

134819

United States General Accounting Office

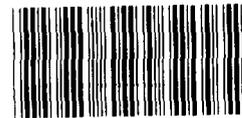
GAO

Report to the Honorable
Ron Marlenee, House of Representatives

December 1987

CROP INSURANCE

Conflict-of-Interest Problems Involving an FCIC Official



134879

**Resources, Community, and
Economic Development Division**

B-209866

December 18, 1987

The Honorable Ron Marlenee
House of Representatives

Dear Mr. Marlenee:

In response to your request of May 14, 1986, and subsequent discussions with your office, we examined whether any potential conflict of interest exists between Mr. E. Ray Fosse's private business interests and his positions as a member of the Board of Directors and Manager of the U.S. Department of Agriculture's (USDA) Federal Crop Insurance Corporation (FCIC).

In accordance with the Federal Crop Insurance Act of 1980, FCIC has expanded crop insurance from a program covering certain counties and crops to a national program covering most major agricultural crops. In doing so, FCIC has gone from a program in which its employees sold and serviced policies, to a program where FCIC operates primarily as a reinsurer of private insurance companies, with the reinsured companies selling and servicing policies.¹

Your main concerns were Mr. Fosse's employment by the Crop Hail Insurance Actuarial Association (CHIAA), which provides services to the reinsured companies; his role in FCIC's movement to reinsurance; and his relationship with reinsured companies. You asked that we determine, for the period of Mr. Fosse's tenure as Board member and FCIC Manager

- what relationship FCIC has had with CHIAA and the income CHIAA receives from services provided to reinsured companies;
- whether Mr. Fosse properly abstained from voting on issues that may have benefited organizations with which he was associated;
- what relationship Mr. Fosse has had with CHIAA, including any compensation he and/or his family received from CHIAA; and
- whether Mr. Fosse had any relationship with reinsured companies or firms other than CHIAA doing business with FCIC.

¹As a reinsurer, FCIC accepts responsibility for part of the risk of claim losses on policies sold by the private companies.

Because violations of conflict-of-interest laws and standards-of-conduct regulations may involve criminal or disciplinary sanctions, their interpretation and enforcement is within the purview of courts, the Department of Justice, the Office of Government Ethics (OGE), and the employing agency (in this case, USDA).² For this reason we offer our judgment only as to whether, based on applicable precedents, Mr. Fosse's actions appear to be in violation of the governing statutes and regulations.

In summary, we found that Mr. Fosse's actions resulted in apparent violations of conflict-of-interest laws and employee standards-of-conduct regulations. These apparent violations resulted from Mr. Fosse's voting on FCIC motions affecting CHIAA's financial interests while employed by CHIAA and his acceptance of about \$2,400 for participating in two conferences sponsored by CHIAA and related organizations while serving on the FCIC Board. Also, cost-of-living increases to a retirement annuity Mr. Fosse receives as a result of his CHIAA employment are dependent on CHIAA's ability and willingness to fund them. Thus, Mr. Fosse has a continuing financial interest in CHIAA which can potentially result in violations of conflict-of-interest statutes.

Mitigating circumstances should be considered in judging the severity of the potential conflict-of-interest problems identified. For example, the 1980 act's requirement that a person experienced in crop insurance be appointed to the Board envisioned the appointment of a person who will work for FCIC on a part-time basis. Thus, such a person could well be expected to have business interests affected by FCIC. USDA's Office of the General Counsel (OGC) recognized the difficulty Mr. Fosse could have in trying to avoid conflict-of-interest situations and provided him with written guidance. The guidance, however, was very general and did not constitute a statutorily authorized waiver of conflict-of-interest laws and regulations. We believe that OGC erred by not advising Mr. Fosse to obtain a waiver.

Background

Under the Federal Crop Insurance Program, FCIC, a wholly owned government corporation, offers agricultural producers protection against unavoidable losses due to natural causes. The program was substantially changed by the Federal Crop Insurance Act of 1980 which, among

²OGE has general responsibility for interpreting conflict-of-interest laws and employee standards-of-conduct regulations.

other things, called for (1) a major expansion of the program and (2) involvement of the private sector in delivering insurance to farmers.

Before 1981 crop insurance was sold primarily by FCIC employees. In 1986, however, private companies that are reinsured by FCIC made 80 percent of the approximately \$380 million of insurance sales, and private companies, called master marketers, made the remainder. The reinsured companies sell insurance policies under their own names, perform all servicing of the policies, and share in any underwriting gains and losses with FCIC. Master marketers sell insurance for FCIC directly and perform only limited servicing of the policies for FCIC.

FCIC receives its overall direction from a seven-member Board of Directors.³ The 1980 act requires, among other things, that one Board member be a nonfederal employee who is experienced in crop insurance. Mr. E. Ray Fosse was appointed to the Board in this capacity on October 1, 1981.

While on the Board, Mr. Fosse was also employed by CHIAA as its Assistant Secretary and Manager until his retirement on June 30, 1983. CHIAA is a nonprofit organization whose membership is made up of reinsured companies and other private crop insurance companies.

Mr. Fosse remained a Board member (special government employee) until he was appointed FCIC Manager on May 15, 1986. The Manager, who is the day-to-day operating head of FCIC, receives direction from the Board. As Manager, Mr. Fosse serves as the Board's chief executive officer.

Appendix I provides more detailed background information on FCIC's organization, Mr. Fosse's role in the program, and federal conflict-of-interest laws and regulations, and describes in detail the scope and methodology of our work.

³As a result of the combining of two USDA offices that the 1980 act required to be represented on the Board, the Board currently has six members.

FCIC's Relationship With Crop Hail Insurance Actuarial Association

CHIAA's major involvement in the crop insurance program is through the management information services it provides to all FCIC reinsured companies. Each reinsured company submits data to CHIAA on the policies it sells and the claims it pays. CHIAA, in turn, computerizes the data for the companies and also submits it to FCIC. FCIC uses the sales and claim data to (1) make and receive payments to and from the reinsured companies and (2) manage the program.

The proportion of FCIC insurance sold by reinsured companies has increased substantially since they were added to FCIC's insurance delivery system in 1981—from none in 1980 to 80 percent of all insurance sold in 1986. Because CHIAA charges the companies a fee for its services which is a percentage of premium income, CHIAA's income from the program increased from \$310,000 in 1981 to \$2.6 million in 1986.

Appendix II presents a more detailed discussion of FCIC's relationship with CHIAA.

Mr. Fosse's Voting Record

As a Board member, Mr. Fosse's voting on some matters appears to have violated a conflict-of-interest statute.⁴ The statute prohibits federal employees from participating, through decision, recommendation, or otherwise, in any determination or other particular matter which affects their own financial interest or those of organizations where they serve as officers or employees.⁵ The statute does allow appointing officials (in this case the Secretary of Agriculture) to waive the statute's prohibitions if the official determines that the employee's financial interests are not so substantial so as to adversely affect his or her services. In the absence of a waiver, Mr. Fosse should have abstained from voting and/or deliberating on any matter affecting the financial interests of CHIAA until his retirement from CHIAA in June 1983.

Mr. Fosse, with one exception, abstained from voting on motions that could favorably affect reinsured companies. He did, however, vote in favor of three motions to change the standard sales and service agreement that sets out the terms and conditions under which the reinsured companies' only competitor—master marketers, who sell FCIC insurance—does business with FCIC. The three motions voted on involved changes that could have had an adverse impact on master marketers'

⁴See 18 U.S.C. 208.

⁵Although the statute's prohibitions include actions other than voting, our review was limited to Mr. Fosse's voting record because the Board minutes do not set forth the Board's deliberations.

ability to compete with the reinsured companies. Because CHIAA's fee is dependent on the reinsured companies' sales, these changes had the potential to benefit CHIAA financially. For instance, one change eliminated a provision under which FCIC paid master marketers a bonus when they exceeded sales goals.

As discussed earlier, there are certain factors that tend to mitigate the severity of the apparent violations of the conflict-of-interest statute resulting from Mr. Fosse's votes. In particular, USDA's OGC recognized the potential problems Mr. Fosse could face because of his CHIAA employment, but did not advise him of the need to obtain a waiver. In OGC's view, the 1980 act, by implication, granted Mr. Fosse a limited exception to the prohibitions of the conflict-of-interest statutes. We disagree with OGC's conclusion and believe a waiver was needed.

Appendix III presents a detailed discussion of the conflict-of-interest issues involving Mr. Fosse's voting record.

Mr. Fosse's Relationship With CHIAA and Other Organizations Raises Conflict-of-Interest Concerns

Mr. Fosse accepted two honorariums to attend conferences sponsored by CHIAA and sister organizations while a Board member that appear to have violated USDA employee standards-of-conduct regulations. Also, since January 1987, Mr. Fosse has had a financial interest in CHIAA, within the meaning of 18 U.S.C. 208, because increases to a pension resulting from his CHIAA employment are dependent on CHIAA's ability and willingness to fund them.

