United States Government Accountability Office

GAO

Report to Congressional Requesters

June 2011

INTERNATIONAL FOOD ASSISTANCE

Funding Development Projects through the Purchase, Shipment, and Sale of U.S. Commodities Is Inefficient and Can Cause Adverse Market Impacts

Accountability * Integrity * Reliability

GAO-11-636

June 2011

INTERNATIONAL FOOD ASSISTANCE

Funding Development Projects through the Purchase, Shipment, and Sale of U.S. Commodities Is Inefficient and Can Cause Adverse Market Impacts

GAO Highlights

Accountability • Integrity • Reliability

Highlights of GAO-11-636, a report to congressional requesters

Why GAO Did This Study

Since the Food Security Act of 1985, Congress has authorized monetization—the sale of U.S. food aid commodities in developing countries to fund development. In fiscal year 2010, more than $300 million was used to procure and ship 540,000 metric tons of commodities to be monetized by the U.S. Agency for International Development and the U.S. Department of Agriculture. Through analysis of agency data, interviews with agency officials, and fieldwork in three countries, this report (1) assesses the extent to which monetization proceeds cover commodity and other associated costs and (2) examines the extent to which U.S. agencies meet requirements to ensure that monetization does not cause adverse market impacts.

What GAO Recommends

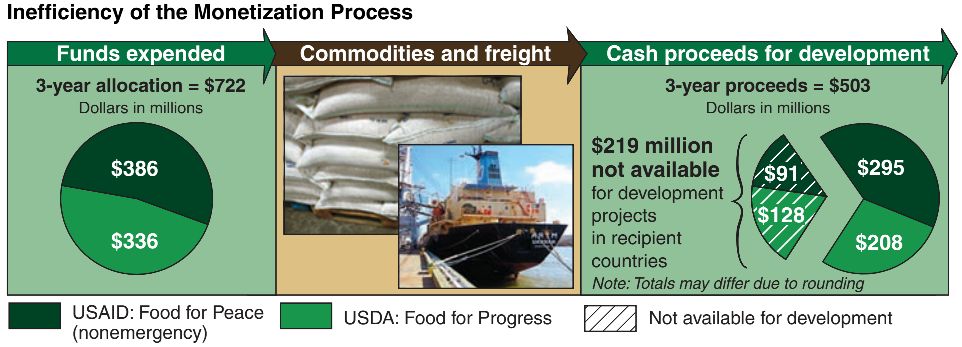
GAO recommends that Congress consider eliminating the 3-year waiting period for foreign vessels that acquire U.S.-flag registry to be eligible to transport U.S. food aid. Further, the USAID Administrator and the Secretary of Agriculture should develop a benchmark for "reasonable market price" for food aid sales; monitor these sales; improve market assessments and coordinate efforts; and conduct post-market impact evaluations. USAID and USDA generally agreed with our recommendations. DOT disagreed with our Matter for Congressional Consideration due to its concern that the proposed statutory change might be detrimental to the U.S. maritime industry.

View GAO-11-636 or key components.
For more information, contact Thomas Melito at (202) 512-9601 or melitot@gao.gov.

What GAO Found

GAO found that the inefficiency of the monetization process reduced funding available to the U.S. government for development projects by $219 million over a 3-year period (see figure below). The process of using cash to procure, ship, and sell commodities resulted in $503 million available for development projects out of the $722 million expended. The U.S. Agency for International Development (USAID) and the U.S. Department of Agriculture (USDA) are not required to achieve a specific level of cost recovery for monetization transactions. Instead, they are only required to achieve reasonable market price, which has not been clearly defined. USAID's average cost recovery was 76 percent, while USDA's was 58 percent. Further, the agencies conduct limited monitoring of sale prices, which may hinder their efforts to maximize cost recovery. Ocean transportation represents about a third of the cost to procure and ship commodities for monetization, and legal requirements to ship 75 percent of the commodities on U.S.-flag vessels further increase costs. Moreover, the number of participating U.S.-flag vessels has declined by 50 percent since 2002, and according to USAID and USDA, this decline has greatly decreased competition. Participation may be limited by rules unique to food aid programs which require formerly foreign-flag vessels to wait 3 years before they are treated as U.S.-flag vessels.

Inefficiency of the Monetization Process



Sources: GAO based on selected transactions from data provided by USAID and USDA.

USAID and USDA cannot ensure that monetization does not cause adverse market impacts because they monetize at high volumes, conduct weak market assessments, and do not conduct post-monetization evaluations. Adverse market impacts may include discouraging food production by local farmers, which could undermine development goals. To help avoid adverse market impacts, the agencies conduct market assessments that recommend limits on programmable volume of commodities to be monetized. However, USAID's assessments were conducted for just a subset of countries and have not yet been updated to reflect changing market conditions, and USDA's assessments contained weaknesses such as errors in formulas. Both agencies have at times programmed for monetization at volumes in excess of limits recommended by their market assessments. Further, the agencies monetized more than 25 percent of the recipient countries' commercial import volume in more than a quarter of cases, increasing the risk of displacing commercial trade. Finally, the agencies do not conduct post-monetization impact evaluations, so they cannot determine whether monetization caused any adverse market impacts.

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Abbreviations List

BEST	Bellmon Estimation for Title II
CCC	Commodity Credit Corporation
IPP	import price parity
ITSH	inland transportation, shipping, and handling
KCCO	Kansas City Commodity Office
NGO	nongovernmental organization
UMR	Usual Marketing Requirement
USAID	U.S. Agency for International Development
USDA	U.S. Department of Agriculture

GAO Accountability * Integrity * Reliability

United States Government Accountability Office
Washington, DC 20548

June 23, 2011

Congressional Requesters

The United States provided nearly $2.3 billion to alleviate world hunger and support development in 2010.[1] This amount accounted for more than half of all global food aid supplies, making the United States the single largest donor of food aid. For almost 30 years, since the enactment of the Food Security Act of 1985,[2] Congress has authorized the sale of U.S. food aid commodities in local and regional markets in developing countries with the proceeds used to fund development activities that address causes and symptoms of food insecurity—a practice known as monetization. In 2010, more than $300 million was used to procure and ship 540,000 metric tons of food assistance to be monetized. To adhere to cargo preference requirements,[3] 75 percent of all U.S. food aid commodities must be shipped on U.S.-flag vessels. According to U.S. agencies, nonemergency[4] food aid resources, including proceeds from monetization, supported development and direct assistance projects that benefited more than 7 million people in 35 developing countries. These development projects include assistance to improve agricultural production, provide health and nutrition activities, and support education and humanitarian needs.

However, the practice of monetizing food aid has long been controversial. Advocates view monetization as a tool to meet the development needs of chronically food-insecure people in many developing countries. Critics view the practice of converting cash to commodities and then back to cash as an inefficient use of resources that may also have adverse market impacts in recipient countries. These market impacts may include displacing commercial trade and discouraging local food production. By

[1]The majority of U.S. food assistance—about two-thirds—represents emergency food aid to respond to immediate food needs created by man-made or natural disasters, with nonemergency food aid representing the remainder.

[2]Pub. L. No. 99-198, Sec. 1111.

[3]In 1985, the Merchant Marine Act of 1936 (Pub. L. No. 83-664) was amended to require that 75 percent of certain foreign food aid be shipped on privately owned U.S.-flag vessels. See 46 U.S.C. 55314.

[4]Nonemergency food aid programs, also known as multi-year development programs, are approved to operate for 3 to 5 years and target chronically food-insecure populations. These nonemergency programs include monetization and/or direct distribution of food aid.

law,[5] the two principal agencies that manage U.S. food assistance—the U.S. Agency for International Development's (USAID) Office of Food for Peace[6] and the U.S. Department of Agriculture's (USDA) Foreign Agricultural Service—must ensure that monetization transactions do not entail substantial disincentive to, or interfere with, domestic production or marketing in that country.

While we recognize the benefits of the development activities that monetization funds, in 2007, we reported that monetization was an inherently inefficient use of food aid.[7] The inefficiencies stem from the process of using U.S. government funds to procure food aid commodities in the United States which are then shipped to the recipient country and sold, with the proceeds used to fund development projects. In that report, we identified various costs associated with the transporting, handling, and selling of commodities that contributed to these inefficiencies.[8] Because U.S. agencies did not collect monetization proceeds data electronically at the time of our review, we found it difficult to assess the extent to which monetization revenues covered the commodity and other costs associated with the practice. We recommended that USAID and USDA develop an information collection system to track monetization transactions, which the agencies have begun to implement.

[5] In 1977, Congress passed the Bellmon Amendment to the Food for Peace Act. The amendment requires that before agencies supply food aid, they must determine (1) that adequate storage facilities are available in the recipient country at the time of exportation of the commodity to prevent spoilage and waste of the commodity and (2) that the distribution of the commodities in the recipient country will not result in a substantial disincentive to, or interference with, domestic production or marketing.

[6] USAID administers Title II programs of the Food for Peace Act, formerly titled The Trade Development and Assistance Act of 1954 and commonly referred to as Pub. L. No. 480. For the purposes of this report, we use the term "Food for Peace" to refer to USAID's food aid activities under Title II. Food for Peace activities include the direct donation of U.S.-grown agricultural commodities for emergency relief and development.

[7] GAO, *Foreign Assistance: Various Challenges Impede the Efficiency and Effectiveness of U.S. Food Aid*, GAO-07-560 (Washington, D.C.: Apr. 13, 2007).

[8] In 2002, the Office of Management and Budget (OMB) recommended decreasing monetization, indicating that the practice can impede U.S. commercial exports, lower market prices, induce black market activity, and thwart market development for U.S. farm products. OMB also raised questions about the economic efficiency of the practice. That same year, the President's Management Agenda suggested that directly feeding the hungry, rather than providing food for development, should be the primary goal of U.S. food aid programs. See GAO-07-560.

In this report, we examine issues related to cost recovery and market impact assessment for monetization. At your request, as part of our work on international food assistance,[9] we (1) assessed the extent to which monetization proceeds cover commodity and other associated costs and (2) examined the extent to which U.S. agencies meet requirements to ensure that monetization does not cause adverse market impacts.

To address these objectives, we analyzed food aid program data provided by USAID, USDA, and USDA's Kansas City Commodity Office (KCCO). USAID has not been collecting monetization cost recovery information systematically and thus could not provide us with comprehensive and reliable data for transactions prior to 2008. Therefore, for the purposes of this report, the agencies generated cost recovery data manually, covering fiscal years 2008 through 2010 for USAID, and fiscal years 2007 through 2009 for USDA.[10] We worked with the agencies to correct errors in the data and determined that the data used in our analysis were sufficiently reliable for our purposes. Further, we examined the differences between U.S.-and foreign-flag ocean freight rates using KCCO data. We also reviewed and analyzed data from the agencies, such as their market assessments, volumes programmed for monetization, import data, consumption data, and the limits set by the agencies for monetization in recipient countries for fiscal years 2008 through 2010. We also interviewed officials from USAID; USDA; the Departments of State and Transportation; and the Office of Management and Budget in Washington, D.C., as well as subject-matter experts in the field of international food aid. In addition, we conducted a survey of the 29 implementing partners who conducted monetization between fiscal years 2008 and 2010 and received a 100

[9]GAO, *International Food Assistance: Better Nutrition and Quality Control Can Further Improve U.S. Food Aid*, GAO-11-491 (Washington, D.C.: May 12, 2011); and GAO, *International School Feeding: USDA's Oversight of the McGovern-Dole Food for Education Program Needs Improvement*, GAO-11-544 (Washington, D.C.: May 19, 2011).

[10]Since some of the records we received from the agencies contained incomplete information, we reported only on those transactions that had sufficient information to calculate cost recovery. For USAID, we were able to use 189 of the 194 monetization transactions the agency reported between fiscal years 2008 and 2010 (99 percent). For USDA, we were able to use 61 of the 66 monetization transactions the agency reported between fiscal years 2007 and 2009 (92 percent). We did not include USDA monetization transactions for fiscal year 2010 because the sales proceeds data provided by the agency for that year were recorded as estimates, not as actual sales data like the other transactions we used in our calculation. In its technical comments, USDA stated that it provided estimated data in situations where implementing partners had not yet called forward for 2010 agreements, or had not yet reached the semiannual reporting deadline, and therefore actual data were unavailable.

percent response rate. We also conducted field work in countries that programmed some of the highest volumes of monetized nonemergency U.S. food aid from fiscal years 2008 through 2010—Bangladesh, Mozambique, and Uganda—and met with officials from U.S. missions, representatives from nongovernmental organizations (NGO) and other implementing partners that directly handle sales and implement development activities, and officials from relevant host government agencies. (Appendix I provides a detailed discussion of our objectives, scope, and methodology. In addition, appendix II provides technical notes on our analysis of ocean freight rates.)

We conducted this performance audit from July 2010 to June 2011 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 objectives. We believe the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Based on our findings in this report, we are proposing that, consistent with rules that apply to the Maritime Security Fleet and vessels transporting other U.S. government cargo, Congress should consider amending the Cargo Preference Act of 1954 to eliminate the 3-year waiting period imposed on foreign vessels that acquire U.S.-flag registry before they are eligible for carriage of preference food aid cargos. This could potentially increase the number of U.S.-flag vessels eligible for carriage of preference food aid cargo, thereby increasing competition and possibly reducing costs. The Department of Transportation (DOT) disagreed with our Matter for Congressional Consideration due to its concern regarding the potentially detrimental impact the statutory change may have on the U.S. maritime industry. However, we maintain that the elimination of the 3-year waiting period can ease entry of new vessels into U.S. food aid programs. We are suggesting this proposed amendment on the basis of factors including the following: First, as USAID and USDA jointly reported in 2009, the number of vessels participating in U.S. food aid programs has declined, thereby limiting competition in transportation contracting and leading to higher freight rates. Second, our analysis shows that food aid shipments on foreign-flag carriers cost the U.S. government, on average, $25 per ton less than U.S.-flag carriers.

Further, we are recommending that the Administrator of USAID and the Secretary of Agriculture (1) jointly develop an agreed-upon benchmark or indicator to determine “reasonable market price” for sales of U.S. food aid for monetization; (2) monitor food aid sales transactions to ensure that the benchmark set to achieve "reasonable market price" in the country where the commodities are being sold is achieved, as required by law; (3) improve market assessments and coordinate to develop them in countries where both USAID and USDA may monetize; and (4) conduct market impact evaluations after monetization transactions have taken place to determine whether they caused adverse market impacts. Both USAID and USDA generally concurred with our recommendations and noted ongoing efforts and plans to address them.

Background

The Practice of Monetization Has Evolved over Time, and Agencies Are Currently Required to Achieve Reasonable Market Price in Monetization Transactions

The authority to monetize food aid was established by the Food Security Act of 1985. The act allowed implementing partners that received nonemergency food aid under USAID's Food for Peace program and USDA's Food for Progress program to monetize some of the food in recipient countries and use the proceeds to cover associated shipping costs. In 1988, the authorized use of monetization funds was expanded to incorporate funding of food-security-related development projects, and in 1995, a minimum monetization level for nonemergency food assistance was set at 10 percent, which was then increased to 15 percent in 1996. The 2002 Farm Bill authorized the McGovern–Dole International Food for Education and Child Nutrition Program and allowed it to raise cash through monetization. (For a description of these program authorities, see appendix III).

The practice of selling commodities for cash to fund development programs originated in part from U.S. government farm subsidies that contributed to a surplus of agricultural commodities owned by the U.S. government. However, the U.S. government no longer has surplus agricultural commodities. Current monetization requires the U.S. government to purchase the commodities from the commercial market and ship them abroad for implementing partners to sell them in another market to generate cash.

Neither USAID nor USDA has been required to achieve a set level of cost recovery following an amendment by the 2002 Farm Bill to the Food for Peace Act. Rather, the agencies are required, by statute, to achieve "reasonable market price" for sales of food aid in recipient countries. Prior to 2002, USAID sought to achieve an average cost recovery that was calculated based on the following formula: either (1) 80 percent of commodity value plus freight value, including associated transport and marketing costs, or (2) 100 percent of free alongside ship[11] price on its monetization transactions. USDA's requirement was to adhere to reasonable market price as its benchmark. According to the conference report for the 2002 Farm Bill,[12] the change from the cost recovery formula to reasonable market price for USAID was made to address two primary concerns. The first concern was that the cost recovery formula requirement was too inflexible, and could either unfairly punish participants where market forces were beyond their control, or not reward situations where the market price was above the formula value. The second concern was that, since both USAID and USDA monetize food aid, sometimes in potentially overlapping markets, having a cost recovery requirement for USAID but not for USDA could cause inconsistencies in monetization and potentially penalizes one or the other agency. The change to a single requirement of reasonable market price for both agencies was intended to establish similar results in determining sales prices.

[11]According to DOT, free alongside ship is a term of sale for which the seller is responsible for delivering the goods to be placed alongside the vessel, and the buyer has to bear all costs and risks of loss of or damage to the goods from that point on.

[12]H. Rept. 107-424.

USAID and USDA Together Monetize More than Half of All Nonemergency Food Aid, Primarily in a Few Countries

In fiscal year 2010, the United States spent about $2.3[13] billion to provide a total of 2.5 million metric tons of food aid commodities to food-insecure countries. Of that amount, almost $800 million was spent on providing USAID and USDA 890,000 metric tons of nonemergency food aid (see fig. 1).[14] This assistance is provided through both monetization and direct distribution, where commodities are provided directly to beneficiaries through implementing partners. While U.S. food aid legislation mandates that a minimum of 15 percent of USAID's Food for Peace nonemergency assistance be monetized, actual levels of monetization far exceed the minimum. In fiscal year 2010, more than 313,000 metric tons of food aid were monetized under USAID's Food for Peace program, accounting for 63 percent of food aid tonnage under that program. In fiscal year 2010, USDA monetized more than 229,000 metric tons of food aid under the Food for Progress program, accounting for 95 percent of food aid tonnage under that program. Monetization has been less prevalent under the McGovern-Dole International Food for Education and Child Nutrition Program since the end of its pilot program in 2003, due to an increase in the amount of cash provided along with food aid for direct distribution. In fiscal year 2010, the McGovern-Dole International Food for Education and Child Nutrition Program did not monetize any food aid shipments.

