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Office of the General Counsel

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October 28, 1999

The Honorable Larry Combest
Chairman, Committee on Agriculture
House of Representatives

The Honorable Bob Goodlatte
Chairman, Subcommittee on Department
Operations, Oversight, Nutrition & Forestry
Committee on Agriculture
House of Representatives

By letter dated October 13, 1999, you asked us to examine the Department of Agriculture's (the Department) use of liquidating and financing accounts for farm credit programs (direct loans and loan guarantees) to cover the cost of administrative settlements of alleged discriminatory treatment of African-American farmers. We understand that your concern involves the source of funds used to pay the administratively settled claims and not the merits of the underlying claims. In response to an inquiry made in June 1998, the Department advised us that it used the farm credit program liquidating and financing accounts to administratively pay compensatory damages for alleged violations of the civil rights of six African-American farmers.

We have examined the legal authority of the Department to use the Credit Reform financing and liquidating accounts as a source of funds for such payments. If the Credit Reform accounts are available, the Department will fund the payments out of the permanent indefinite appropriations¹ provided by the Credit Reform Act to cover reestimates of the costs of direct loans and loan guarantees paid out of the financing and liquidating accounts. On the other hand, if the Credit Reform accounts are not available, the Department will have to charge its salary and expense appropriation. Depending on the amount of these payments, the Department may need to request additional funding to cover the payments of compensatory damages.

¹A permanent indefinite appropriation is an appropriation without time limitation that contains no specific dollar amount. In effect, the General Fund of the Treasury is liable for any amount necessary to cover obligations incurred incident to the stated purpose.

For the reasons explained below, we conclude that the financing and liquidating accounts are not available to pay compensatory damages to the six African-American farmers. We believe that the Department should charge the costs of these payments to the appropriation provided for administrative expenses of the farm credit programs.

BACKGROUND

The Department has reported that it has administratively settled nine claims of alleged discriminatory treatment in its direct and guaranteed loan program brought under the Equal Credit Opportunity Act (ECOA), 15 U.S.C. § 1691. Letter from David H. Harris, Jr., Associate General Counsel, Civil Rights, United States Department of Agriculture (September 18, 1998).² The claimed discriminatory treatment included delays or denials of farm ownership, farm operating and emergency loans as well as denial of loan servicing, loan acceleration, and foreclosure actions. To settle these nine claims, the Department paid \$2,839,000 in compensatory damages. *Id.* at 2. The Department paid four of the nine settlements from liquidating accounts, two from financing accounts, and three from the Farm Service Agency's (FSA)³ Salaries and Expenses account.⁴ Thus, payments for compensatory damages to six of the African-American farmers were paid out of the financing or liquidating accounts created by the Credit Reform Act.

²On January 5, 1999, the Department entered into a consent decree to settle the class action lawsuit, Pigford, et al. v. Glickman, Civil Action No. 97-1978, brought by and for African-American farmers alleging that between January 1, 1981 and July 1997, the Department administered FSA's ownership, operating and emergency loan programs in a racially discriminatory manner. The United States District Court for the District of Columbia subsequently approved the Consent Decree. The source of funds to cover the potential compensatory damage awards pursuant to this settlement are not at issue here, and this opinion does not address that issue, since the consent decree specifically directs that any adjudicators' or arbitrators' awards be paid from the Judgment Fund. Consent Decree at 14. (Jan. 5, 1999).

³The Secretary of Agriculture is authorized to establish the FSA by 7 U.S.C. § 6932 (1994). FSA administers the farm ownership and operating loan programs (both direct and guaranteed) and emergency disaster loans to farmers that the Farmers Home Administration had historically operated. In this decision, we refer to these loan programs as FSA Programs. The Consolidated Farm and Rural Development Act, as amended, Pub. L. No. 87-128, 75 Stat. 294, 307 (1961), is the basic authority for the farm loan programs.

