tob. fairness 2/4/98

INTRODUCTION

— Ek — This is not up to date on where negotiation are, USDA is supposed to get us something next week. Tom 3/13/98

Five separate tobacco program options (including abolishing the Federal Government program) are considered in this package. These options cover all tobacco currently under the quota program--about 98 percent of total production. Flue-cured and burley tobacco comprise 94 percent of U.S. production. Flue-cured is grown mainly in North Carolina, South Carolina, Georgia and Virginia and burley mainly in Kentucky and Tennessee. Both of these tobaccos are used mostly in cigarettes.

Other quota tobaccos are used mainly for snuff, chewing and smoking tobacco. They are grown primarily in Kentucky, Tennessee, Virginia and Wisconsin.

The analysis assumes that current U.S. Government policy and representation with regard to foreign market access and export trade will remain unchanged. It also assumes that the import Tariff Rate Quota (TRQ) will remain in effect for options which do not feature increasing world market price orientation. For those which do, the analysis assumes the TRQ would remain in place for an initial period.

The purpose of this paper is to enumerate options for tobacco quota holders and tobacco producers.

The Options are:

1 Continue Current Program - Minimal Changes

2 Continue Current Program - Substantial Changes

3 Tobacco Income Maintenance Program (similar to Ford Bill)

4 Tobacco Quota Buyout - No Replacement Program (similar to Lugar Bill)

5 Privatized Tobacco Program (similar to Robb Bill)

TOBACCO PROGRAM OPTION - #1

CONTINUE CURRENT PROGRAM - Minimal Changes

Background:

The U.S. Government has operated a price support-production control program for tobacco since the 1930s. In exchange for limiting production, producers are assured minimum prices. Until the No-Net-Cost Tobacco Program Act of 1982, any losses in operating the program were paid by the government. This 1982 Act required that to be eligible for price support, producers of all kinds of tobacco, beginning with the 1982 crop, had to pay assessments to an account established by the cooperative association that makes Federal support loans available to producers. The funds are collected to cover potential losses in operating the price support program. Since 1986, purchasers of burley and flue-cured tobacco have been required to contribute to the No-Net-Cost operation of the program.

Under the loan program, a support price (loan rate) is established for each grade of tobacco. If the buyers are not willing to bid at least the Government loan rate for any lot of tobacco, an eligible producer may receive the lot's designated loan rate less any overhead deduction to cover the loan association's administrative costs. The tobacco is then taken by a cooperative association. Under an agreement with the government's Commodity Credit Corporation (CCC), the association arranges for receiving, redrying, packing, storing, and eventually selling the tobacco under loan.

Under this option, tobacco producers would continue to vote in triennial referenda to determine if the program should continue. Annual marketing quotas and price support levels would be established based on supply and demand criteria and changes in cost of production and prices received by producers, as set forth in current legislation. Quotas would continue to be prorated to individual farms based primarily on historical production for the unit. The following current program provisions would remain:

- Transfer of quotas between farms restricted to within county except for the State of Tennessee where burley tobacco can be transferred to any other county in the State.

- No-Net-Cost program provisions remain unchanged.

Variation:

- However, under this option USDA's administrative cost of operating the tobacco program could be funded by the Tobacco Settlement.

TOBACCO PROGRAM OPTION - #1

IMPACTS:

Production - Tobacco would continue to be grown in traditional producing regions. Overall production would decline from current levels over a 10 year period by about one-third because of increased costs of cigarettes (retail prices are estimated to rise about $1.50 per pack) attributable to the $368.5 billion Tobacco Settlement.

Prices - Producer prices could decline a little because of increased cigarette prices caused by the Tobacco Settlement.

Regional Impact - The distribution of production in growing areas would remain unchanged.

Rent/Lease Costs - Rental and lease costs might decline slightly because of lower prices. The decline in value of quota will reach about $250 million annually by the tenth year.

Operating Unit - Size of operating units would be unchanged.

Trade - Trade patterns would be unaltered. There would be no legal/World Trade Organization (WTO) problems.

Government Involvement - Would remain the same; however, to further minimize Government involvement and help eliminate the subsidy issue, could have USDA's program administrative costs paid by the Tobacco Settlement.

Total Cost of Option - USDA estimated cost related to tobacco activities for FY 1998 are projected at $43.4 million.

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TOBACCO PROGRAM OPTION - #2

CONTINUE CURRENT PROGRAM - Substantial Changes

Background:

The U.S. Government's price support-production control program has largely constrained production to historical production regions. Furthermore, it has assured producers prices that are somewhat above competitive equilibrium levels. Without going to a free market, the program could be changed to permit production to move to the most efficient production areas.

Assuming other components of the current program remain unchanged, the following scenarios are suggested for the current program:

1) Permit tobacco quota to be transferred freely from county to county within States.

2) Permit tobacco quotas to move freely from State to State within the current tobacco belt.

3) Permit tobacco quotas to move freely within the U.S.

4) With the 3 scenarios cited above, gradually ratchet down the price support level.

Unlike options three, four and five, there would be no Government payments to quota holders. This option attempts to capture the effects of greater flexibility of quota movement and more world competitive prices. Also, this option could include having all USDA administrative costs of the tobacco program funded by the Tobacco Settlement.

TOBACCO PROGRAM OPTION - #2

IMPACTS:

Production - Total tobacco production would increase as demand rises as price support levels are ratcheted down near world levels. Production would move from less efficient to more efficient areas. Flue-cured production would shift from the North Carolina-Virginia piedmont to the coastal Carolinas and Georgia-Florida. Burley production would shift away from fringe areas such as North Carolina and West Virginia to Kentucky. It is doubtful much production would occur outside traditional areas due to a lack of infrastructure for producing and selling the crop and a lack of expertise for growing the crop. Also, soils and climate may not be conducive to tobacco production in some areas.

Prices - Prices would decline because of lower supports.

Regional Impact - The distribution of production would change with some regions gaining economic activity and others losing. The magnitude of change would increase if quotas could be transferred across State lines within current production areas. Some additional change, though likely not much beyond the across State line movement, would occur if quotas could be transferred nationwide.

Rent/Lease Costs - Rental and lease costs to producers would decline. Quota owners' incomes would decline significantly. The decline in the annual quota value might be around $250 million after 10 years.

Operating Unit - Size of operating units would increase considerably and the number of operating units would decline sharply from the current 124,000. Furthermore, minimum resource farms (many operated by minority farmers) would discontinue production of tobacco.

Trade - U.S. exports would increase and imports would decline as manufacturers switched back to U.S. leaf. The magnitude of the trade changes would depend on the amount the price support is reduced. This option is not expected to have any WTO implications. This option would, however, impact other countries as the U.S. became more competitive in the world market. Canada, Zimbabwe, Malawi, Argentina and Brazil are some of the countries that would be affected.

Government Involvement - Would remain unchanged except that more States but fewer producers and quota holders might be involved.

Total Cost of Option - USDA estimated cost related to tobacco activities for FY 1998 are projected at $43.4 million and could be funded by the Tobacco Settlement. Program administrative costs could decrease slightly, but insurance costs could increase as tobacco production moves closer to coastal regions.

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TOBACCO PROGRAM OPTION - #3

TOBACCO INCOME MAINTENANCE PROGRAM - (similar to the Ford Bill)

Background:

A major concern of tobacco producers' groups and many others including the Administration and Congress is the impact a Tobacco Settlement would have on producers' incomes. USDA has estimated that the settlement will cause U.S. tobacco production to decline from current levels by one-third over a 10 year period and result in a drop in cash receipts of about $70 million annually. Consequently, various ways to assure producers income continuity have been proposed.

The basic idea in an income maintenance or revenue assurance program is that a group of producers will continue to receive a specified percentage of income of a base period regardless of what happens to demand and price for their product. One way to achieve a specified income would be to provide a strong incentive for tobacco manufacturers to buy a certain amount of tobacco at a specified price. This incentive might involve cigarette tax increases geared to specified purchase reductions. However, this approach would not reflect supply and demand conditions and could be counter to U.S. agreements with the WTO.

Another means of maintaining producer income would be to make payments to producers based on the amount production declines due to the effects of the Tobacco Settlement compared with a prespecified base period. Prices in effect during the current year or average prices in a specified base period could be used to gauge the loss in income. But, the income program would have to be designed to be WTO consistent; otherwise the program would undermine the current TRQ regime. Generally, in order to be WTO consistent, payments to farmers could not be conditioned on current production. Too, any plan that involved compelling domestic purchases by the industry would have WTO problems.

Income maintenance programs tied to current production would create issues under the provisions of the General Agreement on Tariffs and Trade (GATT) as defined by Article 13 of the GATT Agricultural Agreement and Article 5 of the Subsidy Agreement and hence could lead to retaliation or the need for further negotiations under Article 28 of the GATT. Furthermore, regarding purchasing, GATT Article 3 explicitly prohibits domestic content requirements.

TOBACCO PROGRAM OPTION - #3

TOBACCO INCOME MAINTENANCE PROGRAM - (similar to the Ford Bill)

Background:

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The basic idea in an income maintenance or revenue assurance program is that a group of producers will continue to receive a specified percentage of income of a base period regardless of what happens to demand and price for their product. One way to achieve a specified income would be to provide a strong incentive for tobacco manufacturers to buy a certain amount of tobacco at a specified price. This incentive might involve cigarette tax increases geared to specified purchase reductions. However, this approach would not reflect supply and demand conditions and could be counter to U.S. agreements with the WTO.

Another means of maintaining producer income would be to make payments to producers based on the amount production declines due to the effects of the Tobacco Settlement compared with a prespecified base period. Prices in effect during the current year or average prices in a specified base period could be used to gauge the loss in income. But, the income program would have to be designed to be WTO consistent; otherwise the program would undermine the current TRQ regime. Generally, in order to be WTO consistent, payments to farmers could not be conditioned on current production. Too, any plan that involved compelling domestic purchases by the industry would have WTO problems.

Income maintenance programs tied to current production would create issues under the provisions of the General Agreement on Tariffs and Trade (GATT) as defined by Article 13 of the GATT Agricultural Agreement and Article 5 of the Subsidy Agreement and hence could lead to retaliation or the need for further negotiations under Article 28 of the GATT. Furthermore, regarding purchasing, GATT Article 3 explicitly prohibits domestic content requirements.

TOBACCO PROGRAM OPTION - #3

IMPACTS:

Production - Tobacco would continue to be grown in traditional growing areas. Overall production would decline about one-third over a 10 year period because of increased costs of cigarettes attrituable to the Tobacco Settlement.

Prices - Prices could decline slightly because of increased cigarette prices caused by the Tobacco Settlement.

Regional Impact - The distribution of production in growing areas would remain unchanged.

Rent/Lease Costs - Rental and lease costs might decline slightly because of lower prices. The estimated decline in the value of quota will reach about $250 million annually by the tenth year.

Operating Unit - Size of operating units would be unchanged.

Trade - Trade patterns would be unaltered. However, there might be WTO implications if income support was tied to production or used as a production incentive and could produce retaliation.

Government Involvement - Would remain the same; however, to further minimize Government involvement and help eliminate the subsidy issue, have USDA's program administrative costs paid by the Tobacco Settlement.

Total Cost of Option - USDA estimated cost related to tobacco activities for FY 1998 are projected at $43.4 million. Cost of an income support program could vary greatly depending on the nature of the programs and could be as high as $1 billion annually.

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TOBACCO PROGRAM OPTION - #4

TOBACCO QUOTA BUYOUT - NO REPLACEMENT PROGRAM - (similar to the Lugar Bill)

Background:

Because of an expected decline in demand associated with the proposed tobacco settlement, several government officials and other interested parties have discussed how to provide economic assistance to tobacco producers, quota owners and tobacco farming communities.

Ideas about economic assistance are broad-based. However, a key element has included buyout or retirement of quotas. A buyout of quota and payment to nonquota owning producers would serve dual purposes. First, it would provide retirement, retraining or reinvesting funds for current tobacco production stakeholders and second, it would remove the Federal government from its perceived role of supporting tobacco through its role in operating the tobacco price support-production control program.

A quota buyout could be all-at-once or spread over a number of years. A gradual phaseout is preferable because of the severe disruptions that would occur if the 60 year tobacco program were suddenly terminated. Uncertainty about production and prices would create severe problems for farmers in obtaining operating and capital investment loans.