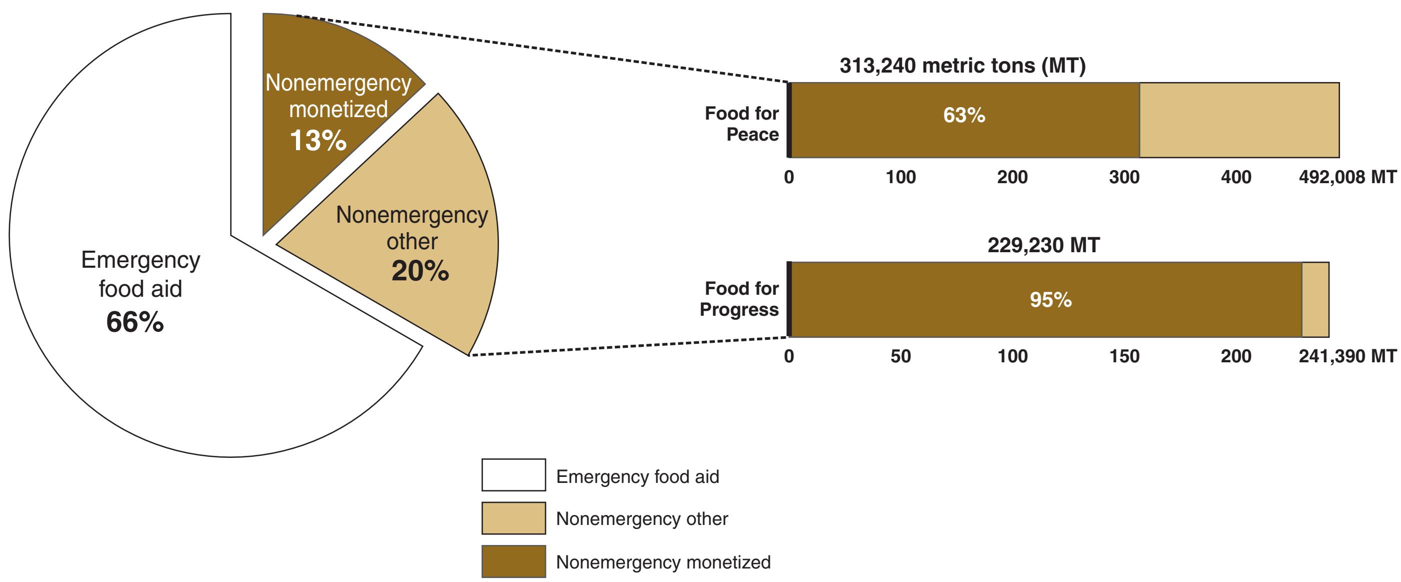
Feed the Future Community Development Fund

Under a new strategy to address global hunger called the Feed the Future initiative, the administration sought the establishment of a Community Development Fund (CDF) to decrease U.S. government reliance on the monetization of food aid to fund development activities. The CDF fund was designed to expand efforts to narrow the gap between humanitarian and development assistance in areas that support food security. However, the mechanisms to use the fund to replace monetization were not included in the law, and the CDF therefore cannot be used to decrease current levels of monetization. According to a USAID official, the agency will continue to work with Congress on future budgets so that appropriate mechanisms to decrease reliance on monetization are incorporated in the law. A $75 million request to fund the CDF was included in the fiscal year 2011 Foreign Operations Budget. While Congress has appropriated funds for the CDF, the final appropriation has not been made public.

[13]All costs represent commodities, freight, and distribution.

[14]The 2008 Farm Bill, Pub. L. No. 110-246, required a minimum level of nonemergency food assistance under Title II—known as the "safe box"—of no less than $375 million in fiscal year 2009. This minimum level goes up to $450 million in fiscal year 2012 and up to $450 million in fiscal year 2012.

Figure 1: Percentage of Funding for Emergency and Nonemergency Food Aid and for Monetization, Fiscal Year 2010



Sources: GAO analysis of USDA and USAID data.

Notes:

1. The total for funding does not add up to 100 percent due to rounding.

2. The totals for emergency and Food for Peace nonemergency include costs for procurement and shipping and do not include administrative or other associated costs. However, the Food for Progress nonemergency total includes administrative or other associated costs because USDA was unable to provide us with this calculation. In fiscal year 2009, these costs constituted 1.43 percent of Food for Progress' total monetization costs.

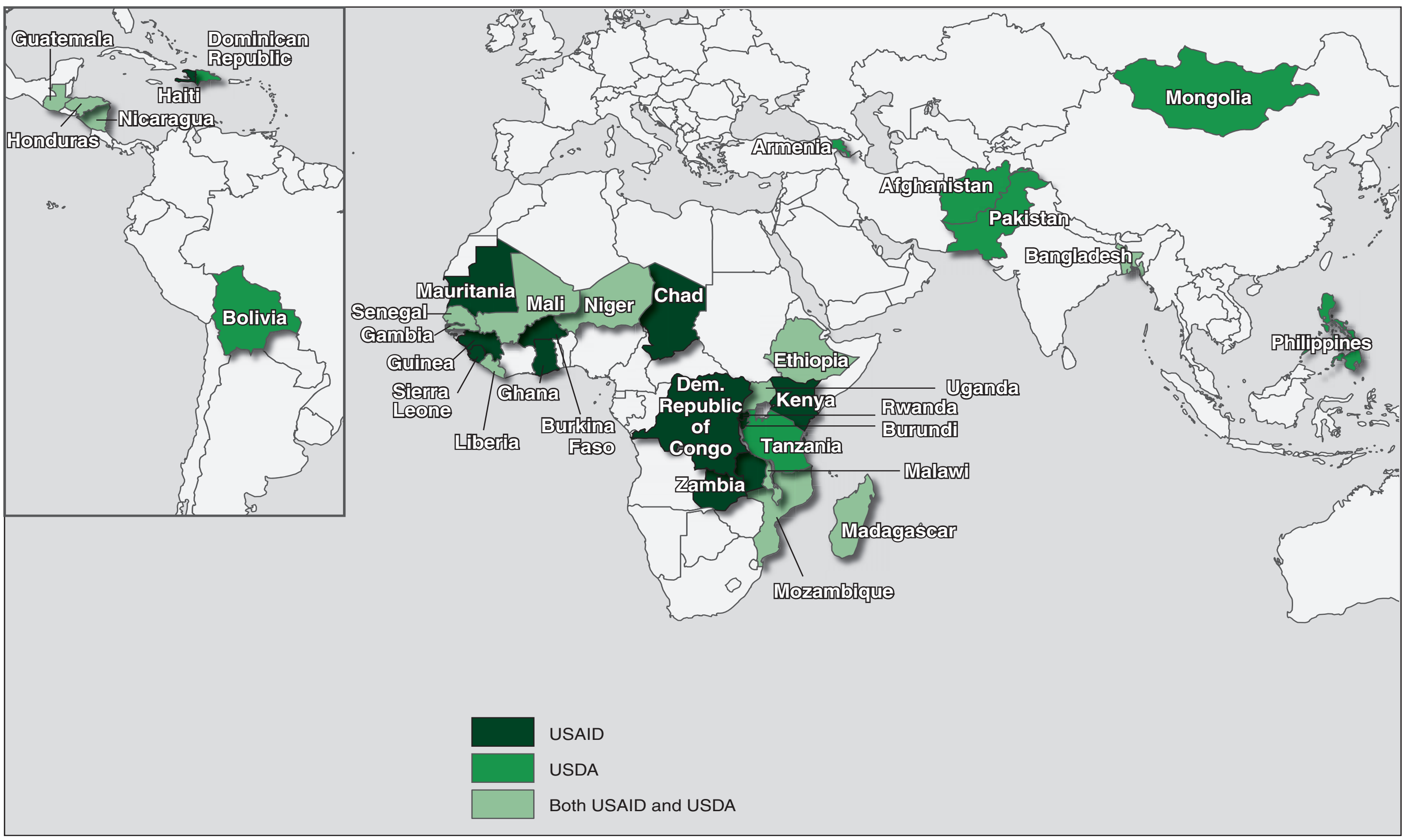
3. The McGovern-Dole International Food for Education and Child Nutrition Program is included in the nonemergency total, but the program did not monetize in 2010.

According to KCCO data, between fiscal years 2008 and 2010, more than 1.3 million metric tons of food aid were programmed for monetization[15] in 34 countries (see fig. 2). The countries in which the largest volumes of commodities were programmed to be monetized during that time period are Bangladesh (220,590 metric tons), Mozambique (202,200 metric tons), Haiti (100,000 metric tons), and Uganda (88,400 metric tons). Together, these four countries accounted for 45 percent of all food aid programmed to be monetized. During that same time period, wheat was the commodity

[15] We define the term "programmed" as the total volume for a given commodity that was approved in a given fiscal year to be monetized, even though the actual shipments of the commodity may occur in subsequent years.

most often programmed for monetization, accounting for about 77 percent of all monetization. Other commodities programmed to be monetized during the same period include soy bean meal, milled rice, vegetable oil, and crude soybean oil. (For a complete list of commodities and volumes programmed to be monetized by country, see appendix IV.)

Figure 2: Countries that Received Monetized Food Aid, Fiscal Years 2008 through 2010



Sources: GAO; Map Resources (map).

Monetization Is a Complex Process that Involves Multiple Entities

Monetization is conducted by implementing partners, usually NGOs that receive grants[16] from USAID or USDA to monetize agreed-upon commodities in certain countries.[17] Monetization grants generally provide development resources over a 3- to 5-year period.[18] The process begins with a call for applications from either USAID or USDA, to which implementing partners respond by submitting grant proposals for development programs that are to be funded in part with monetization proceeds. USAID and USDA independently issue calls for applications and approve applications at different times, based on different guidelines and priorities. Grant proposals include, among other things, information on the commodity to be monetized, commodity volumes requested, estimated sales price, estimated cost recovery, considerations of market impact assessments, and projects that will be funded based on the estimated sales proceeds. Implementing partners that receive grants have the responsibility to manage and oversee the monetization process. As part of their responsibilities, implementing partners must secure a buyer in the recipient country before a call forward (or purchase order) can be approved by the relevant agency. After either USAID or USDA receives a call forward request from the implementing partner in their Web Based Supply Chain Management (WBSCM) system, the agency approves or disapproves the request, which is then routed to KCCO. KCCO purchases the requested commodities from U.S. producers in the United States and ships them to the implementing partner in the recipient country. To adhere to cargo trade preference requirements, DOT assists in identifying qualified ocean carriers to ship the commodities to the recipient country. The commodities are delivered to the implementing partner in the recipient country, where the implementing partner executes the sales contract with the buyer and collects payment. The implementing partner uses the proceeds to implement the development projects. Figure 3

[16]Monetization occurs in agreements structured as grants, rather than contracts. A federal grant is defined as "an award of financial assistance from a federal agency to a recipient to carry out a public purpose of support or stimulation authorized by a law of the United States." See http://www.grants.gov/aboutgrants/grants.jsp (last accessed June 21, 2011).

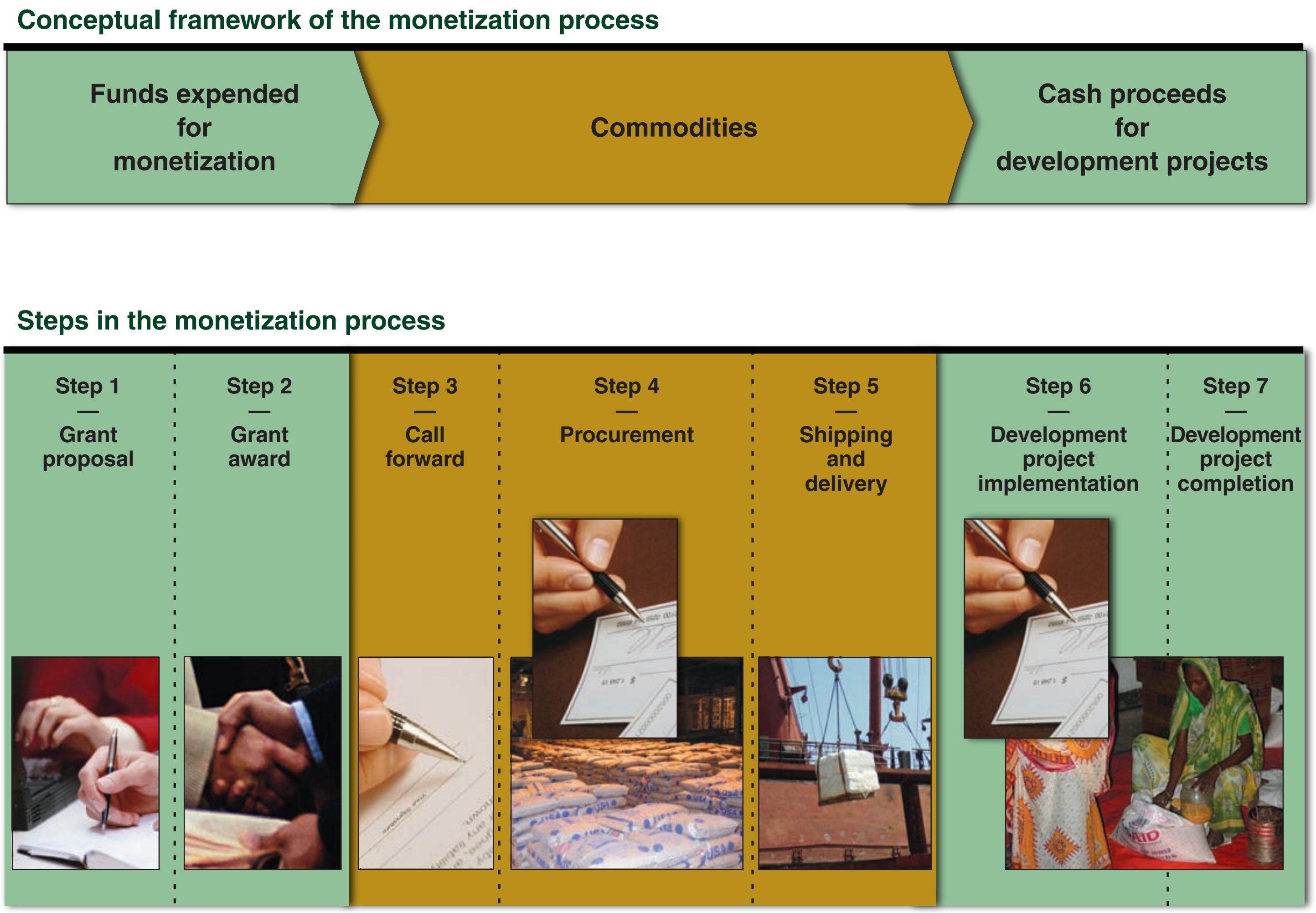
[17]Qualified entities for USAID's Food for Peace programs include NGOs and intergovernmental organizations (such as the World Food Program). Qualified entities for USDA's Food for Progress program may be foreign governments or private entities including non-profit organizations based in the United States but operating programs overseas.

[18]USAID has traditionally called these Multi-Year Assistance Programs (MYAP). However, USAID now refers to them officially as development programs. USDA also typically refers to these grants as Food for Progress agreements.

depicts the general steps in the monetization process, from submitting a grant proposal to obtaining proceeds to completing development projects. (See appendix V for more information). According to an implementing partner we interviewed, the monetization process consists of nearly 50 substeps, including steps to complete the application, conduct market assessments, coordinate requests and shipment, identify buyers and obtain bids, deliver commodities, and collect payments.[19]

[19]For a description of the food aid supply chain, including an interactive graphic and videos of the transportation and logistics process, see GAO-11-491.

Figure 3: Steps in the Monetization Process, from Grant Proposal to Development Project Completion



Sources: GAO analysis of information provided by USAID, USDA, and Implementing partners; GAO and PhotoDisc (photos)

Multimedia Instructions	For more information about the monetization process: • in Web version, hover your mouse over each step • in print version, see Appendix V.

Implementing Partners Can Monetize Food Aid in Various Ways

While implementing partners are not required to follow a particular process to conduct food aid sales for monetization, the two most common approaches reported by implementing partners are the following:

- *Several implementing partners might form a consortium in which one of the partners serves as the selling agent.* Consortiums are often formed when several implementing partners obtain grants for the same country to monetize the same commodity. Generally, one of the implementing partners in the consortium takes the lead in conducting monetization sales. The lead implementing partner is responsible for identifying the buyers; preparing a single call forward drawing from each partner's food allocation; arranging for commodities to be shipped in a single shipment; finalizing the sale in-country; and distributing proceeds among participating consortium members, as appropriate. Typically, the lead implementing partner charges a fee of 3 to 5 percent of total sales to handle monetization, while in some cases, the lead is rotated among consortium members. Fifteen of the 29 implementing partners we interviewed reported being part of a monetization consortium.

- *A single implementing partner might independently sell the commodities granted to it.* When a single implementing partner monetizes only its own commodities, it must hire or train staff to conduct the sales or contract a selling agent to sell the food. Selling agents that we interviewed generally charge a fee of 3 to 5 percent of monetization sales. Fourteen of the 29 implementing partners we interviewed said that they monetize only the food granted to their organization.

Implementing partners generally sell commodities to private buyers in the recipient countries in the open market. Sales are generally conducted through a public tender process organized by the implementing partner or its selling agent, where an open bidding will take place. This is the preferred method for both USAID and USDA, on the assumption that a public tender process will most likely produce a competitive sales price. In some cases, however, implementing partners sell commodities through direct negotiation, where the implementing partners or their agents enter into a one-on-one dialogue with individual buyers. According to USDA officials, monetization sales through direct negotiation are only permitted when the public tender process is not feasible or does not initially result in a sale.

In some cases, implementing partners work with the recipient country's national government to conduct monetization. For example, an implementing partner may enter into direct negotiation with the government, as in the case of Bangladesh, where the government is the buyer and purchases all USAID Food for Peace nonemergency food aid that is monetized in the country. In Haiti, the government requires that monetization transactions to private buyers be facilitated through a government entity called the Monetization Bureau. According to an implementing partner, the bureau must approve each transaction and charges a monetization fee of 2 to 5 percent.