⁴Rosalind D. Gray, Director, Office of Civil Rights, U.S. Department of Agriculture, recently testified before the House Subcommittee on Operations, Oversight, Nutrition and Forestry, Committee on Agriculture. FSA's Salaries and Expenses account is being used to make settlement payments. (Testimony of Rosalind D. Gray, Director, Office of Civil Rights, U.S. Department of Agriculture). After the Hearing, we attempted to clarify the scope of Ms. Gray's statement with the Department's Office of the General Counsel. We wanted to find out whether the Department has changed its position since writing us in September 1998 and actually used only FSA Salaries and Expenses appropriations to make these payments. As of October 27, 1999, we have not received a response to our informal inquiries.

Both the Department and the General Counsel of the Office of Management and Budget (hereinafter OMB) take the view that the Department may charge the financing and liquidating accounts for the compensatory damages awarded to the African-American farmers. Letter from David H. Harris, Jr., Associate General Counsel, Civil Rights, United States Department of Agriculture at 1 (September 18, 1998) and Opinion of Robert G. Damus, General Counsel, Office of Management and Budget, at 1 (undated). More to the point, to the extent that a particular financing or liquidating account's balance was insufficient to cover the payment of compensatory damages, the Department would finance the award from the permanent indefinite appropriation provided to cover reestimates of the costs of outstanding loans and loan guarantees in the financing and liquidating accounts.

As discussed in more detail below, OMB points to the Credit Reform Act's definition of "cost," 2 U.S.C. § 661a(5)(A), and "cost of a direct loan," 2 U.S.C. § 661a(5)(B), to support its position. Because the Credit Reform Act defines "cost of a direct loan" to include "other payments by or to the government over the life of the loan," 2 U.S.C. § 661a(5)(B) (emphasis added),³ OMB's General Counsel argues that the cost of a direct loan "plainly includes any and all costs, including legal costs that arise out of operation of the program," with the exception of administrative costs. Hence, OMB's General Counsel frames the issue as whether "the discrimination settlement [is] an 'administrative cost' or a program (subsidy) cost?" OMB concludes that the administrative payments of compensatory damages are program costs, reasoning that:

"The claims in this case are appropriately described as arising out of program activities. While it could be argued that the discrimination that occurred was based on administrative decisions of individual employees, it is more appropriately described as arising from the entire design and execution of the program, not isolated administrative determinations. If a version of 'redlining' was the problem, it is appropriately viewed as a systemic program issue, not a mere administrative problem."

Opinion of Robert G. Damus, General Counsel, Office of Management and Budget, at 1 (undated).

ANALYSIS

A basic understanding of the statutory scheme underlying the Credit Reform Act is helpful in understanding this issue. Congress enacted the Credit Reform Act to identify the subsidy cost of federal credit programs, to compare the cost of credit

³The Act's definition of the "cost of a loan guarantee" is similar: "The cost of a loan guarantee shall be the net present value when a guaranteed loan is disbursed of the cash flow from: (i) estimated payments by the Government to cover defaults and delinquencies, interest subsidies, or other payments; and (ii) the estimated payments to the Government including origination and other fees, penalties and recoveries. 2 U.S.C.A. § 661a (5)(C).

programs to other methods of delivering benefits, and to allocate resources wisely between credit and other spending programs. Omnibus Budget Reconciliation Act of 1990, Pub. L. No. 101-508, title XIII, subtitle B, 104 Stat. 1388-610, classified at 2 U.S.C. §§ 661-661f (1994). Thus, Congress mandated that for fiscal year 1992 and thereafter, agencies may make new direct loans and loan guarantee commitments only to the extent that Congress has appropriated budget authority to cover the subsidy cost of the loans or loan guarantees. 2 U.S.C. § 661c(b) (1994).

The budget authority appropriated to cover the subsidy cost of the direct loan or loan guarantee is accounted for in a budget account called the credit program account. 2 U.S.C. § 661a(6) (1994). The administrative costs of a direct loan or loan guarantee program are accounted for as a distinct and separately identified sub-account in the credit program account. 2 U.S.C. § 661c(g) (1994). Typically, Congress provides a separate appropriation to cover administrative costs.