Several questions are raised relative to a quota buyout. Among these are: 1) Who are the relevant stakeholders, i.e., quota owners, tenants, hired workers, tobacco warehouse operators and local businesses? Should all tobacco producers, including those producing non-supported tobacco, be included? Where do you draw the line? 2) What is a fair price for quota? Is it $8.00 per pound as proposed in several bills that have been introduced in Congress? Or is it closer to $2.00 per pound, the current selling price of tobacco quota? Perhaps it is somewhere in-between. The $8.00 reflects a 5 percent capitalization rate of an annual quota lease of 40 cents per pound for 20 years and reflects the value associated with essentially a lifetime commitment in human and financial resources to tobacco production. The lower figure - $2.00 per pound - reflects the discounted value associated with an expected 5-year life of the current tobacco program. 3) How much should tenants receive? Clearly, they also have human and capital investments in continuing tobacco production. But, on the whole, their investments are not as large as the quota owners. Some have suggested compensation for them at one-half the rate for the quota owners. 4) What would happen to existing loan stocks? Loan stocks would have to be repriced to move them into the trade. Making up losses on loan repayments for higher priced leaf would be a problem, and would need to be addressed in any buyout. and 5) If the program is phased out over 3, 5, 7 or some other time frame what happens to price supports? Perhaps price supports could be lowered by 25 percent the first year and progressively reduced further until the program is completely terminated.

TOBACCO PROGRAM OPTION - #4

IMPACTS:

Production - Total tobacco production would increase without a program. Flue-cured production might increase by one-half to two-thirds above the 1995-97 level and burley production might rise one-fourth to one-third. Production would move from less efficient to more efficient areas. Flue-cured production would shift from the North Carolina-Virginia piedmont to the coastal Carolinas and Georgia-Florida. Burley production would shift away from fringe areas such as North Carolina, West Virginia and eastern Kentucky to other areas of Kentucky. It is doubtful much production would occur outside traditional areas due to a lack of infrastructure for producing and selling the crop and a lack of expertise for growing the crop. Also, soil and climate may not be conducive to tobacco production in some areas.

Prices - Prices would decline. Prices might decline by 40 cents to 50 cents per pound reflecting the elimination of marketing privilege costs (rent, lease, purchase of quota) and the greater efficiencies associated with movement of production to larger lower-cost operations.

Regional Impact - The distribution of production could change markedly with some higher cost regions such as the Virginia-North Carolina piedmont, Eastern Kentucky and Western North Carolina losing considerable economic base. Furthermore, minimum resource farms (many operated by minority farmers) in these and other tobacco growing areas would be especially hard hit.

Rent/Lease Costs - Rental and lease costs for the rights to market tobacco would be eliminated or phased out (only the cost of using the land itself would continue). Quota owners incomes would be eliminated or phased out.

Operating Unit - Size of operating units would increase significantly and number of producers would decline sharply.

Trade - U.S. leaf exports would increase and imports would decline as manufacturers switched back to U.S. leaf. The magnitude of the trade changes would be significant and U.S. exports could increase as much as 25 percent based on a 50 cent farm level price decline. There would be an impact on other producing countries as U.S. leaf became more competitive in the world market. Canada, Zimbabwe, Malawi, and Brazil are some of the countries affected. There should be no WTO implications, as long as the buyout payments were not conditioned on continued production but were based on something else such as participation in the industry during some base period. Repriced loan stocks moved into trade could be subject to WTO challenge under the Agreement on Subsidies and Countervailing Measures, including countervailing duties.

Government Involvement - Price supports and production controls would be phased out. Domestic grading, import grading and pesticide testing, market news services and export certification services provided by the Agricultural Marketing Service, USDA, could continue.

TOBACCO PROGRAM OPTION - #4

Total Cost of Option - USDA costs would decline and eventually approach or reach zero. Total costs of buying out quota would likely be absorbed by tobacco product manufacturers and could vary widely depending on who was compensated and how much they receive. For example, the cost of paying $8.00 per pound to quota holders would total $13 to $14 billion. Other stake holder costs could more than double this figure.

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TOBACCO PROGRAM OPTION - #5

PRIVATIZED TOBACCO PROGRAM - (similar to the Robb Bill)

Background:

The U.S. Government has operated a price support-production control program for tobacco since the 1930s. This program has caused the farm's assigned marketing quota to have a capitalized value which is incorporated in land valuations, loan debts and related business transactions. Most tobacco producers favor a tobacco program much like the program described in Option #1, the current tobacco program. However, with the continued controversy over the dangers of smoking and health related concerns, many people feel that it is time to "get the Government out of tobacco production".

Under a privatized tobacco program, Congressional approval for the establishment of a Tobacco Corporation to oversee and administer the tobacco program would be needed. This Tobacco Corporation's Board of Directors, composed of all segments of the tobacco industry, would operate the tobacco program much like the oversight currently provided by USDA in its tobacco program administration. The Corporation, with funds received from any Tobacco Settlement legislation would:

- Reimburse quota owners at $8.00 per pound for the equity value of their tobacco marketing quotas. Payments could be spread over a certain number of years as funds become available to the Corporation.
- Provide income support payments to tobacco producers to help in the transition to a world market price for U.S. produced tobacco.
- Provide community development grants to tobacco communities adversely affected by loss of tobacco economies.

The Tobacco Corporation would issue licenses (the equivalent of quotas) to current tobacco producers. These licenses would be nontransferable and adjusted annually by the Corporation based on the anticipated purchases of current crop tobacco. Price support would be provided but gradually reduced from current levels until U.S. tobacco is priced competitively with world tobacco prices. The price support levels would be established by the Tobacco Corporation and funds for administering the program would be borrowed from funds acquired from the Tobacco Settlement.

Tobacco producers would continue to vote in triennial referenda to determine if the Corporation's tobacco program would continue. The USDA would provide information necessary to the Tobacco Corporation to initially establish the licenses for tobacco producers. The Tobacco Corporation could contract with traditional tobacco loan associations to help administer the privatized tobacco program to producers or with any other group of producers as deemed appropriate by the Board of Directors.

TOBACCO PROGRAM OPTION - #5

IMPACTS:

Production - Tobacco would continue to be grown in traditional growing regions. However, as price supports were lowered, production would increase.

Prices - Prices to producers would decline over a set number of years until the U.S. market price for tobacco is comparable to world tobacco market prices. Market transition payments would be made to producers over a set number of years during the period necessary to meet world market prices as determined by the Corporation.

Regional Impact - The distribution of production in growing areas would likely change. As prices fall it is likely that less efficient producers would be forced out of business. Flue-cured production would move out of the piedmont to coastal areas and burley production would become more concentrated in central Kentucky.

Rent/Lease Costs - Rental and lease costs would be eliminated.

Operating Unit - Size of operating units would initially remain relatively stable since licenses would be issued to current producers who have been renting or leasing quota from various quota owners. Then, as exports grow, the average size of operating units would increase.

Trade - U.S. leaf exports would increase and imports would decline as manufacturers switched back to U.S. leaf. The magnitude of the trade changes would depend on the amount farm level prices dropped. However, production in Canada, Zimbabwe, Malawi, Argentina, and Brazil would be affected. The Corporation could be considered a State Trading Enterprise such as those which the U.S. is trying to dismantle under the WTO. Also price support and income support (depending on how they are constructed) could be subject to WTO challenge.

Government Involvement - None from USDA after the initial transition, except to the extent of government involvement in administration of the program by the Corporation. This option has many potential legal problems as it would appear to involve delegating governmental functions to a private group and possible violation of the U.S. Constitution. It is difficult to perceive how the private Corporation would, without an infrastructure or police force, monitor nationwide tobacco production. Furthermore, the system would appear to necessarily involve some continued government oversight which would seem to lead to the conclusion that the option would simply continue the current program in a new, but less effective manner.

Total Cost of Option - Estimated at $20 billion over a several year period.

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VARIOUS TOBACCO BILLS

TOPIC	S. 1310 (Ford) S. 1414, Title IX (McCain)	S. 1313 (Lugar)
Short Title	Long Term Economic Assistance for Farmers (LEAP) Act	Tobacco Transition Act
Funding	Tobacco Community Revitalization Trust Fund of $28.5 billion. Monies come from settlement funds collected from tobacco manufacturers and importers. [Sec 101-102, Sec 911-912]	Tobacco Transition Account, within the National Tobacco Settlement Trust Fund, funded at $15 billion. [Sec 101, 301]
Farmer compensation	Payments to quota owners (up to $8/lb) and tenants for production losses from baseline levels (totaling about $15.8 billion). Quota and no-net-cost price support loan programs maintained with some technical changes. [Sec 201, Sec 921]	Quota owner buyout ($8/lb) and tenant compensation ($1.20/lb) (totaling about $14.7 billion with 100% participation). Mandatory end to quota program and 3-year phase out of price support loan program. [Sec 102-105, 201-202, 211]
Other USDA tobacco activities	All costs for extension services, crop insurance, loan program administration, leaf grading and inspection, and other activities associated with tobacco production will be paid from Trust Fund (totaling about $2.5 billion). [Sec 202, Sec 922]	No provision
Community & Worker Economic Assistance	•Annual economic development grants of $300-350 million for 25 years (totaling $8.3 billion). [Sec 203, Sec 923] •Assistance for displaced industry workers (not more than $500 million). [Sec 301, Sec 931] •Higher education grants for tobacco farm families ($1.4 billion). [Sec 302, Sec 932]	Annual community economic development grants for 3 years (totaling $300 million). [Sec. 111]
Immunity Provisions	Agriculture sector immune to lack of manufacturer compliance with national settlement legislation. [Sec 401, Sec 941]	No provision

VARIOUS TOBACCO BILLS

TOPIC	S.1492, Title IV (Kennedy) H.R. 3028, Title IV (DeLauro)	S.1530, Title VIII (Hatch)
Short Title	Tobacco Market Transition Assistance	Tobacco Transition Act
Funding	Trust Fund (with monies from higher excise taxes) expected to spend $13 billion on farmers and rural development. [Sec 101, subsection 2815]	Tobacco Transition Account of $16 billion. [Sec 101, 811, 841-842]
Farmer compensation	Quota buyout offer to owners ($4/lb), and lessee compensation offer ($4/lb) ($9.2 billion exposure with 100% participation). [Sec 411-414]	Quota owner buyout ($8/lb) and tenant compensation ($1.20/lb) (totaling about $14.7 billion with 100% participation). Mandatory end to quota program and 3-year phase out of price support loan program. [Sec 812-814]
Other USDA tobacco activities	No provision	No provision
Community & Worker Economic Assistance	Annual community economic development grants for 3 years (totaling $3.8 billion). [Sec 431]	•Annual community economic development grants for 3 years (totaling $300 million). [Sec. 821] •Assistance for displaced industry workers (not more than $500 million). [Sec 816] •Education grants for farm families (about $1.4 billion). [Sec 817]
Immunity Provisions	No provision	No provision

VARIOUS TOBACCO BILLS

TOPIC	S. [illegible] (Robb)	
Short Title	Tobacco Market Transition Act	
Funding	Tobacco Community Revitalization Trust Fund funded by amounts from any national tobacco settlement legislation.	
Farmer compensation	Quota owner buyout ($8/lb) and transition payments for active tobacco producers ($2 per pound paid over 5 years). Provides for Tobacco Farmer Individual Retirement Accounts.	
Other USDA tobacco activities	After initial startup of privatized corporation - minimal USDA involvement.	
Community & Worker Economic Assistance	Tobacco Community Economic Development Grants of up to $250 million for each of the FYs 1999-2003, plus to be determined amounts for FYs 2004-2023	
Immunity Provisions	No provision	

Congressional Research Service and
Tobacco and Peanuts Division - FSA - USDA
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total $25 to $30 billion.

tob. fairness 2/4/98

INTRODUCTION

Five separate tobacco program options (including abolishing the Federal Government program) are considered in this package. These options cover all tobacco currently under the quota program--about 98 percent of total production. Flue-cured and burley tobacco comprise 94 percent of U.S. production. Flue-cured is grown mainly in North Carolina, South Carolina, Georgia and Virginia and burley mainly in Kentucky and Tennessee. Both of these tobaccos are used mostly in cigarettes.

