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Office of Inspector General
Southwest Region

Audit Report

Farm Service Agency
Payment Limitation Review in Louisiana

Report No. 03099-181-Te
May 2008

UNITED STATES DEPARTMENT OF AGRICULTURE
OFFICE OF INSPECTOR GENERAL
Southwest Region
101 South Main, Suite 324
Temple, Texas 76501
TEL: 254-743-6565 / FAX: 254-298-1373

May 8, 2008

REPLY TO
ATTN OF: 03099-181-Te

TO: Willie F. Cooper
State Executive Director
Farm Service Agency
Alexandria, Louisiana

FROM: Timothy R. Milliken /s/ Billy R. Engelke for
Regional Inspector General for Audit

SUBJECT: Farm Service Agency Payment Limitation Review in Louisiana

This report presents the results of our audit of the Farm Service Agency Payment Limitation Review in Louisiana. Your written response to the draft report is included as exhibit F, with excerpts, and the Office of Inspector General's (OIG) position incorporated into the relevant sections of the report.

Based on the response, management decisions were reached for Recommendations 1, 3, and 4. Documentation and/or actions needed to reach management decision for Recommendation 2 are described in the OIG Position section of the report.

In accordance with Departmental Regulation 1720-1, please furnish a reply within 60 days describing the corrective action taken or planned and the timeframes for implementation for those recommendations for which management decision has not been reached. Please note that the regulation requires final action be taken within 1 year of each management decision to preclude being listed in the Department's annual Performance and Accountability Report.

We appreciate your timely response and the courtesies and cooperation extended to us by members of your staff during the audit.

Executive Summary

Farm Service Agency Payment Limitation Review in Louisiana (Audit Report No. 03099-181-Te)

Results in Brief

A limitation on the total annual payments that a "person" may receive under agricultural programs has been in effect since the enactment of the Agricultural Act of 1970. "Persons" may be individuals or forms of business organizations, known as "entities." For an individual or entity to be considered a separate "person," the individual or entity must have a separate and distinct interest in the land or crop involved, exercise separate responsibility for this interest, and maintain funds or accounts separate from that of any other individual or entity for this interest.

The Louisiana State Farm Service Agency (FSA) office requested that the Office of Inspector General (OIG) initiate an audit of partnership B's financial records and farming operations. The request was based on concerns identified during FSA's end-of-year review of partnership B's 2000 crop year operations. Based on the findings from its review, the agency was concerned that funds were not being maintained separately between partnership B and partnership A. Therefore, we included partnership A in our review because the two partnerships were so intertwined that it was virtually impossible to analyze one operation without reviewing the other. We reviewed crop years 2000 through 2002 for both partnerships, and the applicable FSA program payments received in Franklin and Catahoula Parishes, Louisiana.

For crop years 2000 through 2002, each partnership contained six members for a total of 12 "persons" for payment limitation purposes. Each partnership is comprised of three individual partners and three corporate partners. All six individual partners are related, and the same individuals make up the mixture of 50-percent stockholders in the six corporations, thus providing each individual with three permitted entities. All of the individuals were related (see exhibit B). Individual A, a medical doctor, was an individual partner in partnership B and a stockholder in two of partnership B's corporate partners. In addition, individual A was the authorized agent for both partnerships, and owns most of the equipment used to operate the farms leased by both partnerships (90 percent of partnership A's equipment and 70 percent of partnership B's equipment is leased from individual A). The partnerships received over $1.4 million in program payments for crop years 2000 through 2002.

We determined that the two partnerships were not separate and distinct for payment limitation purposes because they did not maintain funds and accounts separate from each other, and the members did not exercise separate responsibility for their interests. Basically, the two partnerships were operating as one farming operation to conceal the true interest of individual A. Specifically, the same equipment was shared by the partnerships to conduct their farming operations, funds were shifted between the partnerships and individual A as deemed necessary, and some operating expenses were not timely paid to individuals or entities with direct or indirect interests in the partnerships' farming operations, or were not proportionately shared between the partnerships when compared to the crops and numbers of acres worked. We concluded that these were not the actions of separate operations that take responsibility for expenditures in the year they are due, and that maintain separate funds and accounts.

The farming operations have had a history of improper actions prior to this review. FSA performed an end-of-year review on partnership A for the 1998 crop year. The agency determined that partnership A (1) did not maintain funds or accounts separate from partnership B, (2) did not provide a significant contribution of capital, land, or equipment, and (3) did not meet the cash rent tenant provisions. Based on this determination, partnership A was ineligible for all 1998 program payments. FSA's report also pointed out that partnership A (after being out of farming in 1997) was brought back into farming in 1998 when partnership B increased the size (acres) of its farming operation, and partnership B's program payments from the increased land would have exceeded the payment limitations for the six persons of partnership B. Also, OIG's Investigations staff issued a report[1] on partnership A that determined the partnership concealed some of its 1998 crop year production in order to qualify for disaster payments and an emergency loan totaling $477,792. The investigating agent was told by individual B (individual A's brother) that the investigator needed to talk to individual A about the case because individual B had not had anything to do with the farm for years except to sign his name to papers to help his brother keep the farm going. Individual B and individual C (father to individuals A and B) are individual members and 50-percent shareholders in two of the corporate partners of partnership A that was investigated. This case is still under consideration for prosecution by the Assistant U.S. Attorney.