The Credit Reform Act also created special accounts for each credit program to receive "the cost payment from the credit program account" and "all other cash flows to and from the government resulting from" direct loans and loan guarantees. 2 U.S.C. § 661a(7). For loans made in fiscal year 1992 and thereafter, Congress established "financing" accounts to receive these cash flows, including the appropriation of the subsidy cost. Congress recognized that agency estimates of the subsidy cost of a group of direct loans or loan guarantees (and, as a result, the appropriation of the subsidy cost) would necessarily lack precision. Thus, Congress required agencies to annually reestimate the subsidy cost against current loan performance and economic forecast data. In order to cover any resulting shortages in the financing account, Congress provided permanent indefinite authority to cover the difference between the reestimated cost and the prior year's cost estimate. 2 U.S.C. § 661c (f) (1994). As noted above, the Department has advised that it has used financing accounts, and their permanent indefinite reestimating authority, to fund two discrimination claim settlements arising after fiscal year 1992.

For loans or guarantees made prior to fiscal year 1992, Congress created liquidating accounts to capture all cash flows to and from the government. 2 U.S.C. § 661a(8). Congress provided the liquidating accounts with permanent indefinite authority to make any required payments on obligations of such accounts if funds in those accounts prove insufficient. 2 U.S.C. § 661d(d) (1994). As noted above, the Department has advised that it used the permanent indefinite reestimating authority of the liquidating accounts to fund four payments of compensatory damages incident to claims arising prior to fiscal year 1992. Letter from David H. Harris, Jr., Associate General Counsel, Civil Rights, United States Department of Agriculture (September 18, 1998).

Congress funds the Department's farm ownership and farm operating loans, both direct and guaranteed, as well as emergency disaster direct loans out of the Agricultural Credit Insurance Fund Program Account (Fund). This account is funded by an appropriation to cover the subsidy cost of the loans and loan guarantees, as required by the Credit Reform Act. See, e.g., Agriculture, Rural Development, Food

and Drug Administration and Related Agencies Appropriation Act, 2000, Pub. L. No. 106-78, ___ Stat. ___ (1999). The appropriation for the Fund also typically sets the gross obligational limits for the principal amount of direct and guaranteed loan programs for the fiscal year. *Id.* Lastly, the appropriation provides a separate amount for administrative expenses necessary to carry out the direct and guaranteed loan programs. *Id.* Most of the appropriation for administrative expense is transferred to and merged with the Farm Service Agency Salaries and Expenses account. *Id.*

To measure the cost of direct loan and loan guarantee programs, the Credit Reform Act separately accounts for the cost of a direct loan or loan guarantee (subsidy cost) from the administrative costs or expenses of running the program. Not surprisingly, the language of the Act indicates that Congress took special care to articulate a precise definition of “cost,” “cost of a direct loan” and the “cost of a loan guarantee.” As relevant here, Congress defined “cost” as:

“The estimated long-term cost to the Government of a direct loan or loan guarantee, calculated on a net present value basis or modification thereof, excluding administrative costs and any incidental effects on governmental receipts or outlays.” 2 U.S.C. § 661a(5)(A).

The Act does not define the terms “administrative costs” or “incidental effects,” nor does the legislative history of the Act shed light on those terms. However, the Act does speak to the other side of the equation by specifying, in some detail, the types of cash flows that an agency should include in estimating the “cost” of a loan. In this regard, the Credit Reform Act defines the “cost of direct loan” to include: “the net present value, at the time when the direct loan is disbursed, of the following estimated cash flows: loan disbursements; repayments of principal; and payments of interest and other payments by or to the Government over the life of the loan after adjusting for estimated defaults, prepayments, fees, penalties, and other recoveries.” See 2 U.S.C. § 661a(5)(B)(emphasis added).

As noted earlier, OMB’s General Counsel relies on the phrase “other payments by or to the government” to support the use of the financing accounts (and the permanent indefinite authority available to cover subsidy cost reestimates) to cover the payment of compensatory damages for the alleged civil rights violations. We think such reliance is misplaced. We believe that Congress used the phrase “other payments by or to the government” to capture payments directly related to or flowing from the contractual provisions governing the transaction. The phrase “over the life of the loan” plus the listing of other events and payments associated with a transaction (“after adjusting for estimated defaults . . .”) supports this conclusion. In addition, OMB’s regulation implementing the Credit Reform Act reflects this distinction. OMB Circular A-11 defines “subsidy cost” as:

“The estimated present value of the cash flows from the Government (excluding administrative expenses) less the estimated present value of the cash flows to the Government resulting from a direct loan or loan

guarantee . . . The cash flows are the contractual cash flows adjusted for expected deviations from the contract terms (delinquencies, defaults, prepayments, and other factors.)” OMB Circular A-11 § 33.3 (1998) (emphasis added).