Other quota tobaccos are used mainly for snuff, chewing and smoking tobacco. They are grown primarily in Kentucky, Tennessee, Virginia and Wisconsin.

The analysis assumes that current U.S. Government policy and representation with regard to foreign market access and export trade will remain unchanged. It also assumes that the import Tariff Rate Quota (TRQ) will remain in effect for options which do not feature increasing world market price orientation. For those which do, the analysis assumes the TRQ would remain in place for an initial period.

The purpose of this paper is to enumerate options for tobacco quota holders and tobacco producers.

The Options are:

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3 Tobacco Income Maintenance Program (similar to Ford Bill)

4 Tobacco Quota Buyout - No Replacement Program (similar to Lugar Bill)

5 Privatized Tobacco Program (similar to Robb Bill)

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TOBACCO PROGRAM OPTION - #1

CONTINUE CURRENT PROGRAM - Minimal Changes

Background:

The U.S. Government has operated a price support-production control program for tobacco since the 1930s. In exchange for limiting production, producers are assured minimum prices. Until the No-Net-Cost Tobacco Program Act of 1982, any losses in operating the program were paid by the government. This 1982 Act required that to be eligible for price support, producers of all kinds of tobacco, beginning with the 1982 crop, had to pay assessments to an account established by the cooperative association that makes Federal support loans available to producers. The funds are collected to cover potential losses in operating the price support program. Since 1986, purchasers of burley and flue-cured tobacco have been required to contribute to the No-Net-Cost operation of the program.

Under the loan program, a support price (loan rate) is established for each grade of tobacco. If the buyers are not willing to bid at least the Government loan rate for any lot of tobacco, an eligible producer may receive the lot's designated loan rate less any overhead deduction to cover the loan association's administrative costs. The tobacco is then taken by a cooperative association. Under an agreement with the government's Commodity Credit Corporation (CCC), the association arranges for receiving, redrying, packing, storing, and eventually selling the tobacco under loan.

Under this option, tobacco producers would continue to vote in triennial referenda to determine if the program should continue. Annual marketing quotas and price support levels would be established based on supply and demand criteria and changes in cost of production and prices received by producers, as set forth in current legislation. Quotas would continue to be prorated to individual farms based primarily on historical production for the unit. The following current program provisions would remain:

- Transfer of quotas between farms restricted to within county except for the State of Tennessee where burley tobacco can be transferred to any other county in the State.

- No-Net-Cost program provisions remain unchanged.

Variation:

- However, under this option USDA's administrative cost of operating the tobacco program could be funded by the Tobacco Settlement.

TOBACCO PROGRAM OPTION - #1

IMPACTS:

Production - Tobacco would continue to be grown in traditional producing regions. Overall production would decline from current levels over a 10 year period by about one-third because of increased costs of cigarettes (retail prices are estimated to rise about $1.50 per pack) attributable to the $368.5 billion Tobacco Settlement.

Prices - Producer prices could decline a little because of increased cigarette prices caused by the Tobacco Settlement.

Regional Impact - The distribution of production in growing areas would remain unchanged.

Rent/Lease Costs - Rental and lease costs might decline slightly because of lower prices. The decline in value of quota will reach about $250 million annually by the tenth year.

Operating Unit - Size of operating units would be unchanged.

Trade - Trade patterns would be unaltered. There would be no legal/World Trade Organization (WTO) problems.

Government Involvement - Would remain the same; however, to further minimize Government involvement and help eliminate the subsidy issue, could have USDA's program administrative costs paid by the Tobacco Settlement.

Total Cost of Option - USDA estimated cost related to tobacco activities for FY 1998 are projected at $43.4 million.

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TOBACCO PROGRAM OPTION - #2

CONTINUE CURRENT PROGRAM - Substantial Changes

Background:

The U.S. Government's price support-production control program has largely constrained production to historical production regions. Furthermore, it has assured producers prices that are somewhat above competitive equilibrium levels. Without going to a free market, the program could be changed to permit production to move to the most efficient production areas.

Assuming other components of the current program remain unchanged, the following scenarios are suggested for the current program:

1) Permit tobacco quota to be transferred freely from county to county within States.

2) Permit tobacco quotas to move freely from State to State within the current tobacco belt.

3) Permit tobacco quotas to move freely within the U.S.

4) With the 3 scenarios cited above, gradually ratchet down the price support level.

Unlike options three, four and five, there would be no Government payments to quota holders. This option attempts to capture the effects of greater flexibility of quota movement and more world competitive prices. Also, this option could include having all USDA administrative costs of the tobacco program funded by the Tobacco Settlement.

IMPACTS:

Production - Total tobacco production would increase as demand rises as price support levels are ratcheted down near world levels. Production would move from less efficient to more efficient areas. Flue-cured production would shift from the North Carolina-Virginia piedmont to the coastal Carolinas and Georgia-Florida. Burley production would shift away from fringe areas such as North Carolina and West Virginia to Kentucky. It is doubtful much production would occur outside traditional areas due to a lack of infrastructure for producing and selling the crop and a lack of expertise for growing the crop. Also, soils and climate may not be conducive to tobacco production in some areas.

Prices - Prices would decline because of lower supports.

Regional Impact - The distribution of production would change with some regions gaining economic activity and others losing. The magnitude of change would increase if quotas could be transferred across State lines within current production areas. Some additional change, though likely not much beyond the across State line movement, would occur if quotas could be transferred nationwide.

Rent/Lease Costs - Rental and lease costs to producers would decline. Quota owners' incomes would decline significantly. The decline in the annual quota value might be around $250 million after 10 years.

Operating Unit - Size of operating units would increase considerably and the number of operating units would decline sharply from the current 124,000. Furthermore, minimum resource farms (many operated by minority farmers) would discontinue production of tobacco.

Trade - U.S. exports would increase and imports would decline as manufacturers switched back to U.S. leaf. The magnitude of the trade changes would depend on the amount the price support is reduced. This option is not expected to have any WTO implications. This option would, however, impact other countries as the U.S. became more competitive in the world market. Canada, Zimbabwe, Malawi, Argentina and Brazil are some of the countries that would be affected.

Government Involvement - Would remain unchanged except that more States but fewer producers and quota holders might be involved.

Total Cost of Option - USDA estimated cost related to tobacco activities for FY 1998 are projected at $43.4 million and could be funded by the Tobacco Settlement. Program administrative costs could decrease slightly, but insurance costs could increase as tobacco production moves closer to coastal regions.

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TOBACCO PROGRAM OPTION - #3

TOBACCO INCOME MAINTENANCE PROGRAM - (similar to the Ford Bill)

Background:

A major concern of tobacco producers' groups and many others including the Administration and Congress is the impact a Tobacco Settlement would have on producers' incomes. USDA has estimated that the settlement will cause U.S. tobacco production to decline from current levels by one-third over a 10 year period and result in a drop in cash receipts of about $70 million annually. Consequently, various ways to assure producers income continuity have been proposed.

The basic idea in an income maintenance or revenue assurance program is that a group of producers will continue to receive a specified percentage of income of a base period regardless of what happens to demand and price for their product. One way to achieve a specified income would be to provide a strong incentive for tobacco manufacturers to buy a certain amount of tobacco at a specified price. This incentive might involve cigarette tax increases geared to specified purchase reductions. However, this approach would not reflect supply and demand conditions and could be counter to U.S. agreements with the WTO.

Another means of maintaining producer income would be to make payments to producers based on the amount production declines due to the effects of the Tobacco Settlement compared with a prespecified base period. Prices in effect during the current year or average prices in a specified base period could be used to gauge the loss in income. But, the income program would have to be designed to be WTO consistent; otherwise the program would undermine the current TRQ regime. Generally, in order to be WTO consistent, payments to farmers could not be conditioned on current production. Too, any plan that involved compelling domestic purchases by the industry would have WTO problems.

Income maintenance programs tied to current production would create issues under the provisions of the General Agreement on Tariffs and Trade (GATT) as defined by Article 13 of the GATT Agricultural Agreement and Article 5 of the Subsidy Agreement and hence could lead to retaliation or the need for further negotiations under Article 28 of the GATT. Furthermore, regarding purchasing, GATT Article 3 explicitly prohibits domestic content requirements.

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Another means of maintaining producer income would be to make payments to producers based on the amount production declines due to the effects of the Tobacco Settlement compared with a prespecified base period. Prices in effect during the current year or average prices in a specified base period could be used to gauge the loss in income. But, the income program would have to be designed to be WTO consistent; otherwise the program would undermine the current TRQ regime. Generally, in order to be WTO consistent, payments to farmers could not be conditioned on current production. Too, any plan that involved compelling domestic purchases by the industry would have WTO problems.

Income maintenance programs tied to current production would create issues under the provisions of the General Agreement on Tariffs and Trade (GATT) as defined by Article 13 of the GATT Agricultural Agreement and Article 5 of the Subsidy Agreement and hence could lead to retaliation or the need for further negotiations under Article 28 of the GATT. Furthermore, regarding purchasing, GATT Article 3 explicitly prohibits domestic content requirements.

TOBACCO PROGRAM OPTION - #3

IMPACTS:

Production - Tobacco would continue to be grown in traditional growing areas. Overall production would decline about one-third over a 10 year period because of increased costs of cigarettes attrituable to the Tobacco Settlement.

Prices - Prices could decline slightly because of increased cigarette prices caused by the Tobacco Settlement.

Regional Impact - The distribution of production in growing areas would remain unchanged.

Rent/Lease Costs - Rental and lease costs might decline slightly because of lower prices. The estimated decline in the value of quota will reach about $250 million annually by the tenth year.

Operating Unit - Size of operating units would be unchanged.

Trade - Trade patterns would be unaltered. However, there might be WTO implications if income support was tied to production or used as a production incentive and could produce retaliation.

Government Involvement - Would remain the same; however, to further minimize Government involvement and help eliminate the subsidy issue, have USDA's program administrative costs paid by the Tobacco Settlement.

Total Cost of Option - USDA estimated cost related to tobacco activities for FY 1998 are projected at $43.4 million. Cost of an income support program could vary greatly depending on the nature of the programs and could be as high as $1 billion annually.

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TOBACCO PROGRAM OPTION - #4

TOBACCO QUOTA BUYOUT - NO REPLACEMENT PROGRAM - (similar to the Lugar Bill)

Background:

Because of an expected decline in demand associated with the proposed tobacco settlement, several government officials and other interested parties have discussed how to provide economic assistance to tobacco producers, quota owners and tobacco farming communities.

Ideas about economic assistance are broad-based. However, a key element has included buyout or retirement of quotas. A buyout of quota and payment to nonquota owning producers would serve dual purposes. First, it would provide retirement, retraining or reinvesting funds for current tobacco production stakeholders and second, it would remove the Federal government from its perceived role of supporting tobacco through its role in operating the tobacco price support-production control program.

A quota buyout could be all-at-once or spread over a number of years. A gradual phaseout is preferable because of the severe disruptions that would occur if the 60 year tobacco program were suddenly terminated. Uncertainty about production and prices would create severe problems for farmers in obtaining operating and capital investment loans.

Several questions are raised relative to a quota buyout. Among these are: 1) Who are the relevant stakeholders, i.e., quota owners, tenants, hired workers, tobacco warehouse operators and local businesses? Should all tobacco producers, including those producing non-supported tobacco, be included? Where do you draw the line? 2) What is a fair price for quota? Is it $8.00 per pound as proposed in several bills that have been introduced in Congress? Or is it closer to $2.00 per pound, the current selling price of tobacco quota? Perhaps it is somewhere in-between. The $8.00 reflects a 5 percent capitalization rate of an annual quota lease of 40 cents per pound for 20 years and reflects the value associated with essentially a lifetime commitment in human and financial resources to tobacco production. The lower figure - $2.00 per pound - reflects the discounted value associated with an expected 5-year life of the current tobacco program. 3) How much should tenants receive? Clearly, they also have human and capital investments in continuing tobacco production. But, on the whole, their investments are not as large as the quota owners. Some have suggested compensation for them at one-half the rate for the quota owners. 4) What would happen to existing loan stocks? Loan stocks would have to be repriced to move them into the trade. Making up losses on loan repayments for higher priced leaf would be a problem, and would need to be addressed in any buyout. and 5) If the program is phased out over 3, 5, 7 or some other time frame what happens to price supports? Perhaps price supports could be lowered by 25 percent the first year and progressively reduced further until the program is completely terminated.