Recommendations In Brief

We recommend that the Louisiana State FSA office determine whether a scheme or device was adopted to evade the 2000 through 2002 payment limitation provisions, and, if so determined, collect program payments totaling over $1.4 million[2] from the two partnerships. If the State office determines a scheme was not adopted, we recommend that the State office determine

[1] Report of Investigation [ ], dated January 29, 2003.
[2] See exhibit E.

whether the 12 members of the two partnerships should be combined to be one "person" for payment limitation purposes, and collect payments applicable to each of the 3 years that exceed the amount allowed one "person."

Agency Response

A letter from the Louisiana State Executive Director dated April 28, 2008, stated that the Louisiana State FSA Committee, at its meeting on April 9, 2008, reviewed the subject audit and concurred with the findings. The committee determined that the members of partnerships A and B did not meet the procedural requirements to be recognized as persons for 2000 through 2002. Also, the State committee determined that the members of partnerships A and B adopted and participated in a scheme or device designed to evade the rules of payment limitation and payment eligibility for the years 2000 through 2002. A decision letter will be issued within 30 days and the collection process will be initiated.

OIG Position

We agree with the action taken by the Louisiana State FSA Committee. To reach management decision, we need a copy of the bill for collection for amounts owed to the Government and support that the amounts have been entered as a receivable on FSA's accounting records. If final action occurred, evidence of collection would suffice.

Abbreviations Used in This Report

CFR	Code of Federal Regulations
CPA	Certified Public Accountant
FSA	Farm Service Agency
OIG	Office of Inspector General
PFC	Production Flexibility Contract

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Background and Objective

Background

The Louisiana State Farm Service Agency (FSA) office conducted an end-of-year review for crop year 2000 on partnership B and identified evidence of possible payment limitation violations. The agency was concerned that funds were not being maintained separately between partnership B and partnership A. Because of these concerns, the State office requested that the Office of Inspector General (OIG) perform a review of partnerships B's financial records and farming operations to determine the extent of payment limitation rule violations. OIG included partnership A in the review because the two partnerships were so intertwined that it was virtually impossible to analyze one operation without reviewing the other.

A limitation on the total annual payments that a "person" may receive under agricultural programs has been in effect since enactment of the Agricultural Act of 1970. Subsequent legislation, including the Food Security Act of 1985; the Omnibus Budget Reconciliation Act of 1987; and the Food, Agricultural, Conservation, and Trade Act of 1990 modified the provisions that define a "person" and the rules for payment limitation and payment eligibility.

"Persons" are the units to which payment limitations currently apply. Persons may be human beings (individuals) or forms of business organizations, known as "entities." For an individual or entity to be considered a separate "person," the individual or entity must have a separate and distinct interest in the land or crop involved, exercise separate responsibility for this interest, and maintain funds or accounts separate from that of any other individual or entity for this interest.

The Federal Agriculture Improvement and Reform Act of 1996 amended the provisions of the Food Security Act of 1985 to:

- provide a $40,000 limitation per fiscal year on the total payments made to a person under one or more production flexibility contracts (PFC);
- provide a $50,000 limitation on the total payments made to a person under one or more PFCs (this limitation applies to the 7-year life of the contract);
- provide a $75,000 limitation on the amount of marketing loan gains and loan deficiency payments a person may receive; and
- apply the payment limitation and payment eligibility requirements and restrictions of the 1985 Act to payments made under a PFC, marketing loan gains, and loan deficiency payments.

Most recently, the Farm Security and Rural Investment Act of 2002 amended the provisions of the Food Security Act of 1985 to provide, in part, a $40,000 limitation per crop year on the total direct payments and a $65,000 limitation per crop year on the total counter-cyclical payments made to a person under one or more direct and counter-cyclical program contracts on covered commodities.

Current payment limitation administration has two major aspects: preventing the use of multiple legal entities to avoid the effective application of the payment limitations (payment recipients can receive payments through no more than three entities) and making payments to only "active farmers" (recipients must be "actively engaged in farming"). Types of business organizations that reduce farmers' risks, such as corporations or limited partnerships, count as a single payment limit "person." Types of organizations where producers pool resources but are individually liable for claims against the farm, such as general partnerships, can potentially have as many payment limit "persons" as there are members. In addition, an individual, as a sole proprietor or a member of a joint operation or a partnership, may also receive payments from two other entities that may be corporations or limited partnerships. As a result, the administration of payment limits creates incentives for producers to organize their farms in ways that would not occur in the absence of the payment limitations.

To be eligible for specified farm program payments, producers must be "actively engaged in farming." To be actively engaged, producers must contribute time (labor or management) and capital (land or equipment or operating expenses) to the farming operation. This actively engaged concept is an effort to define who is truly a farmer. The actively engaged rule is relaxed for share-rent landowners; they are considered to be actively engaged. This provision benefits operators by facilitating the sharing of production and marketing risks between operators and landowners. Determining active management is very difficult, and lack of clear criteria likely facilitates the creation of persons for payment limitation purposes.

A History of Improper Actions by the Partnerships

There have been other improper actions concerning these farming operations prior to this review.

<u>FSA's Review of Partnership A</u>:

FSA performed an end-of-year review on partnership A for the 1998 crop year. Based on the facts from the review team and explanations from individual A and the certified public accountant (CPA), the Franklin Parish FSA office issued a letter dated November 20, 2001, to partnership A with the following determinations:

- The members of partnership A did not have separate and distinct interest in the land or crop involved, and did not maintain funds or accounts separate from that of any other individual or entity for such interest. Therefore, the members of partnership A are not considered separate persons for payment limitation purposes.