Mr. Fosse was given a \$2,000 honorarium for attending a February 1985 annual meeting of crop insurers in Maui, Hawaii, and a \$435 honorarium for attending a March 1986 annual meeting of crop insurers in Washington, D.C. Mr. Fosse's acceptance of the two honorariums appears to have violated USDA's regulation prohibiting employees from accepting any gifts or other things of value from an organization having business or financial relations with USDA (referred to as a prohibited source).

The \$2,000 honorarium was paid by the American Association of Crop Insurers (AACI), a lobby group that cosponsored the conference with CHIAA and another organization. Because all of AACI's members are reinsured companies, and because reinsured companies have financial relations with FCIC through the reinsurance program, AACI itself is considered a prohibited source under guidance issued by OGE. The \$435 honorarium was paid by CHIAA which, because it does business directly with FCIC, is also a prohibited source.

The \$2,000 honorarium also appears to have violated USDA's regulation that requires employees to avoid situations where they appear to be using public office for private gain. Mr. Fosse told us that he attended the conference as a private citizen and stated this in his speech. However, we do not believe that such a statement would have countered the appearance that Mr. Fosse was attending the conference as an FCIC Board member because, among other things, the conference brochure identified him as a member of FCIC's Board of Directors.

Moreover, periodic cost-of-living increases to a retirement annuity Mr. Fosse receives from CHIAA creates the possibility of further conflict-of-interest violations. Because the basic annuity is fully funded and CHIAA has no control over the fund, the annuity itself does not give Mr. Fosse a financial interest in CHIAA. However, under a retirement plan CHIAA initiated in January 1987, Mr. Fosse will receive annual cost-of-living increases to his annuity that are not fully funded. The increases are dependent on CHIAA's ability and willingness to fund them. As a result, the increases create a financial interest which, by law, precludes Mr. Fosse from participating in matters affecting CHIAA. To participate in such matters in the future, Mr. Fosse should obtain a waiver from the Secretary of Agriculture.

Appendix IV presents a more detailed discussion of Mr. Fosse's apparent violations of conflict-of-interest laws and employee standards-of-conduct regulations.

Mr. Fosse Had No Financial Interest in Other Firms Dealing With FCIC

We found no evidence that Mr. Fosse had any financial interest in a private firm, other than CHIAA, that did business directly with FCIC. Although Mr. Fosse owned stock in a private firm that offered brokerage and consulting services to reinsured companies, that holding was not prohibited and we were unable to identify any FCIC matter affecting that firm's financial interests. Mr. Fosse sold the stock when he was appointed as the FCIC Manager.

Appendix V presents a more detailed discussion of Mr. Fosse's financial interests with private firms.

Recommendation

In view of Mr. Fosse's continuing financial interest in CHIAA, we recommend that the Secretary of Agriculture direct Mr. Fosse to abstain from participating in FCIC matters affecting CHIAA unless and until the Secretary grants him a waiver of 18 U.S.C. 208 prohibitions. (See app. IV.)

Agency Comments

USDA said that while our opinion differs from that of USDA's General Counsel, Mr. Fosse followed USDA's legal advice in voting on motions before the Board. Thus, it said that to now conclude that Mr. Fosse's conduct was in violation of the law because of USDA's failure to issue him a waiver would "elevate form over substance." Nonetheless, USDA said that it intends to issue Mr. Fosse a waiver because of the continuing financial interest created by the periodic cost-of-living increases to his CHIAA pension. In addition, USDA said that it is examining the questions we raised regarding the honorariums and that appropriate action will be taken after the examination is completed.

We believe our report adequately recognizes that mitigating circumstances should be considered in judging the severity of the apparent violations of 18 U.S.C. 208 resulting from Mr. Fosse's voting record and that the problem stems from the opinion rendered by USDA's General Counsel. Had the Secretary issued a waiver similar in scope to the General Counsel's written opinion, we believe that Mr. Fosse probably could have voted on the four motions. Nonetheless, we still believe that Mr. Fosse's votes on the four motions without a proper waiver were apparent violations of the law. USDA's detailed comments are addressed in applicable appendixes of this report and are included in their entirety in appendix VI.

Major contributors to this report are listed in appendix VII. We are sending copies of the report to the Directors of the Office of Management and Budget and Office of Government Ethics and to the Secretary of Agriculture.

Sincerely yours,



J. Dexter Peach
Assistant Comptroller General

Contents

Letter		1
<hr/>		
Appendix I		10
Background	Private Sector Involvement in Federal Crop Insurance Program	10
	Makeup of FCIC's Board of Directors	10
	Information on Mr. Fosse's Government and Private Roles	11
	Federal Conflict-of-Interest Laws and Standards-of-Conduct Regulations	12
	Objectives, Scope, and Methodology	12
<hr/>		
Appendix II		15
FCIC's Relationship With the Crop Hail Insurance Actuarial Association	Description of CHIAA's Services	15
<hr/>		
Appendix III		17
Mr. Fosse's Voting Record Appears to Present Some Conflict-of-Interest Concerns	Potential for Conflict of Interest Created by Mr. Fosse's CHIAA Employment	18
	Votes on Matters That Could Benefit CHIAA	18
	Provisions of 1980 Act Do Not Provide Exemptions to Conflict-of-Interest Statute	22
	Conclusions	25
	Agency Comments and Our Evaluation	25
<hr/>		
Appendix IV		27
Mr. Fosse's Relationship With CHIAA and Other Organizations Has Resulted in Apparent Violations of Laws and Regulations	Acceptance of Honorariums Appears to Have Violated USDA Regulations	27
	Annuity and Cost-of-Living Increases	32
	Conclusions	33
	Recommendation	34
	Agency Comments	34

<p>Appendix V Mr. Fosse Had No Financial Interest in Private Firms Doing Business Directly With FCIC</p>	<p>35</p>
<p>Appendix VI Comments From the U.S. Department of Agriculture</p>	<p>36</p>
<p>Appendix VII Major Contributors to This Report</p>	<p>39 39 39 39</p>
<p>Table</p>	<p>16</p>

Resources, Community, and Economic Development	39
Division, Washington, D.C.	
Office of the General Counsel, Washington, D.C.	39
Washington Regional Office	39

Table II.1: Growth of Reinsured Companies' Sales and CHIAA's Income, Calendar Years 1981-86	16
------------------------------------------------------------------------------------------------	----

Abbreviations

AACI	American Association of Crop Insurers
C.F.R.	Code of Federal Regulations
CHIAA	Crop Hail Insurance Actuarial Association
FCIC	Federal Crop Insurance Corporation
GAO	General Accounting Office
GS	general schedule
NCLIA	National Crop Insurance Association
OGC	Office of the General Counsel
OGE	Office of Government Ethics
OPM	Office of Personnel Management
P.L.	Public Law
RCED	Resources, Community, and Economic Development Division (GAO)
TFR	Treaty Facultative Reinsurance Company
U.S.C.	United States Code
USDA	Department of Agriculture

Background

The Federal Crop Insurance Program, administered by the U.S. Department of Agriculture's (USDA) Federal Crop Insurance Corporation (FCIC), a wholly owned government corporation, offers agricultural producers protection against economic losses due to adverse weather and other natural hazards. Although the program was established in 1938, before 1980 it operated on a limited basis and covered only selected crops and counties. The Federal Crop Insurance Act of 1980 (P.L. 96-365) expanded the program to all crops nationwide.

Private Sector Involvement in Federal Crop Insurance Program

In addition to expanding the program's scope, the 1980 act involved the private sector in delivering crop insurance to farmers. Although crop insurance was sold primarily by FCIC before 1981, in 1986, 80 percent of insurance sales was made by private insurance companies that are reinsured by FCIC. FCIC reinsures the companies against a part of the risk and shares underwriting gains and losses with them. The reinsured companies sell and service policies under their own names and adjust losses on claims made by farmers. FCIC compensates them for their services on a commission basis (currently 34 percent of premiums). Master marketers sell the remaining 20 percent of FCIC insurance directly on FCIC's behalf. They service policies to a limited extent, but do not share in gains and losses. FCIC also pays them on a commission basis (currently 17.5 percent of premiums).¹

Makeup of FCIC's Board of Directors

The 1980 act also changed the makeup of FCIC's Board of Directors, which provides the overall management of the program. Prior to the 1980 act, the Board consisted of five members: the FCIC manager, two high-level USDA officials, and two private industry representatives with experience in crop insurance. The act enlarged the Board to seven members and required that the Board consist of the FCIC Manager (the Board's chief executive officer); the two Under Secretaries or Assistant Secretaries of Agriculture responsible for federal crop insurance and farm credit programs;² one person experienced in crop insurance but not employed by the federal government; and three active farmers who are crop insurance policyholders from different geographic areas of the

¹For additional information on private sector involvement, see Federal Crop Insurance Corporation Needs to Improve Decision-Making (GAO/RCED-87-77, July 23, 1987).

²Since April 12, 1982, the Under Secretary for Small Community and Rural Development has had responsibility for both areas.

country but not federal employees. Private Board members are compensated on a per-diem basis, receiving a salary equivalent to a GS-18's plus reimbursement for actual travel and subsistence expenses.³

Information on Mr. Fosse's Government and Private Roles

Mr. E. Ray Fosse was appointed to the FCIC's Board on October 1, 1981, in accordance with the 1980 act's requirement to have a member who is experienced in crop insurance but not a federal employee. Mr. Fosse served in this capacity as a special government employee until May 15, 1986, when he was appointed as FCIC's Manager. As such, he now serves as a member and chief executive officer of the Board.