TOBACCO PROGRAM OPTION - #4

IMPACTS:

Production - Total tobacco production would increase without a program. Flue-cured production might increase by one-half to two-thirds above the 1995-97 level and burley production might rise one-fourth to one-third. Production would move from less efficient to more efficient areas. Flue-cured production would shift from the North Carolina-Virginia piedmont to the coastal Carolinas and Georgia-Florida. Burley production would shift away from fringe areas such as North Carolina, West Virginia and eastern Kentucky to other areas of Kentucky. It is doubtful much production would occur outside traditional areas due to a lack of infrastructure for producing and selling the crop and a lack of expertise for growing the crop. Also, soil and climate may not be conducive to tobacco production in some areas.

Prices - Prices would decline. Prices might decline by 40 cents to 50 cents per pound reflecting the elimination of marketing privilege costs (rent, lease, purchase of quota) and the greater efficiencies associated with movement of production to larger lower-cost operations.

Regional Impact - The distribution of production could change markedly with some higher cost regions such as the Virginia-North Carolina piedmont, Eastern Kentucky and Western North Carolina losing considerable economic base. Furthermore, minimum resource farms (many operated by minority farmers) in these and other tobacco growing areas would be especially hard hit.

Rent/Lease Costs - Rental and lease costs for the rights to market tobacco would be eliminated or phased out (only the cost of using the land itself would continue). Quota owners incomes would be eliminated or phased out.

Operating Unit - Size of operating units would increase significantly and number of producers would decline sharply.

Trade - U.S. leaf exports would increase and imports would decline as manufacturers switched back to U.S. leaf. The magnitude of the trade changes would be significant and U.S. exports could increase as much as 25 percent based on a 50 cent farm level price decline. There would be an impact on other producing countries as U.S. leaf became more competitive in the world market. Canada, Zimbabwe, Malawi, and Brazil are some of the countries affected. There should be no WTO implications, as long as the buyout payments were not conditioned on continued production but were based on something else such as participation in the industry during some base period. Repriced loan stocks moved into trade could be subject to WTO challenge under the Agreement on Subsidies and Countervailing Measures, including countervailing duties.

Government Involvement - Price supports and production controls would be phased out. Domestic grading, import grading and pesticide testing, market news services and export certification services provided by the Agricultural Marketing Service, USDA, could continue.

Total Cost of Option - USDA costs would decline and eventually approach or reach zero. Total costs of buying out quota would likely be absorbed by tobacco product manufacturers and could vary widely depending on who was compensated and how much they receive. For example, the cost of paying $8.00 per pound to quota holders would total $13 to $14 billion. Other stake holder costs could more than double this figure.

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TOBACCO PROGRAM OPTION - #5

PRIVATIZED TOBACCO PROGRAM - (similar to the Robb Bill)

Background:

The U.S. Government has operated a price support-production control program for tobacco since the 1930s. This program has caused the farm's assigned marketing quota to have a capitalized value which is incorporated in land valuations, loan debts and related business transactions. Most tobacco producers favor a tobacco program much like the program described in Option #1, the current tobacco program. However, with the continued controversy over the dangers of smoking and health related concerns, many people feel that it is time to "get the Government out of tobacco production".

Under a privatized tobacco program, Congressional approval for the establishment of a Tobacco Corporation to oversee and administer the tobacco program would be needed. This Tobacco Corporation's Board of Directors, composed of all segments of the tobacco industry, would operate the tobacco program much like the oversight currently provided by USDA in its tobacco program administration. The Corporation, with funds received from any Tobacco Settlement legislation would:

- Reimburse quota owners at $8.00 per pound for the equity value of their tobacco marketing quotas. Payments could be spread over a certain number of years as funds become available to the Corporation.
- Provide income support payments to tobacco producers to help in the transition to a world market price for U.S. produced tobacco.
- Provide community development grants to tobacco communities adversely affected by loss of tobacco economies.

The Tobacco Corporation would issue licenses (the equivalent of quotas) to current tobacco producers. These licenses would be nontransferable and adjusted annually by the Corporation based on the anticipated purchases of current crop tobacco. Price support would be provided but gradually reduced from current levels until U.S. tobacco is priced competitively with world tobacco prices. The price support levels would be established by the Tobacco Corporation and funds for administering the program would be borrowed from funds acquired from the Tobacco Settlement.

Tobacco producers would continue to vote in triennial referenda to determine if the Corporation's tobacco program would continue. The USDA would provide information necessary to the Tobacco Corporation to initially establish the licenses for tobacco producers. The Tobacco Corporation could contract with traditional tobacco loan associations to help administer the privatized tobacco program to producers or with any other group of producers as deemed appropriate by the Board of Directors.

IMPACTS:

Production - Tobacco would continue to be grown in traditional growing regions. However, as price supports were lowered, production would increase.

Prices - Prices to producers would decline over a set number of years until the U.S. market price for tobacco is comparable to world tobacco market prices. Market transition payments would be made to producers over a set number of years during the period necessary to meet world market prices as determined by the Corporation.

Regional Impact - The distribution of production in growing areas would likely change. As prices fall it is likely that less efficient producers would be forced out of business. Flue-cured production would move out of the piedmont to coastal areas and burley production would become more concentrated in central Kentucky.

Rent/Lease Costs - Rental and lease costs would be eliminated.

Operating Unit - Size of operating units would initially remain relatively stable since licenses would be issued to current producers who have been renting or leasing quota from various quota owners. Then, as exports grow, the average size of operating units would increase.

Trade - U.S. leaf exports would increase and imports would decline as manufacturers switched back to U.S. leaf. The magnitude of the trade changes would depend on the amount farm level prices dropped. However, production in Canada, Zimbabwe, Malawi, Argentina, and Brazil would be affected. The Corporation could be considered a State Trading Enterprise such as those which the U.S. is trying to dismantle under the WTO. Also price support and income support (depending on how they are constructed) could be subject to WTO challenge.

Government Involvement - None from USDA after the initial transition, except to the extent of government involvement in administration of the program by the Corporation. This option has many potential legal problems as it would appear to involve delegating governmental functions to a private group and possible violation of the U.S. Constitution. It is difficult to perceive how the private Corporation would, without an infrastructure or police force, monitor nationwide tobacco production. Furthermore, the system would appear to necessarily involve some continued government oversight which would seem to lead to the conclusion that the option would simply continue the current program in a new, but less effective manner.

Total Cost of Option - Estimated at $20 billion over a several year period.

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VARIOUS TOBACCO BILLS

Topic	S. 1310 (Ford) S. 1414, Title IX (McCain)	S. 1313 (Lugar)
Short Title	Long-Term Economic Assistance for Farmers (LEAF) Act	Tobacco Transition Act
Funding	Tobacco Community Revitalization Trust Fund of \$28.5 billion. Monies come from settlement funds collected from tobacco manufacturers and importers. [Sec 101-102, Sec 911-912]	Tobacco Transition Account, within the National Tobacco Settlement Trust Fund, funded at \$15 billion. [Sec 101, 301]
Farmer compensation	Payments to quota owners (up to \$8/lb) and tenants for production losses from baseline levels (totaling about \$15.8 billion). Quota and no-net-cost price support loan programs maintained with some technical changes. [Sec 201, Sec 921]	Quota owner buyout (\$8/lb) and tenant compensation (\$1.20/lb) (totaling about \$14.7 billion with 100% participation). Mandatory end to quota program and 3-year phase out of price support loan program. [Sec 102-105, 201-202, 211]
Other USDA tobacco activities	All costs for extension services, crop insurance, loan program administration, leaf grading and inspection, and other activities associated with tobacco production will be paid from Trust Fund (totaling about \$2.5 billion). [Sec 202, Sec 922]	No provision
Community & Worker Economic Assistance	•Annual economic development grants of \$300-350 million for 25 years (totaling \$8.3 billion). [Sec 203, Sec 923] •Assistance for displaced industry workers (not more than \$500 million). [Sec 301, Sec 931] •Higher education grants for tobacco farm families (\$1.4 billion). [Sec 302, Sec 932]	Annual community economic development grants for 3 years (totaling \$300 million). [Sec. 111]
Immunity Provisions	Agriculture sector immune to lack of manufacturer compliance with national settlement legislation. [Sec 401, Sec 941]	No provision

VARIOUS TOBACCO BILLS

TOPIC	S.1492, Title IV (Kennedy) H.R. 3028, Title IV (DeLauro)	S.1530, Title VIII (Hatch)
Short Title	Tobacco Market Transition Assistance	Tobacco Transition Act
Funding	Trust Fund (with monies from higher excise taxes) expected to spend $13 billion on farmers and rural development. [Sec 101, subsection 2815]	Tobacco Transition Account of $16 billion. [Sec 101, 811, 841-842]
Farmer compensation	Quota buyout offer to owners ($4/lb), and lessee compensation offer ($4/lb) ($9.2 billion exposure with 100% participation). [Sec 411-414]	Quota owner buyout ($8/lb) and tenant compensation ($1.20/lb) (totaling about $14.7 billion with 100% participation). Mandatory end to quota program and 3-year phase out of price support loan program. [Sec 812-814]
Other USDA Tobacco activities	No provision	No provision
Community & Worker Economic Assistance	Annual community economic development grants for 3 years (totaling $3.8 billion). [Sec 431]	•Annual community economic development grants for 3 years (totaling $300 million). [Sec. 821] •Assistance for displaced industry workers (not more than $500 million). [Sec 816] •Education grants for farm families (about $1.4 billion). [Sec 817]
Immunity Provisions	No provision	No provision

VARIOUS TOBACCO BILLS

TOPIC	S.[illegible] (Robb)	
Short Title	Tobacco Market Transition Act	
Funding	Tobacco Community Revitalization Trust Fund funded by amounts from any national tobacco settlement legislation.	
Farmer Compensation	Quota owner buyout ($8/lb) and transition payments for active tobacco producers ($2 per pound paid over 5 years). Provides for Tobacco Farmer Individual Retirement Accounts.	
Other USDA tobacco activities	After initial startup of privatized corporation - minimal USDA involvement	
Community & Worker Economic Assistance	Tobacco Community Economic Development Grants of up to $250 million for each of the FYs 1999-2003, plus to be determined amounts for FYs 2004-2023	
Immunity Provisions	No provision	

Congressional Research Service and
Tobacco and Peanuts Division - FSA - USDA
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INTRODUCTION

Five separate tobacco program options (including abolishing the Federal Government program) are considered in this package. These options cover all tobacco currently under the quota program--about 98 percent of total production. Flue-cured and burley tobacco comprise 94 percent of U.S. production. Flue-cured is grown mainly in North Carolina, South Carolina, Georgia and Virginia and burley mainly in Kentucky and Tennessee. Both of these tobaccos are used mostly in cigarettes.

Other quota tobaccos are used mainly for snuff, chewing and smoking tobacco. They are grown primarily in Kentucky, Tennessee, Virginia and Wisconsin.

The analysis assumes that current U.S. Government policy and representation with regard to foreign market access and export trade will remain unchanged. It also assumes that the import Tariff Rate Quota (TRQ) will remain in effect for options which do not feature increasing world market price orientation. For those which do, the analysis assumes the TRQ would remain in place for an initial period.

The purpose of this paper is to enumerate options for tobacco quota holders and tobacco producers.

The Options are:

1 Continue Current Program - Minimal Changes

2 Continue Current Program - Substantial Changes

3 Tobacco Income Maintenance Program (similar to Ford Bill)

4 Tobacco Quota Buyout - No Replacement Program (similar to Lugar Bill)

5 Privatized Tobacco Program (similar to Robb Bill)

TOBACCO PROGRAM OPTION - #1

CONTINUE CURRENT PROGRAM - Minimal Changes

Background:

The U.S. Government has operated a price support-production control program for tobacco since the 1930s. In exchange for limiting production, producers are assured minimum prices. Until the No-Net-Cost Tobacco Program Act of 1982, any losses in operating the program were paid by the government. This 1982 Act required that to be eligible for price support, producers of all kinds of tobacco, beginning with the 1982 crop, had to pay assessments to an account established by the cooperative association that makes Federal support loans available to producers. The funds are collected to cover potential losses in operating the price support program. Since 1986, purchasers of burley and flue-cured tobacco have been required to contribute to the No-Net-Cost operation of the program.