- Partnership A did not provide a significant contribution of land, capital, or equipment; therefore, the members are not actively engaged and were not at risk in farming.

- Partnership A did not meet the cash rent tenant provisions.

- Partnership A did not adopt or participate in adopting a scheme or device designed to evade the payment limitation. There are some indications of scheme and device in the summary of findings; however, based on the review of the entire file, the committee determined the partnership did not intentionally commit scheme and device.

- Because of the above determination, partnership A is ineligible for all 1998 benefits and, therefore, owes a refund of all 1998 funds plus applicable interest.

In a letter dated December 20, 2001, partnership A requested that the committee reconsider its determination. In a letter dated March 8, 2002, partnership A informed the Franklin Parish FSA office that it was withdrawing its request for reconsideration regarding the determination of eligibility for the 1998 farm program year and requested to establish a repayment agreement and pay in installments.

Basically, the review team found that, in reality, partnership B financed partnership A throughout the crop year. Individual A and the CPA explained that this occurred because, in the spring of 1998, partnership A, after not farming in 1997, decided to farm again for 1998. This resulted in a delay in loan approval for partnership A in 1998, and the CPA added that the firm was using an accounting system that was sophisticated in its abilities to permit separate accounting of farms with only one checking account. Therefore, due to the time constraints of the late decision for partnership A to resume farming for 1998, and the time delay of the loan approval, it was decided to continue using the single checking account for the 1998 season. Further, the CPA told the review team that prior to 1998 both partnership A and partnership B maintained separate checking accounts and separate books. **(Note:** As shown in the Findings and Recommendations section of this report, we found that the partnerships still were not maintaining funds separate for crop years 2000 through 2002.**)** Also, the FSA review team found there was confusion surrounding the designation of the PFC payments for a farm owned by individual A. On June 5, 1998, shares were designated on the farm showing partnership B receiving 100 percent of the PFC payments. On June 30, 1998, the shares were revised to show partnership A receiving 100 percent of the PFC payments. The payments on this farm totaled $43,502 for 1998. Individual A, partner in partnership B and acting as power of attorney for partnerships A and B, made both of the designations. The review team concluded that it appeared that, on both June 5, 1998, and June 30, 1998, individual A would have known who was producing the crops on his farm. Also, the team stated that it would appear individual A would have known that partnership B, with six members, had total payment limitations of $240,000 (six members @ $40,000 each) and had reached $234,220 of this limitation on the other 15 farms operated by partnership B. (**Note**: Our audit showed that if partnership B would have continued to work the farm in question, partnership B's $43,502 payments on the farm would have been reduced by $37,722 due to payment limitation [$240,000 limitation - $234,220 payments on other farms = $5,780 remaining to claim]. Therefore, individual A brought partnership A back into farming to receive the maximum eligible payments on all the farms.) This supports our findings under Section 1 of this report.

<u>OIG-Investigations' Review of Partnership A</u>:

Also, OIG-Investigations issued Report of Investigation [ ], dated January 29, 2003, which concluded that partnership A made false statements to FSA in connection with its 1998 disaster claim and received $477,792 in benefits ($126,522 for disaster payments and a $351,270 emergency loan) to which it was not entitled. The investigation disclosed that partnership A sold 45,000 hundredweight of rice for $345,135, produced in 1998, but never reported the production to FSA. The failure to report this production enabled the partnership to qualify for 1998 crop year disaster payments and a 1998 emergency loan. Further, to secure the loan, partnership A's collateral included a cotton gin and an airplane. Both of these items actually belonged to individual A and were disposed of without applying the proceeds to the loan—the airplane was destroyed in a storm and individual A received $25,000 in insurance proceeds; individual A sold the gin equipment for over $100,000 and applied the proceeds to a personal loan. Individual A submitted all necessary documents to FSA for the disaster and loan programs. Individual A and his father (individual C, who is also a partner in partnership A) said they were unaware the additional 45,000 hundredweight of rice had not been reported to FSA. Individual C added that he did not own the gin equipment or the airplane and did not know they were listed as collateral on the security agreement for partnership A's emergency loan. Individual A said he was unaware the airplane was listed on the security agreement and, therefore, did not report the $25,000 insurance settlement to FSA. Also, individual A said he hired a farm manager in February 1998 to manage the production of the 1998 rice crop. However, the farm manager stated that individual A booked the rice at the elevator and handled all of the business surrounding the sale of the rice. The manager did not know in whose name the rice was sold, and he never went to the elevator. Individual C stated that he did not remember how much rice the partnership produced in 1998, and did not recall all the circumstances surrounding the $345,135 check for the unreported rice. He did not remember if he physically picked up the check or if the check was received in the mail. However, he did recall the check was made out to partnership A and the bank, that he endorsed it, and the proceeds were applied against the outstanding loan at the bank. In a conversation with the OIG investigator, individual B (also a partner in partnership A and brother to individual A) referred the OIG investigator to individual A about the issue because individual B had not had anything to do with the farm for years except to sign his (individual B's) name to papers to help individual A keep the farm going.

Objective

The audit objective was to determine whether payment limitation provisions were violated by partnership B and/or partnership A for crop years 2000 through 2002.