Monetization Funds Are Used for a Broad Range of Development Projects

Development projects funded through monetization are expected to address food insecurity in recipient countries. According to USAID guidance, goals of nonemergency food aid programming are to reduce risks and vulnerabilities to food insecurity and increase food availability, access, utilization, and consumption. Within this framework, monetization is built around two main objectives—to enhance food security and generate foreign currency to support development activities. Therefore, the range of activities that USAID funds through monetization includes projects to improve and promote sustainable agricultural production and marketing; natural resource management; nonagricultural income generation; health, nutrition, water and sanitation; education; emergency preparedness and mitigation; vulnerable group feeding; and social safety nets. According to USDA guidance, commodities for monetization are made for use in developing countries and emerging democracies that have made commitments to introduce or expand free enterprise elements in their agricultural economies. Within these constraints, USDA gives priority consideration to proposals for countries that have economic and social indicators that demonstrate the need for assistance. These indicators include income level, prevalence of child stunting, political freedom, USDA overseas coverage, and other considerations such as market conditions. Therefore, according to USDA, development projects funded through monetization by the agency's Food for Progress program should focus on private sector development of agricultural sectors such as improved agricultural techniques, marketing systems, and farmer education. Figure 4 provides examples of USAID and USDA projects funded through monetization in countries that we visited.

Figure 4: Examples of Development Projects Funded through Food for Peace and Food for Progress Grants that Include Monetization

Activity	Grant information	Objectives	Examples
Agriculture development 	In 2006, USAID awarded ACDI/VOCA a 5-year, $74 million Food for Peace grant in Uganda–the largest award in ACDI/VOCA's history	ACDI/VOCA is working to improve food production and use for approximately 139,000 smallholder farmer beneficiaries throughout the life of the project	• Provide technical assistance and training in agronomic methods, post-harvest handling, group savings, and management • By the end of fiscal year 2010, approximately 66,724 farmers had received technical trainings to increase their food security and resilience to future shocks • During the same time period, farmer groups had accumulated approximately $80,000 in group savings
Microfinancing 	In 2009, USDA awarded FINCA a 3-year, $4.58 million Food for Progress grant in Uganda	FINCA program objectives included providing a national microfinance program, developing a specialty agricultural loan program, conducting social and economic client investments, and providing agricultural development subgrants	• As of December 2010 more than $1 million in microloans provided to 5,912 clients • $250,000 in specialty agricultural loans budgeted for 150 farmers • Two subgrants budgeted for NGOs to train farmers
Education and health 	In 2008, USDA provided Planet Aid a 3-year, $20 million Food for Progress grant in Mozambique	Planet Aid's program objectives include providing food and assistance for people with HIV/AIDS, including AIDS orphans; increasing the number of teachers in rural areas; training farmers; and developing infrastructure necessary to provide training for teachers	• Established seven programs providing 700,000 people with HIV/AIDS education and counseling • Through 50 existing soy canteen programs, served 500,000 nutritious meals to recipients, including people with HIV/AIDS, AIDS orphans, and community volunteers • Trained 900 teachers through a 2.5-year primary school teacher-training program • Support the completion and equipment of One World University
Community development 	In 2010, USAID awarded CARE a $120 million, 5-year Food for Peace grant in Bangladesh	CARE will use funds to sponsor the Shouhardo II program, which has the goal of reducing vulnerability to food insecurity in 370,000 poor and extremely poor households	• The program will provide access to and utilization of nutritious and enhanced foods • Empower women in poor and extremely poor households to be actively engaged in initiatives to reduce food insecurity • Work with community members, government institutions, and NGOs to reduce food insecurity and to be better prepared to respond to disasters.

Sources: USAID, USDA, and NGO program documents; GAO (photos).

Funding Generated for Development Projects through Monetization Is Less than Originally Expended, and Various Factors Adversely Affect Cost Recovery

Proceeds generated through monetization to fund development projects are less than what the U.S. government expends to procure and ship the commodities that are monetized. USAID and USDA are not required to achieve a specific level of cost recovery for their monetization transactions. Instead, they are only required to achieve reasonable market price, which has not been clearly defined. More than one-third of the monetization transactions we examined fell short of import parity price, a quantifiable measure of reasonable market price. Various factors can adversely impact cost recovery. For instance, ocean transportation constitutes a substantial cost to the U.S. government, and cargo preference requirements raise this cost even further. Furthermore, USAID and USDA conduct only limited monitoring of the sales prices, though monitoring is necessary to ensure that the implementing partners generate as much funding as possible for their development projects. The agencies' monitoring efforts are further hindered by deficiencies in their reporting and information management systems. Finally, implementing partners face increased risk and uncertainty in their project budgets due to long lag times throughout the approval and sales process.

Funding Generated for Development Projects through Monetization Was Less than Originally Expended

Proceeds generated to fund development projects through monetization were less than what the U.S. government expended to procure and ship the monetized commodities. Cost recovery, the ratio between the proceeds the implementing partners generate through monetization and the cost the U.S. government incurs to procure and ship the commodities to recipient countries for monetization, is an important measure to assess the efficiency of the monetization process in generating development funding. Table 1 shows USAID's and USDA's average cost recovery, from fiscal years 2008 through 2010 and fiscal years 2007 through 2009, respectively, as well as their lowest and highest cost recovery transactions.[20] The table also shows the difference, in dollars, between the proceeds from monetization sales to fund development projects, and the

[20]We calculated cost recovery over a 3-year period for each agency. USAID's data cover fiscal years 2008 through 2010 and USDA's data cover fiscal years 2007 through 2009. USDA provided us with estimated sales prices for all but one fiscal year 2010 monetization transaction. We did not include USDA monetization transactions for fiscal year 2010 because the sales proceeds data provided by the agency for that year were recorded as estimates, not as actual sales data like the other transactions we used in our calculation. In its technical comments, USDA stated that it provided estimated data in situations where implementing partners had not yet called forward for fiscal year 2010 agreements, or had not yet reached the semiannual reporting deadline, and therefore actual data were unavailable.

cost to the U.S. government to procure and ship the commodities. (For a detailed discussion of our methodology for calculating cost recovery, see appendix I).

Table 1: Summary of USAID and USDA Cost Recovery on Selected Monetization Transactions

	USAID (fiscal years 2008 through 2010)	USDA (fiscal years 2007 through 2009)
Average cost recovery	76%[a]	58%[a]
Lowest cost recovery recorded	34%	25%
Highest cost recovery recorded	165%	88%
Reported difference between proceeds, generated through monetization, to fund development projects and the cost the U.S. government incurred to procure and ship commodities to recipient countries for monetization	-$91 million	-$128 million
	Combined reported difference for USAID and USDA equals -$219 million	

Sources: GAO analysis of USAID and USDA data.

Notes:

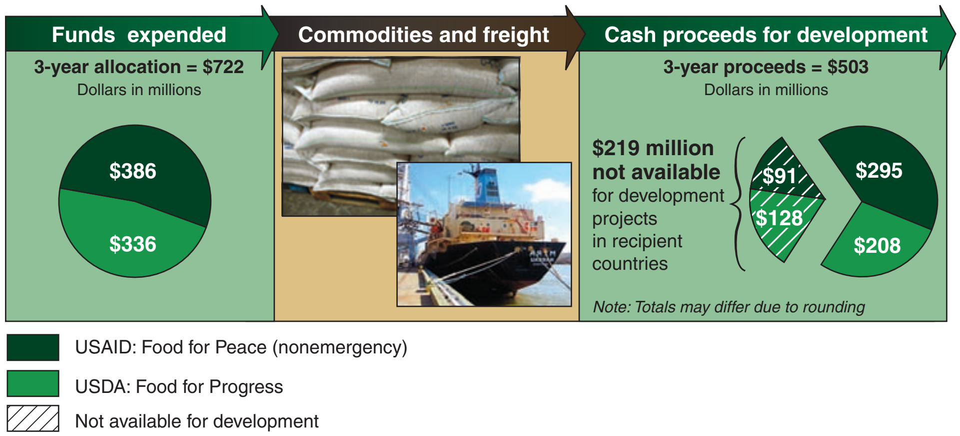
1. Cost recovery is the ratio between the proceeds the implementing partners generate through monetization and the cost the U.S. government incurs to procure and ship the commodities to recipient countries for monetization. The higher the ratio, the more cash is generated to fund development projects.

2. Since some of the records we received from the agencies contained incomplete information, we reported only on those transactions that had sufficient information to calculate cost recovery. For USAID, we were able to use 189 of the 194 monetization transactions the agency reported between fiscal years 2008 and 2010 (99 percent). For USDA, we were able to use 61 of the 66 monetization transactions the agency reported between fiscal years 2007 and 2009 (92 percent).

[a]The average cost recovery reported is a weighted average, which we calculated by dividing the total sales proceeds by the total commodity procurement and shipping cost.

We found that between fiscal years 2008 and 2010, USAID achieved an average cost recovery of 76 percent, or about $91 million less in proceeds than what the U.S. government spent on procuring and shipping commodities, over these 3 years. USDA achieved an average cost recovery of 58 percent, or about $128 million less than what was expended between fiscal years 2007 and 2009. Therefore, a combined total of $219 million of appropriated funds was ultimately not available for development projects. Figure 5 shows funds being used for procuring and shipping commodities, with the commodities then being sold for cash, and the difference between the final proceeds and the original expended amounts, for both USAID and USDA.

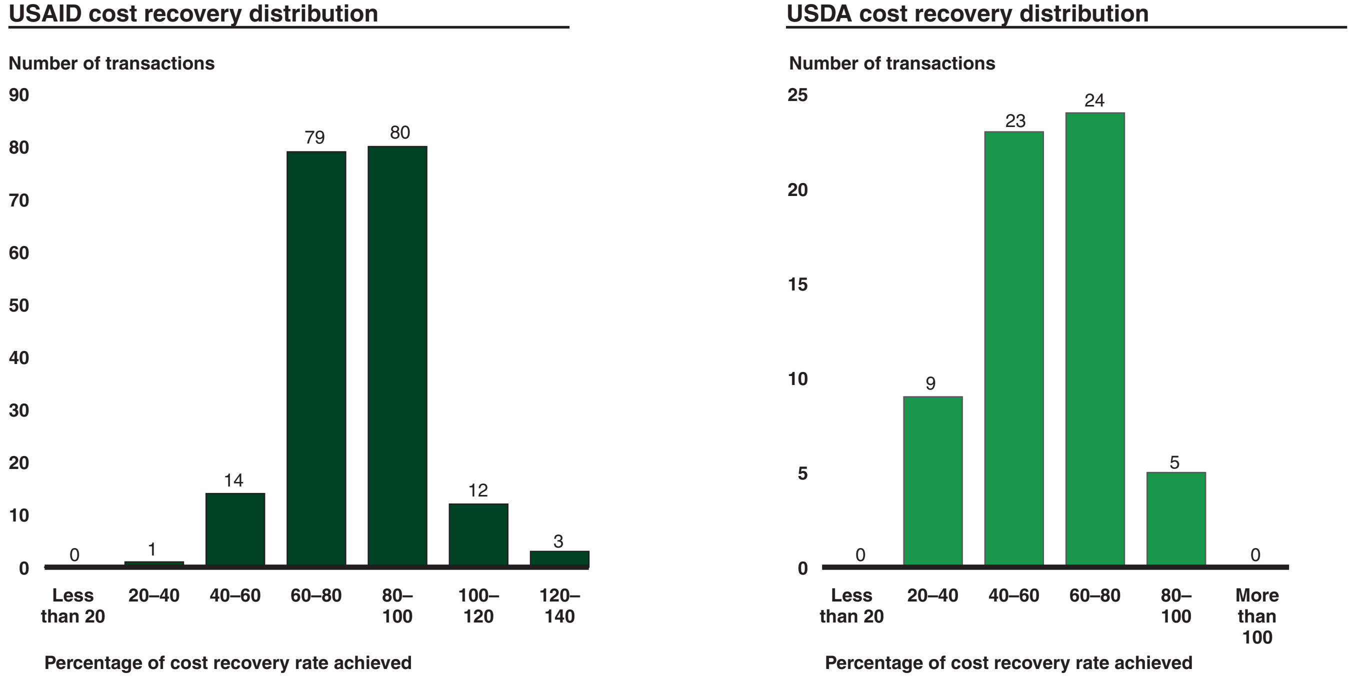
Figure 5: Difference in Funds Expended and Cash Proceeds Resulting from USAID and USDA Monetization



Sources: GAO based on selected transactions from data provided by USAID and USDA.

USAID's cost recovery rates ranged from 34 percent to 165 percent, while USDA's ranged from 25 percent to 88 percent. While USAID's monetization transactions most often achieved cost recovery between 60 and 100 percent, USDA's transactions most often achieved between 40 and 80 percent cost recovery. Fifteen of USAID's monetization transactions achieved cost recovery greater than 100 percent, meaning that the amount of proceeds generated exceeded the costs the government incurred, while none of USDA's monetization transactions did so. Figure 6 shows the distribution of cost recovery over the 3 years we examined for these selected monetization transactions by USAID and USDA, respectively.

Figure 6: USAID and USDA Cost Recovery Distribution for Selected Monetization Transactions



Sources: GAO analysis of USAID and USDA data.

Notes:

1. Cost recovery is the ratio between the proceeds the implementing partners generate through monetization and the amount the U.S. government expends to procure and ship the commodities for monetization. The higher the ratio, the more cash is generated to fund development projects.

2. Since some of the records we received from the agencies contained incomplete information, we reported only on those transactions that had sufficient information to calculate cost recovery. For USAID, we were able to use 189 of the 194 monetization transactions the agency reported between fiscal years 2008 and 2010 (99 percent). For USDA, we were able to use 61 of the 66 monetization transactions the agency reported between fiscal years 2007 and 2009 (92 percent).

USDA's level of cost recovery is lower for government-to-government monetization transactions, which accounted for about 18 percent of USDA's monetization from fiscal years 2007 through 2009. While most grants involving monetization are provided to NGOs and educational institutions, USDA also allows monetization by sovereign governments, known as government-to-government monetization.[21] These transactions are completed by host country governments, largely through the same

[21]USAID did not provide any monetization grants to sovereign governments through Food for Peace in the time period we examined, fiscal years 2008 through 2010.

process that is used by other implementing partners. Implementing partners of government-to-government monetization between fiscal years 2007 and 2010 have included Afghanistan, the Dominican Republic, El Salvador, Nicaragua, Niger, and Pakistan. Government-to-government transactions achieved an average cost recovery level of 45 percent from fiscal year 2007 through 2009.[22]

Our cost recovery calculations included costs for commodity procurement and ocean shipping but did not include other costs that are not solely associated with monetization. USAID and USDA incur these additional costs when they provide funding for direct distribution and monetization of food aid, as follows:

- USAID provides its implementing partners with cash from two sources to cover administrative costs other than commodity procurement and ocean shipping costs that are associated with monetization. The first source is internal transportation, shipping, and handling (ITSH), which is cash for shipping and handling the commodities, if necessary, once they arrive at the destination port, to the final point of sale. The second source is funding through Section 202(e) of the Food for Peace Act, which is provided to implementing partners to assist in meeting administrative, personnel, distribution, and other costs associated with Food for Peace programs.[23] Since most Food for Peace grants include both monetized and direct distribution food aid, USAID does not track ITSH and 202(e) specifically for monetization purposes. However, in 2010, ITSH and 202(e) costs for all of USAID nonemergency assistance, including both monetization and direct distribution, were $123.3 million, or about 30 percent of USAID's total nonemergency costs for the year.
- According to agency officials, USDA provides its implementing partners with cash through Commodity Credit Corporation (CCC) funds, to cover various administrative costs that are associated with food aid. While this

[22]In the time period we examined, fiscal years 2007 through 2009, we found eight government-to-government transactions for which we were able to obtain sufficient information. When government-to-government monetization transactions are excluded from the calculation of an overall USDA cost recovery average, the average increases from 58 to 61 percent.

[23]Section 202(e) of the Food for Peace Act (7 U.S.C. 1722(e)) authorizes USAID to make cash available to implementing partners to support Food for Peace programs in (1) establishing new programs; (2) meeting specific administrative, management, personnel, and internal transportation and distribution costs for carrying out Food for Peace programs; and (3) improving methodologies for food aid programs.

money primarily covers administrative costs associated with the implementation of development projects, some of it pays for costs associated with the monetization process. The CCC is an agency within USDA that authorizes the sale of agricultural commodities to other government agencies and foreign governments and authorizes the donation of food to domestic, foreign, or international relief agencies. The CCC also assists in the development of new domestic and foreign markets and marketing facilities for agricultural commodities. According to a USDA official, such costs could include hiring a monetization agent to facilitate a monetization transaction, or the salaries and benefits of the staff that carry out the monetization transaction. USDA provided implementing partners $23 million in CCC funding between fiscal years 2008 and 2010. USDA stated that it provided $3.57 million in a combination of CCC funding and monetization proceeds to cover the administrative costs associated with monetization from fiscal years 2007 through 2009.

Agencies Do Not Have a Cost Recovery Benchmark and Are Only Required to Achieve Reasonable Market Price, which Has Not Been Clearly Defined

Neither USAID nor USDA currently has a required minimum cost recovery benchmark for monetization transactions, and there is no specific target that monetization transactions must reach or exceed. Instead, the Food for Peace Act requires that monetization transactions through both USAID and USDA achieve "reasonable market price" in the recipient countries where U.S. commodities are monetized. The statute does not define reasonable market price, and does not refer to a specific cost recovery benchmark.

USAID recommends two sales methods in its 1998 *Monetization Field Manual*—which has not been updated since its issuance—to achieve reasonable market price, but neither of these methods provides a specific metric.[24] More than three-quarters of the implementing partners we surveyed said they used the field manual as a source of guidance on monetization. Both USAID and USDA have stated a preference for the first method—conducting sales by public tender—to determine a reasonable market price. According to the field manual, public tender, generally an open auction where traders are allowed to bid on the commodities, allows competitive price information to determine the market price for monetized food aid. When public tender sales are not feasible, the manual recommends direct negotiation between buyers and sellers as a second, alternative method. Both agencies recommend taking into account prices

[24]According to USAID, as of June 2011 the manual was being revised, but had not yet been officially reissued.

for the same or comparable commodities from other suppliers in the marketplace in order to achieve reasonable market price. Specifically, USAID states that reasonable market price is one which "compares favorably with the lowest landed price or parity price for the same or comparable commodity from competing suppliers."