Under the loan program, a support price (loan rate) is established for each grade of tobacco. If the buyers are not willing to bid at least the Government loan rate for any lot of tobacco, an eligible producer may receive the lot's designated loan rate less any overhead deduction to cover the loan association's administrative costs. The tobacco is then taken by a cooperative association. Under an agreement with the government's Commodity Credit Corporation (CCC), the association arranges for receiving, redrying, packing, storing, and eventually selling the tobacco under loan.

Under this option, tobacco producers would continue to vote in triennial referenda to determine if the program should continue. Annual marketing quotas and price support levels would be established based on supply and demand criteria and changes in cost of production and prices received by producers, as set forth in current legislation. Quotas would continue to be prorated to individual farms based primarily on historical production for the unit. The following current program provisions would remain:

- Transfer of quotas between farms restricted to within county except for the State of Tennessee where burley tobacco can be transferred to any other county in the State.

- No-Net-Cost program provisions remain unchanged.

Variation:

- However, under this option USDA's administrative cost of operating the tobacco program could be funded by the Tobacco Settlement.

TOBACCO PROGRAM OPTION - #1

IMPACTS:

Production - Tobacco would continue to be grown in traditional producing regions. Overall production would decline from current levels over a 10 year period by about one-third because of increased costs of cigarettes (retail prices are estimated to rise about $1.50 per pack) attributable to the $368.5 billion Tobacco Settlement.

Prices - Producer prices could decline a little because of increased cigarette prices caused by the Tobacco Settlement.

Regional Impact - The distribution of production in growing areas would remain unchanged.

Rent/Lease Costs - Rental and lease costs might decline slightly because of lower prices. The decline in value of quota will reach about $250 million annually by the tenth year.

Operating Unit - Size of operating units would be unchanged.

Trade - Trade patterns would be unaltered. There would be no legal/World Trade Organization (WTO) problems.

Government Involvement - Would remain the same; however, to further minimize Government involvement and help eliminate the subsidy issue, could have USDA's program administrative costs paid by the Tobacco Settlement.

Total Cost of Option - USDA estimated cost related to tobacco activities for FY 1998 are projected at $43.4 million.

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TOBACCO PROGRAM OPTION - #2

CONTINUE CURRENT PROGRAM - Substantial Changes

Background:

The U.S. Government's price support-production control program has largely constrained production to historical production regions. Furthermore, it has assured producers prices that are somewhat above competitive equilibrium levels. Without going to a free market, the program could be changed to permit production to move to the most efficient production areas.

Assuming other components of the current program remain unchanged, the following scenarios are suggested for the current program:

1) Permit tobacco quota to be transferred freely from county to county within States.

2) Permit tobacco quotas to move freely from State to State within the current tobacco belt.

3) Permit tobacco quotas to move freely within the U.S.

4) With the 3 scenarios cited above, gradually ratchet down the price support level.

Unlike options three, four and five, there would be no Government payments to quota holders. This option attempts to capture the effects of greater flexibility of quota movement and more world competitive prices. Also, this option could include having all USDA administrative costs of the tobacco program funded by the Tobacco Settlement.

TOBACCO PROGRAM OPTION - #2

IMPACTS:

Production - Total tobacco production would increase as demand rises as price support levels are ratcheted down near world levels. Production would move from less efficient to more efficient areas. Flue-cured production would shift from the North Carolina-Virginia piedmont to the coastal Carolinas and Georgia-Florida. Burley production would shift away from fringe areas such as North Carolina and West Virginia to Kentucky. It is doubtful much production would occur outside traditional areas due to a lack of infrastructure for producing and selling the crop and a lack of expertise for growing the crop. Also, soils and climate may not be conducive to tobacco production in some areas.

Prices - Prices would decline because of lower supports.

Regional Impact - The distribution of production would change with some regions gaining economic activity and others losing. The magnitude of change would increase if quotas could be transferred across State lines within current production areas. Some additional change, though likely not much beyond the across State line movement, would occur if quotas could be transferred nationwide.

Rent/Lease Costs - Rental and lease costs to producers would decline. Quota owners' incomes would decline significantly. The decline in the annual quota value might be around $250 million after 10 years.

Operating Unit - Size of operating units would increase considerably and the number of operating units would decline sharply from the current 124,000. Furthermore, minimum resource farms (many operated by minority farmers) would discontinue production of tobacco.

Trade - U.S. exports would increase and imports would decline as manufacturers switched back to U.S. leaf. The magnitude of the trade changes would depend on the amount the price support is reduced. This option is not expected to have any WTO implications. This option would, however, impact other countries as the U.S. became more competitive in the world market. Canada, Zimbabwe, Malawi, Argentina and Brazil are some of the countries that would be affected.

Government Involvement - Would remain unchanged except that more States but fewer producers and quota holders might be involved.

Total Cost of Option - USDA estimated cost related to tobacco activities for FY 1998 are projected at $43.4 million and could be funded by the Tobacco Settlement. Program administrative costs could decrease slightly, but insurance costs could increase as tobacco production moves closer to coastal regions.

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TOBACCO PROGRAM OPTION - #3

TOBACCO INCOME MAINTENANCE PROGRAM - (similar to the Ford Bill)

Background:

A major concern of tobacco producers' groups and many others including the Administration and Congress is the impact a Tobacco Settlement would have on producers' incomes. USDA has estimated that the settlement will cause U.S. tobacco production to decline from current levels by one-third over a 10 year period and result in a drop in cash receipts of about $70 million annually. Consequently, various ways to assure producers income continuity have been proposed.

The basic idea in an income maintenance or revenue assurance program is that a group of producers will continue to receive a specified percentage of income of a base period regardless of what happens to demand and price for their product. One way to achieve a specified income would be to provide a strong incentive for tobacco manufacturers to buy a certain amount of tobacco at a specified price. This incentive might involve cigarette tax increases geared to specified purchase reductions. However, this approach would not reflect supply and demand conditions and could be counter to U.S. agreements with the WTO.

Another means of maintaining producer income would be to make payments to producers based on the amount production declines due to the effects of the Tobacco Settlement compared with a prespecified base period. Prices in effect during the current year or average prices in a specified base period could be used to gauge the loss in income. But, the income program would have to be designed to be WTO consistent; otherwise the program would undermine the current TRQ regime. Generally, in order to be WTO consistent, payments to farmers could not be conditioned on current production. Too, any plan that involved compelling domestic purchases by the industry would have WTO problems.

Income maintenance programs tied to current production would create issues under the provisions of the General Agreement on Tariffs and Trade (GATT) as defined by Article 13 of the GATT Agricultural Agreement and Article 5 of the Subsidy Agreement and hence could lead to retaliation or the need for further negotiations under Article 28 of the GATT. Furthermore, regarding purchasing, GATT Article 3 explicitly prohibits domestic content requirements.

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Another means of maintaining producer income would be to make payments to producers based on the amount production declines due to the effects of the Tobacco Settlement compared with a prespecified base period. Prices in effect during the current year or average prices in a specified base period could be used to gauge the loss in income. But, the income program would have to be designed to be WTO consistent; otherwise the program would undermine the current TRQ regime. Generally, in order to be WTO consistent, payments to farmers could not be conditioned on current production. Too, any plan that involved compelling domestic purchases by the industry would have WTO problems.

Income maintenance programs tied to current production would create issues under the provisions of the General Agreement on Tariffs and Trade (GATT) as defined by Article 13 of the GATT Agricultural Agreement and Article 5 of the Subsidy Agreement and hence could lead to retaliation or the need for further negotiations under Article 28 of the GATT. Furthermore, regarding purchasing, GATT Article 3 explicitly prohibits domestic content requirements.

TOBACCO PROGRAM OPTION - #3

IMPACTS:

Production - Tobacco would continue to be grown in traditional growing areas. Overall production would decline about one-third over a 10 year period because of increased costs of cigarettes attrituable to the Tobacco Settlement.

Prices - Prices could decline slightly because of increased cigarette prices caused by the Tobacco Settlement.

Regional Impact - The distribution of production in growing areas would remain unchanged.

Rent/Lease Costs - Rental and lease costs might decline slightly because of lower prices. The estimated decline in the value of quota will reach about $250 million annually by the tenth year.

Operating Unit - Size of operating units would be unchanged.

Trade - Trade patterns would be unaltered. However, there might be WTO implications if income support was tied to production or used as a production incentive and could produce retaliation.

Government Involvement - Would remain the same; however, to further minimize Government involvement and help eliminate the subsidy issue, have USDA's program administrative costs paid by the Tobacco Settlement.

Total Cost of Option - USDA estimated cost related to tobacco activities for FY 1998 are projected at $43.4 million. Cost of an income support program could vary greatly depending on the nature of the programs and could be as high as $1 billion annually.

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TOBACCO PROGRAM OPTION - #4

TOBACCO QUOTA BUYOUT - NO REPLACEMENT PROGRAM - (similar to the Lugar Bill)

Background:

Because of an expected decline in demand associated with the proposed tobacco settlement, several government officials and other interested parties have discussed how to provide economic assistance to tobacco producers, quota owners and tobacco farming communities.

Ideas about economic assistance are broad-based. However, a key element has included buyout or retirement of quotas. A buyout of quota and payment to nonquota owning producers would serve dual purposes. First, it would provide retirement, retraining or reinvesting funds for current tobacco production stakeholders and second, it would remove the Federal government from its perceived role of supporting tobacco through its role in operating the tobacco price support-production control program.

A quota buyout could be all-at-once or spread over a number of years. A gradual phaseout is preferable because of the severe disruptions that would occur if the 60 year tobacco program were suddenly terminated. Uncertainty about production and prices would create severe problems for farmers in obtaining operating and capital investment loans.

Several questions are raised relative to a quota buyout. Among these are: 1) Who are the relevant stakeholders, i.e., quota owners, tenants, hired workers, tobacco warehouse operators and local businesses? Should all tobacco producers, including those producing non-supported tobacco, be included? Where do you draw the line? 2) What is a fair price for quota? Is it $8.00 per pound as proposed in several bills that have been introduced in Congress? Or is it closer to $2.00 per pound, the current selling price of tobacco quota? Perhaps it is somewhere in-between. The $8.00 reflects a 5 percent capitalization rate of an annual quota lease of 40 cents per pound for 20 years and reflects the value associated with essentially a lifetime commitment in human and financial resources to tobacco production. The lower figure - $2.00 per pound - reflects the discounted value associated with an expected 5-year life of the current tobacco program. 3) How much should tenants receive? Clearly, they also have human and capital investments in continuing tobacco production. But, on the whole, their investments are not as large as the quota owners. Some have suggested compensation for them at one-half the rate for the quota owners. 4) What would happen to existing loan stocks? Loan stocks would have to be repriced to move them into the trade. Making up losses on loan repayments for higher priced leaf would be a problem, and would need to be addressed in any buyout. and 5) If the program is phased out over 3, 5, 7 or some other time frame what happens to price supports? Perhaps price supports could be lowered by 25 percent the first year and progressively reduced further until the program is completely terminated.

TOBACCO PROGRAM OPTION - #4

IMPACTS:

Production - Total tobacco production would increase without a program. Flue-cured production might increase by one-half to two-thirds above the 1995-97 level and burley production might rise one-fourth to one-third. Production would move from less efficient to more efficient areas. Flue-cured production would shift from the North Carolina-Virginia piedmont to the coastal Carolinas and Georgia-Florida. Burley production would shift away from fringe areas such as North Carolina, West Virginia and eastern Kentucky to other areas of Kentucky. It is doubtful much production would occur outside traditional areas due to a lack of infrastructure for producing and selling the crop and a lack of expertise for growing the crop. Also, soil and climate may not be conducive to tobacco production in some areas.

Prices - Prices would decline. Prices might decline by 40 cents to 50 cents per pound reflecting the elimination of marketing privilege costs (rent, lease, purchase of quota) and the greater efficiencies associated with movement of production to larger lower-cost operations.

