shortages or surpluses, thereby facilitating plans for any government action that might be taken. The information that NASS compiles and distributes is considered by economists to be critical to an efficiently functioning market economy. It is argued that the absence of NASS data would most severely disadvantage farmers and government officials, who are least able to

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<sup>7</sup> <http://www.ers.usda.gov/briefing/tobacco/>.

<sup>8</sup> <http://www.fas.usda.gov/cots/tobacco.asp>.

<sup>9</sup> <http://www.usda.gov/nass/pubs/estindx3.htm#tobacco>.

obtain information through alternative sources. Tobacco is one in a long list of commodities on which NASS staff collects information. The estimated cost of this effort for tobacco is \$231,000 in FY2005, and the budget for FY2007 is \$231,000.

**Table 1. USDA Tobacco-Related Net Budgetary Expenditures, Estimated FY2006 and Budgeted FY2007**

| <b>USDA Agency<br/>—Activity or program</b>  | <b>FY2006<br/>Estimate \$000</b> | <b>FY2007<br/>Budget \$000</b> |
|--|----------------------------------|--------------------------------|
| Commodity Credit Corporation/Farm Service Agency   |                                  |                                |
| —Administrative expenses of tobacco buyout   | 1,827                            | 0                              |
| —Tobacco price support operations  | 0                                | 0                              |
| —Direct income support payments tobacco farms  | 0                                | 0                              |
| Risk Management Agency   |                                  |                                |
| —Crop insurance (tobacco crop loss indemnity payments and administrative expenses, less grower premiums)             | 27,883                           | 28,702                         |
| Agricultural Marketing Service   |                                  |                                |
| —Market news reporting (collection and dissemination of auction market prices and sales volume data)                 | 190                              | 194                            |
| Cooperative State Research, Education, and Extension Service   |                                  |                                |
| —Special research grant on alternative uses of tobacco   | 329                              | 0                              |
| Economic Research Service  |                                  |                                |
| —Economic analysis and projections (supply, demand, and trade analysis, and projections related to tobacco)          | 123                              | 125                            |
| Foreign Agricultural Service   |                                  |                                |
| —World market analysis (collection and analysis of foreign country economic data on tobacco production and trade)    | 200                              | 205                            |
| National Agricultural Statistics Service   |                                  |                                |
| —Agricultural statistics collection (data collection on U.S. tobacco acreage, crop condition, yield, and production) | 231                              | 231                            |
| Total USDA net expenditures for tobacco-related activities   | 30,783                           | 29,457                         |

**Source:** Data are from the USDA's Office of Budget and Program Analysis, Program-By-Program Summary, Estimated Costs Related to Tobacco Activities, 2006.

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