Findings and Recommendations

Section 1. Payment Limitation Provisions Violated – True Nature of Farming Operation Concealed and Members Were Not Separate Persons

Finding 1

Partnership A and partnership B certified to FSA that they were separate farming operations and received program payments in Franklin and Catahoula Parishes. Each partnership is comprised of three individual partners and three corporate partners. All six individual partners are related, and the same individuals make up the mixture of 50-percent stockholders in the six corporations (see exhibit B).

Individual A is an individual partner and 50-percent stockholder in two of the corporate partners for partnership B and is the authorized agent for both partnership A and partnership B. Documentation submitted to the Franklin Parish FSA office, and certified to by the individuals involved, indicated that the partnerships were separate farming operations. Based on this information, the county office determined that each of the two partnerships was comprised of six separate persons—thereby qualifying for 12 payment limitations and enabling the partnerships to receive over $1.4 million in program payments for crop years 2000 through 2002 (see exhibit E).

However, we found that the partnerships were not separate and distinct for payment limitation purposes because they did not maintain separate funds and accounts, and the members did not exercise separate responsibility for their interests. We concluded that the two partnerships did not conduct their operations as represented to FSA—that the partnerships operated as one operation and were used to conceal the true interest of individual A. Farms (and acres within these farms) leased by individual A and partnership B were prorated through subleases to both partnerships in such a manner as to ensure there were no reductions of program payments for payment limitation. For 2000-2002, partnership A reported it leased 90 percent of its equipment, and partnership B reported it leased 70 percent of its equipment. Both partnerships leased their equipment from individual A. When we compared the partnerships' equipment lists we found that the partnerships shared use of over 95 percent of the equipment items leased from individual A. In addition, both partnerships hired 80 percent of their labor–the majority of which was paid to corporate partner F, which is 50-percent owned by individual A. Also, records showed that funds were shifted between the two partnerships, and between individual A and the partnerships. Further, land leases were not always paid in the year of responsibility, and some operating expenses were not proportionally paid by each partnership in relation to the acres operated. We believe these actions were not arm's-length transactions for normal operations where each individual/entity is separate and at risk for its respective financial obligations.

Regulations[3] state that the following acts may be considered a scheme or device to evade the payment limitation provisions:

- concealing information that affects the application of the payment limitation provisions;
- submitting false or erroneous information; or
- creating fictitious entities for the purpose of concealing the interest of a person in a farming operation.

Regulations[4] further state that for an individual or entity to be considered a separate person, the individual or entity must:

- have a separate and distinct interest in the land or crop involved;
- exercise separate responsibility for this interest; and
- maintain funds or accounts separate from that of any other individual or entity for this interest.

We believe this case is another example of how producers, over the years, have evaded the payment limitation provisions by establishing partnerships, on paper, with unneeded individual and corporate partners in order to maximize the number of "persons" for payment limitation purposes. We say unneeded because, in this case, as in prior audit cases, one individual makes virtually all the decisions and, in the end, that person reaps the major benefits from the operations.

From the records we were able to review,[5] listed below are various transactions that show the two partnerships were not separate and distinct and that each member was not at risk for its interest in the farming operations.

Land Was Prorated Between Partnerships A and B to Maximize Program Benefits, and Partnership A Did Not Pay All Land Leases for 2000 and 2001

Land leases were not properly reported to FSA for partnership A. Partnership A's Farm Operating Plan for Payment Eligibility Review for a Joint Venture or General Partnership (form CCC-502B) filed with the county office showed that the partnership leased all the land directly from the owners. Individual A signed for all the members of partnership A on the 502U. Our review disclosed that all but one of the farms used in both operations were leased directly from the owners by partnership B (in which individual A is an

[3] Title 7, Code of Federal Regulations (CFR), section 1400.5.
[4] 7 CFR 1400.3(b).
[5] See the Scope and Methodology section of the report for discussion of limitation to records and interviews.

individual partner and shareholder in two corporate partners). The other farm was leased by individual A, then subleased to partnership B, who in turn subleased a portion of the land to partnership A. Partnership A had only one check paid directly to the owners of its leased land—the rest of its lease payments were for land subleased from partnership B. In some cases, the same fields were shared by both partnerships. We question this arrangement because it not only allows individual A to divide the land between the partnerships to ensure that all Government payments associated with the total acres are received without exceeding the payment limitation provisions—it sets up the possibility of shifting production to take advantage of disaster claims and emergency loans.[6]

Also, partnership A did not pay for all of its leased land in 2000 and 2001. Instead, the lease payments were established as accounts payable to partnership B. Specifically, partnership A did not pay lease payments of $55,948 in 2000 and $114,030 in 2001. These amounts were still included in its accounts payable balance of $184,248 to partnership B at the end of 2001. Therefore, partnership B financed partnership A for 2 years by not requiring partnership A to pay its lease in the years the payments were due. Also, these were not the actions of operations that are separate and distinct, and partnership A was not responsible for its interest in the operation. We could not determine if this continued in 2002 because we could not obtain the records for that year to perform the analysis. Despite our repeated requests for that year's records, the producers and their representatives did not provide them. The attorney stated that the records had apparently been lost or misplaced while being moved to three different locations.