More than One-Third of the Monetization Transactions We Examined Fell Short of Import Price Parity, a Quantifiable Measure of Reasonable Market Price

We found that more than one-third of the monetization transactions we reviewed, carried out in various years and countries, were conducted at prices below a quantitative and objective metric for reasonable market price that could be used across time, markets, and individual transactions. In the absence of a quantitative benchmark of reasonable market price, we used the prices of comparable commercial imports for a given country, commodity, and year—the IPP referred to in USAID's guidance. Others in the economics field, including researchers of food aid and monetization, use IPP as a measure of market price in a given country and time frame.[25] Additionally, the World Food Program, the single largest multilateral provider of food aid in the world, uses IPP to determine whether or not to procure its food in a given market, in order to gain an accurate picture of the potential impact the purchase may have.[26] Comparing monetization sales prices to the IPP tells us the extent to which the monetization transaction occurred at a fair and competitive market price for commercially imported commodities.[27] We found that more than one-third of the 42 transactions we examined, for which we had IPP and sales price data, had prices lower than 90 percent of the commercial import prices, an

[25]For example, see David Tschirley, Cynthia Donovan, and Michael T. Weber, "Food Aid and Food Markets: Lessons from Mozambique," *Food Policy*, vol. 21, no. 2 (1996): 189–209.

[26]See GAO, *International Food Assistance: Local and Regional Procurement Can Enhance the Efficiency of U.S. Food Aid*, but Challenges May Constrain Its Implementation, GAO-09-570 (Washington, D.C.: May 29, 2009).

[27]Specifically, we used IPPs that were calculated by Fintrac, the independent contractor hired by USAID to conduct market assessments for countries where Food for Peace nonemergency food aid is monetized. Fintrac's detailed methodology for calculating IPP is included in its market analyses of each country, provided to USAID and available publicly. See http://www.usaid.gov/our_work/humanitarian_assistance/ffp/bellmonana.html (last accessed June 21, 2011).

indication that they might have been able to achieve higher prices.[28] For example, in 2008, USAID allowed an implementing partner in Burkina Faso to monetize rice at a price that was 67 percent of the IPP, while at the same time in Guatemala, USAID permitted monetization of vegetable oil at 70 percent of the IPP.[29]

Ocean Transportation Costs Can Reduce the Amount of Funding Generated through Monetization

Ocean freight cost is a significant component of the monetization cost,[30] and due in part to cargo preference requirements, U.S.-flag carriers have higher shipping rates on average than foreign-flag carriers, further lowering cost recovery. The cargo preference mandate requires that 75 percent of U.S. food aid be shipped on U.S.-flag vessels.[31] Another mandate, known as the Great Lakes Set-Aside, requires that up to 25 percent of Title II bagged food aid tonnage be allocated to Great Lakes ports each month.[32] These legal requirements limit competition and potentially reduce food aid shipping capacity, leading to higher freight rates. Figure 7 shows the share of freight costs in food aid procurement and the costs associated with cargo preference for monetized food aid.

[28]When calculating the IPPs, Fintrac uses a margin of error of plus or minus 10 percent around the IPP to account for imperfect market information. Similarly, we allowed for a margin of error of plus or minus 10 percent around the IPP when we compared the IPPs to implementing partners' sales prices. We did not independently assess the underlying data of Fintrac's IPP, but reviewed their methods and data sources, which we found reasonable for the purpose of establishing that a number of transactions have prices lower than 90 percent of commercial import prices.

[29]In another example, in 2000 the USDA Inspector General reported that 95 percent of the commodities monetized in the transactions it investigated in one country, amounting to more than 307,000 metric tons, were sold for less than the competitive price in 1994.

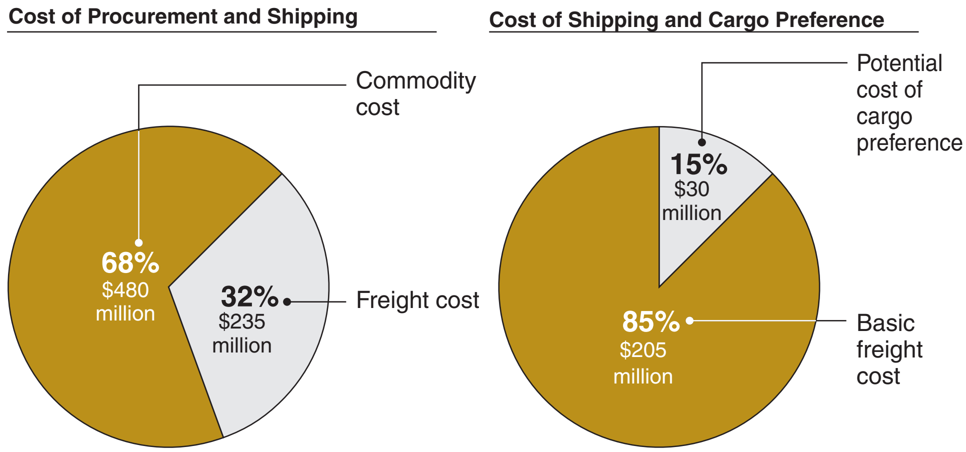
[30]In the context of monetization cost recovery, commodity cost includes commodity procurement cost and ocean freight cost.

[31]The difference between the costs of shipping U.S. food aid on U.S.-flag rather than foreign-flag vessels as a result of cargo preference requirements is known as the ocean freight differential (OFD). The Food Security Act of 1985 requires DOT to reimburse food aid agencies for a portion of the OFD cost and for ocean transportation costs that exceed 20 percent of total program costs. This report analyzes the freight rate differences between U.S.- and foreign-flag carriers, using the ocean freight rates that U.S. agencies paid prior to cargo freight differential reimbursement. According to DOT, the total amount of OFD for fiscal years 2008 through 2010 was $342 million. We estimated the OFD for monetization transactions from this time period is approximately $64 million. USAID and USDA stated that the OFD reimbursements for monetization are transferred to general food aid accounts for the agencies, and can be used to fund either emergency or nonemergency programs.

[32]For further discussion of cargo preference, see GAO, *Maritime Security Fleet: Many Factors Determine Impact of Potential Limits on Food Aid Shipments*, GAO-04-1065 (Washington, D.C.: Sept. 13, 2004).

(For a detailed discussion of our methodology in assessing the costs associated with cargo preference, see appendix II.)

Figure 7: Share of Freight Costs and Costs of Cargo Preference for Monetized Food Aid between Fiscal Years 2008 and 2010



Source: GAO analysis of KCCO data.

Between fiscal years 2008 and 2010, ocean shipping accounted for about one-third, or $235 million, of the cost to procure and ship monetized food aid (see fig. 7). For low-value commodities, such as bulk wheat, ocean shipping costs take up a higher percentage of the total cost. In 15 percent of the monetization transactions between fiscal years 2008 and 2010, shipping costs accounted for more than 40 percent of the total cost of procurement and shipping, amounting to more than $91 million in ocean shipping. For several of these transactions, shipping cost was higher than commodity procurement cost. For example, while it cost $3.9 million to purchase the shipment of 10,000 metric tons of wheat to be sent to Malawi in 2008 for monetization, it cost $4.5 million in ocean shipping.

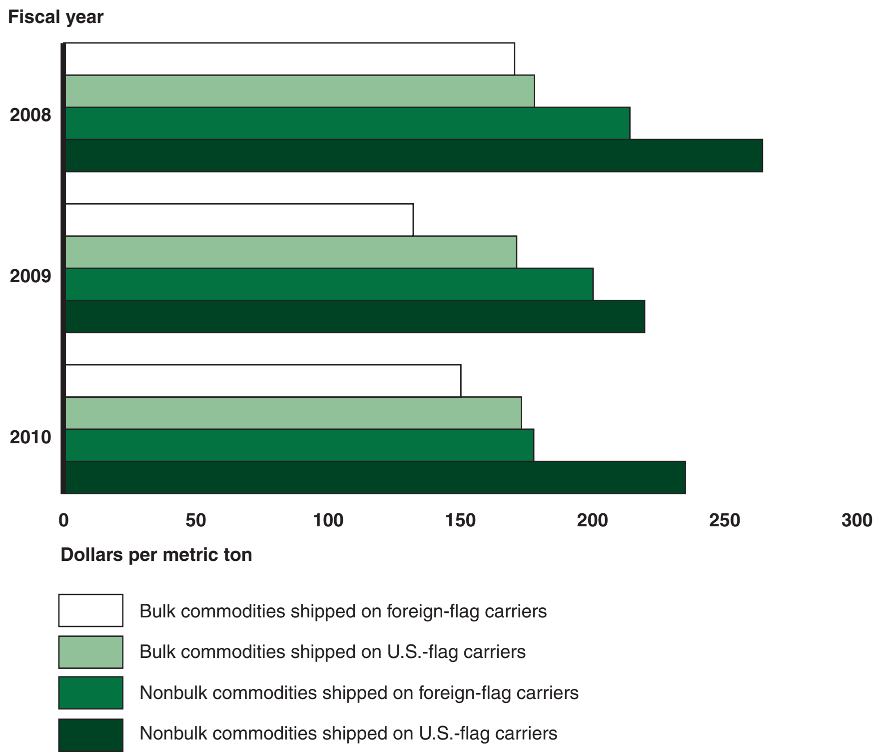
The freight rate for USAID and USDA food aid shipments on foreign-flag carriers cost on average $25 per ton[33] less than the freight rate on U.S.-flag carriers, controlling for shipping routes, the shipping time and term, and the type of commodities shipped. The difference in freight rate between U.S.- and foreign-flag carriers also depends on the type of commodities

[33]The 95 percent confidence interval is between $20 per ton and $31 per ton. (For a detailed discussion of the regression analysis, see appendix II).

shipped. Figure 8 shows the difference in the average freight rate per metric ton between U.S.- and foreign-flag carriers. The freight rate for bulk commodities averaged $8 per ton lower and the rate for non-bulk commodities averaged $30 per ton lower for foreign-flag carriers than U.S.-flag carriers for shipments with the same shipping routes and the same shipping times and terms. We estimate that between fiscal years 2008 and 2010, cargo preference potentially cost the food aid programs approximately $30 million because of the higher rates U.S.-flag carriers charged. When surveyed, 19 of the 29 implementing partners stated that allowing more shipping on foreign-flag carriers would "greatly improve" or "very greatly improve" cost recovery rates.[34]

[34]Numerous other factors were cited by the implementing partners we surveyed as factors that would greatly or very greatly improve cost recovery, including increasing third-country monetization, allowing for regional monetization, and reducing proposal process time. (For a full list of these factors, see fig. 15 in appendix VI).

Figure 8: Freight Rate Differentials between U.S.- and Foreign-Flag Carriers, Fiscal Years 2008 through 2010



Source: GAO analysis of KCCO data.

Food aid shipping competition may be further limited by the requirement in the Cargo Preference Act that foreign-built vessels that reflag into the U.S. registry wait 3 years before participating in the transportation of food aid cargo. According to a DOT official, the 3-year requirement was established in 1961 to provide employment opportunities to U.S. shipyards by discouraging vessels from reflagging into and out of the U.S. registry. The requirement, which does not apply to the Maritime Security Fleet[35] or to vessels transporting cargos financed by the U.S. Export-Import Bank, seeks to ensure that vessels transporting 75 percent of food aid are not only U.S.-flagged, but also constructed in U.S. shipyards. However, since

[35]The Maritime Security Fleet comprises vessels that participate in the Maritime Security Program, a program established by the Maritime Security Act of 1996 that provides funding to U.S. vessels participating in international trade, to support the Department of Defense. See GAO-04-1065.

2005, U.S. shipyards have built only two new U.S-flag vessels appropriate for transporting food aid and these vessels have not been awarded a food aid contract. Further, DOT has no record of an ocean transportation contract awarded to a U.S.-flag vessel that reflagged into the U.S. registry and waited the 3 years prior to applying for food aid contracts.

Limited competition contributes to fewer ships winning the majority of the food aid shipping contracts. Based on KCCO data, from fiscal years 2002 to 2010, the number of U.S.-flag vessels awarded food aid contracts declined by 50 percent, from 134 to 67 vessels.[36] In a 2009 report to Congress,[37] USAID and USDA stated that, due to the declining size of the U.S.-flag commercial fleet, USAID and USDA are forced to compete with the Department of Defense and other exporters for space aboard the few remaining U.S.-flag vessels, thereby limiting competition in transportation contracting and leading to higher freight rates. When surveyed about what could be done to improve the monetization process, 13 implementing partners with USAID and 16 with USDA stated that exploring options for lowering transportation costs would lead to “great” or “very great” improvement.[38]

USAID’s and USDA’s Monitoring of the Sales Prices that Implementing Partners Achieve through Monetization Is Limited

USAID and USDA conduct only limited monitoring of the sales prices that implementing partners achieve through monetization to ensure that the transactions generate as much funding as possible for the development projects funded by monetization proceeds. While implementing partners report cost recovery data to USAID and USDA, the agencies do not use the data to monitor sales prices over time. USAID requires annual reports on multiyear assistance programs (MYAP), referred to as pipeline and resource estimate proposals, to be submitted for the coming fiscal year. Additionally, implementing partners report their monetization proceeds in

[36]The decline in the number of U.S.-flag vessels could be due to a variety of reasons besides capacity, including a reduction in tonnage of food aid shipped over this period, and increased demand by the Department of Defense. Studying the cause of this decline was outside the scope of our review.

[37]USAID and USDA, *Report Regarding Efforts to Improve Procurement Planning* (Washington, D.C.: Jan. 21, 2009).

[38]The implementing partners we surveyed cited other steps that the agencies could take to greatly or very greatly improve the monetization process, including providing support for implementing partners when complications arise, streamlining the proposal process, and harmonizing planning time frames between USAID and USDA. (For a full list of these steps, see fig. 13 and fig. 14 in appendix VI).

Annual Results Reports. These reports include fiscal year levels of metric tonnage to be called forward, anticipated monetization proceeds, and any 202(e) or ITSH funds used for the program, which encompass both direct distribution and monetization activities.[39] In addition, they record the results of any monetization transactions from the previous year. USDA requires semiannual reports, known as Logistics and Monetization Reports. These reports record the metric tonnage of commodity monetized in that time period. In addition, they record the date and price at which the commodity was sold, as well as the date received and a breakdown of the specific use of the funds.

As part of the review and evaluation criteria of proposals, USAID's 1998 *Monetization Field Manual* requires verification that the amount of money generated in the monetization transaction(s) meets or exceeds the cost recovery benchmark. However, USAID officials said that they no longer hold implementing partners accountable for meeting the cost recovery benchmark of 80 percent referenced in the field manual, because (1) the 2002 Farm Bill changed the requirement to achieving "reasonable market price," and (2) USAID has not officially reissued the field manual since 1998. Although the USAID mission in-country can recommend against monetization transactions if it disagrees with the sales price analysis conducted by the implementing partner in its attempts to sell the commodity, USAID officials told us that the missions have never made such recommendations. Furthermore, USAID stated that the agency has not established criteria to monitor sale prices. According to USAID officials, because food aid monetization transactions are governed by grants, not contracts, the agency cannot be overly directive towards its implementing partners. USAID works to have ongoing conversations with the implementing partners in order to identify potential problems, troubleshoot, and help with potential alternatives.

USDA does not have a process to monitor sale prices either. USDA officials in charge of the Food for Progress program told us that they did not know what the level of cost recovery of monetization transactions is and did not have enough information to develop an estimate. USDA

[39]Beginning in its fiscal year 2010 guidance, USAID has stated that it will no longer approve proposals for 100 percent monetization. Instead, it states that Title II nonemergency MYAPs must be some mix of direct distribution and monetization. As such, 202(e) and ITSH funds are provided to the entire program, and not segmented out between monetization and direct distribution, making it extremely difficult to quantify the amount used solely for monetization activities.

officials said that they rely on their agricultural attachés to act as a "reality check" in determining reasonable market price, and determine acceptable cost recovery on a case-by-case basis, looking at the U.S. prices and the circumstances surrounding the sale.

The agencies' monitoring of monetization cost recovery is further hindered by deficiencies in their reporting and information management systems. USAID and USDA acknowledged that their current information systems are not capable of systematically capturing cost recovery information, which would help them monitor the sales prices implementing partners achieve. Both agencies had to manually generate the cost recovery information to fulfill our data request by going through the individual reports submitted by implementing partners to collect the information needed to calculate cost recovery for monetization transactions, inputting them into a spreadsheet for us to conduct our analysis. Furthermore, these spreadsheets contained numerous errors and inconsistencies. Examples include transactions that were recorded in the incorrect year, double-counted, or not counted at all. In other instances, the calculation of cost recovery was incorrect, due to incorrect values inputted into the cells. In addition, multiple transactions were missing the actual sales prices. In our 2007 report, we recommended that both USAID and USDA develop an information collection system to track monetization transactions. Despite this recommendation, both USAID and USDA acknowledged that their current information systems are still not capable of systematically capturing cost recovery information. Both USAID and USDA are in the process of implementing information systems that aim to better capture the information generated by the implementing partners regarding monetization transactions. USAID plans to have its new information system fully operational by summer 2012, including monitoring and evaluation components. USDA's Food Aid Information System will tie into its procurement, payment, and accounting system—Web Based Supply Chain Management—tracking budgeting and planning, solicitations, proposals and negotiations, payment and compliance for the Foreign Agricultural Service. The final components of the system are due to come online in fall 2011.

Long Lag Times Increase Market Risk for Implementing Partners and Hinder Their Ability to Accurately Budget for Project Implementation

Long lag times between a monetization proposal's approval by USAID or USDA and the time of the commodities' final sale increases the transaction's exposure to market volatility. This makes it difficult to accurately project the funding level monetization can generate, and to design and implement the development projects accordingly. Two-thirds of the implementing partners we surveyed said that if they received less funding than expected, they would curtail the scope of their projects as well as the number of beneficiaries served. One implementing partner commented that while monetization transactions must do their best to achieve "reasonable market price," timing is a constraint. The process of getting a proposal approved, finding a foreign buyer, and conducting an actual sale can be time-consuming, and market conditions can change significantly from when the implementing partners first submitted the proposals. For example, when an implementing partner monetized through USDA's Food for Progress program in Bangladesh, it submitted its initial proposal in August 2008, including the volume and estimated sales prices for the proposed commodity, but the sale of the commodities was not made until 17 months later, in December 2009. Market conditions changed significantly during the process from the time of the initial proposal to the final sale, and the commodity price fell by close to 40 percent, leading to a diminished return on the transaction. The implementing partner's actual sales price of $800 per metric ton was more than a third less than the estimated price in the original proposal of $1,300 per metric ton. In another example, an implementing partner stated that it wanted to monetize its commodities at a certain point when prices were high, but missed the opportunity to do so due to delays in the approval process. As a result, its cost recovery was lower than estimated. This situation forced the implementing partner to reduce its number of beneficiaries by roughly a third, and eliminate one of its targeted geographical regions within the country. All but 2 of the 29 implementing partners we surveyed reported that they experienced delays during monetization transactions at least "sometimes." In addition, 19 of the 29 implementing partners we surveyed reported that delivery delays were a factor that hindered their ability to conduct monetization.[40]

[40]Numerous other factors were cited by the implementing partners we surveyed as hindering monetization, including shortage of buyers, host country government opposition, and shortage of staff with market expertise. (For a full list of these factors, see fig. 12 in appendix VI.)