When first appointed to FCIC's Board of Directors, Mr. Fosse was employed by the Crop Hail Insurance Actuarial Association (CHIAA) as Assistant Secretary and Manager. In this capacity, Mr. Fosse was in charge of managing CHIAA's operations. He was employed by CHIAA from February 26, 1968, until his retirement on June 30, 1983. Thus, Mr. Fosse served on FCIC's Board of Directors and as Assistant Secretary and Manager of CHIAA concurrently during the period October 1, 1981, to June 30, 1983.

CHIAA is a nonprofit organization that, among other things, provides its members with research, statistical, and rate-making services. CHIAA is supported by members and subscribers. Also, it processes financial and statistical data on crop insurance premiums and indemnities (claims) for private companies that are reinsured by FCIC.

Mr. Fosse has long been on record as an advocate of reinsurance. For example, in June 1977 Mr. Fosse submitted a study report proposing a reinsurance program to congressional committees, Members of Congress, the Secretary of Agriculture, and to the Office of Management and Budget. The proposal set forth the objective of providing crop insurance entirely by private industry with only a reinsurance function for government.

³General schedule (GS) salary scale for U.S. government employees.

Federal Conflict-of-Interest Laws and Standards-of-Conduct Regulations

Federal conflict-of-interest laws and standards of conduct are provided by statute, executive order, and regulations issued by the Office of Personnel Management (OPM) and by individual agencies such as USDA. The U.S. Office of Government Ethics (OGE) has general responsibility for interpreting these laws and regulations.

Certain conflict-of-interest statutes establish specific standards for special government employees, such as private sector members of FCIC's Board of Directors, that are less stringent than the standards applicable to regular employees. However, the conflict-of-interest statute, 18 U.S.C. 208, requires that both regular and special government employees must disqualify themselves from acting personally and substantially in any "judicial or other proceeding, application, request for a ruling, or other determination . . . or other particular matter" that might affect their own financial interests or the financial interests of organizations in which they serve as officers or employees.

Executive orders setting standards of conduct for government officers and employees and the OPM regulations established pursuant to 18 U.S.C. 208 apply less rigorous standards to special government employees than to regular employees. However, OPM regulations direct federal agencies to establish their own regulations, and the USDA regulations established pursuant to OPM's directive generally apply the standards for regular employees and special employees as well.

Objectives, Scope, and Methodology

Our overall objective was to determine whether any potential conflict of interest existed between Mr. E. Ray Fosse's private business interests and his positions as FCIC Board member and Manager. The scope and methodology of work relating to each of our specific objectives follow.

To determine FCIC's relationship with CHIAA, we (1) interviewed FCIC and CHIAA officials and (2) reviewed FCIC and CHIAA records and files. We also obtained financial information from FCIC and CHIAA to determine the income CHIAA earned from the services it provided the private companies reinsured by FCIC during the period 1981-86.

To determine whether Mr. Fosse properly abstained from voting on issues considered by the Board that may have benefited organizations he was associated with, we reviewed the minutes of Board meetings held during the period October 5, 1981, to December 10, 1986. (The minutes record the outcome of the votes but not the Board's deliberations.) Also, we interviewed (1) Mr. Fosse to determine why he did or did not abstain

from voting on certain issues, (2) the Secretary of the Board to obtain information on the Board's operations, (3) officials of associations representing reinsured companies and master marketers to obtain their views on the impact certain issues voted on by the Board had on their members, and (4) officials of USDA's Office of the General Counsel (OGC) and FCIC's Personnel Department to determine the guidance these organizations provided Mr. Fosse on conflict-of-interest issues.

To determine Mr. Fosse's relationship with CHIAA, we (1) interviewed Mr. Fosse and officials of CHIAA, (2) reviewed applicable CHIAA records, including payroll data, (3) reviewed information from, and interviewed officials of, CHIAA and the Connecticut General Life Insurance Company regarding a pension Mr. Fosse receives as a result of his previous employment with CHIAA, (4) reviewed the financial disclosure statements Mr. Fosse filed with USDA, one when he was appointed to the Board in 1981 and another when he was appointed Manager, and (5) reviewed Mr. Fosse's travel vouchers regarding trips to conventions sponsored by CHIAA and other associations having reinsured companies as members.

To determine whether Mr. Fosse had any relationship with private firms other than CHIAA that do business with FCIC, we (1) interviewed Mr. Fosse, (2) reviewed his financial statements, and (3) interviewed officials of various private firms and organizations such as CHIAA, a consulting firm Mr. Fosse held stock in, and reinsured companies Mr. Fosse had provided consulting service to. To determine Mr. Fosse's relationship with the consulting firm he held stock in, we interviewed officials of the company and two reinsured companies it provided services to and reviewed various documents and records relating to the company's incorporation and business.

Our review was conducted primarily at FCIC's headquarters in Washington, D.C., where we interviewed USDA and OGE officials and reviewed applicable records and files. We reviewed applicable legislation and legislative history, OPM and USDA regulations, and applicable opinions of the Department of Justice and OGE. Our review covered the period October 1981 through June 1987.

We made our review between October 1986 and June 1987 in accordance with generally accepted government auditing standards. Because violations of conflict-of-interest laws and standards-of-conduct regulations may involve criminal or disciplinary sanctions, their interpretation is within the purview of courts, the Department of Justice, OGE, and/or the

**Appendix I
Background**

affected government agency.⁴ For this reason, we offer our judgment only as to whether, based on applicable precedents, Mr. Fosse's actions appear to be in violation of the governing statutes and regulations.

⁴See B-223545, July 25, 1986 and B-150186, Aug. 24, 1986.

FCIC's Relationship With the Crop Hail Insurance Actuarial Association

The Crop Hail Insurance Actuarial Association, among other things, provides financial management information services to all private insurance companies that are reinsured by FCIC. Because the reinsurance program has expanded greatly and because the reinsured companies compensate CHIAA on a percent-of-premium basis, CHIAA's income from services related to FCIC's program has increased from about \$310,000 in calendar year 1981 to about \$2.6 million in calendar year 1986.

Description of CHIAA's Services

CHIAA is an unincorporated, voluntary, nonprofit association which is headquartered in Chicago, Illinois. Although CHIAA is in a nonprofit tax status, its members are for-profit crop insurance companies, many of which are involved in FCIC's reinsurance program. The officers of the association and its executive committee are officials of member companies.

CHIAA and its sister organizations—the American Association of Crop Insurers (AACI) and the National Crop Insurance Association (NCIA)—provide services to insurers of agricultural crops and work as a team to develop expanded insurance protection for commercial producers of agricultural products. The membership of CHIAA and NCIA is made up of FCIC-reinsured companies and companies that provide farmers with insurance for hail damage to their crops, whereas the membership of AACI is made up entirely of reinsured companies. Among other things, CHIAA provides its members with actuarial services; NCIA provides loss adjustment services; and AACI performs lobbying services.

CHIAA's main role in the reinsurance program is to provide financial management services to the reinsured companies. Each reinsured company submits data to CHIAA on the policies it sells and the claims it pays. CHIAA uses a computer to consolidate the data from each company and also submits the data for all companies on computerized tapes to FCIC. FCIC uses the sales and claims data to (1) make payments to and receive payments from the reinsured companies and (2) manage the program.

CHIAA's fee for its data-processing service is based on a percentage of premiums written by the reinsured companies. Although the actual percentage varies from year to year depending on the income and expenses incurred by CHIAA, the average for the 1981-85 period was less than 1 percent. FCIC compensates the reinsured companies for the cost of this and other administrative and operating costs they incur through the fee it pays the companies (34 percent of premiums).

**Appendix II
 FCIC's Relationship With the Crop Hail
 Insurance Actuarial Association**

Since FCIC added reinsured companies to its crop insurance delivery system in 1981, the companies have sold a growing share of FCIC insurance. In 1981, the year the program began, reinsured companies handled about 10 percent of crop insurance sales whereas in 1986, the reinsured companies handled about 80 percent of all sales. Because all reinsured companies use CHIAA's services and pay a fee based on a percentage of premiums, CHIAA's income has grown proportionately. (See table II.1.)

**Table II.1: Growth of Reinsured
 Companies' Sales and CHIAA's Income,
 Calendar Years 1981-86**

Dollars in thousands

Calendar year	Reinsured companies' crop insurance sales	CHIAA's income from services provided to reinsured companies
1981	\$12,700	\$310
1982	77,200	525
1983	95,730	1,236
1984	259,652	1,242
1985	309,840	1,776
1986	Not available	2,588

Source: CHIAA financial reports.

In addition to the financial management information services it provides reinsured companies, CHIAA has been involved in the crop insurance program in other ways. CHIAA has prepared studies, done actuarial research in conjunction with the establishment of FCIC insurance policies for relatively minor crops such as cranberries, and developed actuarial data needed by USDA's Office of the Inspector General. According to Mr. Fosse, the tasks that CHIAA has done directly for FCIC were either done on a cost-reimbursable basis or free of charge.