The Same Essential Equipment Was Used to Work All Land by Both Partnerships A and B, and Partnership B Double-Paid Its 2001 Equipment Lease

Partnership A did not own a tractor—only about 10 implements. Partnership B owned only three tractors (obtained in 1991 with a total value of under $6,000), but had more implements than did partnership A. On the farm operating plans submitted to FSA for the 1999-2002 crop years, partnership A listed that 90 percent of its equipment was leased, and partnership B listed that 70 percent of its equipment was leased. Both partnerships had lease agreements for virtually the same equipment from individual A. Specifically, for 2000, we found that 164 of the 173 items individual A leased to partnership A were also leased to partnership B (i.e., individual A leased the same 164 single pieces of equipment to both partnership A and partnership B for the 2000 crop year). In essence, 95 percent of the leased farm equipment was leased by both partnerships, and the partnerships would have had to share control over use of that equipment throughout the crop year. The other nine items listed on partnership A's equipment list, included two combines, two headers, and a grain drill, which seem reasonable since partnership A was the

[6] See "OIG Investigative Review of Partnership A" under the Background section of the report.

only partnership to grow grain sorghum in 2000. However, one of the additional line items on partnership A's list was described as "other equipment" for a cost of $33,960—19 percent of the total lease amount of $178,000. This seems odd since some other individual line items were listed for less than $10.

For 2001, partnership A leased 169 equipment items, and partnership B leased 167 (99 percent) of the same items leased by partnership A. The two items leased by partnership A, but not by partnership B, were a combine and a grain drill. It would not seem reasonable for partnership A to lease the combine and grain drill in 2001 because it did not grow any grain sorghum—both partnerships reportedly grew only cotton for 2001. Also, "other equipment" was still a line item on partnership A's list, but had no charge as compared to the $33,960 for the same line item in 2000.

In all, the lease amount for partnership A in 2001 was $149,578 and for partnership B was $166,709. In 2000, partnership A paid $178,000 and partnership B paid $210,000. The lease agreements were prepared as stand-alone, yearly agreements with rates and terms established at the inception of the lease and payment due at the end of the calendar year. This type lease agreement would preclude the payment of rates based on actual equipment use. The agreements did not indicate that these equipment items were shared, nor did they explain how the cost to each partnership was prorated (by the hour, day, acres worked, etc.). Also, we could not get an explanation from the producers because we were denied interviews. We question this arrangement under the rules of separate and distinct because, if one partnership has the equipment leased, how can the other partnership (if really a separate operation) lease and have control of the same equipment at the same time?

Further, we found that partnership B paid its 2001 equipment lease of $166,709 to individual A twice. Records show that on June 6, 2001, partnership B paid individual A the $166,709 for the 2001 equipment lease, and this amount was part of the total equipment expense reported on the partnership's 2001 tax return. Then, more than 1½ years later, on December 30, 2002, another check was written to individual A for $166,709 with the notation that it was for the 2001 equipment lease. (The 2002 equipment lease of $170,000 had been paid to individual A on July 23, 2002, and the $166,709 paid in December 2002 was not part of the total equipment expense reported on the partnership's 2002 tax return.) Without further explanation from the partnership or individual A (see Scope and Methodology section) we cannot determine the true nature of this payment to individual A.

Equipment Repair/Maintenance and Fuel Costs Were Not Commensurate Compared to the Acres Operated

The partnerships' equipment lease agreements with individual A stated that the partnerships were responsible for any repair/maintenance of the leased equipment. Since both partnerships leased the same equipment and worked approximately the same number of acres, the repair and maintenance costs should be similar. However, in 2000, partnership B paid $99,240 in repair/maintenance, while partnership A paid only $9,174. In 2001, partnership B had expenses of $114,468 for equipment repair, and partnership A had $3,686. We were not provided information as to which items of equipment were repaired; however, for the number of acres worked by both partnerships, these amounts are not proportionate. In 2000, partnership A operated 2,874.17 acres (1,026.27 cotton, and 1,847.9 grain sorghum), and partnership B operated 2,570.21 acres of cotton. In 2001, partnership A operated 2,307.9 acres of cotton, and partnership B operated 2,911.1 acres of cotton. Therefore, while each partnership operated about 50 percent of the acres, partnership B paid 92 percent and 97 percent of the repair/maintenance for 2000 and 2001, respectively (see exhibit C). We were not provided records sufficient to determine the equipment repair expenses of the partnerships for 2002.

Besides the large disparity in maintenance/repair cost between the two partnerships, there also was a large disparity in the partnerships' fuel expenses when compared to acres operated. Although each partnership operated about the same number of acres, partnership B paid 76 percent of the partnerships' total fuel costs in 2000 and 87 percent in 2001 (see exhibit C).

Partnerships Paid Labor Expenses Through Corporate Members

Each partnership reported on its Farm Operating Plans for 1999-2002 that 80 percent of its labor was hired; however, the partnerships generally did not directly pay the individuals who performed the labor. Instead, the partnerships each paid two of the corporate partners of partnership B for labor, and, for 2000, partnership A also paid the third corporate partner of partnership B for labor, and partnership B paid (or reimbursed) partnership A for labor. (See exhibit D.) From the limited records of the partnerships, we determined that the majority of the partnerships' labor expense payments went to corporation F of partnership B. (Individual A is a 50-percent stockholder of corporation F.) For example, the total labor expense for both partnerships in 2000 was $211,690, of which at least 69 percent ($146,835)[7] was paid by the partnerships to corporation F. For 2001, corporation F was reimbursed for 67 percent ($110,900) of the labor expenses totaling $165,770 for the two partnerships. Since individual A declined to talk with OIG, we could not determine why the labor expenses were handled in this manner. Despite our repeated requests, we were not provided access to the corporate records

[7] $174,300 paid directly to corporation F, less unspecified labor expense reductions totaling $27,465 = $146,835. (See also exhibit D.)

needed to determine the exact nature of the labor expense transactions between the partnerships and the corporations (e.g., whether the payments by the partnerships to the corporations matched the actual labor expenses paid by the corporations). Also, sufficient records were not provided to determine the total labor expenses for both partnerships in 2002; however, we did have enough information to determine that partnership B continued to pay the corporations for labor expenses, and that corporation F claimed the payments as farm income resulting from custom hire on the Internal Revenue Service form Profit or Loss From Farming (Schedule F). Of partnership B's total labor expenses of $103,621 reported on its 2002 tax return, 93 percent ($95,985) was paid to corporation F.