USAID and USDA Cannot Ensure that Monetization Does Not Cause Adverse Market Impacts because They Program Monetization at High Volumes, Conduct Weak Market Assessments, and Do Not Conduct Post-Monetization Evaluations

By law, USAID and USDA must ensure that monetization transactions do not entail substantial disincentive to, or interference with, domestic production or marketing of the same or similar commodities.[41] In addition, the agencies are to ensure that the transactions do not cause disruption in normal patterns of commercial trade. However, we found that the volume programmed[42] for monetization was more than 25 percent of the commercial import volume, in more than a quarter of the cases, increasing the risk of displacing commercial trade.[43] As part of an effort to meet its legal requirements, in 2008, USAID hired a private contractor as an independent third party to conduct market analyses and recommend commodities and volumes to monetize without causing adverse market impact. Separately, USDA conducts assessments called the Usual Marketing Requirement (UMR) that determine the maximum volume of a given commodity to be programmed for monetization without disrupting commercial trade, and relies on its implementing partners to conduct broader market analyses to address the Bellmon requirements. However, we found that USAID's assessments were conducted for a limited number of countries and have not yet been updated to reflect changing market conditions. We also found that USDA's UMRs contained weaknesses, such as a lack of methodology and errors in formulas. Further, we found that USAID's and USDA's recommended limits for monetization differed significantly from each other, and that the volume of commodity programmed for monetization by the agencies has at times exceeded the recommended limits. Finally, because both agencies do not conduct post-monetization market impact evaluations, they cannot determine the effectiveness of steps taken to ensure that monetization transactions do not cause adverse market impacts and what, if any, adverse impacts may have resulted. These adverse impacts may include discouraging food

[41] In 1977, Congress passed the Bellmon Amendment to the Food for Peace Act. The amendment requires that before agencies supply food aid, they must determine (1) that adequate storage facilities are available in the recipient country at the time of exportation of the commodity to prevent spoilage and waste of the commodity and (2) that the distribution of the commodities in the recipient country will not result in a substantial disincentive to, or interference with, domestic production or marketing.

[42] We define the term "programmed" as the total volume for a given commodity that was approved in a given fiscal year to be monetized, even though the actual shipments of the commodity may occur in subsequent years.

[43] For the purposes of this report, we define the term "case" as the total volume of a given commodity programmed for monetization by USAID and/or USDA in a given country in a given year.

production by local farmers, which in turn could undermine the food security goals of the development projects funded by monetization.

USAID and USDA Are Required to Ensure that Monetization Does Not Cause Adverse Market Impacts, but the Volume Programmed for Monetization in More than a Quarter of Cases May Have Increased the Risk of Displacing Commercial Trade

USAID and USDA Are Required by Law to Ensure that Monetization Does Not Cause Adverse Market Impacts that May Run Counter to Development Goals

By law, USAID and USDA are required to ensure that monetization transactions do not lead to adverse market impacts, such as causing disincentives to, or interference with, domestic production or marketing of the same or similar commodities. Additionally, the agencies are to ensure that the transactions avoid causing disruption in normal patterns of commercial trade, which is also an adverse market impact. Monetization has the potential to discourage food production by local farmers, and as a result may undermine the broader agricultural development and food security goals of the Food for Peace and Food for Progress programs. For example, when large volumes of food are monetized at once, the prices of the same or competitive commodities in the recipient country may be depressed, creating disincentives to local producers and possibly resulting in a decline in local production. The risk of depressing prices increases when the commodities arrive while supply is at a peak, such as during a harvest period for the same or competitive commodities. Monetization also has the potential to displace commercial trade, especially if the monetized food is sold on more favorable terms than what is available commercially. Buyers in the recipient country, such as domestic importers and millers, would then have an incentive to purchase monetized commodities over commercial ones. When sold in significant volumes, monetized food has the potential to substantially reduce demand for exports from the United States, other developed countries, and regional partners, thus hurting competitive commercial trade. Furthermore, if local production decreases or if commercial trade is displaced, repeated monetization of food aid commodities over time can increase the risk of market dependency on this source of food.

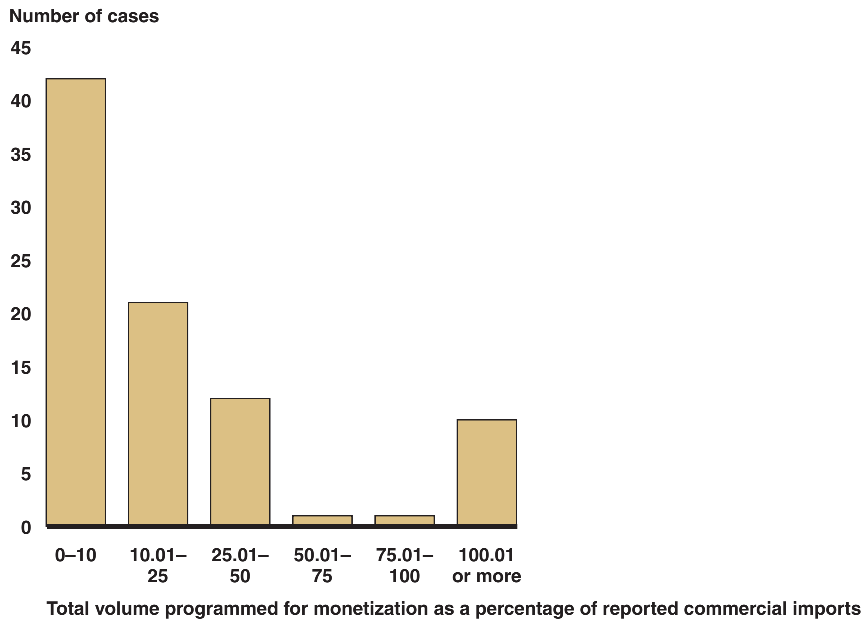
Food Aid Programmed for Monetization Constituted More than 25 Percent of Commercial Import Volume in More than a Quarter of Cases, Increasing the Risk of Displacing Commercial Trade

Food aid programmed for monetization constituted more than 25 percent of commercial import volume in more than a quarter of cases for certain commodities between fiscal years 2008 and 2010. As mentioned earlier, monetized food aid has the potential to displace commercial trade from developed countries or regional partners, a cost that impacts U.S. agribusiness and other exporters of the same commodity. Monetizing large volumes of food aid relative to commercial import volume increases the risk that commercial trade is displaced. Fintrac recommends that the total volume monetized of a given commodity should not exceed 10 percent of the commodity's commercial import volume in a given country in a given year.[44] We examined the total volume programmed for monetization by both agencies for each commodity in each country and each year between fiscal years 2008 and 2010, for which we could obtain the commercial import volume—a total of 87 cases.[45] For each country and year, we compared the total volume programmed for monetization of a given commodity to the commodity's reported commercial import volume. We found that the total volume programmed for monetization as a percentage of the reported commercial import volume ranged from less than 1 percent to 1,190 percent during this period. In about half of the 87 cases, the total volume programmed for monetization exceeded 10 percent of the commercial import volume. Further, in 24 of the 87 cases, the total volume programmed for monetization exceeded 25 percent of the reported commercial import volume for that commodity. Moreover, in 10 of the 87 cases, the total volume programmed for monetization was more than 100 percent of the reported commercial import volume. For example, about 30,000 metric tons of wheat were programmed for monetization in Uganda in 2008, which was more than 1.5 times the reported commercial import volume of wheat for that year. Figure 9 shows the distribution of the total volume programmed for monetization by both agencies as a percentage of the reported commercial imports.

[44] In August 2008, USAID hired a private contractor—Fintrac—under a 3-year pilot program to carry out an independent market analysis, known as the Bellmon Estimation for Title II, for 20 priority countries identified by the agency. According to Fintrac, the "10-percent rule" is only a general guideline and is not always followed by USAID. However, we were told by Fintrac that monetizing amounts that are below the 10 percent limit would not cause substantial trade disruption.

[45] We used the reported commercial import volumes found in USDA's UMR assessments. We were able to examine 87 cases, for which a UMR was available, of a total of 93 cases between fiscal years 2008 and 2010.

Figure 9: Distribution of Total Volume Programmed for Monetization as a Percentage of Reported Commercial Imports between Fiscal Years 2008 and 2010



Sources: GAO analysis of USAID and USDA data.

USAID and USDA Conduct Market Assessments to Meet Legal Requirements but These Market Assessments Contain Weaknesses

USAID Conducts Market Assessments to Determine Recommended Monetization Levels but These Have Been Conducted For a Limited Number of Countries and Do Not Include Projection Analyses

USAID uses a private contractor to conduct market assessments to help ensure that monetization transactions do not entail substantial disincentive to domestic production, as required by the Bellmon Amendment, for its 20 priority countries. In August 2008, USAID hired Fintrac to improve the market analysis required before food aid programs are approved in recipient countries, known as the Bellmon Estimation for Title II (BEST).[46] Prior to 2008, USAID made determinations about market impact based solely on the Bellmon analyses conducted by its implementing partners, who as the recipients of monetization grants are not independent. As of May 2011, 13 of the 20 BEST analyses had been completed.[47] According to USAID, the BEST analysis is to complement and not substitute the implementing partners' market analyses and surveillance. Therefore, in many cases implementing partners continue to conduct their own market analysis, which estimates the price they are likely to receive for the commodity to be monetized. Overall, 17 of the 29 implementing partners we surveyed stated that the BEST analysis was sufficient for determining which commodities to monetize and 13 of the 29 implementing partners stated that it was sufficient for determining how much to monetize.

The methodology for the BEST analysis includes identifying potential commodities to be monetized, ensuring that recipient country policies and regulations are favorable (i.e., there are no barriers or restrictions on the commodity to be monetized), reviewing local market structure as well as previous and planned food aid initiatives, and examining the likelihood of achieving fair and competitive market price. In conducting its analysis,

[46] USAID was authorized $22 million in the 2008 Farm Bill to improve monitoring of nonemergency food aid, part of which was used to fund BEST.

[47] USAID's contract with Fintrac is slated to end in 2011, and USAID has not determined whether the program will be extended or if this approach will become permanent. However, according to a USAID official, the agency is committed to continue conducting independent market analysis after the initial program comes to an end, and will seek resources to do so.

Fintrac also considers the latest 5-year trends in import volumes and domestic production data to ensure that the commodity to be monetized has been imported in significant volumes and that local production is insufficient to meet demand. As noted above, another important step in the analysis is to assess the likelihood that the monetized commodity will achieve fair and competitive market price. Fintrac uses the IPP as the most precise estimate of fair and competitive price for commercially-imported commodities. As discussed earlier, the IPP is the price a commercial importer in the recipient country pays to import the same or similar commodities from the most common exporting country.[48] Based on all of these components, Fintrac makes a recommendation on monetization. When Fintrac recommends monetization, it does so in volumes that generally do not exceed 10 percent of the commodity's commercial import volume in order to avoid substantial displacement of trade. Fintrac's analysis also relies on field visits to obtain additional data, and interviews with stakeholders in the recipient country such as implementing partners; commercial importers; and potential buyers, including millers and processors. According to Fintrac, its methodology allows it to replicate these market assessments from country to country and ensures that all implementing partners are provided with the same information for their monetization applications.

USAID's ability to ensure that monetization does not cause adverse market impact is limited, because the BEST analyses have only been conducted for a limited number of countries and have not yet been updated to reflect changes in market conditions. While Fintrac has conducted 13 BEST analyses, these analyses were available for only 11 of 63 cases in which USAID monetized since 2008.[49] For the remaining cases, USAID relied on Bellmon analyses conducted by their implementing partners, which are not independent. In addition, while the BEST offers an independent and consistent methodology and considers the latest 5 year trends in import volumes and domestic production data, it is not updated to capture

[48]To calculate the IPP, Fintrac adds such costs as ocean freight to point of import; duties, taxes and other charges; and inland transportation to final destination. Because these components are estimates that are imprecise, the analysis allow for a margin of error of plus or minus 10 percent, (i.e., the sale price of a commodity to be monetized is likely to be within 10 percent of the IPP).

[49]As mentioned earlier, for the purposes of this report, we define the term "case" as the total volume of a given commodity programmed for monetization by either USAID and/or USDA in a given country in a given year. We examined 63 cases between fiscal years 2008 and 2010 in which a commodity was programmed for monetization by USAID.

changes in market conditions that may occur by the time sales transactions take place. We found that in certain cases, in the interval between the completion of the BEST and the sale of the monetized commodity, there was a relatively long lag, during which market conditions may have changed. Further, MYAPs generally last for 3 to 5 years, and monetization sales can take place in each of those years. The BEST would likely not be useful for monetization transactions that take place beyond the initial MYAP approval. According to USAID, while there is market information that changes rapidly and requires continued assessments, the BEST includes historical and cyclical information that can be used for many years. However, we found that the BEST does not include projection analysis that could take into account potential price spikes and the volatile nature of the market. As a result, the findings in the BEST have the potential to be irrelevant by the time the commodities reach the recipient country and implementing partners may not have adequately considered the impact of monetization on local markets and trade when applying for grants.

USDA Conducts Market Assessments to Determine Recommended Monetization Levels but These Assessments Contain Weaknesses

USDA relies on its implementing partners to conduct market analyses that are used to address the Bellmon requirements. As the recipients of both the monetized commodities and the proceeds of their sales, implementing partners lack independence in conducting market analyses. Further, USDA does not provide guidance to the implementing partners on what methodology should be used for the market assessments that are intended to address Bellmon requirements. USDA does not conduct its own Bellmon requirement assessments to verify whether or not the conclusions reached by the implementing partners are reliable or reasonable. Without doing so, USDA cannot accurately determine whether monetization will result in substantial disincentive to, or interference with, domestic production or marketing of the same or similar commodities. USDA officials explained that they are currently unable to conduct independent analyses, such as those conducted by Fintrac, due to lack of resources. However, these officials also stated that they encouraged implementing partners to use the BEST analysis when available.

USDA conducts its own market assessment—the UMR—to meet its requirement to determine that monetization does not cause disruption in normal patterns of commercial trade. The UMR for a given commodity is an Excel spreadsheet that contains data on the recipient country's consumption needs or apparent consumption, imports, and production. USDA determines the maximum allowable volume for U.S. programming, including monetization, for a given commodity in a specific country and year by subtracting the volume of imports and production from that of the consumption needs or apparent consumption,[50] as follows:

Maximum Allowable Volume for U.S. Programming = Consumption + Exports + Stocks – (Domestic Production + Imports)

USDA officials told us that the UMRs are conducted after they receive monetization grant applications and that they issue about 30 to 40 UMRs per year. According to USDA officials, UMRs are not shared with the public because the information is intended solely for the use of U.S. government agencies, and the UMRs are considered market-sensitive because they include forecasts about consumption needs. Further, USDA officials told us that the UMRs are not held to the same rigorous review and verification processes that official USDA documents intended for external distribution must undergo.

We found weaknesses in the UMRs, such as no explanation or source for values used to calculate the consumption needs or apparent consumption in each UMR. In addition, some of the UMRs we reviewed included errors in formulas and mistakes in calculations. The standard methodology for estimating consumption would show it as the sum of production and imports minus exports adjusted for the changes in stock. However, the consumption needs and apparent consumption figures in the spreadsheets are not based on any formula and appear as a data entry. For example, the consumption need noted in one UMR was more than double the consumption need that was calculated for that commodity using the standard methodology mentioned above. In another UMR, the consumption need was 80 percent greater than the calculated amount using the standard methodology. Further, our review of the UMRs showed that while data sources are listed at the bottom of these spreadsheets, it is impossible to identify which information came from which of the listed sources. In addition, we found errors in formulas and mistakes in calculations in 8 of the 12 UMRs that we reviewed.[51] For example, columns in the Excel spreadsheets were not added correctly and resulted in totals that were smaller than the components summed to create them. We also

[50]Two other factors—stocks and export—also enter the computation, but these tend to be relatively small.

[51]We requested UMRs for every monetization transaction conducted between 2008 and 2010 and received a total of 87 UMRs in multiple deliveries. We reviewed all 87 UMRs. However, our comments concerning errors are limited to the initial delivery of 12 UMRs.

found inconsistencies in how numbers and formulas were created. In addition, averages that were supposed to be based on 5 years' worth of data were based on only 3 years' worth of data and treated as averages of 5 years' worth of data. In other cases, calculations included figures that should have been excluded, such as concessionary sales. Further, we found that some formulas included circular references, meaning that the total of the summation was also included as part of the summation itself. When we shared these findings with USDA, the agency corrected the eight UMRs. Such weaknesses impact the calculation for the maximum volume of recommended food aid programming and ultimately the decisions on how much food aid can be monetized. USDA officials told us that they conduct ad-hoc spot checks of the UMRs but do not have a formal quality control process in place.

USAID and USDA Recommend Differing Limits for Monetization and In Some Cases Have Exceeded the Recommended Limits

USAID's and USDA's Recommended Limits for Monetization Differ Significantly from Each Other

The assessments that USAID and USDA use to help set recommended limits for monetization volumes vary widely in their conclusions. In all of the 12 cases in which we could compare USAID's and USDA's limits, these limits were significantly different from each another. In some cases, the UMR analyses recommended monetization of a commodity, while the BEST did not. For example, the 2010 UMR for wheat in Burundi concluded that up to 6,000 metric tons of wheat could be monetized, but the 2010 BEST analysis for Burundi concluded that the market was not suitable for monetization of any commodity, including wheat, and recommended that regional monetization be considered. Further, in all 12 cases, the maximum allowable volume for U.S. programming found in the UMR was higher than the recommended maximum volume found in the BEST (see table 2). According to Fintrac, these volumes vary greatly because USAID conducts its assessments based on multiple factors, including the purchasing power of the buyers, which impacts the ability of the market to absorb additional commodities.