According to FCIC officials, CHIAA staff are in daily contact with FCIC staff on various matters. Most often, CHIAA staff call to obtain information about FCIC policies and procedures.

Mr. Fosse's Voting Record Appears to Present Some Conflict-of-Interest Concerns

Mr. Fosse's votes on four motions during the period he concurrently served on the Board and was employed by the Crop Hail Insurance Actuarial Association—October 1981 through June 1983—appear to have violated conflict-of-interest statutes and regulations. Although three of these votes appear to be in accord with the written guidance USDA's Office of the General Counsel provided Mr. Fosse, that guidance did not have the legal effect of a waiver of the conflict-of-interest statute (18 U.S.C. 208(a)). The vote on the fourth motion occurred before the guidance was issued. Because Mr. Fosse did not have a waiver issued by the Secretary of Agriculture, we believe he should not have voted on the four motions affecting the financial interests of CHIAA and reinsured companies.

While we believe that Mr. Fosse voted on some matters that he apparently should not have, the mandatory composition of the Board and other factors should be considered in judging the severity of the problem. Mr. Fosse was appointed to the Board in accordance with the 1980 act's requirement that a person experienced in crop insurance be appointed. This requirement envisioned the appointment of a person who would work for FCIC on a part-time basis and be expected to have business interests in the insurance industry that would be affected by FCIC policies and practices.

Although USDA's OGC recognized the difficulty Mr. Fosse could have in trying to avoid conflict-of-interest problems while employed by CHIAA and provided him with written guidance, it did not advise him of the need to obtain a waiver. In its written guidance, OGC said that the 1980 act, by implication, granted Mr. Fosse a limited exception to the prohibitions of the conflict-of-interest statutes and USDA's standards-of-conduct regulations. We disagree with OGC's conclusion and believe that a waiver from the prohibitions of the conflict-of-interest statutes and regulations was needed. Nonetheless, had the Secretary issued a waiver similar in scope to the General Counsel's written guidance, we believe Mr. Fosse probably could have voted on the four motions.

Also, all four of the motions voted on by the Board passed unanimously. We cannot say what influence, if any, Mr. Fosse's position on these matters had on the votes of other Board members. However, given that the Board unanimously adopted the motions, it is clear that the motions would have been adopted even had Mr. Fosse abstained from voting on them.

Potential for Conflict of Interest Created by Mr. Fosse's CHIAA Employment

Under the conflict-of-interest statute, 18 U.S.C. 208, regular and special government employees must disqualify themselves from participating in matters that might affect their own financial interests or the interests of organizations in which they serve as an officer or employee. The Department of Justice has interpreted section 208 as limiting an employee's participation in a particular governmental matter, even though the matter may have a rather broad impact. In determining whether participation is proscribed by section 208, the appropriate consideration is whether the governmental matter has a direct and predictable effect on any of the financial interests covered by that section.¹ In accordance with the statute and the Department of Justice's interpretation, while serving as an officer and employee of CHIAA (from Oct. 1981 to June 1983), Mr. Fosse should have disqualified himself from voting on any matter that could have had a direct and predictable effect on CHIAA's financial interests.

The statute's requirements, however, can be waived by the government official responsible for the employee's appointment. To grant such a waiver, the appointing official must make a determination that the financial interest disclosed by the employee is not so substantial that it would likely affect the integrity of the employee's services.

We found no evidence that Mr. Fosse had any financial interest in CHIAA or any other organization or company doing business with FCIC between June 1983, when he retired from CHIAA, and January 1987, when he began receiving cost-of-living increases to his CHIAA retirement annuity. Because he had no such financial interests during this period, Mr. Fosse could have voted on any matter considered by the Board involving reinsurance without violating the conflict-of-interest statute or regulations governing USDA employee conduct. We did not review Mr. Fosse's actions on the Board after December 10, 1986.

Votes on Matters That Could Benefit CHIAA

During the period October 1981 through June 1983, FCIC's Board of Directors held 17 official meetings (3 were telephone conference calls). Mr. Fosse participated in all but one of these meetings. Mr. Fosse told us that as a general rule, he abstained from voting on (1) motions put before the Board that could have a positive impact on master marketers and reinsured companies and (2) approval of the standard agreements with master marketers and reinsured companies. Also, he said that after he retired from CHIAA, he no longer abstained from voting.

¹See 2 Op. OLC 151 (1978).

**Appendix III
Mr. Fosse's Voting Record Appears to Present
Some Conflict-of-Interest Concerns**

As discussed earlier, in the absence of a waiver, Mr. Fosse should have abstained on all motions that could have a direct and predictable affect on CHIAA's business. This would have required that Mr. Fosse abstain from voting or deliberating on matters that could have a financial impact on reinsured companies or on master marketers.²

Mr. Fosse, with one exception, abstained from voting on motions that had a positive and direct impact on reinsured companies. He did, however, vote on three motions that could have a negative impact on master marketers, which, therefore, could have a financial impact on CHIAA through increases in the reinsured companies' business volume. As discussed earlier, Mr. Fosse's votes on the three motions were in accord with the written guidance provided him by USDA's OGC.

Our review of the minutes of Board meetings showed that Mr. Fosse voted on one motion that had a positive and direct impact on reinsured companies. In this instance, he voted in favor of a motion to adopt the official FCIC expansion philosophy. On October 6, 1981 (about 1 month before OGC's guidance was issued), the Board approved a memorandum on FCIC's expansion philosophies that was submitted to it by the FCIC Chairman.³ The memorandum set forth a list of expansion philosophies, which included the following:

1. Deliver the vast majority of FCIC insurance through the private insurance sector with major emphasis on the reinsurance concept.
2. Deliver insurance through the government sector only when no private insurance delivery system is available.

The Board's adoption of the above philosophies clearly favored reinsured companies and, we believe, set the stage for expanding their business and that of CHIAA.

In accordance with the expansion philosophy adopted by the Board, FCIC began eliminating sales by FCIC employees. Many of the employees terminated by FCIC began selling crop insurance as independent agents. In a memorandum submitted to the Board of Directors in July 1982, the then Manager of FCIC said that sales data for crop year 1981 showed that the bulk of new business was sold by individual agents who were former

²Because Board minutes do not set forth the discussions held by the Board, we could not determine what deliberations took place and who participated therein.

³The title of Chairman of FCIC was later changed to Manager.

Appendix III
Mr. Fosse's Voting Record Appears to Present
Some Conflict-of-Interest Concerns

FCIC employees. This effort, he said, did not continue in 1982 because FCIC required the agents to affiliate with either a master marketer or a reinsured company. Around this time, master marketers and reinsured companies were competing to recruit the individual agents and thus obtain their insurance business.

Mr. Fosse abstained from voting on the overall master marketing agreements which set forth the contract provisions between FCIC and master marketers. He did, however, vote on several matters to amend or otherwise change the agreements. Many of these motions could be viewed as having a negative impact on the master marketers, particularly their ability to recruit and maintain agents. In fact, most of these changes were being lobbied for by the American Association of Crop Insurers—an organization representing reinsured companies.

A summary of these changes along with the views of AACI and master marketers follow. We do not present this information to question the merits of the changes voted on, but rather to demonstrate that they could be expected to adversely affect master marketers and thus help to increase the business of the reinsured companies and CHIAA.

1. On January 5, 1982, Mr. Fosse voted in favor of a motion to eliminate provisions of the agreement under which FCIC allowed master marketers to pay sales commissions to their sales agents in advance of premium collection from the policyholder. The payment of advance commissions was a long-standing FCIC practice. The change was approved for the master marketing agreement covering the 1983 crop year.⁴ In a September 24, 1981, letter to FCIC, the AACI, of which Mr. Fosse was Recording Secretary at the time, voiced opposition to the advance commissions and other practices. Because reinsured companies did not pay the agents advance sales commissions and master marketers did, the reinsured companies considered themselves to be at a disadvantage in recruiting agents.

2. On May 11, 1982, Mr. Fosse voted in favor of a motion to amend the master marketing agreement for crop year 1983 to make it effective only for the 1982 fall-planted crops so as to permit the Board to consider proposed changes for the 1983-spring-planted crops. After adopting this motion, the Board voted on a second motion proposing changes to the

⁴A crop year is denoted by the calendar year in which the crop is harvested.

Appendix III
Mr. Fosse's Voting Record Appears to Present
Some Conflict-of-Interest Concerns

master marketing agreement involving, among other things, agent training, licensing of agents, and liability for premium collection. Mr. Fosse voted in favor of this motion, and the Board also approved it.

Regarding agents training, the approved change required master marketer agents to receive a minimum of 20 hours of certified training for each crop they sold. FCIC provided the training at the agent's expense. A background paper that FCIC management submitted to the Board on this matter stated that after receiving the training, an agent would have to pass a written test and be certified to sell crop insurance. FCIC has no similar certification process for agents employed by reinsured companies.