Funds Shifted Between Partnerships A and B and Individual A as Needed

Partnership A's and B's general ledgers showed that funds were loaned back and forth between the partnerships and individual A. For example, in January 2000 partnership A drew $250,000 on its 1999 operating loan, and then, within the same month, loaned the same amount to partnership B. Partnership B did not secure its financing from a bank until July 2000, well into the crop year, and past planting season. Therefore, we conclude that partnership A was financing partnership B for almost half the year.

Also, individual A had a 1999 carryover of notes payable to partnership A of almost $388,000, and still had an outstanding balance of almost $375,000 at the end of 2000, and over $198,000 at the end of 2001. Although we were not provided any of partnership A's accounting records for 2002, the 2002 bank statements for partnership B showed that funds were still going back and forth between the partnerships and individual A in 2002.

Further, even though partnership A had a net loss of $100,838 for 2000, it still carried the notes receivable from individual A of almost $375,000. We question whether the members of a true separate entity could afford to sustain a loss while carrying a receivable of this amount for an individual outside its partnership.

In addition, individual A, at the same time, was financing partnership B. Partnership B's general ledger showed that individual A had outstanding loans to partnership B totaling over $389,000 at the beginning of 2000. We conclude this is just another way that individual A is shifting all resources (money, land, equipment, and labor) between the two partnerships as he sees fit (i.e., partnerships A and B and individual A are neither exercising separate responsibility for their interests in the land or crops involved, nor maintaining funds or accounts separate and distinct from one another). Further, individual A's balance of loans to partnership B was reduced to $5,109 by the end of 2000, and reduced to zero by the end of 2001. Therefore, individual A got his money back from partnership B, while his balance to partnership A remained outstanding.

Although each partnership did borrow funds from banks, there was numerous other shifting of funds or unpaid obligations between the partnerships and individual A through accounts receivable and accounts payable in addition to those discussed above. When FSA performed its end-of-year review on partnership A for the 1998 crop year, it found that partnership A did not maintain separate funds from partnership B and was not at risk for certain farming obligations. The CPA for both partnerships explained to the FSA review team that 1998 was an unusual year in that partnership A came back into farming in the spring of 1998 after not farming in 1997. Partnership A's late return to farming caused a delay in obtaining partnership A's financing (review team found that partnership B financed partnership A). Moreover, according to FSA's report concerning the 1998 end-of-year review, the automated accounting system used by the CPA at that time permitted only the separate accounting of farms with a common checking account. The CPA assured the review team that, prior to 1998, both partnerships maintained separate checking accounts and separate books (see Background section for more details). We concluded that, for crop years 2000 through 2002, the partnerships still were not maintaining separate funds and exercising separate responsibilities for certain interests in the farming operations. We also noted that both partnerships utilized individual A's flying service for aerial application in both 2000 and 2001, and hired individual A to perform custom farming in 2000. These are avenues for funds to flow from both partnerships to individual A.

Individual A Ran the Show—Used Partnerships A and B to Maximize Program Payments

As shown in the Scope and Methodology section of the report, individual A would not talk with OIG, and the attorney reported that additional records requested by OIG were either lost or misplaced. The CPA who kept the partnerships' and individual A's books for the period of our review would not explain any of the transactions for the partnerships' limited journals or adjusting entries to which we were given access. Also, individual A's attorney withdrew as a go-between for OIG's requests for records from individual A. This was after we had been advised by the attorney that our requests for information for either partnership should go to individual A, who was the authorized agent for both partnerships. Therefore, we could not determine the extent to which individual A benefited from these farming operations. However, we believe the information presented above shows that this was practically one operation, with individual A controlling the land, equipment, labor, and funds to give the appearance that there were two separate and distinct operations. This conclusion also is supported by prior findings reported by FSA and OIG-Investigations (see *"History of Improper Actions"* in Background section). For example, individual A's brother, individual B (individual partner and 50-percent owner of two corporate partners in partnership A), told an OIG investigator that he had not had anything to do with the farm for years except to sign his name to papers to help his brother (individual A) keep the farm going. Further, FSA stated in its end-of-year review report that individual A added partnership A in 1998 (partnership had not farmed in 1997) when he added additional acres and realized that the six persons in partnership B would not cover all the program payments. (Again, see FSA's review of partnership A in Background section.) Therefore, we conclude that these partnerships contained shell corporations and individuals who were not truly actively engaged in farming in order to conceal the true interest of individual A in the farming operation. Further, we conclude the producers concealed information, and/or submitted false or erroneous information that would have affected the application of the payment limitation provisions.

Recommendation 1

Determine whether the producers adopted a scheme or device to evade payment limitation provisions for crop years 2000 through 2002.

Agency Response.