Regional Impact - The distribution of production could change markedly with some higher cost regions such as the Virginia-North Carolina piedmont, Eastern Kentucky and Western North Carolina losing considerable economic base. Furthermore, minimum resource farms (many operated by minority farmers) in these and other tobacco growing areas would be especially hard hit.

Rent/Lease Costs - Rental and lease costs for the rights to market tobacco would be eliminated or phased out (only the cost of using the land itself would continue). Quota owners incomes would be eliminated or phased out.

Operating Unit - Size of operating units would increase significantly and number of producers would decline sharply.

Trade - U.S. leaf exports would increase and imports would decline as manufacturers switched back to U.S. leaf. The magnitude of the trade changes would be significant and U.S. exports could increase as much as 25 percent based on a 50 cent farm level price decline. There would be an impact on other producing countries as U.S. leaf became more competitive in the world market. Canada, Zimbabwe, Malawi, and Brazil are some of the countries affected. There should be no WTO implications, as long as the buyout payments were not conditioned on continued production but were based on something else such as participation in the industry during some base period. Repriced loan stocks moved into trade could be subject to WTO challenge under the Agreement on Subsidies and Countervailing Measures, including countervailing duties.

Government Involvement - Price supports and production controls would be phased out. Domestic grading, import grading and pesticide testing, market news services and export certification services provided by the Agricultural Marketing Service, USDA, could continue.

TOBACCO PROGRAM OPTION - #4

Total Cost of Option - USDA costs would decline and eventually approach or reach zero. Total costs of buying out quota would likely be absorbed by tobacco product manufacturers and could vary widely depending on who was compensated and how much they receive. For example, the cost of paying $8.00 per pound to quota holders would total $13 to $14 billion. Other stake holder costs could more than double this figure.

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TOBACCO PROGRAM OPTION - #5

PRIVATIZED TOBACCO PROGRAM - (similar to the Robb Bill)

Background:

The U.S. Government has operated a price support-production control program for tobacco since the 1930s. This program has caused the farm's assigned marketing quota to have a capitalized value which is incorporated in land valuations, loan debts and related business transactions. Most tobacco producers favor a tobacco program much like the program described in Option #1, the current tobacco program. However, with the continued controversy over the dangers of smoking and health related concerns, many people feel that it is time to "get the Government out of tobacco production".

Under a privatized tobacco program, Congressional approval for the establishment of a Tobacco Corporation to oversee and administer the tobacco program would be needed. This Tobacco Corporation's Board of Directors, composed of all segments of the tobacco industry, would operate the tobacco program much like the oversight currently provided by USDA in its tobacco program administration. The Corporation, with funds received from any Tobacco Settlement legislation would:

- Reimburse quota owners at $8.00 per pound for the equity value of their tobacco marketing quotas. Payments could be spread over a certain number of years as funds become available to the Corporation.

- Provide income support payments to tobacco producers to help in the transition to a world market price for U.S. produced tobacco.

- Provide community development grants to tobacco communities adversely affected by loss of tobacco economies.

The Tobacco Corporation would issue licenses (the equivalent of quotas) to current tobacco producers. These licenses would be nontransferable and adjusted annually by the Corporation based on the anticipated purchases of current crop tobacco. Price support would be provided but gradually reduced from current levels until U.S. tobacco is priced competitively with world tobacco prices. The price support levels would be established by the Tobacco Corporation and funds for administering the program would be borrowed from funds acquired from the Tobacco Settlement.

Tobacco producers would continue to vote in triennial referenda to determine if the Corporation's tobacco program would continue. The USDA would provide information necessary to the Tobacco Corporation to initially establish the licenses for tobacco producers. The Tobacco Corporation could contract with traditional tobacco loan associations to help administer the privatized tobacco program to producers or with any other group of producers as deemed appropriate by the Board of Directors.

IMPACTS:

Production - Tobacco would continue to be grown in traditional growing regions. However, as price supports were lowered, production would increase.

Prices - Prices to producers would decline over a set number of years until the U.S. market price for tobacco is comparable to world tobacco market prices. Market transition payments would be made to producers over a set number of years during the period necessary to meet world market prices as determined by the Corporation.

Regional Impact - The distribution of production in growing areas would likely change. As prices fall it is likely that less efficient producers would be forced out of business. Flue-cured production would move out of the piedmont to coastal areas and burley production would become more concentrated in central Kentucky.

Rent/Lease Costs - Rental and lease costs would be eliminated.

Operating Unit - Size of operating units would initially remain relatively stable since licenses would be issued to current producers who have been renting or leasing quota from various quota owners. Then, as exports grow, the average size of operating units would increase.

Trade - U.S. leaf exports would increase and imports would decline as manufacturers switched back to U.S. leaf. The magnitude of the trade changes would depend on the amount farm level prices dropped. However, production in Canada, Zimbabwe, Malawi, Argentina, and Brazil would be affected. The Corporation could be considered a State Trading Enterprise such as those which the U.S. is trying to dismantle under the WTO. Also price support and income support (depending on how they are constructed) could be subject to WTO challenge.

Government Involvement - None from USDA after the initial transition, except to the extent of government involvement in administration of the program by the Corporation. This option has many potential legal problems as it would appear to involve delegating governmental functions to a private group and possible violation of the U.S. Constitution. It is difficult to perceive how the private Corporation would, without an infrastructure or police force, monitor nationwide tobacco production. Furthermore, the system would appear to necessarily involve some continued government oversight which would seem to lead to the conclusion that the option would simply continue the current program in a new, but less effective manner.

Total Cost of Option - Estimated at $20 billion over a several year period.

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VARIOUS TOBACCO BILLS

TOPIC	S. 1310 (Ford) S. 1414 Title IX (McCain)	S. 1313 (Lugar)
Short Title	Long Term Economic Assistance for Farmers (LEAF) Act	Tobacco Transition Act
Funding	Tobacco Community Revitalization Trust Fund of $28.5 billion. Monies come from settlement funds collected from tobacco manufacturers and importers. [Sec 101-102, Sec 911-912]	Tobacco Transition Account, within the National Tobacco Settlement Trust Fund, funded at $15 billion. [Sec 101, 301]
Farmer compensation	Payments to quota owners (up to $8/lb) and tenants for production losses from baseline levels (totaling about $15.8 billion). Quota and no-net-cost price support loan programs maintained with some technical changes. [Sec 201, Sec 921]	Quota owner buyout ($8/lb) and tenant compensation ($1.20/lb) (totaling about $14.7 billion with 100% participation). Mandatory end to quota program and 3-year phase out of price support loan program. [Sec 102-105, 201-202, 211]
Other USDA tobacco activities	All costs for extension services, crop insurance, loan program administration, leaf grading and inspection, and other activities associated with tobacco production will be paid from Trust Fund (totaling about $2.5 billion). [Sec 202, Sec 922]	No provision
Community & Worker Economic Assistance	•Annual economic development grants of $300-350 million for 25 years (totaling $8.3 billion). [Sec 203, Sec 923] •Assistance for displaced industry workers (not more than $500 million). [Sec 301, Sec 931] •Higher education grants for tobacco farm families ($1.4 billion). [Sec 302, Sec 932]	Annual community economic development grants for 3 years (totaling $300 million). [Sec. 111]
Immunity Provisions	Agriculture sector immune to lack of manufacturer compliance with national settlement legislation. [Sec 401, Sec 941]	No provision

VARIOUS TOBACCO BILLS

TOPIC	S. 1492, Title IV (Kennedy) H.R. 3028, Title IV (DeLauro)	S. 1530, Title VIII (Hatch)
Short Title	Tobacco Market Transition Assistance	Tobacco Transition Act
Funding	Trust Fund (with monies from higher excise taxes) expected to spend $13 billion on farmers and rural development. [Sec 101, subsection 2815]	Tobacco Transition Account of $16 billion. [Sec 101, 811, 841-842]
Farmer compensation	Quota buyout offer to owners ($4/lb), and lessee compensation offer ($4/lb) ($9.2 billion exposure with 100% participation). [Sec 411-414]	Quota owner buyout ($8/lb) and tenant compensation ($1.20/lb) (totaling about $14.7 billion with 100% participation). Mandatory end to quota program and 3-year phase out of price support loan program. [Sec 812-814]
Other USDA tobacco activities	No provision	No provision
Community & Worker Economic Assistance	Annual community economic development grants for 3 years (totaling $3.8 billion). [Sec 431]	•Annual community economic development grants for 3 years (totaling $300 million). [Sec. 821] •Assistance for displaced industry workers (not more than $500 million). [Sec 816] •Education grants for farm families (about $1.4 billion). [Sec 817]
Immunity Provisions	No provision	No provision

VARIOUS TOBACCO BILLS

TOPIC	Sen. (Robb)	
Short Title	Tobacco Market Transition Act	
Funding	Tobacco Community Revitalization Trust Fund funded by amounts from any national tobacco settlement legislation.	
Farmer Compensation	Quota owner buyout ($8/lb) and transition payments for active tobacco producers ($2 per pound paid over 5 years). Provides for Tobacco Farmer Individual Retirement Accounts.	
Other USDA tobacco activities	After initial startup of privatized corporation - minimal USDA involvement.	
Community & Worker Economic Assistance	Tobacco Community Economic Development Grants of up to $250 million for each of the FYs 1999-2003, plus to be determined amounts for FYs 2004-2023	
Immunity Provisions	No provision	

Congressional Research Service and
Tobacco and Peanuts Division - FSA - USDA
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5 - Privatized Program
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total $25 to $30 billion.

TOBACCO PROGRAM OPTIONS
(Impacts Compared with Pre-Tobacco Settlement)

TOPIC	Opt.1 - Current Program - Minimal Change	Opt. 2- Current Program - Substantial Changes	Opt. 3 - Income Maintenance Program	Opt. 4 - Quota Buy-out - No Program	Opt. :
Production	Decline by one-third over 10 years.	Increase and move to more efficient areas.	Decline by one-third over 10 years.	Increase and move to more efficient areas.	Woul are lo
Prices	Decline slightly.	Would decline.	Decline slightly.	Would decline to near world prices.	Woul prices
Regional Impact	Unchanged	Some shift to more efficient producing areas.	Unchanged.	Distribution of production could change considerably.	Large
Rent/Lease Costs	Decline slightly per lb. Total quota value declines significantly.	Cost would decline as would quota owner's income.	Decline slightly per lb. Total quota value declines significantly.	Quota rent would be eliminated.	Quota
Operating Unit	Unchanged.	Size would increase considerably and many small and minority farmers would stop production.	Unchanged.	Increase significantly with many small and minority farmers ceasing production.	Size v grow. small Optio
Trade Level/ Policy	Unchanged.	Exports would increase, imports would decline.	Unchanged. Could have WTO implications.	Exports up- imports down. WTO implications possible.	Expor WTO
USDA Involvement	Remain the same. USDA's Adm. Cost could be covered.	Unchanged - USDA's Adm. Cost covered.	Remain the same.	Largely phased out.	Large
Cost	$43.4 million in FY 98, if Adm. Cost covered.	$43.4 million for FY 98.	$43.4 million for FY 98. Income maintenance could total $1 billion annually.	Could total $25 to $30 billion.	Could

Note: All costs are assumed to be covered by increased cigarette taxes or Tobacco Settlement funds. s:\director\fo_draft\sideby.side

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INTRODUCTION

Five separate tobacco program options (including abolishing the Federal Government program) are considered in this package. These options cover all tobacco currently under the quota program--about 98 percent of total production. Flue-cured and burley tobacco comprise 94 percent of U.S. production. Flue-cured is grown mainly in North Carolina, South Carolina, Georgia and Virginia and burley mainly in Kentucky and Tennessee. Both of these tobaccos are used mostly in cigarettes.

Other quota tobaccos are used mainly for snuff, chewing and smoking tobacco. They are grown primarily in Kentucky, Tennessee, Virginia and Wisconsin.

The analysis assumes that current U.S. Government policy and representation with regard to foreign market access and export trade will remain unchanged. It also assumes that the import Tariff Rate Quota (TRQ) will remain in effect for options which do not feature increasing world market price orientation. For those which do, the analysis assumes the TRQ would remain in place for an initial period.