Table 2: Monetization Limits Set by USAID and USDA for the Same Commodity in the Same Country and Same Year, between Fiscal Years 2008 and 2010

Country	Commodity	Year	USAID's recommended maximum found in BEST (metric tons)	USDA's maximum allowable for programming found in UMR (metric tons)
Bangladesh	Vegetable oil	2010	56,000	85,000
Bangladesh	Wheat	2010	169,000	268,100
Burkina Faso	Rice	2010	22,094	90,600
Burundi	Wheat	2010	0	6,000
Liberia	Rice	2010	3,427	34,500
Liberia	Vegetable oil	2010	0	45,700
Liberia	Wheat	2010	1,994	8,300
Malawi	Vegetable oil	2009	3,800	8,000
Malawi	Wheat	2009	8,000	29,200
Sierra Leone	Wheat	2010	0	15,900
Uganda	Wheat	2009	31,000[a]	53,000
Uganda	Wheat	2010	31,000[a]	109,300

Sources: GAO analysis of USAID and USDA data.

[a]This BEST analysis included limits for both USAID and USDA. The total of those limits equaled 31,000 metric tons, of which a 23,500 metric ton limit was set for USAID programming and a 7,500 metric ton limit for USDA programming.

The Volume of Commodity Programmed for Monetization by the Agencies Has at Times Exceeded Recommended Monetization Limits

The volume of commodity programmed for monetization has at times exceeded the recommended limits set by the agencies. The purpose of setting these limits is to help ensure that these transactions do not cause adverse market impacts. However, the limits have been exceeded by the very agencies that set them. We examined the total volume programmed for monetization by each agency and the aggregate of both agencies for each commodity in each country and each year between fiscal years 2008 and 2010 (for a complete list, see table 5 in appendix IV). We then compared these totals to the recommended limits found in the BEST and

UMRs.[52] We found that USAID exceeded the limits recommended by the BEST analyses in 6 of 11 possible cases. For example, the 2010 BEST analysis for Liberia recommended that a maximum of 3,427 metric tons of rice could be monetized; however, USAID programmed 10,100 metric tons of rice to be monetized in Liberia in 2010. In addition, USDA exceeded the recommended limit found in the BEST in 2 of 3 possible cases. For example, in 2009 USDA programmed 15,000 metric tons of wheat in Uganda to be monetized, despite a recommendation in the BEST analysis that USDA should not monetize more than 7,500 metric tons of wheat. We also found that USDA exceeded the limit set by its UMR in 5 of 34 possible cases. For example, in 2008 USDA programmed 6,000 metric tons of soybean meal to be monetized in Armenia when the maximum allowable volume was set at 200 metric tons in the corresponding UMR. USAID exceeded the UMR's limit for U.S. programming in 10 of 59 possible cases. For example, in 2009, USAID monetized 2,390 metric tons of rice in Senegal even though the corresponding UMR did not recommend programming any rice for monetization. See table 3 for all the cases in which USAID and/or USDA exceeded the limit recommended by the BEST analysis and/or set by the UMR between fiscal years 2008 and 2010.

[52]Our analysis is based on the cases in which USAID and/or USDA programmed monetization for a commodity and a recommended limit was set by the BEST analysis and/or the UMR. Specifically, for USAID we examined the 11 cases in which USAID programmed monetization for a commodity and a BEST was available and the 59 cases in which USAID programmed monetization for a commodity and a UMR was available. For USDA, we examined the 3 cases in which USDA programmed monetization for a commodity and a BEST was available and the 34 cases in which USDA programmed monetization for a commodity and a UMR was available. Further, there were 6 cases in which both USAID and USDA programmed monetization for the same commodity in the same country and same year. For all 6 of those cases a BEST and/or a UMR was available.

Table 3: Cases in which USAID and/or USDA Exceeded the Limit Recommended by the BEST and/or the UMR between Fiscal Years 2008 and 2010

Country	Commodity	Year	Volume programmed by USAID (metric tons)	Volume programmed by USDA (metric tons)	Total volume programmed by both agencies (metric tons)	USAID's recommended maximum found in BEST (metric tons)	USDA's maximum allowable for programming found in UMR (metric tons)
Cases in which the volume USAID programmed for monetization exceeded the limit recommended by the BEST							
Burundi	Wheat	2010	8,000	0	8,000	0	6,000
Liberia	Rice	2010	10,100	0	10,100	3,427	34,500
Liberia	Vegetable oil	2010	500	0	500	0	45,700
Liberia	Wheat	2010	3,080	0	3,080	1,994	8,300
Malawi	Wheat	2009	21,140	30,000	51,140	8,000	29,200
Sierra Leone	Wheat	2010	1,900	0	1,900	0	15,090
Cases in which the volume USDA programmed for monetization exceeded the limit recommended by the BEST							
Malawi	Wheat	2009	21,140	30,000	51,140	8,000	29,200
Uganda	Wheat	2009	21,550	15,000	36,550	31,000[a]	53,000
Cases in which the volume USDA programmed for monetization exceeded the maximum allowable for programming found in the UMR							
Armenia	Soybean meal	2008	0	6,000	6,000	n/a	200
Gambia	Vegetable oil	2008	0	4,500	4,500	n/a	-37,000[b]
Malawi	Wheat	2008	9,140	10,000	19,140	n/a	-18,100[c]
Malawi	Wheat	2009	21,140	30,000	51,140	8,000	29,200
Senegal	Vegetable oil	2008	0	2,840	2,840	n/a	-1,000
Cases in which the volume USAID programmed for monetization exceeded the maximum allowable for programming found in the UMR							
Burkina Faso	Rice	2008	4,780	0	4,780	n/a	-64,900
Burundi	Wheat	2009	13,090	0	13,090	n/a	6,700
Burundi	Wheat	2010	8,000	0	8,000	0	6,000
Haiti	Wheat	2009	45,710	0	45,710	n/a	35,800
Malawi	Wheat	2008	9,140	10,000	19,140	n/a	-18,100[c]
Malawi	Wheat	2010	11,500	0	11,500	n/a	8,600
Niger	Rice	2009	11,360	0.00	11,360	n/a	800
Rwanda	Vegetable oil	2009	760	0.00	760	n/a	500
Senegal	Rice	2008	2,900	0.00	2,900	n/a	2,500
Senegal	Rice	2009	2,390	0.00	2,390	n/a	-97,700

Country	Commodity	Year	Volume programmed by USAID (metric tons)	Volume programmed by USDA (metric tons)	Total volume programmed by both agencies (metric tons)	USAID's recommended maximum found in BEST (metric tons)	USDA's maximum allowable for programming found in UMR (metric tons)
Cases in which the total volume programmed for monetization by both USAID and USDA exceeded the limit recommended by the BEST and/or the UMR							
Malawi	Wheat	2008	9,140	10,000	19,140	n/a	-18,100[c]
Malawi	Wheat	2009	21,140	30,000	51,140	8,000	29,200
Uganda	Wheat	2009	21,550	15,000	36,550	31,000[a]	53,000

Sources: GAO analysis of USAID and USDA data.

Notes:

1. Areas shaded in grey highlight the volume programmed for monetization and the limit that was exceeded.

2. "0" denotes that the BEST analysis did not recommend monetization of the commodity in that country and year and "n/a" indicates that a BEST analysis was not available for this country and year.

3. According to USDA, when the UMR's maximum allowable for U.S. programming is a negative number, programming for monetization is not recommended for the commodity in that country and year.

[a]This BEST analysis included limits for both USAID and USDA. The total of those limits equaled 31,000 metric tons, of which a 23,500 metric ton limit was set for USAID programming and a 7,500 metric ton limit for USDA programming.

[b]Upon reviewing a draft of this report that we provided the agencies for comment, USDA provided us with a version of the 2008 UMR for Gambia vegetable oil that was dated a month after the UMR that was originally provided. We did not include this UMR in our analysis because agency officials previously stated that UMRs are not updated monthly.

[c]In the comments USDA provided to us on the draft of this report, USDA stated that the 2008 UMR for Malawi wheat contained information in a footnote that it recognized as relevant to programming decisions. However, we found that USDA did not adjust the maximum allowable for U.S. programming in that specific UMR to account for the information included in the footnote.

Further, for 3 of 6 possible cases in which both agencies programmed the same commodity for monetization in the same country and the same year, the combined volume programmed for monetization by both agencies exceeded the recommendation in the BEST and/or the UMR. For example, for wheat in Malawi in 2009, the BEST recommended 8,000 metric tons and the UMR set the limit at 29,200 metric tons; however, both agencies programmed wheat for monetization and their combined total of 51,140 metric tons was more than six times the BEST's recommendation and 75 percent above the UMR's limit.

According to USAID officials, the recommended limits are at times exceeded because these market assessments are part of a larger decision-making process, which includes informal discussions between headquarters, the field-mission, and the implementing partners. Officials stated that through these discussions a decision on the commodity choice and volume to be monetized is made. However, USAID acknowledged that these discussions and the rationale for the decisions are not systematically documented. According to USDA officials, the agency considers other market information after agreements are signed and the UMRs are not the only information used to make programming decisions. Further, USDA officials stated that in some cases, they have documented the justification to exceed the programming limits set by the UMR. However, USDA did not provide this documentation for the cases that are discussed in this report.

USAID and USDA Do Not Conduct Impact Evaluations after Monetization Transactions Have Taken Place to Determine Actual Market Impact

The actual impacts of programming monetization and monetizing above the limits recommended by the BEST and UMR have not been determined, since neither USAID nor USDA conduct evaluations after monetization transactions have taken place. Both agencies require implementing partners to report the sales price achieved for their monetization transactions, and USAID's *Monetization Field Manual* recommends that implementing partners establish a process for regularly monitoring local market prices. However, USAID and USDA have neither used the data on sale prices reported by the implementing partners to assess the impact monetization had on local production and trade nor established ways to systematically monitor the local markets in countries where they monetize. USAID and USDA have depended on the BEST, UMR, and market assessments conducted by their implementing partners to help meet their requirement to ensure that monetization does not result in adverse market impacts in the recipient countries. However, without conducting evaluations after monetization has occurred, they cannot determine the impact the sale of donated food had on local production and trade. Furthermore, they cannot assess the effectiveness of the BEST and UMR in preventing adverse market impact. According to a 2009 study by the Partnership to Cut Hunger and Poverty in Africa,[53] for the United States to demonstrate commitment to minimizing market risks in recipient countries, more systematic evaluation of the monetization process is needed.

[53]Emmy Simmons, "Monetization of Food Aid: Reconsidering U.S. Policy and Practice," *Partnership to Cut Hunger and Poverty in Africa* (June 2009).

Conclusions

Providing developing countries with assistance to improve food security is a vital humanitarian and foreign policy objective. However, monetization of U.S. food aid—the U.S. government's primary approach to meeting this objective—is an inherently inefficient way to fund development projects and can cause adverse market impacts in recipient countries. The monetization process results in the expenditure of a significant amount of appropriated funds in unrelated areas such as transportation and logistics, rather than development projects. Moreover, the potential for adverse market impacts, such as artificially suppressing the price of a commodity due to excessive monetization, could work against the agricultural development goals for which the funding was originally provided. The inefficiencies of monetization stem directly from the multiple transactions required by the process and, except in rare cases, prevent full cost recovery on monetization transactions. Therefore, as a source of funding for development assistance, monetization cannot be as efficient as a standard development program which provides cash grants directly to implementing partners.

While monetization continues, however, it is important that the agencies strive to maximize the resources available for implementing development projects funded through monetization. The absence of a clearly defined benchmark or indicator for reasonable market price hinders their efforts to forestall transactions that provide a very low rate of return. In addition, since the agencies conduct only limited monitoring of the sales prices that implementing partners achieve through monetization, they cannot ensure that the transactions obtain the highest price and thereby generate as much funding as possible for development projects. The agencies are required by law to ensure that monetization does not cause adverse market impacts, but their market assessments contain weaknesses that diminish their usefulness for informing decisions on what, where, whether, and how much to monetize. Moreover, whatever limits these assessments attempt to establish are often exceeded and could contribute to disincentives to local food production and displacement of commercial trade. Furthermore, without conducting post-monetization transaction impact evaluations, the agencies cannot determine the actual impacts of monetization, even when the volume of the commodity monetized is more than 25 percent of the commodity's commercial import volume. Finally, transportation costs constitute about a third of the overall costs of monetization over the 3-year period we examined, and the 3-year reflagging rule—which only applies to food aid and not to the defense agencies and the U.S. Export-Import Bank—can limit competition among ships eligible to transport U.S. food aid, further increasing cost.

Matter for Congressional Consideration

Consistent with rules that apply to the Maritime Security Fleet and vessels transporting other U.S. government cargo, Congress should consider amending the Cargo Preference Act of 1954 to eliminate the 3-year waiting period imposed on foreign vessels that acquire U.S.-flag registry before they are eligible for carriage of preference food aid cargos. This could potentially increase the number of U.S.-flag vessels eligible for carriage of preference food aid cargo, thereby increasing competition and possibly reducing costs.

Recommendations for Executive Action

To improve the extent to which monetization proceeds cover commodity and other associated costs and the agencies' ability to meet requirements to ensure that monetization does not cause adverse market impacts, we recommend that the Administrator of USAID and the Secretary of Agriculture take the following four actions:

1. jointly develop an agreed-upon benchmark or indicator to determine "reasonable market price" for sales of U.S. food aid for monetization;

2. monitor food aid sales transactions to ensure that the benchmark set to achieve "reasonable market price" in the country where the commodities are being sold is achieved, as required by law;

3. improve market assessments and coordinate to develop them in countries where both USAID and USDA may monetize; and

4. conduct market impact evaluations after monetization transactions have taken place to determine whether they caused adverse market impacts.

Agency Comments and Our Evaluation

USAID and USDA, the two principal agencies that manage U.S. food aid monetization programs, and DOT, the principal agency responsible for the implementation of cargo preference rules, provided written comments on a draft of this report. We have reprinted their comments in appendixes VII, VIII, and IX, respectively. These agencies also provided technical comments and updated information, which we have incorporated throughout this report, as appropriate. The Department of State and the Office of Management and Budget did not provide written comments.

DOT disagreed with our Matter for Congressional Consideration on the basis of its concern regarding the potentially detrimental impact the statutory change may have on the U.S. maritime industry. However, we maintain that Congress should consider amending the Cargo Preference Act of 1954 to eliminate the 3-year waiting period imposed on foreign vessels that acquire U.S.-flag registry before they are eligible for carriage of preference food aid cargos. We are suggesting this proposed amendment on the basis of the following four factors: First, the number of vessels participating in U.S. food aid programs has declined. In a 2009 report to Congress, USAID and USDA jointly stated that, due to the declining size of the U.S.-flag commercial fleet, USAID and USDA are forced to compete with the Department of Defense and other exporters for space aboard the few remaining U.S.-flag vessels, thereby limiting competition in transportation contracting and leading to higher freight rates. Second, our analysis of ocean transportation costs showed that food aid shipments on foreign-flag carriers cost the U.S. government, on average, $25 per ton less than U.S.-flag carriers. Third, although the 3-year requirement was established to provide employment opportunities to U.S. shipyards, since 2005, U.S. shipyards have built only two new U.S.-flag vessels appropriate for transporting food and the vessels have not been awarded a food aid contract. Fourth, the 3-year rule applies only to food aid and not to defense agencies and the U.S. Export-Import Bank. The elimination of the 3-year waiting period can ease entry of new vessels into the U.S. food aid program, with the potential to increase competition among eligible U.S.-flag ships and reduce the cost of transportation. DOT also said that we overstated the overall cost of transportation. Our calculation of transportation cost was based on an analysis of all actual monetization transactions over a 3-year period and is thus a precise calculation of the actual cost to the U.S. government. In addition, DOT said that the number of vessels participating in the program has declined by less than what we found. However, our analysis was based on the number of actual vessels booked for all food aid contracts awarded from fiscal years 2002 to 2010.

USAID generally concurred with our recommendations, noting ongoing and planned actions to address them. Specifically, USAID stated that it will work with USDA to explore options of setting a benchmark or indicator for the sale of U.S. food aid through monetization. USAID noted that it has regional and country-based food aid monitoring and evaluation specialists who review U.S. food aid programs, including monetization sales, and that the agency's BEST project is well-accepted by its implementing partners. Additionally, USAID is updating its *Monetization Field Manual*, which includes market assessment guidance. Finally, USAID stated that it will explore possible cost-effective ways to conduct post-sale market impact evaluations with its partners.

USDA also generally concurred with our recommendations, stating that they will be useful in ongoing efforts to generate cash development resources and improve overall program management. USDA noted that an advantage of monetization is that it can encourage commercial markets for agricultural products and contribute to other market-building activities. However, we found that the agencies cannot ensure that monetization does not cause adverse market impacts, including discouraging food production by local farmers. USDA also noted actions it is exploring to reduce the cost of food aid shipments, such as the recipient host government paying for the cost of ocean transportation and combining shipments to obtain volume discounts. Further, USDA stated that it will work with USAID to develop improved benchmarks for reasonable local market prices. Finally, USDA stated that it will coordinate with USAID to improve market assessments and it will consider revising its regulations to require market impact evaluations.

We are sending copies of this report to interested members of Congress, the Administrator of USAID, the Secretary of Agriculture, and relevant agency heads. The report is also available at no charge on the GAO Web site at http://www.gao.gov.

If you or your staffs have any questions about this report, please contact me at (202) 512-9601 or melitot@gao.gov. Contact points for our Office of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made major contributions to this report are listed in appendix X.

Thomas Melito

Thomas Melito
Director, International Affairs and Trade

List of Requesters

The Honorable Debbie Stabenow
Chairwoman
The Honorable Pat Roberts
Ranking Member
Committee on Agriculture, Nutrition, and Forestry
United States Senate

The Honorable Richard G. Lugar
Ranking Member
Committee on Foreign Relations
United States Senate

The Honorable Frank D. Lucas
Chairman
The Honorable Collin C. Peterson
Ranking Member
Committee on Agriculture
House of Representatives

The Honorable Ileana Ros-Lehtinen
Chairman
The Honorable Howard L. Berman
Ranking Member
Committee on Foreign Affairs
House of Representatives

The Honorable Donald M. Payne
Ranking Member
Subcommittee on Africa, Global Health,
and Human Rights
Committee on Foreign Affairs
House of Representatives

Appendix I: Objectives, Scope, and Methodology

Our objectives were to (1) assess the extent to which monetization proceeds cover commodity and other associated costs and (2) examine the extent to which U.S. agencies meet requirements to ensure that monetization does not cause adverse market impacts.