The Louisiana State FSA Committee, at its meeting on April 9, 2008, determined that the members of partnerships A and B adopted and participated in a scheme or device designed to evade the rules of payment limitation and payment eligibility for the years 2000 through 2002.

OIG Position.

We agree with the State Committee's management decision.

Recommendation 2

If an adverse determination is made for Recommendation 1, collect program payments subject to limitation for each year for which a scheme or device was adopted and for the subsequent year. (The producers' payments subject to limitation totaled over $1.4 million for the 2000 through 2002 crop years. See exhibit E.)

Agency Response

The Louisiana State FSA Committee will issue a decision letter within 30 days and the collection process will be initiated.

OIG Position

We agree with planned action by the State Committee. To reach management decision, we need a copy of the bill for collection for amounts owed to the Government and support that the amounts have been entered as receivables on FSA's accounting records. If final action occurred, evidence of collection would suffice.

Recommendation 3

If an adverse scheme or device determination is not made under Recommendation 1, determine whether the two partnerships and their 12 members should be combined to be one "person" for crop years 2000 through 2002 payment limitation purposes.

Agency Response.

In addition to determining that a scheme or device was adopted, the State Committee also determined that the members of partnerships A and B did not meet the procedural requirements to be recognized as persons for 2000 through 2002.

OIG Position.

We agree with the State Committee's management decision.

Recommendation 4

For each year for which it is determined in Recommendation 3 that the two partnerships and their members should be combined to be one "person," collect all program payments issued the combined producers in excess of the amount allowed for one "person."

Agency Response.

The Louisiana State FSA Committee will issue a decision letter within 30 days, and the collection process will be initiated.

OIG Position.

We agree with the State Committee's management decision. (Amounts owed to the Government are included in the amount to be collected under Recommendation 2.)

Scope and Methodology

The scope of the review included the 2000 through 2002 crop year farming operations of partnerships A and B and related individuals (who had direct or indirect interests in the partnerships). The individuals had no other reported farming interests outside their direct and indirect interests in the two partnerships. Partnerships A and B received farm program payments in Franklin and Catahoula Parishes for crop years 2000 through 2002. Field work was performed from May 4, 2004, to February 2, 2008.

To accomplish the audit objective, we reviewed payment limitation regulations, policies, and procedures.[8] We interviewed officials at the Louisiana State and Franklin Parish FSA offices. As applicable, we reviewed 2000 through 2002 program records and farm operating plans for both partnership A and partnership B maintained by the Franklin Parish FSA. In addition, we reviewed the 1992 amended partnership agreements for both partnerships, the 2000 and 2001 depreciation schedules for equipment each partnership owned, and 2000 and 2001 equipment leases with individual A. The State office also provided partnership B's land leases with various land owners; land subleases between partnership B and partnership A, applicable to the 2000 and 2001 crop years; and partnership B's 2002 checking account records, to include monthly statements and cancelled checks.

The former CPA for both partnerships provided the 2000 and 2001 Internal Revenue Service Form 1065, Return of Partnership Income, for both partnerships, and the Schedule K-1, Partner's Share of Income, Credits, Deductions, etc., for each member of both partnerships. In addition, the CPA provided the 2000 and 2001 financial statements for both partnerships with supporting general ledgers, transaction registers, equipment depreciation schedules, and various worksheets detailing expenses and adjusting journal entries. Further, the CPA provided records pertaining to the 2000 and 2001 operating loans with the bank for each partnership.

Significant constraints were imposed on the audit approach by limitations on access to certain producer records and individuals. Specifically, our review was limited because additional documentation requested for both partnerships, through individual A's attorney, was not provided. Also, we were unable to interview[9] the producers to obtain clarification on the available records we did obtain. The attorney stated that the records we requested had apparently been lost or misplaced while being moved to three different locations and referred us to the CPA. Although the CPA provided us what records he had, he said he

[8] 7 CFR 1400 and FSA *Handbook 1-PL* (Revision 1).

[9] At a brief, unscheduled meeting with individual A at the county office (he happened to come in the office while the auditor was there), individual A instructed the auditor to contact him for all questions concerning both partnerships since he was the authorized agent for both. After repeated attempts to contact individual A, we spoke with his attorney who, in turn, instructed us to process all questions concerning the partnerships through him. The attorney also advised individual A not to conduct interviews with OIG.

would not provide any explanations to our questions because he had recently been sued by, and no longer worked for, individual A. Aside from the Schedules K-1, we were not provided any accounting records for the partnerships' corporate members. Cumulatively, this lack of cooperation limited our evaluation of the total financial transactions of the partnerships, individuals, and corporate partners.

We conducted this performance audit in accordance with generally accepted Government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

Exhibit A – *Summary of Monetary Results*

FINDING NUMBER	RECOMMENDATION NUMBER	DESCRIPTION	AMOUNT	CATEGORY
1	2	Payment Limitation Provisions Violated – True Nature of Farming Operation Concealed and Members Were Not Separate Persons	$1,432,622[10]	Questioned Costs – Recovery Recommended
TOTAL MONETARY RESULTS			**$1,432,622**	

[10] The amount has been rounded to the nearest dollar and is relative to a determination of scheme or device. (See exhibit E for amounts questioned.) A lesser amount will be recovered if the partnerships and their members are combined as one "person." (See also Recommendation 4.)

