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While a tobacco buyout has been considered for years, support for it among producers has grown considerably as the program has sputtered. As Kelly Tiller of the Agricultural Policy Analysis Center at the University of Tennessee has observed, the very tobacco program that made tobacco a stable and profitable crop was also responsible for its swift decline. In addition to insulating U.S. producers from the vagaries of the global market, the program also greatly limited available responses to the rise of low-cost leaf available from overseas markets. The shift to contract production, coupled with the ongoing legal and financial woes facing the tobacco industry, has contributed to the essential breakdown of the quota system.

How the Buyout Works

The tobacco buyout provision of the Jobs Creation Act pays quota owners to choose to enter into a payment contract valued at $7 per pound of basic quota they owned in 2002. Tobacco growers can enter into a contract for $3 per pound of their 2002 effective quota if they were an active producer in the 2002, 2003, or 2004 marketing year. Growers active in all three years will receive the full $3 per pound buyout. Growers active in one or two of these years will receive payments of $1 per pound or $2 per pound, respectively. For kinds of tobacco with acreage-based quotas, the pound-equivalent is derived from the quota holder or grower's 2002 allotment and the three-year (2001-2003) county average yield for that kind of tobacco for quota holders and the three-year (2001-2003) farm average for growers.

Payments to quota holders and growers are to be evenly divided into 10 annual payments, beginning in 2005. Payments to quota owners are taxable as capital gains; for producers, they are treated as ordinary income. Payments can be paid directly to financial institutions, which allow growers and quota holders to "securitize" their buyout, accepting a lump sum or accelerated payment from a bank in exchange for the full 10 years of payments. These payments are funded entirely through payments made by tobacco manufacturers and importers, with each entity paying in according to their domestic market share. The total cost of the buyout is $10.1 billion over the life of the buyout, most of which is for direct payments to growers and quota holders. Table 1 illustrates the total and annual buyout payments by state for the top six tobacco producing states. A complete listing of tobacco buyout payments by state and type of tobacco is available online at *www.slcatlanta.org/tobacco.htm*.

Total and Annual Buyout Payments by State

	Total Buyout Payments ($ millions)			Annual Buyout Payments ($ millions)		
State	Quota Owner Payments	Grower Payments	Total Buyout Payments	Quota Owner Payments	Grower Payments	Total Buyout Payments
North Carolina	2,752	1,191	3,943	275	119	394
Kentucky	1,736	733	2,469	174	73	247
Tennessee	528	240	768	53	24	77
South Carolina	508	216	725	51	22	73
Virginia	458	208	667	46	21	67
Georgia	429	183	612	43	18	61

table 1

Source: Kelly Tiller and Will Snell, Tobacco Quota Buyout: Summary Information, University of Kentucky and University of Tennessee, October 11, 2004

Because the USDA maintains a pool of tobacco as a component of the program, the buyout provides for an incremental sell-off of existing pool stocks, with a $500 million allowance in the legislation to cover any losses the USDA may incur in the sale of these pool stocks. With the 2005 season, the federal tobacco program will end, and with it, the quantity and geographic restrictions on tobacco production. Beginning with the 2005 season, growers will be able to produce as much tobacco as they wish on any land they wish. Price supports and other components of the safety net also will disappear, as will the Phase II payments made by tobacco companies to growers.

Significantly absent from the buyout legislation is any regulation of tobacco by the Food and Drug Administration (FDA). FDA regulation had been a component of several buyout proposals over the years, and was debated with the current legislation, but was dropped during the negotiations of the Congressional Conference Committee.

Impact of the Buyout

The tobacco buyout is significant for Southern states for several reasons. Tobacco is a keystone agricultural crop in a limited part of the region, but where it is a dominant crop, it