Although approved by the Board, another change involving licensing was not incorporated in the revised 1983 agreement. This change would have required master marketer sales agents and companies to be licensed under applicable state laws beginning with crop year 1984 sales. In a May 7, 1982, letter to the then Under Secretary of Small Community and Rural Development, AACI said that a decision should be made immediately to require that all agents be licensed by the states. The Board's approval of this licensing requirement became the subject of a long-term controversy because the master marketers viewed the requirement as part of FCIC's attempt to eliminate them. In a May 8, 1986, report to the FCIC Board, the master marketers contended that states require that an agent be sponsored by an insurance company to be licensed and that many master marketers could not qualify as a sponsoring insurance company.⁵

Another proposed change involving liability for premium collection was approved by the Board but not incorporated into the revised 1983 agreement. This change would have made the master marketers liable for the collection and payment of farmers' premiums in the same manner as reinsured companies. AACI said in its May 1982 letter that while reinsured companies required agents to guarantee the farmers' premium payment, such was not the case for master marketers and others selling FCIC insurance directly. It said that this difference had stymied the transfer to, and writing of business by, the reinsured companies.

⁵See An Objection to Licensing Requirements of the Federal Crop Insurance Corporation Imposed Upon Agents Operating Under Sales and Service Agreements, May 8, 1986.

The FCIC management background paper recognized problems with imposing such a requirement, noting that in the case of master marketers, the premium is owed to FCIC. Thus, it said that the master marketers could end up with uncollectible debts and no legal recourse to collect them. For this and other reasons, FCIC did not incorporate this change into the revised 1983 agreement.

3. On July 21, 1982, Mr. Fosse voted in favor of a revised sales commission rate and other changes covering the 1983 crop year master marketing agreement for spring-planted crops that the Board approved. These changes, among other things, eliminated the payment to master marketers of a 2-percent bonus on premiums that exceeded certain sales objectives, reduced commissions on policies with annual premiums over \$10,000, and required that sales commissions not be paid until and unless the farmers' premium was paid in full.

The AACI voiced opposition to the payment of bonuses and advance commissions in its September 1981 and May 1982 letters, noting that reinsured companies did not follow these practices. AACI discussed the relative compensation paid to master marketers and reinsured companies in the context of the competition between the two types of companies in recruiting insurance agents. At the time, much of FCIC's insurance was sold by independent agents who would be choosing between going with a reinsured company or master marketer. Relative compensation was important to attracting these agents, who would more than likely bring their customers to whichever company they chose.

Provisions of 1980 Act Do Not Provide Exemptions to Conflict-of-Interest Statute

Based on the Department of Justice's interpretation of 18 U.S.C. 208, it appears that Mr. Fosse should have abstained from voting on the matters discussed above because USDA did not grant him a waiver executed in accordance with the criteria set forth in the statute. On the other hand, Mr. Fosse's actions appear to generally fall within the broad parameters of proper Board participation that were set forth by a USDA Associate General Counsel in a memorandum dated November 21, 1981. This memorandum provided what we believe is improper guidance on potential conflict-of-interest problems that might confront Mr. Fosse and other private-sector Board members. The guidance was issued after Mr. Fosse attended his first Board meeting and voted on FCIC's expansion philosophy.

**Appendix III
Mr. Fosse's Voting Record Appears to Present
Some Conflict-of-Interest Concerns**

The Associate General Counsel expressed the view that the Congress, in mandating that the FCIC Board include three policyholders and one person experienced in the crop insurance business, recognized the potential for conflicts of interest and "... by implication granted to these individuals a limited exception to the prohibitions contained in Federal criminal law prohibiting conflicts of interest on the parts of Federal employees" The Associate General Counsel concluded that the Board member experienced in the crop insurance industry does not violate 18 U.S.C. 208 or USDA's conduct regulations merely by virtue of his involvement in the crop insurance industry. As to Mr. Fosse, in particular, the Associate stated that:

"... The individual currently designated as a member experienced in the crop insurance industry is Mr. E. Ray Fosse, Executive Secretary and Manager of the Crop Hail Insurance Actuarial Association, Inc. (CHIAA), an organization which, apparently without competition, provides actuarial services to the 17 crop hail insurance companies reinsured by FCIC. As noted, above, we believe the scope of the exception we imply is limited. Thus, we think that Mr. Fosse should not take part in deliberation or voting on any matter that directly affects his company's interest, such as the question of whether to require companies reimbursed by FCIC themselves to perform actuarial services they currently contract out or to require them to contract out actuarial services within their capability."

We disagree with the Associate General Counsel's conclusion that the Congress, in mandating that Board membership include an individual from the crop insurance industry, intended a limited exemption from the conflict-of-interest laws for such a member. We know of no legal authority for holding 18 U.S.C. 208 inapplicable, even in part, to a special executive branch government employee in the absence of an exemption or waiver properly executed in accordance with the criteria set forth in the statute. The conflict-of-interest problems inherent in the 1980 act's requirement to appoint a Board member with ties to the crop insurance industry, however, should be taken into account in determining whether to exercise the waiver authority of section 208 and in defining the scope of any such waiver.

Section 208 was enacted in 1962 as part of a major revision of the federal conflict-of-interest laws contained in title 18 U.S.C. One of the major accomplishments of that revision was the enactment of a uniform body of conflict-of-interest laws applicable to individuals who, like Mr. Fosse, serve the government on an intermittent basis. In part, this responded to the government's growing dependence on the expertise of individuals

**Appendix III
Mr. Fosse's Voting Record Appears to Present
Some Conflict-of-Interest Concerns**

from private life.⁶ The 1962 act specifically repealed the myriad conflict-of-interest exemptions which had been in effect for executive branch employees and imposed a generalized distinction between full-time government employees and a new category of special government employees made up of all those employed by the government for less than 130 days a year. Although certain of the revised conflict-of-interest statutes provide separate standards for regular and special government employees, 18 U.S.C. 208 applies the same standards to both. With regard to section 208, a May 2, 1973, President's memorandum entitled Preventing Conflicts of Interest on the Part of Special Government Employees recognizes that the government's interest in obtaining the services of special government employees can be met through use of the waiver authority contained in section 208.

It is significant that 18 U.S.C. 208(b) provides specific authority for the government official responsible for an employee's appointment to authorize a waiver based on a determination that the employee's interest "... is not so substantial as to be deemed likely to affect the integrity of the services which the government may expect from such ... employee. ...". The Congress intended that agencies use the waiver authority where appropriate to exempt individuals from the restrictions otherwise imposed by 18 U.S.C. 208, and we know of no court decision or interpretation by the Department of Justice or the Office of Government Ethics recognizing even a partial exemption based on the statutory requirement to appoint an employee with a particular qualification or affiliation.

The Department of Justice has recognized that the granting of such a waiver is a matter committed by statute to the broad discretion of the official responsible for the particular employee's appointment. Given this broad discretion, it may well have been appropriate for the Secretary to grant a waiver permitting Mr. Fosse to deliberate and vote on the matters he did. Although we disagree with the Associate General Counsel's finding of an implicit congressional exemption, the conclusion reached suggests that USDA's OGC would have recommended that the Secretary approve a waiver had OGC determined that one was necessary. Had the Secretary issued a waiver with language similar in scope to the Associate General Counsel's written guidance, we believe that Mr. Fosse could probably have voted on the four motions.

⁶See Perkins, The New Federal Conflict of Interest Law, 76 Harvard L. R. 1113, 1123 (1963).

Conclusions

While serving as an officer and employee of CHIAA, Mr. Fosse's vote on several motions before the FCIC Board affecting CHIAA's financial interest appears to have violated the conflict-of-interest provisions of 18 U.S.C. 208. Mr. Fosse's participation in the actions of the Board to (1) adopt a policy of emphasizing reinsurance sales and (2) impose various requirements on master marketers that could adversely affect their ability to compete with reinsured companies could have been expected to have a direct and predictable effect on CHIAA's financial interest.

Mr. Fosse's participation in the Board's actions to impose requirements on master marketers appears to have been in accord with the guidance USDA's OGC provided the private-sector Board members. However, we believe that the guidance incorrectly interpreted 18 U.S.C. 208 and did not constitute an official waiver of the act. To waive the requirements of the statute, the Secretary of Agriculture would have had to make a determination that Mr. Fosse's employment by CHIAA did not constitute an interest so substantial that it would likely affect the integrity of Mr. Fosse's services. Mr. Fosse's vote on the Board's determination to emphasize reinsurance sales occurred before the OGC guidance was issued, thus the guidance has no bearing on this vote.

Despite the apparent violations of the conflict-of-interest laws created by some of Mr. Fosse's votes, some factors mitigate the severity of the problem. The requirement of the Federal Crop Insurance Act of 1980 that a person having crop insurance experience be appointed envisioned the appointment of a person to a part-time position who could be expected to have private interests that would be affected by FCIC policies and practices. Further, although legally insufficient to act as a waiver, the OGC guidance sanctioned Mr. Fosse's participation in matters that could have negatively affected master marketers.