Exhibit B *– Members' Shares of Partnerships and Their Familial Relationships to Individual A*

Partnership A:

Individual C (Father)	16.67 percent
Individual B (Brother)	16.67 percent
Individual D (Cousin)	16.67 percent
Corporation A	16.67 percent
Individual D	50 percent
Individual B	50 percent
Corporation B	16.66 percent
Individual C	50 percent
Individual B	50 percent
Corporation C	16.66 percent
Individual C	50 percent
Individual D	50 percent

Partnership B:

Individual A	16.67 percent
Individual E (Uncle)	16.67 percent
Individual F (Nephew)	16.67 percent
Corporation D	16.67 percent
Individual A	50 percent
Individual E	50 percent
Corporation E	16.66 percent
Individual E	50 percent
Individual F	50 percent
Corporation F	16.66 percent
Individual A	50 percent
Individual F	50 percent

Exhibit C - *Comparison of Identified Farming Expenses in Relation to Acres Worked*

Program Year	Partnership	Acres 3/	% 1/	Equipment Leased from Individual A 2/	% 1/	Equipment Maintenance and Repair	% 1/	Fuel	% 1/	Labor	% 1/	Fertilizer	% 1/	Seed	% 1/	Chemicals	% 1/
2000	Partnership B	2,570.21	47	$210,000	54	$ 99,240	92	$60,572	76	$133,690	63	$160,840	64	$110,965	59	$230,612	57
	Partnership A	2,874.17	53	$178,000	46	$ 9,174	8	$19,167	24	$ 78,000	37	$ 90,906	36	$ 78,666	41	$170,912	43
TOTAL		**5,444.38**	**100**	**$388,000**	**100**	**$108,414**	**100**	**$79,739**	**100**	**$211,690**	**100**	**$251,746**	**100**	**$189,631**	**100**	**$401,524**	**100**
2001	Partnership B	2,911.10	56	$166,709	53	$114,468	97	$36,019	87	$ 95,270	57	$111,500	68	$163,611	60	$204,277	51
	Partnership A	2,307.90	44	$149,578	47	$ 3,686	3	$ 5,232	13	$ 70,500	43	$ 52,042	32	$108,101	40	$197,663	49
TOTAL		**5,219.00**	**100**	**$316,287**	**100**	**$118,154**	**100**	**$41,251**	**100**	**$165,770**	**100**	**$163,542**	**100**	**$271,712**	**100**	**$401,940**	**100**

1/ Percentage of total for both partnerships.

2/ Both partnerships lease virtually the same equipment from individual A.

3/ Year 2000: partnership B – all acres were in cotton; partnership A – 1,026.27 acres of cotton and 1,847.9 acres of milo. Year 2001: all acres for both partnerships were in cotton.

Exhibit D – Payroll/Labor Expenses

PROGRAM YEARS 2000 AND 2001 PAYROLL EXPENSE FOR PARTNERSHIPS A AND B

PROGRAM YEAR	PARTNERSHIP	LABOR PAYEES						Reductions	Total
		Corporation F	Corporation E	Corporation D	Partnership A	Individual A	Various Others		
2000	Partnership A	$ 68,500	$22,500	$12,000				1/ $25,000	$ 78,000
	Partnership B	$105,800	$ 6,000		2/ $20,000	$100	$4,255	3/ $ 2,465	$133,690
	Totals	**$174,300**	**$28,500**	**$12,000**	**$20,000**	**$100**	**$4,255**	**$27,465**	**$211,690**
2001	Partnership A	$ 18,000	$52,500						$ 70,500
	Partnership B	$ 92,900	$ 2,000				$ 370		$ 95,270
	Totals	**$110,900**	**$54,500**				**$ 370**		**$165,770**

1/ Journal entries reduced partnership A's labor expense by $25,000.

2/ Partnership B paid partnership A $20,000, apparently to reimburse partnership A for labor payment. Unable to determine which corporation(s) partnership A had paid for partnership B's labor.

3/ Partnership B initially classified legal and accounting expense totaling $465 as labor. Journal entry reduced labor expense $2,000. Unable to determine origin of $2,000 reduction.

Exhibit E *– Program Years 2000 Through 2002 Program Payments Subject to Limitations for Partnerships A and B*

PROGRAM YEAR*	PARTNERSHIP A	PARTNERSHIP B	TOTAL
2000	$182,167	$599,573	$ 781,740
2001	$192,892	$315,233	$ 508,125
2002	$ 58,773	$ 83,984	$ 142,757
TOTAL	**$433,832**	**$998,790**	**$1,432,622**

* = Neither of the partnerships, nor the corporate members of either partnership, received program benefits in 2003. (Payments for program years 2000 through 2002 are rounded to nearest dollar.)

Exhibit F – *Agency Response*

United States Department of Agriculture

Farm and Foreign Agricultural Services

Farm Service Agency

Louisiana State FSA Office
3737 Government St
Alexandria, LA
71302-3395

DATE: April 28, 2008

TO: OIG - Audits
[ ]

FROM: Willie Cooper
State Executive Director

SUBJECT: Audit 03099-181-Te [ ]

The Louisiana FSA State Committee, at its meeting on April 9, 2008, reviewed subject audit and concurred with the findings. The Committee determined that the members of [ ] and [ ] did not meet the procedural requirements to be recognized as persons for 2000 through 2002. Also, the State Committee determined that the members of [ ] and [ ] adopted and participated in a scheme or device designed to evade the rules of payment limitation and payment eligibility for the years 2000 through 2002.

A decision letter will be issued within 30 days and the collection process will be initiated.

If I can be of further assistance, please feel free to contact this office.