To address these objectives, we analyzed emergency and nonemergency food aid program data provided by the U.S. Agency for International Development (USAID), the U.S. Department of Agriculture (USDA), and USDA's Kansas City Commodity Office (KCCO). Our analysis focused on nonemergency food aid that was monetized. The agencies relied on various reports their implementing partners submitted to manually generate the cost recovery data for fiscal years 2008 through 2010 for our review. We worked with the agencies to correct errors in the data and determined that the data used in our analysis were sufficiently reliable for our purposes.

We surveyed all the nongovernmental organizations (NGO) that served as implementing partners under USAID and USDA and conducted monetization between fiscal years 2008 through 2010. To determine the universe of NGOs that served as implementing partners during this time period, we obtained a list of all implementing partners with call forwards for monetized food aid from KCCO between fiscal years 2008 and 2010, which consisted of a total of 33 implementing partners. Three of these implementing partners were foreign governments and we excluded these from our sample. A fourth implementing partner was excluded because it had not conducted monetization before the end of fiscal year 2010. As a result, we determined that the universe of implementing partners that had monetized between fiscal years 2008 and 2010 was 29. We developed a structured instrument for our survey in October of 2010, and pre-tested it on two implementing partners. The instrument contained both closed and open ended questions in four general areas: (1) the monetization process, (2) the U.S. government role, (3) market analysis, and (4) cost recovery. We sent the instrument to all 29 implementing partners via e-mail in November 2010 and received completed instruments from all 29 of them. As part of our process for this survey, we conducted phone interviews with each implementing partner after we received its completed instrument to ensure the accuracy of their responses.

In Washington, D.C., we interviewed officials from USAID, USDA, the Departments of State and Transportation, and the Office of Management and Budget. We also met with a number of subject matter experts, as well as officials representing NGOs that serve as implementing partners to USAID and USDA in carrying out U.S. food aid monetization programs overseas. In addition, we conducted field work in three of the four countries that programmed some of the highest volumes of nonemergency monetized U.S. food aid between fiscal years 2008 and 2010—Bangladesh, Mozambique, and Uganda—and met with officials from U.S. missions, representatives from NGOs and other implementing partners that directly handle sales and implement development activities, and in Uganda and Mozambique, officials from relevant host government agencies.

To determine the level of cost recovery, we obtained data from USAID and USDA on commodity costs, which include the procurement and ocean freight cost, and sales price for each monetization transaction. For the purposes of this report, we defined cost recovery as the ratio between sales proceeds from monetization and the cost to the U.S. government to procure and ship the commodities. We did not include transactions for which the agencies did not have actual sales prices. We analyzed cost recovery by agency, year, commodity, and recipient country to study the variations in the level of cost recovery. In order to analyze cost recovery, we took the following steps:

- *Cleaned the data*. We found many errors and discrepancies in the data we obtained from USAID and USDA, and sent questions asking them to explain the discrepancies we found and make corrections.
- *Calculated cost recovery*. Using the cleaned data, we calculated the cost recovery for each transaction and for the USAID and USDA programs in total. The program average we reported is a weighted average, the ratio between the sum of sales proceeds and the sum of commodity and freight costs.
- *Estimated the difference between the proceeds generated through monetization and the cost the U.S. government incurred to procure and ship the commodities*. To do so, subtracted the total cost the U.S. government incurred on procurement and shipping monetized food aid commodities from the total proceeds generated.

We also estimated the extent to which freight costs account for the cost to the U.S. government for U.S. food aid procurement and shipping. In addition, we looked at how cargo preference affects cost recovery by examining the freight rate differentials between U.S.- and foreign-flag carriers, in shipping U.S. food aid. (For a detailed description of our methodology for this analysis, see appendix II.)

To examine the extent to which USAID and USDA meet requirements to ensure that monetization does not cause adverse market impacts, we conducted a literature search to identify relevant studies and papers on the effect of monetization on recipient countries and trade. In addition, we conducted interviews with officials from USAID and USDA; representatives from NGOs engaged in monetization; and experts from academia with extensive research, published work, and experience in the field. We reviewed the federal requirements and agency documents such as policies and guidelines, the Bellmon Estimate for Title II (BEST) analyses, and the Usual Marketing Requirement (UMR). We also analyzed data from KCCO, USAID, and USDA on commodities that were programmed for monetization between fiscal years 2008 and 2010, including volumes programmed for monetization, import data, and consumption data in recipient countries. Specifically, we

- Examined the total volume programmed for monetization by both agencies for each commodity in each country and each year between fiscal years 2008 and 2010, for which we could obtain the commercial import volume using the UMR. We compared the total volume monetized of a given commodity to the commodity's commercial import volume. To assess the data, we interviewed cognizant agency officials at USDA and reviewed documentation; however, we did not independently verify the underlying source data. We determined that the data we used were sufficiently reliable for our purposes.

- Reviewed the 7 BESTs and 87 UMRs that were available for all of the monetization cases that occurred between fiscal years 2008 and 2010. For the purposes of this report, we define the term "case" as the total volume of a given commodity programmed for monetization by either USAID and/or USDA in a given country in a given year.

- Examined the limits set by the BEST and the UMR and compared them to each other.

- Examined the monetization cases that occurred between fiscal years 2008 and 2010 and compared them to limits set by the BEST and/or the UMR. As we created a data set from the agencies' documents and calculations to assess the extent to which USDA and USAID had exceeded the limits they set for monetization, we determined that it was beyond the scope of this engagement to assess the agencies' underlying data. We did, however, check the internal logic of the agencies' documents and their calculations. We consulted with the agencies if we found discrepancies and either had the agencies make the necessary corrections or did not use the data in our analysis.

We also assessed both agencies' efforts to monitor and evaluate the impact of monetization transactions.

We conducted this performance audit from July 2010 to June 2011 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 objectives. We believe the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Appendix II: Technical Notes on Analysis of Differences in Ocean Freight Rates between U.S.- and Foreign-Flag Carriers

To determine whether, and the extent to which, ocean freight rates differ between U.S.-and foreign-flag carriers in shipping U.S. food aid, we obtained data from the Kansas City Commodity Office (KCCO) and developed two regression models to estimate the differences in freight rates between U.S.-and foreign-flag carriers while controlling for various factors that affect the freight rate.

Data

We obtained data from KCCO, a division of the Department of Agriculture (USDA) responsible for procuring U.S. food aid commodities. The data contain more than 5,000 food aid purchase transactions between 2007 and 2010. For each transaction, we had the following information:

1. Name of program: Food for Peace, Food for Progress, or McGovern-Dole International Food for Education and Child Nutrition Program
2. Request number
3. Name of the recipient country
4. Name of the implementing partner
5. Name of the commodity
6. Type of food aid: monetization or direct delivery
7. Fiscal year the program is approved
8. Name of the port where commodity is loaded in the U.S
9. Date when commodity arrives at load port
10. Name of the port where commodity is discharged
11. Metric tons of commodity
12. Total commodity cost
13. Total freight cost
14. Shipping term

Table 4 presents the summary statistics of the data.

Table 4: Summary Statistics of KCCO's Data on Food Aid Purchase Transactions between Fiscal Years 2007 and 2010

Variable	Mean	Standard deviation	Maximum	Minimum
Metric tons	1,469	4,291	54,000	0.64
Commodity costs	$570,917	$1,064,689	$14,400,000	$0
Freight costs	$258,061	$598,893	$8,347,336	$0

Source: GAO analysis of KCCO data.

Note: This table presents the average, standard deviation, and maximum and minimum of the numeric variables in the 5,440 food aid procurement and shipping transactions between fiscal years 2007 and 2010.

We generated a new variable called *pertonfreight*, measured in dollars per metric ton, by dividing total freight cost by metric tons. Table 5 compares the difference in freight rate between foreign and U.S.-flag carriers by commodity type (bulk vs. non-bulk) and by year without controlling for shipping routes or shipping terms. The results show that in general U.S. flag carriers charge higher freight rates than foreign flag carriers. However, part of the difference could be explained by shipping routes or shipping terms, which we incorporated in the regression analysis.

Table 5: Freight Rate by Year, Commodity Type, and Carrier Type

	Non-bulk (dollars per ton)		Bulk (dollars per ton)	
Year	U.S.-flag carrier	Foreign-flag carrier	U.S.-flag carrier	Foreign-flag carrier
2008	$264	$214	$178	$170
2009	220	200	171	132
2010	235	178	173	150

Source: GAO analysis of KCCO data.

Note: Since the 2007 data are incomplete, we did not include them in this table.

Regression Model Specification and Results

Regression Model 1 and Results

In order to analyze the difference in ocean freight rate between U.S.-and foreign-flag carriers while controlling for various factors which affect freight rates, we performed a multivariate regression analysis. We attempted to explain the differences in freight rates using the shipping routes, shipping time, shipping terms, commodities shipped, and the ownership of the carriers.[1]

Equation 1:

*Freight rate = a0 + (a1 * load port dummy) + (a2 * discharge port dummy) + (a3 * year dummy) + (a4 * bulk dummy) + (a5 * shipping term dummy) + (a6 *flag dummy)*

Where:

- *load port dummy* is a set of variables indicating where commodities were loaded.
- *discharge port dummy* is a set of variables indicating where commodities were unloaded.
- *year dummy* is a set of variables indicating the year the commodities were shipped.
- *bulk dummy* is a variable indicating if the commodities shipped were bulk (bulk dummy=1) or non-bulk *(bulk dummy=0);*
- *term dummy* is a set of variables indicating which of the four different shipping terms we used.
- *flag dummy* is a variable indicating if the ocean carriers were foreign-flag carriers *(flag dummy=1)* or U.S.-flag carriers *(flag dummy=0)*.

A negative and significant coefficient a6 would indicate that foreign-flag carriers charge a lower freight rate than U.S.-flag carriers after controlling for shipping routes, shipping time, commodity type, and shipping terms. Table 6 presents the main regression results for model 1.

[1]We assume these variables are independent of each other and are not correlated.

Table 6: Main Regression Results for Regression Model 1

Observations	**5416**			
R-square	70%			
	Coefficient	**Standard error**	**T-value**	**P-value**
Constant (a0)				
Constant	-74.5	49.8	-1.5	0.1
Year dummy (a3)				
Year 2 (2008)	17.03	3.9	4.5	0
Year 3 (2009)	-22.1	3.9	4.5	0
Year 4 (2010)	21.4	4	-5.3	0
Bulk dummy (a4)				
Bulk	-89.3	4	-22.6	0
Flag dummy (a6)				
Flag	-25.2	2.7	-9.2	0

Source: GAO analysis of KCCO data.

Note: In addition to the variables listed above, our regression also included dummy variables for 34 load ports, 116 discharge ports, and 3 different shipping terms.

Regression Model 2 and Results

In order to capture the difference in freight rate between U.S.-and foreign-flag carriers on bulk and non-bulk commodities, we ran a regression with an interactive term flag * bulk.

Equation 2:

*Freight rate = a0 + (a1 * load port dummy) + (a2 * discharge port dummy) + (a3 * year dummy) + (a4 * bulk dummy) + (a5 * shipping term dummy) + (a6 *flag dummy) + (a7 * (flag * bulk)*

For bulk commodities (bulk=1), and foreign-flag carriers (flag=1), Equation 2 becomes:

Equation 3:

*Freight rate = a0+ (a1 * load port dummy) + (a2 * discharge port dummy) + (a3 * year dummy) + (a4 * 1) + (a5 * shipping term dummy) + (a6 *1)+[a7*(1*1)]*

For bulk commodities (bulk=1) and U.S.-flag carriers (flag=0), Equation 2 becomes:

Equation 4:

*freight rate = a0+ (a1 * load port dummy) + (a2 * discharge port dummy) + (a3 * year dummy) + (a4 * 1) + (a5 * shipping term dummy) + (a6 *0)+[a7*(0*1)]*

The difference between Equation 3 and Equation 4 yields a6+a7, which is the difference in freight rate between U.S.-and foreign-flag carriers for bulk commodities.

Similarly, for non-bulk commodities (bulk=0), and foreign-flag carriers (flag=1), Equation 2 becomes:

Equation 5:

*freight rate = a0+ (a1 * load port dummy) + (a2 * discharge port dummy) + (a3 * year dummy) + (a4 * 0) + (a5 * shipping term dummy) + (a6 *1)+[a7*(0*1)]*

For bulk commodities (bulk=0) and U.S.-flag carriers (flag=0), Equation 2 becomes:

Equation 6:

*freight rate = a0+ (a1 * load port dummy) + (a2 * discharge port dummy) + (a3 * year dummy) + (a4 * 0) + (a5 * shipping term dummy) + (a6 *0)+[a7*(0*0)]*

The difference between Equation 5 and Equation 6 yields a6, which is the difference in freight rate between U.S.-and foreign-flag carriers for non-bulk commodities.

Table 7 presents the main regression results for model 2.

Table 7: Main Regression Results for Regression Model 2

Observations	**5416**			
R-Square	70%			
	Coefficient	**Standard error**	**T-value**	**P-value**
Constant (a0)				
Constant	-75.6	49.8	-1.5	0.1
Year dummy (a3)				
Year 2 (2008)	18.1	3.9	4.7	0
Year 3 (2009)	-21.1	3.9	-5.4	0
Year 4 (2010)	-20.8	4.0	-5.2	0
Bulk dummy (a4)				
Bulk	-92.0	4.0	-22.8	0
Flag dummy (a6)				
Flag	-30.1	3.1	-9.7	0
*Flag*bulk (a7)*				
Flag*bulk	22.4	6.6	3.4	0

Source: GAO analysis of KCCO data.

Note: In addition to the variables listed above, our regression also included dummy variables for 34 load ports, 116 discharge ports, and 3 different shipping terms.

Appendix III: Program Authorities

The United States has principally employed six programs to deliver food aid: Public Law 480 Titles I, II, and III; Food for Progress; the McGovern-Dole International Food for Education and Child Nutrition; and the Local and Regional Procurement Project. Three of these programs allow for monetization: Title II (renamed Food for Peace), Food for Progress, and McGovern-Dole International Food for Education and Child Nutrition. Table 8 provides a summary of these food aid programs by program authority.

Table 8: U.S. Food Aid by Program Authority

	Food for Peace					
Program	**Title I**	**Title II**	**Title III**	**Food for Progress**	**McGovern-Dole International Food for Education and Child Nutrition**	**Local and Regional Procurement Project**
Total cost in fiscal year 2010 (thousands of dollars)	$19,698.9	$1,932,471.6	$0	$146,423.1	$174,489.7	$23,811
Managing agency	USDA	USAID	USAID	USDA	USDA	USDA
Year established	1954	1954	1954	1985	2003	2008
Description of assistance	Concessional sales of agricultural commodities	Donation of commodities to meet emergency and nonemergency needs; commodities may be monetized	Donation of commodities to governments of least developed countries	Donation of commodities to developing countries and emerging democracies; commodities may be monetized	Donation of commodities and provision of financial and technical assistance in foreign countries; commodities may be monetized	4-year pilot program to examine the timeliness and efficiency of local and regional procurement as a tool to enhance U.S. government food assistance programs
Type of assistance	Nonemergency	Emergency and nonemergency	Nonemergency	Emergency and nonemergency	Nonemergency	Emergency
Implementing partners	Governments and private entities	World Food Program and NGOs	Governments	Governments, agricultural trade organizations, inter-governmental organizations, NGOs, and cooperatives	Governments, private entities, inter-governmental organizations	See implementing partners for Title II, Title III, and Food for Progress programs

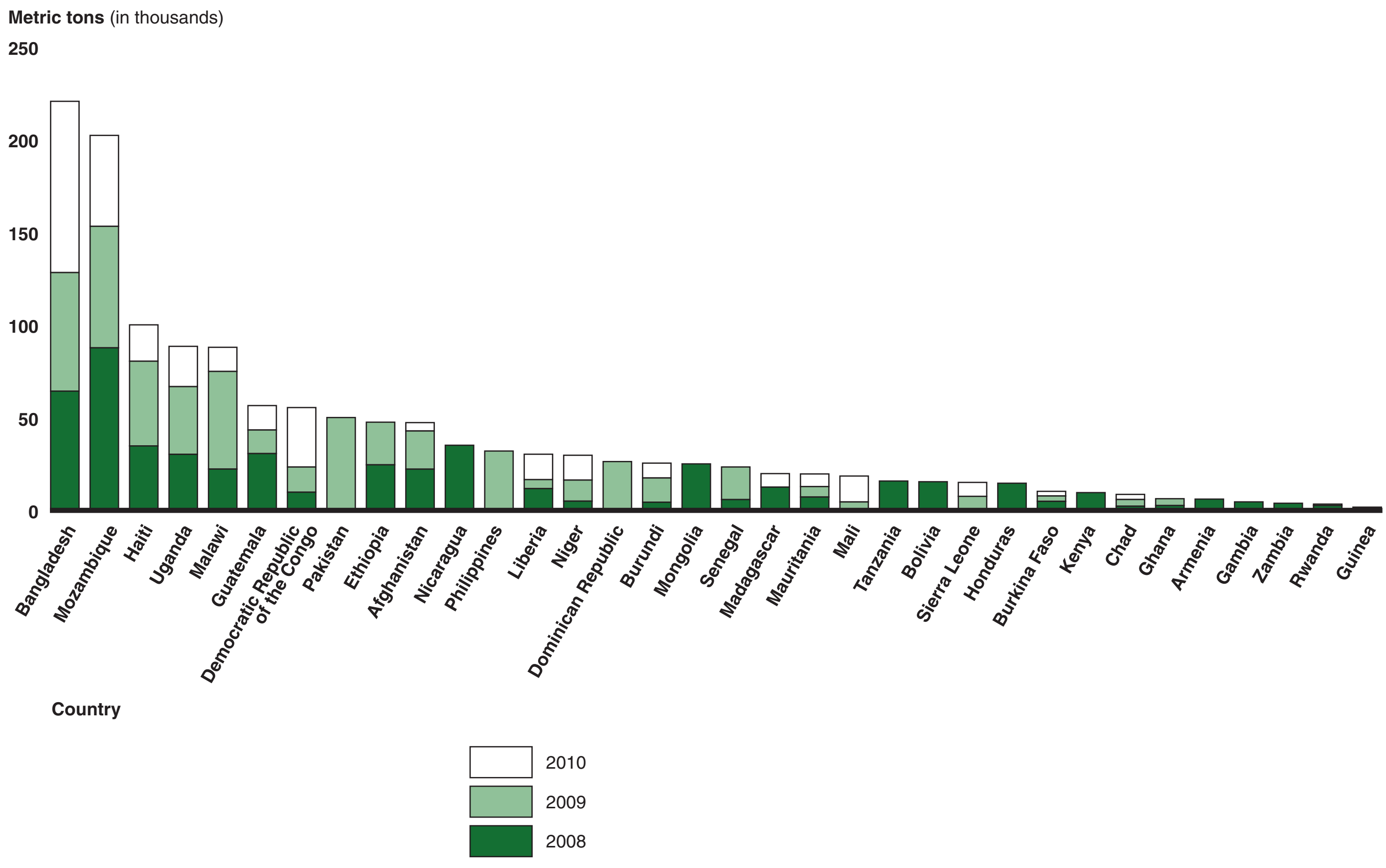
Sources: GAO analysis of USAID and USDA data.