Agency Comments and Our Evaluation

In commenting on a draft of this report (see app. VI), the Secretary of Agriculture stated that although the question of a waiver for Mr. Fosse was not brought to his or his predecessor's attention, had it been, he has no doubt that Mr. Fosse would have been granted a waiver. He said that while our interpretation of the law differs from USDA's regarding the effects of the Federal Crop Insurance Act of 1980 on the restrictions contained in 18 U.S.C. 208, Mr. Fosse followed the advice USDA's OGC gave him at the time in voting on motions before the Board. Thus, the Secretary said that to now conclude that Mr. Fosse's conduct violated the law because of USDA's failure to issue him a waiver, would "elevate form over substance." Recognizing our disagreement with the USDA Associate

**Appendix III
Mr. Fosse's Voting Record Appears to Present
Some Conflict-of-Interest Concerns**

General Counsel's opinion as to whether the need for a waiver was obviated by a statutory exemption to 18 U.S.C. 208, the Secretary said that the error, if there was one, was USDA's and not Mr. Fosse's.

We have recognized in our report that mitigating circumstances should be considered in judging the severity of the apparent violations, particularly that USDA's OGC did not advise Mr. Fosse of the need to obtain a waiver. Generally, we agree that the error was USDA's. Had the Secretary issued a waiver similar in scope to the Associate General Counsel's written guidance we believe that Mr. Fosse could probably have voted on the four motions. Nevertheless, we still believe that Mr. Fosse's votes on the four motions without a proper waiver were an apparent violation of 18 U.S.C. 208.

Mr. Fosse's Relationship With CHIAA and Other Organizations Has Resulted in Apparent Violations of Laws and Regulations

In addition to the apparent conflict-of-interest violations resulting from Mr. Fosse's voting record while employed by the Crop Hail Insurance Actuarial Association, we found three other questionable instances resulting from his relationship with CHIAA and related organizations. Two instances involve apparent violations of standards-of-conduct regulations related to the acceptance of honorariums totalling about \$2,400 to cover the costs of lodging and travel expenses for two conferences sponsored by CHIAA and sister organizations. The third instance involves periodic cost-of-living increases to Mr. Fosse's CHIAA retirement annuity. Because CHIAA can exercise control over future cost-of-living increases (but not the basic annuity), Mr. Fosse currently has a financial interest in CHIAA which, without an appropriately executed waiver, precludes him from participating in matters involving CHIAA.

Acceptance of Honorariums Appears to Have Violated USDA Regulations

In May 1986, Mr. Fosse filed a financial statement disclosing his financial interests over the period October 1981 to May 1986. The statement showed that he accepted two honorariums while serving as a Board member prior to his appointment as Manager. One was an honorarium of \$2,000 to cover his and his wife's travel and lodging costs for attending a February 1985 conference in Maui, Hawaii, and another was an honorarium of \$435 to cover the costs of lodging and related expenses to a March 1986 conference in Washington, D.C. Both conferences were cosponsored by CHIAA and two related organizations. Mr. Fosse's acceptance of these honorariums appears to have violated USDA's regulations (1) prohibiting employees from accepting any gifts or other things of monetary value from any interested party, including an organization or person having business or financial relations with USDA and/or (2) requiring employees to avoid situations that might result in, or create the appearance of, using public office for private gain.

Maui, Hawaii, Conference

In February 1985, Mr. Fosse attended the fifth annual meeting of crop insurers in Maui, Hawaii, which was cosponsored by CHIAA, the American Association of Crop Insurers (the organization providing lobbying services), and the National Association of Crop Insurers (the organization providing loss adjustment services). Each of the associations hosted the conference for one day during the February 24-26, 1985, period. According to Mr. Fosse, his participation in the conference consisted of one formal speech given on the first day of the conference and discussions and presentations in small workshop-type groups. According to Mr. Fosse, his formal speech, entitled The Challenging Future, dealt with

**Appendix IV
Mr. Fosse's Relationship With CHIAA and
Other Organizations Has Resulted in
Apparent Violations of Laws and Regulations**

how insurance companies should conduct business in general. He said that he did not specifically talk about FCIC's insurance program.

Mr. Fosse was in Hawaii from February 24 to March 4, 1985. The \$2,000 honorarium was to cover travel expenses for himself and his wife, payment of their hotel bill while at the 3-day conference, and payment of their meals taken at the hotel. Mr. Fosse said that AACI reimbursed him for the plane tickets and that his hotel room and meals were charged to AACI's account.

Although Mr. Fosse told us that he attended the conference as a private citizen and stated this in his speech at the conference, he was a member of FCIC's Board of Directors at the time of the conference, and the conference brochure listed him as such. Also, an AACI official told us that Mr. Fosse was invited both as a Board member and as a crop insurance expert.

**Washington, D.C.,
Conference**

In March 1986, Mr. Fosse attended the sixth annual meeting of crop insurers in Washington, D.C., also cosponsored by CHIAA, AACI, and NCAI. According to Mr. Fosse, he was not a featured speaker as he had been at the prior year's conference but did participate in a panel discussion in which he spoke on the problems companies have in administering multi-peril crop insurance.

Mr. Fosse told us that the \$435 honorarium was provided by CHIAA and was primarily to cover his hotel costs and meals. He said that he paid for his own transportation to the conference from his home in Marion, Illinois. Although Mr. Fosse was a Board member at the time of the conference, he said that he attended the conference as a private citizen and former manager of CHIAA. We found no evidence to the contrary.

**Regulations Regarding
Acceptance of
Honorariums From
Interested Parties**

Under USDA regulations, a USDA employee, including a special government employee, cannot accept an honorarium or anything of monetary value from an interested party even when the employee is acting in a personal capacity. Thus, even if Mr. Fosse attended the two conferences as a private citizen, as he maintains, his acceptance of the two honorariums appears to have violated USDA regulations.

USDA regulations (7 C.F.R. 735-12) prohibit employees from accepting for themselves or another person, directly or indirectly any gift, gratuity, favor, entertainment, loan, unusual discount, special consideration, or

**Appendix IV
Mr. Fosse's Relationship With CHIAA and
Other Organizations Has Resulted in
Apparent Violations of Laws and Regulations**

any other thing of monetary value from any interested party. An interested party (also referred to as a prohibited source) is defined as one who has or is seeking to engage in procurement activities or other contractual business or financial relations with USDA, conducts operations or activities regulated by USDA, or has interests that may substantially be affected by the performance or nonperformance of the official duty of the employee concerned.

The Office of Government Ethics has issued two pertinent opinions interpreting an OPM regulation which the USDA regulation covering both regular and special employees implements. In one opinion, OGE held that if a prohibited source requests an employee to speak at a program on any subject, the employee is prohibited from accepting an honorarium or any other thing of monetary value from that entity.¹ In another opinion, OGE held that even when travelling in a personal capacity, a federal employee may not accept travel expenses or any gift from a prohibited source.² This opinion also held that an agency should treat as a prohibited source an organization that is not itself a prohibited source if all or a substantial majority of its members are prohibited sources.

As discussed earlier, all of AACI's members are companies that are reinsured by FCIC and, therefore, in accordance with OGE's opinion, AACI should be treated as a prohibited source. CHIAA is also a prohibited source because it does business directly with FCIC.

**Compliance With USDA's
Regulations Regarding Use
of Public Office for Private
Gain**

Mr. Fosse's acceptance of the \$2,000 honorarium for the Hawaii trip also appears to have violated USDA's regulations requiring employees to avoid situations in which it appears that they are trading on their position. USDA regulation 7 C.F.R. 735-11, which applies to both regular and special employees, requires that employees shall avoid any action that might result in, or create the appearance of, using public office for private gain. A somewhat similar USDA regulation applying specifically to special employees (7 C.F.R. 735-13) requires that an employee shall not use his or her government employment for a purpose that is, or gives the appearance of, being motivated by the desire for private gain for themselves or another person, particularly one with whom they have family, business,

¹See United States Office of Government Ethics, Participating in Privately-Sponsored Seminars or Conferences for Compensation (Oct. 23, 1985).

²See United States Office of Government Ethics, Summary of Acceptance and Disclosure of Travel Expenses and Related Gifts (May 1, 1984, amended Aug. 24, 1984).

**Appendix IV
Mr. Fosse's Relationship With CHIAA and
Other Organizations Has Resulted in
Apparent Violations of Laws and Regulations**

or financial ties. Mr. Fosse's acceptance of the \$2,000 honorarium from AACI appears to have violated both of these regulations.

The OGE opinions previously discussed also state that:

1. A government employee must be concerned with appearances even if the employee's receipt of compensation or travel expenses for attendance at a conference is not prohibited by a more specific regulation. In instances where the employee gives a speech on matters substantially related to the activities of his or her agency, the interest in avoiding any appearance of using public office for private gain may preclude the employee from receiving compensation from the sponsoring organization.

2. An employee should avoid situations where it appears that the employee or the organization sponsoring the conference is trading on the employee's government position. Neither the employee nor the sponsoring organization should use the employee's government title when the employee is appearing in his or her personal capacity.

The OGE opinion was rendered on an OPM regulation that is virtually the same as USDA's implementing regulation except that the OPM regulation applies to regular employees only, whereas the USDA regulation applies to both regular and special employees. For this reason we believe that OGE's interpretation of the OPM regulation would be the same for the USDA regulation.