Furthermore, OMB’s regulatory definition of “administrative costs” clearly distinguishes the cost of administering a loan program from the expected contractual cash flows. OMB Circular A-11 defines “administrative costs” to include such expenses as “the costs of operating separate offices or units that make policy decisions for credit programs,” “the cost of all activities related to credit extension, loan servicing, write-off, and close out,” and “the cost of monitoring credit programs and private lenders for compliance with laws and regulations.” OMB Circular A-11, § 33.4(a)(1998)(emphasis added).

OMB’s guidance reasonably articulates these concepts consistent with the language and objectives of the Credit Reform Act. Viewed from the perspective of OMB Circular A-11, it is difficult to relate the administrative payment of compensatory damages for alleged discriminatory treatment to the “contractual cash flows adjusted for expected deviations from the contract terms.” Although the OMB Circular’s definition of “administrative costs” does not directly speak to the issue here, there is a clear nexus between components of its definition of administrative costs and the administrative payment of compensatory damages for alleged violations of the civil rights of African-American farmers.⁶ In our view, “the cost of all activities related to credit extension” and “the cost of monitoring credit programs . . . for compliance with laws” relates directly to the type of costs at issue here.

OMB’s position, particularly as it relates to charging administrative payments of compensatory damages for loans not made, fundamentally conflicts with the statutory definition of the “cost” of a loan. The Credit Reform Act is replete with language specifying that the “cost” of a direct loan or loan guarantee for the purposes of the act is determined by reference to loans or loan guarantees made. “Cost” is defined as “the net present value, at the time when the direct loan is disbursed.” 2 U.S.C. 661a(5)(B) (emphasis added). Moreover, the authority to re-estimate a group of loans or loan guarantees explicitly requires an increase in the estimate of the cost of loans or guarantees outstanding, or in the terms of the statute, loans or loan guarantees made. 2 U.S.C. § 661c(f).

⁶Prior Comptroller General decisions have consistently concluded that administrative settlements requiring “corrective” payments are chargeable to the appropriation covering the cost of administering the program or activity. 68 Comp. Gen. 600 (1989)(loss in Personal Funds of Patients Trust Account should be charged to Department of Veterans Affairs appropriation account supporting the administration of the trust fund); 67 Comp. Gen. 342 (1988)(Bureau of Indian Affairs should adjust deficiencies in trust fund resulting from erroneous payments by charging general administrative expenses); Cf. B-257334, June 30, 1995 (Department of Agriculture, Food Safety and Inspection Service, should charge compensatory damage award in an employee discrimination complaint to salaries and expenses account); B-272984, Sept. 26, 1996 (Federal Aviation Administration should pay administrative settlement costs in an employee discrimination settlement from salaries and expenses account).

Finally, although not a legal basis for our opinion, we believe that our conclusion furthers budgetary and programmatic accountability. Congress regularly appropriates the amounts available for administrative expenses of these programs. To the extent that the Department will now or in the future divert funds from other administrative activities to cover administrative payments of compensatory damages or require an additional appropriation of administrative expenses, Congress can provide oversight of these trade-offs through the annual appropriations process. The alternative, namely the use of the permanent indefinite authority of the financing and liquidating accounts to cover payments of compensatory damages for alleged violations of the civil rights of the African-American farmers, does not provide the same level of oversight and budgetary visibility of the Department's corrective actions in this area.

In summary, we believe that Congress did not intend that the administrative payments of compensatory damages for alleged violations of the civil rights of African-American farmers should be considered to be part of the "cost" of a loan or loan guarantee for the purposes of the Credit Reform Act, especially where no loan or guarantee was made. Rather, we believe that the compensatory damage awards is properly chargeable to the administrative expense appropriation provided to cover the cost of administering the direct loan and guaranteed loan programs.

Sincerely yours,



Robert P. Murphy
General Counsel