The purpose of this paper is to enumerate options for tobacco quota holders and tobacco producers.

The Options are:

1 Continue Current Program - Minimal Changes

2 Continue Current Program - Substantial Changes

3 Tobacco Income Maintenance Program (similar to Ford Bill)

4 Tobacco Quota Buyout - No Replacement Program (similar to Lugar Bill)

5 Privatized Tobacco Program (similar to Robb Bill)

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TOBACCO PROGRAM OPTION - #1

CONTINUE CURRENT PROGRAM - Minimal Changes

Background:

The U.S. Government has operated a price support-production control program for tobacco since the 1930s. In exchange for limiting production, producers are assured minimum prices. Until the No-Net-Cost Tobacco Program Act of 1982, any losses in operating the program were paid by the government. This 1982 Act required that to be eligible for price support, producers of all kinds of tobacco, beginning with the 1982 crop, had to pay assessments to an account established by the cooperative association that makes Federal support loans available to producers. The funds are collected to cover potential losses in operating the price support program. Since 1986, purchasers of burley and flue-cured tobacco have been required to contribute to the No-Net-Cost operation of the program.

Under the loan program, a support price (loan rate) is established for each grade of tobacco. If the buyers are not willing to bid at least the Government loan rate for any lot of tobacco, an eligible producer may receive the lot's designated loan rate less any overhead deduction to cover the loan association's administrative costs. The tobacco is then taken by a cooperative association. Under an agreement with the government's Commodity Credit Corporation (CCC), the association arranges for receiving, redrying, packing, storing, and eventually selling the tobacco under loan.

Under this option, tobacco producers would continue to vote in triennial referenda to determine if the program should continue. Annual marketing quotas and price support levels would be established based on supply and demand criteria and changes in cost of production and prices received by producers, as set forth in current legislation. Quotas would continue to be prorated to individual farms based primarily on historical production for the unit. The following current program provisions would remain:

- Transfer of quotas between farms restricted to within county except for the State of Tennessee where burley tobacco can be transferred to any other county in the State.

- No-Net-Cost program provisions remain unchanged.

Variation:

- However, under this option USDA's administrative cost of operating the tobacco program could be funded by the Tobacco Settlement.

TOBACCO PROGRAM OPTION - #1

IMPACTS:

Production - Tobacco would continue to be grown in traditional producing regions. Overall production would decline from current levels over a 10 year period by about one-third because of increased costs of cigarettes (retail prices are estimated to rise about $1.50 per pack) attributable to the $368.5 billion Tobacco Settlement.

Prices - Producer prices could decline a little because of increased cigarette prices caused by the Tobacco Settlement.

Regional Impact - The distribution of production in growing areas would remain unchanged.

Rent/Lease Costs - Rental and lease costs might decline slightly because of lower prices. The decline in value of quota will reach about $250 million annually by the tenth year.

Operating Unit - Size of operating units would be unchanged.

Trade - Trade patterns would be unaltered. There would be no legal/World Trade Organization (WTO) problems.

Government Involvement - Would remain the same; however, to further minimize Government involvement and help eliminate the subsidy issue, could have USDA's program administrative costs paid by the Tobacco Settlement.

Total Cost of Option - USDA estimated cost related to tobacco activities for FY 1998 are projected at $43.4 million.

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TOBACCO PROGRAM OPTION - #2

CONTINUE CURRENT PROGRAM - Substantial Changes

Background:

The U.S. Government's price support-production control program has largely constrained production to historical production regions. Furthermore, it has assured producers prices that are somewhat above competitive equilibrium levels. Without going to a free market, the program could be changed to permit production to move to the most efficient production areas.

Assuming other components of the current program remain unchanged, the following scenarios are suggested for the current program:

1) Permit tobacco quota to be transferred freely from county to county within States.

2) Permit tobacco quotas to move freely from State to State within the current tobacco belt.

3) Permit tobacco quotas to move freely within the U.S.

4) With the 3 scenarios cited above, gradually ratchet down the price support level.

Unlike options three, four and five, there would be no Government payments to quota holders. This option attempts to capture the effects of greater flexibility of quota movement and more world competitive prices. Also, this option could include having all USDA administrative costs of the tobacco program funded by the Tobacco Settlement.

TOBACCO PROGRAM OPTION - #2

IMPACTS:

Production - Total tobacco production would increase as demand rises as price support levels are ratcheted down near world levels. Production would move from less efficient to more efficient areas. Flue-cured production would shift from the North Carolina-Virginia piedmont to the coastal Carolinas and Georgia-Florida. Burley production would shift away from fringe areas such as North Carolina and West Virginia to Kentucky. It is doubtful much production would occur outside traditional areas due to a lack of infrastructure for producing and selling the crop and a lack of expertise for growing the crop. Also, soils and climate may not be conducive to tobacco production in some areas.

Prices - Prices would decline because of lower supports.

Regional Impact - The distribution of production would change with some regions gaining economic activity and others losing. The magnitude of change would increase if quotas could be transferred across State lines within current production areas. Some additional change, though likely not much beyond the across State line movement, would occur if quotas could be transferred nationwide.

Rent/Lease Costs - Rental and lease costs to producers would decline. Quota owners' incomes would decline significantly. The decline in the annual quota value might be around $250 million after 10 years.

Operating Unit - Size of operating units would increase considerably and the number of operating units would decline sharply from the current 124,000. Furthermore, minimum resource farms (many operated by minority farmers) would discontinue production of tobacco.

Trade - U.S. exports would increase and imports would decline as manufacturers switched back to U.S. leaf. The magnitude of the trade changes would depend on the amount the price support is reduced. This option is not expected to have any WTO implications. This option would, however, impact other countries as the U.S. became more competitive in the world market. Canada, Zimbabwe, Malawi, Argentina and Brazil are some of the countries that would be affected.

Government Involvement - Would remain unchanged except that more States but fewer producers and quota holders might be involved.

Total Cost of Option - USDA estimated cost related to tobacco activities for FY 1998 are projected at $43.4 million and could be funded by the Tobacco Settlement. Program administrative costs could decrease slightly, but insurance costs could increase as tobacco production moves closer to coastal regions.

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TOBACCO PROGRAM OPTION - #3

TOBACCO INCOME MAINTENANCE PROGRAM - (similar to the Ford Bill)

Background:

A major concern of tobacco producers' groups and many others including the Administration and Congress is the impact a Tobacco Settlement would have on producers' incomes. USDA has estimated that the settlement will cause U.S. tobacco production to decline from current levels by one-third over a 10 year period and result in a drop in cash receipts of about $70 million annually. Consequently, various ways to assure producers income continuity have been proposed.

The basic idea in an income maintenance or revenue assurance program is that a group of producers will continue to receive a specified percentage of income of a base period regardless of what happens to demand and price for their product. One way to achieve a specified income would be to provide a strong incentive for tobacco manufacturers to buy a certain amount of tobacco at a specified price. This incentive might involve cigarette tax increases geared to specified purchase reductions. However, this approach would not reflect supply and demand conditions and could be counter to U.S. agreements with the WTO.

Another means of maintaining producer income would be to make payments to producers based on the amount production declines due to the effects of the Tobacco Settlement compared with a prespecified base period. Prices in effect during the current year or average prices in a specified base period could be used to gauge the loss in income. But, the income program would have to be designed to be WTO consistent; otherwise the program would undermine the current TRQ regime. Generally, in order to be WTO consistent, payments to farmers could not be conditioned on current production. Too, any plan that involved compelling domestic purchases by the industry would have WTO problems.

Income maintenance programs tied to current production would create issues under the provisions of the General Agreement on Tariffs and Trade (GATT) as defined by Article 13 of the GATT Agricultural Agreement and Article 5 of the Subsidy Agreement and hence could lead to retaliation or the need for further negotiations under Article 28 of the GATT. Furthermore, regarding purchasing, GATT Article 3 explicitly prohibits domestic content requirements.

TOBACCO PROGRAM OPTION - #3

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Another means of maintaining producer income would be to make payments to producers based on the amount production declines due to the effects of the Tobacco Settlement compared with a prespecified base period. Prices in effect during the current year or average prices in a specified base period could be used to gauge the loss in income. But, the income program would have to be designed to be WTO consistent; otherwise the program would undermine the current TRQ regime. Generally, in order to be WTO consistent, payments to farmers could not be conditioned on current production. Too, any plan that involved compelling domestic purchases by the industry would have WTO problems.

Income maintenance programs tied to current production would create issues under the provisions of the General Agreement on Tariffs and Trade (GATT) as defined by Article 13 of the GATT Agricultural Agreement and Article 5 of the Subsidy Agreement and hence could lead to retaliation or the need for further negotiations under Article 28 of the GATT. Furthermore, regarding purchasing, GATT Article 3 explicitly prohibits domestic content requirements.

TOBACCO PROGRAM OPTION - #3

IMPACTS:

Production - Tobacco would continue to be grown in traditional growing areas. Overall production would decline about one-third over a 10 year period because of increased costs of cigarettes attrituable to the Tobacco Settlement.

Prices - Prices could decline slightly because of increased cigarette prices caused by the Tobacco Settlement.

Regional Impact - The distribution of production in growing areas would remain unchanged.

Rent/Lease Costs - Rental and lease costs might decline slightly because of lower prices. The estimated decline in the value of quota will reach about $250 million annually by the tenth year.

Operating Unit - Size of operating units would be unchanged.

Trade - Trade patterns would be unaltered. However, there might be WTO implications if income support was tied to production or used as a production incentive and could produce retaliation.

Government Involvement - Would remain the same; however, to further minimize Government involvement and help eliminate the subsidy issue, have USDA's program administrative costs paid by the Tobacco Settlement.

Total Cost of Option - USDA estimated cost related to tobacco activities for FY 1998 are projected at $43.4 million. Cost of an income support program could vary greatly depending on the nature of the programs and could be as high as $1 billion annually.

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TOBACCO PROGRAM OPTION - #4

TOBACCO QUOTA BUYOUT - NO REPLACEMENT PROGRAM - (similar to the Lugar Bill)

Background:

Because of an expected decline in demand associated with the proposed tobacco settlement, several government officials and other interested parties have discussed how to provide economic assistance to tobacco producers, quota owners and tobacco farming communities.

Ideas about economic assistance are broad-based. However, a key element has included buyout or retirement of quotas. A buyout of quota and payment to nonquota owning producers would serve dual purposes. First, it would provide retirement, retraining or reinvesting funds for current tobacco production stakeholders and second, it would remove the Federal government from its perceived role of supporting tobacco through its role in operating the tobacco price support-production control program.

A quota buyout could be all-at-once or spread over a number of years. A gradual phaseout is preferable because of the severe disruptions that would occur if the 60 year tobacco program were suddenly terminated. Uncertainty about production and prices would create severe problems for farmers in obtaining operating and capital investment loans.

Several questions are raised relative to a quota buyout. Among these are: 1) Who are the relevant stakeholders, i.e., quota owners, tenants, hired workers, tobacco warehouse operators and local businesses? Should all tobacco producers, including those producing non-supported tobacco, be included? Where do you draw the line? 2) What is a fair price for quota? Is it $8.00 per pound as proposed in several bills that have been introduced in Congress? Or is it closer to $2.00 per pound, the current selling price of tobacco quota? Perhaps it is somewhere in-between. The $8.00 reflects a 5 percent capitalization rate of an annual quota lease of 40 cents per pound for 20 years and reflects the value associated with essentially a lifetime commitment in human and financial resources to tobacco production. The lower figure - $2.00 per pound - reflects the discounted value associated with an expected 5-year life of the current tobacco program. 3) How much should tenants receive? Clearly, they also have human and capital investments in continuing tobacco production. But, on the whole, their investments are not as large as the quota owners. Some have suggested compensation for them at one-half the rate for the quota owners. 4) What would happen to existing loan stocks? Loan stocks would have to be repriced to move them into the trade. Making up losses on loan repayments for higher priced leaf would be a problem, and would need to be addressed in any buyout. and 5) If the program is phased out over 3, 5, 7 or some other time frame what happens to price supports? Perhaps price supports could be lowered by 25 percent the first year and progressively reduced further until the program is completely terminated.