As far as the extent that the \$2,000 honorarium enabled Mr. and Mrs. Fosse to travel to and stay in Hawaii during the AACI conference is concerned, the honorarium conferred a benefit and thus resulted in a private gain to Mr. Fosse. Some factors tend to create at least the appearance that this gain was a consequence of Mr. Fosse's position as an FCIC Board member. The conference brochure lists Mr. Fosse as a speaker in his capacity as an FCIC Board member, and the AACI's Executive Vice-President told us that he invited Mr. Fosse both as an FCIC Board member and as an expert on crop insurance. Moreover, Mr. Fosse's speech appears to have been related, at least indirectly, to reinsurance.

Although neither Mr. Fosse nor AACI could provide us with a copy of the speech Mr. Fosse presented, Mr. Fosse and the Executive Vice-President of AACI told us that the speech focused on the future of the crop insurance industry. Because FCIC's reinsurance program is a major part of the

**Appendix IV
Mr. Fosse's Relationship With CHIAA and
Other Organizations Has Resulted in
Apparent Violations of Laws and Regulations**

total crop insurance industry's business, it appears that at a minimum, the speech indirectly would have related to FCIC's reinsurance program.

Although Mr. Fosse's general expertise was a factor in AACI's selecting him as a speaker, we do not believe that any disclaimer he made at the conference that he was not speaking in his governmental capacity would have countered the appearance created by the conference brochure's representing Mr. Fosse as an FCIC Board member and his involvement in the Board's reinsurance work.

On the basis of the fact that the AACI identified Mr. Fosse as an FCIC Board member, and that Mr. Fosse's speech related to FCIC's business, we conclude that Mr. Fosse's acceptance of the \$2,000 honorarium created the appearance of using public office for private gain and of using his public office for a purpose that gave the appearance of being motivated by a desire for private gain. On this basis, there was an apparent violation of USDA regulations 7 C.F.R. 735-11 and 735-13.

Mr. Fosse's acceptance of the \$435 honorarium for the sixth annual conference apparently did not violate USDA regulations governing the use of public office for private gain. We have no information suggesting that Mr. Fosse was invited to the conference as an FCIC Board member or that he attended the conference in other than a private capacity. Although he did speak on a subject at least indirectly related to FCIC's reinsurance program—problems that reinsured companies have in administering the crop insurance program—this speech apparently was given informally during a panel discussion.

Mitigating Circumstances

We believe that the lack of adequate guidance by USDA mitigates to some degree the apparent violations that resulted from Mr. Fosse's acceptance of the honorariums. The guidance provided to Mr. Fosse in USDA's Office of the General Counsel's November 3, 1981, memorandum does not delineate between activities that would or would not violate USDA's regulations governing employee conduct. The lack of specific guidance on the acceptance of honorariums coupled with the conclusion that the 1980 act provided Mr. Fosse a limited exemption from the conflict-of-interest statutes and regulations could have provided Mr. Fosse with some basis to conclude that he could have accepted the honorariums.

Annuity and Cost-of-Living Increases

Because the retirement annuity Mr. Fosse receives from CHIAA is fully vested and funded and because CHIAA has no control over the fund, the annuity itself does not constitute a financial interest, which would preclude Mr. Fosse from participating in matters affecting CHIAA. However, increases to Mr. Fosse's annuity made after January 1987, although involving relatively small amounts, would constitute such an interest because the increases are dependent on CHIAA's willingness and ability to fund them and CHIAA does have some control over how the funds it contributes are invested.³ Thus, Mr. Fosse should not participate in matters involving CHIAA without a waiver issued by the Secretary of Agriculture under the authority of 18 U.S.C. 208(b). Mr. Fosse had no such waiver as of September 1987.

At the time of Mr. Fosse's retirement from CHIAA, CHIAA purchased an annuity for Mr. Fosse from the Connecticut General Life Insurance Company that was fully funded and fully vested. CHIAA has no control over how the funds establishing the annuity are invested, and Mr. Fosse would continue to receive the pension in the event that CHIAA went out of business. Under CHIAA's retirement plan in effect at the time of his retirement, Mr. Fosse did not receive cost-of-living increases to his basic pension. However, under a retirement plan CHIAA adopted in January 1987, CHIAA funds cost-of-living increases to the retirement annuity on a periodic basis. Moreover, CHIAA can direct the general areas in which such funds are invested. For example, it could direct that the fund be invested in guaranteed deposit accounts, stocks, short-term certificates, or public bonds. Also, continuation of the increases is dependent on CHIAA's (1) willingness to continue to fund the plan and (2) ability to stay in business.

Depending on how it is funded, a retirement annuity paid to a government employee by a private entity may constitute a financial interest under subsection 18 U.S.C. 208(a) and thus bar the employee from participating in matters involving the private entity.⁴ In an opinion on this issue, OGE held that a government employee's vested rights in a private corporation's pension plan give the employee a financial interest in a particular matter whenever, by virtue of the vested rights, the employee is in a position to gain or lose from developments in, or resolution of, the matter. Whether a financial interest exists depends both on the nature

³Since his retirement from CHIAA on June 30, 1983, Mr. Fosse has received only one cost-of-living increase, which was effective January 1987.

⁴Subsection 208(a) applies to special government employees.

**Appendix IV
Mr. Fosse's Relationship With CHIAA and
Other Organizations Has Resulted in
Apparent Violations of Laws and Regulations**

of the particular matter and the terms of the pension agreement.⁵ Significantly, OGE stated that section 208 does not require that the financial interest be substantial. Also, OGE said that where an annuity purchased for a government employee under a pension has been fully paid for, ordinarily the employee will not have a financial interest in matters affecting the sponsoring organization.

Consistent with the OGE opinion, we do not think Mr. Fosse's basic CHIAA annuity constitutes a financial interest in CHIAA that would bar him from participating in Board matters which would have a direct and predictable outcome on CHIAA's business or, more specifically, in matters affecting FCIC's reinsurance business. The CHIAA annuity was fully funded and vested, was not controlled in any way by CHIAA or its employees, and would continue to be paid if CHIAA went out of business.

In our opinion, however, the cost-of-living increases provided for under CHIAA's current retirement plan do give Mr. Fosse a financial interest in CHIAA within the meaning of section 208 and USDA's implementing regulations (7 C.F.R. 0.735-14(a)). Although the amount of money involved is not substantial—the increase Mr. Fosse was given in January 1987 will amount to about \$500 in 1987—the financial interest need not be substantial to invoke the prohibitions of 18 U.S.C. 208(a). However, the statute does provide for the granting of a waiver if, among other things, the agency determines that the financial interest is not so substantial as to be deemed likely to affect the integrity of the services that may be expected from an employee. In our opinion, Mr. Fosse should not work on FCIC matters that would have a direct and predictable effect on CHIAA's business until he obtains such a waiver.

Conclusions

Although Mr. Fosse's acceptance of honorariums for participating in the two conferences sponsored by CHIAA and related organizations appears to have violated USDA's regulations, there are factors which lessen the severity of the apparent violations. The USDA's legal guidance to Mr. Fosse did not identify specific actions that were precluded by conflict-of-interest laws and regulations. The guidance also reached the erroneous conclusion that the 1980 act provided Mr. Fosse with a limited exemption from these laws and regulations, which appears to provide Mr. Fosse with some basis to conclude that he could have accepted the honorariums.

⁵See United States Office of Government Ethics, 83 OGE 1 (Jan. 7, 1983).

**Appendix IV
Mr. Fosse's Relationship With CHIAA and
Other Organizations Has Resulted in
Apparent Violations of Laws and Regulations**

Under the pension plan CHIAA adopted in January 1987, cost-of-living increases provided to Mr. Fosse are dependent upon CHIAA's ability and willingness to fund them. Also, CHIAA exercises some control over the moneys it provides to fund the increases. In view of the above, the pension increases give Mr. Fosse a financial interest in CHIAA within the meaning of 18 U.S.C. 208 and, therefore, in the absence of a waiver, he should not work on FCIC matters that would have a direct and predictable effect on CHIAA's business.

Recommendation

We recommend that the Secretary of Agriculture direct Mr. Fosse to abstain from participating in FCIC matters affecting CHIAA unless and until the Secretary grants him a waiver of 18 U.S.C. 208 prohibitions.

Agency Comments

The Secretary of Agriculture said that the questions we raised regarding Mr. Fosse's acceptance of the two honorariums are being examined and that appropriate action will be taken after the review is completed. Also, the Secretary said that he intends to grant Mr. Fosse a waiver pursuant to 18 U.S.C. 208(b) for the financial interest Mr. Fosse has in CHIAA as a result of the unfunded pension increases.

Mr. Fosse Had No Financial Interest in Private Firms Doing Business Directly With FCIC

On the basis of our review of the two financial statements Mr. Fosse submitted to USDA and our discussions with Mr. Fosse and officials of various private firms and organizations, we found no evidence that Mr. Fosse had any financial interest in a reinsured company or other firm that did business directly with FCIC other than CHIAA. Mr. Fosse did own stock in a private firm that offered brokerage and consulting services to reinsured companies; however, such ownership did not violate any conflict-of-interest statute or regulation. He sold the stock when he became Manager of FCIC in May 1986.

Neither of the two financial disclosure reports Mr. Fosse submitted to USDA—the first, when he was appointed to the Board in October 1981, and the second, when he was appointed Manager in May 1986—listed any financial interest in private firms that did business with FCIC.¹ According to Mr. Fosse, the May 1986 statement listed all his financial interests during the 1981-86 period. Also, Mr. Fosse told us that he had no financial interest in any such firm since his appointment to the Board in October 1981.

Mr. Fosse and his wife did own a one-third share in the Treaty Facultative Reinsurance Company (TFR), Inc., which provides consulting and brokerage services to reinsured companies but does not do business directly with FCIC. According to Mr. Fosse, he and his wife purchased the stock for \$500 on May 4, 1984, and sold the stock back to the company for the same amount when he became FCIC Manager in May 1986. While a shareholder, Mr. Fosse performed two consulting assignments for TFR that involved reinsured companies. TFR paid him a total of about \$1,000 for his services and travel expenses on the two assignments.

We found no participation by Mr. Fosse in Board matters having a direct and predictable effect on the financial interest of TFR. Thus, we found no impropriety in Mr. Fosse's relations with TFR. Unlike CHIAA, TFR's revenues are not directly related to the volume of reinsurance premiums collected by reinsured companies. Although the expansion of reinsurance could have increased TFR's potential business opportunities, such potential in our opinion would not constitute a direct and predictable effect on TFR's financial interests under 18 U.S.C. 208.

¹After we alerted USDA's OGC that private-sector Board members were not submitting annual statements, action was taken to require that this be done.

Comments From the U.S. Department of Agriculture



DEPARTMENT OF AGRICULTURE
OFFICE OF THE SECRETARY
WASHINGTON, D.C. 20250

October 30, 1987

Honorable Charles A. Bowsher
Comptroller General of the
United States
General Accounting Office
Washington, D.C. 20548

Dear Mr. Bowsher:

I would like to take this opportunity to comment on the draft of your proposed report entitled Conflict-of-Interest Problems Involving an FCIC Official (GAO/RCED-88-24). The report concerns the activities of Mr. E. Ray Fosse as a member of the Board of Directors of the Federal Crop Insurance Corporation (FCIC) and, later, as Manager of FCIC.

Shortly after Mr. Fosse joined the FCIC Board, this Department's Office of the General Counsel (OGC) issued an opinion regarding the propriety of certain individuals (including Mr. Fosse) serving as members of the FCIC Board in light of their involvement with the crop insurance industry, either as policy holders or, in Mr. Fosse's case, as an officer of an organization, the Crop Hail Insurance Actuarial Association (CHIAA), that was a part of the crop insurance industry. The OGC opinion concluded that ". . . Congress, by implication, granted to these individuals a limited exception to the prohibitions contained in Federal criminal law prohibiting conflicts of interest on the parts of Federal employees . . . and in the Department's regulations on Employee Responsibilities and Conduct"

The opinion in question, which was addressed to the Inspector General of the Department of Agriculture and to the Chairman of FCIC, was a legal opinion issued by OGC which concluded that Mr. Fosse, as well as the three policy holder members of the FCIC Board, were, to a limited extent, granted a statutory exception from the provisions of Federal criminal law, including the provisions of 18 U.S.C. 208(a).

Your report disagrees with the advice given by OGC in regard to the effects of the Federal Crop Insurance Act of 1980 on the restrictions contained in 18 U.S.C. 208 and concludes that an 18 U.S.C. 208(b) waiver should have been issued to Mr. Fosse. I recognize, as did the OGC memorandum, that this matter is a legal question subject to differing interpretations. Assuming

Appendix VI
Comments From the U.S. Department
of Agriculture

that your interpretation of the statutes is correct, I concede that this Department inadvertently erred in not issuing an 18 U.S.C. 208(b) waiver to Mr. Fosse in 1981, when he was appointed to the FCIC Board. Assuming, however, that our interpretation of the statutes in question is correct, there would have been no need to issue an 18 U.S.C. 208(b) waiver, and in fact, to do so would have been inconsistent with the OGC interpretation.

At the time Mr. Fosse was appointed to the FCIC Board, I was serving as the Deputy Secretary of Agriculture. This matter was never brought to my attention nor, so far as I have been able to ascertain, was it brought to the attention of then-Secretary John R. Block. Thus, neither he nor I ever considered the matter or even addressed the possibility of issuing a waiver to Mr. Fosse. Had either I or the Secretary been asked, at the time, to consider granting a waiver to Mr. Fosse, I have no doubt we would have concluded that Mr. Fosse's employment by CHIAA was not so substantial as to be deemed likely to affect the integrity of the services which the Government could have expected from him. Based on that conclusion, Mr. Fosse would have been granted the relief provided by section 208(b) of title 18 U.S.C. Furthermore, now that this matter has been brought to my attention, I do intend to issue Mr. Fosse an 18 U.S.C. 208(b) waiver in regard to the small increase in his pension from CHIAA that is granted by CHIAA itself and not fully funded.

Your report notes that Mr. Fosse's actions were consistent with the advice he received from OGC and it concludes that "[h]ad the Secretary issued a waiver with language similar to [OGC's] written guidance, we believe that Mr. Fosse could have properly voted on the four motions". I agree that Mr. Fosse followed the advice given him at the time, and acted without any wrongful intent. To now conclude that Mr. Fosse's conduct was in violation of the law because of this Department's failure to issue to him a waiver which we both conclude would have been completely appropriate, surely would elevate form over substance. This is essentially a dispute between your lawyers and mine -- was a 208(b) waiver necessary or was such a waiver obviated by a statutory exemption from section 208 -- and the error, if there was one, was this Department's, not Mr. Fosse's. I hope you will give further consideration to these views before issuance of any report that concludes that Mr. Fosse's actions appear to have violated Federal conflict of interest laws.

**Appendix VI
Comments From the U.S. Department
of Agriculture**

The report also criticizes Mr. Fosse's acceptance, from parties that would appear to be interested parties as that term is defined in the Department's regulations on Employee Responsibilities and Conduct, of reimbursement for expenses of attending two meetings relating to crop insurance. Please be advised that the questions raised by Mr. Fosse's acceptance of those payments are currently being examined and appropriate action will be taken after this review is complete.

Sincerely,



Richard E. Lyng
Secretary

Major Contributors to This Report

**Resources,
Community, and
Economic
Development Division,
Washington, D.C.**

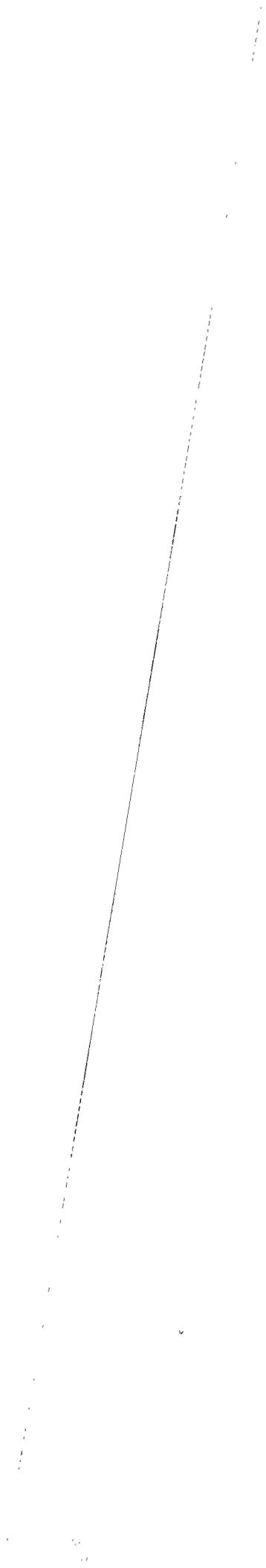
Brian P. Crowley, Senior Associate Director, (202) 275-5138
John W. Harman, Associate Director
Cliff Fowler, Group Director
Richard A. Renzi, Assignment Manager
Earl P. Williams, Jr., Writer/Editor
Julian L. King, Information Processing Assistant
Michelle Y. Perry, Clerk-Typist

**Office of the General
Counsel, Washington,
D.C.**

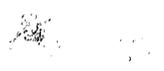
Richard Seldin, Attorney
Leslie L. Wilcox, Attorney

**Washington Regional
Office**

Jennifer M. Thomas, Evaluator-in-Charge
Virginia Beas Proano, Evaluator
John Vocino, Evaluator



4-57



Requests for copies of GAO reports should be sent to:

U.S. General Accounting Office
Post Office Box 6015
Gaithersburg, Maryland 20877

Telephone 202-275-6241

The first five copies of each report are free. Additional copies are \$2.00 each.

There is a 25% discount on orders for 100 or more copies mailed to a single address.

Orders must be prepaid by cash or by check or money order made out to the Superintendent of Documents.

**United States
General Accounting Office
Washington, D.C. 20548**

**Official Business
Penalty for Private Use \$300**

Address Correction Requested

**First-Class Mail
Postage & Fees Paid
GAO
Permit No. G100**