TOBACCO PROGRAM OPTION - #4

IMPACTS:

Production - Total tobacco production would increase without a program. Flue-cured production might increase by one-half to two-thirds above the 1995-97 level and burley production might rise one-fourth to one-third. Production would move from less efficient to more efficient areas. Flue-cured production would shift from the North Carolina-Virginia piedmont to the coastal Carolinas and Georgia-Florida. Burley production would shift away from fringe areas such as North Carolina, West Virginia and eastern Kentucky to other areas of Kentucky. It is doubtful much production would occur outside traditional areas due to a lack of infrastructure for producing and selling the crop and a lack of expertise for growing the crop. Also, soil and climate may not be conducive to tobacco production in some areas.

Prices - Prices would decline. Prices might decline by 40 cents to 50 cents per pound reflecting the elimination of marketing privilege costs (rent, lease, purchase of quota) and the greater efficiencies associated with movement of production to larger lower-cost operations.

Regional Impact - The distribution of production could change markedly with some higher cost regions such as the Virginia-North Carolina piedmont, Eastern Kentucky and Western North Carolina losing considerable economic base. Furthermore, minimum resource farms (many operated by minority farmers) in these and other tobacco growing areas would be especially hard hit.

Rent/Lease Costs - Rental and lease costs for the rights to market tobacco would be eliminated or phased out (only the cost of using the land itself would continue). Quota owners incomes would be eliminated or phased out.

Operating Unit - Size of operating units would increase significantly and number of producers would decline sharply.

Trade - U.S. leaf exports would increase and imports would decline as manufacturers switched back to U.S. leaf. The magnitude of the trade changes would be significant and U.S. exports could increase as much as 25 percent based on a 50 cent farm level price decline. There would be an impact on other producing countries as U.S. leaf became more competitive in the world market. Canada, Zimbabwe, Malawi, and Brazil are some of the countries affected. There should be no WTO implications, as long as the buyout payments were not conditioned on continued production but were based on something else such as participation in the industry during some base period. Repriced loan stocks moved into trade could be subject to WTO challenge under the Agreement on Subsidies and Countervailing Measures, including countervailing duties.

Government Involvement - Price supports and production controls would be phased out. Domestic grading, import grading and pesticide testing, market news services and export certification services provided by the Agricultural Marketing Service, USDA, could continue.

TOBACCO PROGRAM OPTION - #4

Total Cost of Option - USDA costs would decline and eventually approach or reach zero. Total costs of buying out quota would likely be absorbed by tobacco product manufacturers and could vary widely depending on who was compensated and how much they receive. For example, the cost of paying $8.00 per pound to quota holders would total $13 to $14 billion. Other stake holder costs could more than double this figure.

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TOBACCO PROGRAM OPTION - #5

PRIVATIZED TOBACCO PROGRAM - (similar to the Robb Bill)

Background:

The U.S. Government has operated a price support-production control program for tobacco since the 1930s. This program has caused the farm's assigned marketing quota to have a capitalized value which is incorporated in land valuations, loan debts and related business transactions. Most tobacco producers favor a tobacco program much like the program described in Option #1, the current tobacco program. However, with the continued controversy over the dangers of smoking and health related concerns, many people feel that it is time to "get the Government out of tobacco production".

Under a privatized tobacco program, Congressional approval for the establishment of a Tobacco Corporation to oversee and administer the tobacco program would be needed. This Tobacco Corporation's Board of Directors, composed of all segments of the tobacco industry, would operate the tobacco program much like the oversight currently provided by USDA in its tobacco program administration. The Corporation, with funds received from any Tobacco Settlement legislation would:

- Reimburse quota owners at $8.00 per pound for the equity value of their tobacco marketing quotas. Payments could be spread over a certain number of years as funds become available to the Corporation.

- Provide income support payments to tobacco producers to help in the transition to a world market price for U.S. produced tobacco.

- Provide community development grants to tobacco communities adversely affected by loss of tobacco economies.

The Tobacco Corporation would issue licenses (the equivalent of quotas) to current tobacco producers. These licenses would be nontransferable and adjusted annually by the Corporation based on the anticipated purchases of current crop tobacco. Price support would be provided but gradually reduced from current levels until U.S. tobacco is priced competitively with world tobacco prices. The price support levels would be established by the Tobacco Corporation and funds for administering the program would be borrowed from funds acquired from the Tobacco Settlement.

Tobacco producers would continue to vote in triennial referenda to determine if the Corporation's tobacco program would continue. The USDA would provide information necessary to the Tobacco Corporation to initially establish the licenses for tobacco producers. The Tobacco Corporation could contract with traditional tobacco loan associations to help administer the privatized tobacco program to producers or with any other group of producers as deemed appropriate by the Board of Directors.

IMPACTS:

Production - Tobacco would continue to be grown in traditional growing regions. However, as price supports were lowered, production would increase.

Prices - Prices to producers would decline over a set number of years until the U.S. market price for tobacco is comparable to world tobacco market prices. Market transition payments would be made to producers over a set number of years during the period necessary to meet world market prices as determined by the Corporation.

Regional Impact - The distribution of production in growing areas would likely change. As prices fall it is likely that less efficient producers would be forced out of business. Flue-cured production would move out of the piedmont to coastal areas and burley production would become more concentrated in central Kentucky.

Rent/Lease Costs - Rental and lease costs would be eliminated.

Operating Unit - Size of operating units would initially remain relatively stable since licenses would be issued to current producers who have been renting or leasing quota from various quota owners. Then, as exports grow, the average size of operating units would increase.

Trade - U.S. leaf exports would increase and imports would decline as manufacturers switched back to U.S. leaf. The magnitude of the trade changes would depend on the amount farm level prices dropped. However, production in Canada, Zimbabwe, Malawi, Argentina, and Brazil would be affected. The Corporation could be considered a State Trading Enterprise such as those which the U.S. is trying to dismantle under the WTO. Also price support and income support (depending on how they are constructed) could be subject to WTO challenge.

Government Involvement - None from USDA after the initial transition, except to the extent of government involvement in administration of the program by the Corporation. This option has many potential legal problems as it would appear to involve delegating governmental functions to a private group and possible violation of the U.S. Constitution. It is difficult to perceive how the private Corporation would, without an infrastructure or police force, monitor nationwide tobacco production. Furthermore, the system would appear to necessarily involve some continued government oversight which would seem to lead to the conclusion that the option would simply continue the current program in a new, but less effective manner.

Total Cost of Option - Estimated at $20 billion over a several year period.

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VARIOUS TOBACCO BILLS

TOPIC	S. 1310 (Ford) S. 1414 Title IX (McCain)	S. 1313 (Lugar)
Short Title	Long-Term Economic Assistance for Farmers (LEAP) Act	Tobacco Transition Act
Funding	Tobacco Community Revitalization Trust Fund of $28.5 billion. Monies come from settlement funds collected from tobacco manufacturers and importers. [Sec 101-102, Sec 911-912]	Tobacco Transition Account, within the National Tobacco Settlement Trust Fund, funded at $15 billion. [Sec 101, 301]
Farmer compensation	Payments to quota owners (up to $8/lb) and tenants for production losses from baseline levels (totaling about $15.8 billion). Quota and no-net-cost price support loan programs maintained with some technical changes. [Sec 201, Sec 921]	Quota owner buyout ($8/lb) and tenant compensation ($1.20/lb) (totaling about $14.7 billion with 100% participation). Mandatory end to quota program and 3-year phase out of price support loan program. [Sec 102-105, 201-202, 211]
Other USDA tobacco activities	All costs for extension services, crop insurance, loan program administration, leaf grading and inspection, and other activities associated with tobacco production will be paid from Trust Fund (totaling about $2.5 billion). [Sec 202, Sec 922]	No provision
Community & Worker Economic Assistance	•Annual economic development grants of $300-350 million for 25 years (totaling $8.3 billion). [Sec 203, Sec 923] •Assistance for displaced industry workers (not more than $500 million). [Sec 301, Sec 931] •Higher education grants for tobacco farm families ($1.4 billion). [Sec 302, Sec 932]	Annual community economic development grants for 3 years (totaling $300 million). [Sec. 111]
Immunity Provisions	Agriculture sector immune to lack of manufacturer compliance with national settlement legislation. [Sec 401, Sec 941]	No provision

VARIOUS TOBACCO BILLS

TOPIC	S. 1492, Title IV (Kennedy) H.R. 3028, Title IV (DeLauro)	S. 1530, Title VIII (Hatch)
Short Title	Tobacco Market Transition Assistance	Tobacco Transition Act
Funding	Trust Fund (with monies from higher excise taxes) expected to spend $13 billion on farmers and rural development. [Sec 101, subsection 2815]	Tobacco Transition Account of $16 billion. [Sec 101, 811, 841-842]
Farmer compensation	Quota buyout offer to owners ($4/lb), and lessee compensation offer ($4/lb) ($9.2 billion exposure with 100% participation). [Sec 411-414]	Quota owner buyout ($8/lb) and tenant compensation ($1.20/lb) (totaling about $14.7 billion with 100% participation). Mandatory end to quota program and 3-year phase out of price support loan program. [Sec 812-814]
Other USDA tobacco activities	No provision	No provision
Community & Worker Economic Assistance	Annual community economic development grants for 3 years (totaling $3.8 billion). [Sec 431]	•Annual community economic development grants for 3 years (totaling $300 million). [Sec. 821] •Assistance for displaced industry workers (not more than $500 million). [Sec 816] •Education grants for farm families (about $1.4 billion). [Sec 817]
Immunity Provisions	No provision	No provision

VARIOUS TOBACCO BILLS

TOPIC	S.[illegible] (Robb)	
Short Title	Tobacco Market Transition Act	
Funding	Tobacco Community Revitalization Trust Fund funded by amounts from any national tobacco settlement legislation.	
Farmer compensation	Quota owner buyout ($8/lb) and transition payments for active tobacco producers ($2 per pound paid over 5 years). Provides for Tobacco Farmer Individual Retirement Accounts.	
Other USDA tobacco activities	After initial startup of privatized corporation - minimal USDA involvement.	
Community & Worker Economic Assistance	Tobacco Community Economic Development Grants of up to $250 million for each of the FYs 1999-2003, plus to be determined amounts for FYs 2004-2023	
Immunity Provisions	No provision	

Congressional Research Service and
Tobacco and Peanuts Division - FSA - USDA
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5 - Privatized Program
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total $25 to $30 billion.

TOBACCO PROGRAM OPTIONS
(Impacts Compared with Pre-Tobacco Settlement)

TOPIC	Opt.1 - Current Program - Minimal Change	Opt. 2- Current Program - Substantial Changes	Opt. 3 - Income Maintenance Program	Opt. 4 - Quota Buy-out - No Program	Opt. :
Production	Decline by one-third over 10 years.	Increase and move to more efficient areas.	Decline by one-third over 10 years.	Increase and move to more efficient areas.	Woul are lo
Prices	Decline slightly.	Would decline.	Decline slightly.	Would decline to near world prices.	Woul prices
Regional Impact	Unchanged	Some shift to more efficient producing areas.	Unchanged.	Distribution of production could change considerably.	Large
Rent/Lease Costs	Decline slightly per lb. Total quota value declines significantly.	Cost would decline as would quota owner's income.	Decline slightly per lb. Total quota value declines significantly.	Quota rent would be eliminated.	Quota
Operating Unit	Unchanged.	Size would increase considerably and many small and minority farmers would stop production.	Unchanged.	Increase significantly with many small and minority farmers ceasing production.	Size v grow. small Optio
Trade Level/ Policy	Unchanged.	Exports would increase, imports would decline.	Unchanged. Could have WTO implications.	Exports up- imports down. WTO implications possible.	Expor WTO
USDA Involvement	Remain the same. USDA's Adm. Cost could be covered.	Unchanged - USDA's Adm. Cost covered.	Remain the same.	Largely phased out.	Large
Cost	$43.4 million in FY 98, if Adm. Cost covered.	$43.4 million for FY 98.	$43.4 million for FY 98. Income maintenance could total $1 billion annually.	Could total $25 to $30 billion.	Could

Note: All costs are assumed to be covered by increased cigarette taxes or Tobacco Settlement funds. s:\director\fo_draft\sidebby.side