Note: Programs that allow for monetization are shaded in grey.

Appendix IV: Total Volume and Commodities Programmed for Monetization by Country from Fiscal Years 2008 through 2010

As previously mentioned, between fiscal years 2008 and 2010, more than 1.3 million metric tons of food aid were programmed for monetization in 34 countries. Figure 10 shows the total volume of commodities programmed for monetization in each country by the U.S. Agency for International Development (USAID) and U.S. Department of Agriculture (USDA) between fiscal years 2008 and 2010. Table 9 shows the volume of each commodity programmed for monetization by country, program, and year. Figure 11 provides a percentage breakdown of the commodities programmed for monetization by USAID and USDA between fiscal years 2008 and 2010.

Figure 10: Total Volume Programmed for Monetization by USDA and USAID by Country and Year between Fiscal Years 2008 and 2010



Source: GAO analysis of Kansas City Commodity Office (KCCO) data.

Table 9: Volumes of Commodity Programmed for Monetization by Country, Program, and Fiscal Year between Fiscal Years 2008 and 2010

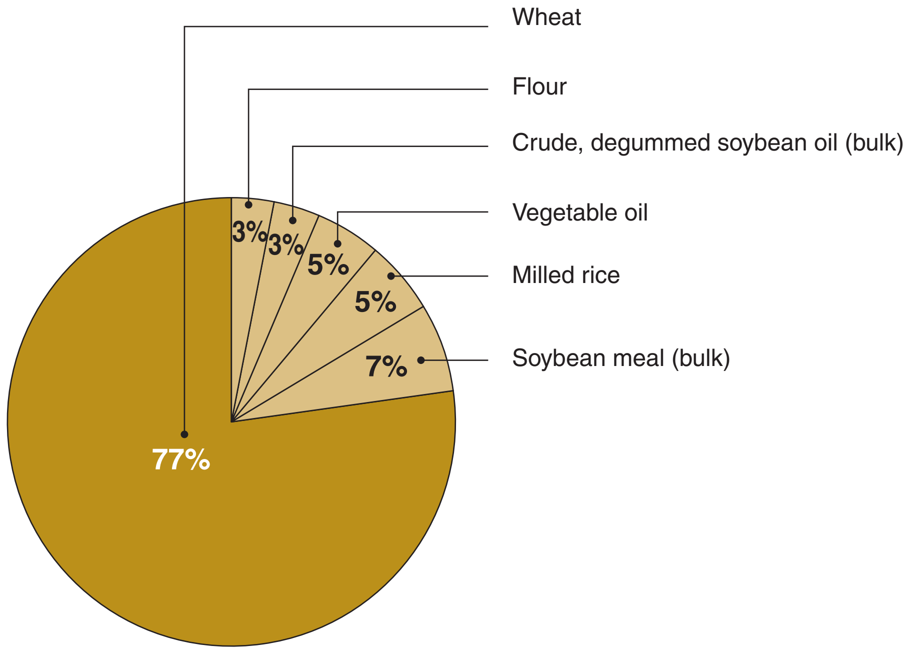
Country	Commodity	Program	Fiscal year 2008 (metric tons)	Fiscal year 2009 (metric tons)	Fiscal year 2010 (metric tons)	Grand total (metric tons)
Afghanistan	Bread flour	Food for Progress	10,940	0	0	10,940
	Hard red winter wheat (bulk)	Food for Progress	0	10,000	0	10,000
	Vegetable oil	Food for Progress	11,210	10,600	4,500	26,310
Armenia	Soybean meal (bulk)	Food for Progress	6,000	0	0	6,000
Bangladesh	Crude, degummed soybean oil (bulk)	Food for Progress	0	4,850	0	4,850
	Hard red winter wheat (bulk)	Food for Peace	39,380	0	0	39,380
	Soft white wheat (bulk)	Food for Peace	24,860	59,120	92,380	176,360
Bolivia	Hard red winter wheat (bulk)	Food for Progress	15,370	0	0	15,370
Burkina Faso	Milled rice	Food for Peace	4,780	2,910	2,500	10,190
Burundi	Hard red winter wheat (bulk)	Food for Peace	4,310	13,090	8,000	25,400
Chad	Bread flour	Food for Peace	2,180	3,600	2,760	8,540
Democratic Republic of Congo	Hard red winter wheat (bulk)	Food for Peace	9,710	13,600	32,070	55,380
Dominican Republic	Crude, degummed soybean oil (bulk)	Food for Progress	0	1,250	0	1,250
	Northern spring wheat (bulk)	Food for Progress	0	25,000	0	25,000
Ethiopia	Hard red winter wheat (bulk)	Food for Progress	20,000	23,000	0	43,000
	Vegetable oil	Food for Peace	4,490	0	0	4,490
Gambia	Vegetable oil	Food for Progress	4,500	0	0	4,500
Ghana	Hard red winter wheat (bulk)	Food for Peace	2,540	3,680	0	6,220
Guatemala	Crude, degummed soybean oil (bulk)	Food for Peace	5,420	6,730	13,170	25,320
	Soybean meal (bulk)	Food for Education	10,140	5,990	0	16,130
		Food for Progress	15,000	0	0	15,000
Guinea	Vegetable oil	Food for Peace	1,000	650	0	1,650
Haiti	Bread flour	Food for Peace	0	0	19,000	19,000
	Hard red winter wheat (bulk)	Food for Peace	34,690	45,710	0	80,400
	Vegetable oil	Food for Peace	0	0	600	600

Country	Commodity	Program	Fiscal year 2008 (metric tons)	Fiscal year 2009 (metric tons)	Fiscal year 2010 (metric tons)	Grand total (metric tons)
Honduras	Northern spring wheat (bulk)	Food for Peace	5,760	0	0	5,760
	Soybean meal (bulk)	Food for Progress	8,800	0	0	8,800
Kenya	Northern spring wheat (bulk)	Food for Peace	9,500	0	0	9,500
Liberia	All purpose flour	Food for Peace	0	0	1,900	1,900
	Bread flour	Food for Progress	1,000	0	0	1,000
	Hard red winter wheat	Food for Peace	0	0	1,180	1,180
	Milled rice	Food for Progress	8,300	0	0	8,300
		Food for Peace	0	4,860	10,110	14,970
	Vegetable oil	Food for Progress	2,360	0	0	2,360
		Food for Peace	0	0	500	500
Madagascar	Hard red winter wheat (bulk)	Food for Progress	12,450	0	0	12,450
	Vegetable oil	Food for Peace	0	0	7,300	7,300
Malawi	Crude, degummed soybean oil (bulk)	Food for Peace	3,050	1,550	1,500	6,100
	Hard red spring wheat (bulk)	Food for Progress	0	10,000	0	10,000
	Hard red winter wheat	Food for Progress	10,000	0	0	10,000
	Hard red winter wheat (bulk)	Food for Peace	9,140	21,140	11,500	41,780
	Northern spring wheat (bulk)	Food for Progress	0	20,001	0	20,001
Mali	Hard red winter wheat (bulk)	Food for Progress	0	0	10,000	10,000
	Vegetable oil	Food for Peace	0	4,460	3,980	8,440
Mauritania	Hard red winter wheat (bulk)	Food for Peace	7,110	0	6,810	13,920
	Soft red winter	Food for Peace	0	5,650	0	5,650
Mongolia	Hard red winter wheat (bulk)	Food for Progress	25,000	0	0	25,000
Mozambique	Hard red winter wheat (bulk)	Food for Progress	56,660	20,000	0	76,660
		Food for Peace	30,940	45,560	49,040	125,540
Nicaragua	Crude, degummed soybean oil (bulk)	Food for Progress	1,000	0	0	1,000
	Northern spring wheat (bulk)	Food for Progress	27,340	0	0	27,340
		Food for Peace	6,710	0	0	6,710

Country	Commodity	Program	Fiscal year 2008 (metric tons)	Fiscal year 2009 (metric tons)	Fiscal year 2010 (metric tons)	Grand total (metric tons)
Niger	Milled rice	Food for Peace	0	11,360	13,380	24,740
	Vegetable oil	Food for Progress	4,910	0	0	4,910
Pakistan	Soft white wheat (bulk)	Food for Progress	0	50,000	0	50,000
Philippines	Soybean meal (bulk)	Food for Progress	0	31,930	0	31,930
Rwanda	Vegetable oil	Food for Peace	2,540	760	0	3,300
Senegal	Crude, degummed soybean oil (bulk)	Food for Progress	2,840	4,200	0	7,040
	Milled rice	Food for Peace	2,900	2,390	0	5,290
	Soybean meal (bulk)	Food for Progress	0	11,000	0	11,000
Sierra Leone	Bread flour	Food for Peace	0	0	1,900	1,900
	Hard red winter wheat (bulk)	Food for Peace	0	7,500	0	7,500
	Milled rice	Food for Peace	0	0	5,550	5,550
	Vegetable oil	Food for Peace	0	0	50	50
Tanzania	Northern spring wheat (bulk)	Food for Progress	15,750	0	0	15,750
Uganda	Hard red winter wheat (bulk)	Food for Progress	0	15,000	0	15,000
		Food for Peace	30,140	21,550	21,710	73,400
Zambia	Hard red winter wheat (bulk)	Food for Peace	3,760	0	0	3,760
Grand total			**514,480**	**518,691**	**321,390**	**1,354,561**

Source: GAO analysis of KCCO data.

Figure 11: Commodities Programmed for Monetization by USDA and USAID between Fiscal Years 2008 and 2010



Source: GAO analysis of KCCO data.

Appendix V: Steps in the Monetization Process from Grant Proposal to Development Project Completion

The following table further outlines the steps in the monetization process from grant application through development project completion depicted in figure 3.

Table 10: Steps in the Monetization Process from Grant Proposal to Development Project Completion

Step 1: Grant proposal
• The U.S. Agency for International Development (USAID) and the U.S. Department of Agriculture (USDA) independently issue calls for proposals and approve proposals at different times, based on each agency's individual guidelines and priorities. • Market assessments are considered in the application process to address Bellmon requirements. • Grant proposals for both agencies must include, among other things, information on the commodity to be monetized, commodity volumes requested, estimated sales price, estimated cost recovery, and projects that will be implemented based on the estimates.
Step 2: Grant award
• USAID evaluates the proposals and makes award decisions. USAID provides multi-year grants that can last for 3 to 5 years. USAID grants generally include a combination of food aid for direct distribution and monetization. Grants specify the amount of commodities granted to an implementing partner for monetization. • USDA evaluates the proposals and makes award decisions. USDA provides multi-year grants that can last 1 to 3 years. USDA authorizes 100 percent monetization grants, but some can include food for direct distribution. The grant agreements specify the volume of commodities granted to an implementing partner for monetization.
Step 3: Call forward
• As a general practice USAID and USDA require implementing partners to obtain sale contacts before submitting a call forward (request order) for food shipments. • Implementing partners seek potential buyers in-country through open tender/bidding (the preferred method of sale by USAID and USDA) or direct negotiation. • Implementing partners enter into sales contracts with buyers; these contracts specify the terms of delivery and sales prices.
Step 4: Procurement
• The implementing partner submits a commodity request to USAID's Office of Food for Peace (FFP) or USDA's Foreign Agriculture Service (FAS). • USAID-FFP or USDA-FAS reviews and approves the commodity request or call forward and sends it to USDA's Farm Service Agency's Kansas City Commodity Office (KCCO) through the Web-Based Supply Chain Management System. • KCCO issues invitation for bids to commodity vendors and ocean freight bids to ocean carriers to offer their products to USDA, makes recommendations to USAID-FFP or USDA-FAS as to the reasonableness of the commodity prices, and procures commodities as instructed. • Commodity vendor delivers commodities to the ocean vessel either at the vendor's facility (plant), a bridge location, or a domestic port, based on the terms of the contract.

Step 5: Shipping and delivery

Ocean transport

- The implementing partners select a licensed freight forwarder to arrange for shipment to the recipient country.
- The freight forwarder receives offers from steamship companies interested in transporting commodities. These offers are combined with commodity offers and evaluated to determine the lowest landed cost to purchase and ship the commodities.
- Implementing partners obtain information from USAID or USDA on the lowest landed cost and award ocean transportation contracts based on this information, provided the vessels can meet their programmatic needs.
- USAID’s Transportation Division and USDA-FAS, with input from the Department of Transportation’s Maritime Administration, confirm that the rates received from the ocean carrier are fair and reasonable in those cases where a fair and reasonable rate guideline is required.
- Ocean vessel departs from the domestic port.
- Ocean vessel arrives at the foreign port.

Discharge and delivery to purchaser

- The commodities are delivered to the implementing partner in the beneficiary country; the implementing partner executes the sales contract and collects payment from the buyer.
- The implementing partner can take possession of the commodities either at the ocean vessel or at its final destination, or possession can be transferred to the buyer at the port, depending on sales contract.
- Some host government officials conduct quality inspections by sampling and testing the commodities.

Step 6: Development project implementation

- Development projects funded through monetization are expected to address food insecurity in priority countries.
- Development projects funded by USAID through monetization include programs to improve and promote sustainable agricultural production and marketing, natural resource management, nonagricultural income generation, health, nutrition, water and sanitation, education, emergency preparedness and mitigation, vulnerable group feeding, and social safety nets.
- According to USDA, development projects funded by USDA through monetization should focus on private sector development of agricultural sectors such as improved agricultural techniques, marketing systems, and farmer education. Figure 4 provides examples of USAID and USDA projects funded through monetization in countries that we visited.

Step 7: Development project completion

- Implementing partners provide status reports to USAID or USDA.
- Implementing partners complete the projects and fulfill their close-out requirements.

Sources: GAO based on information provided by USAID and USDA.

Note: This is a general description of the monetization process, not every step may be included, and steps may vary from transaction to transaction.

Appendix VI: Results from Survey of Implementing Partners

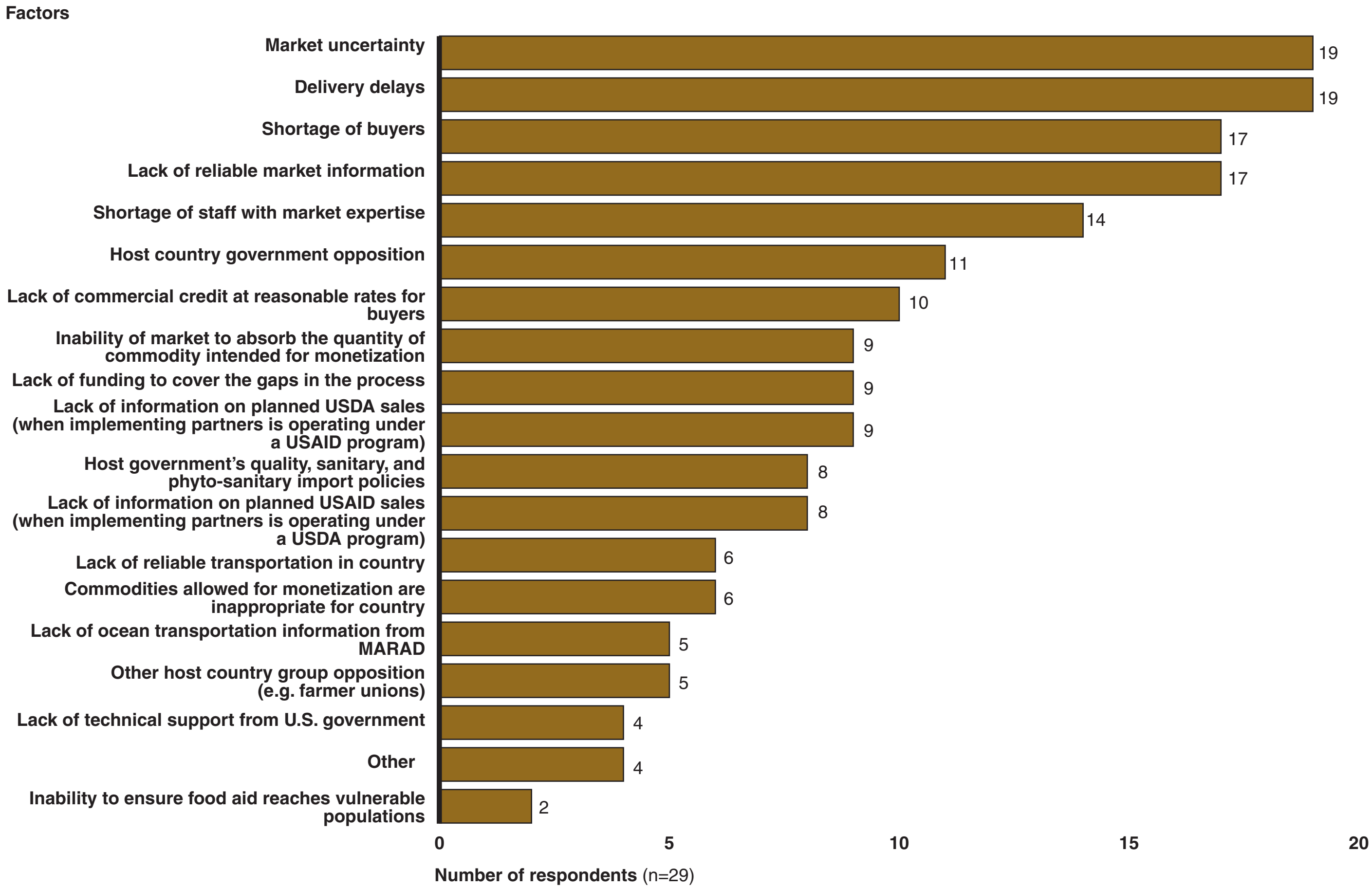
We conducted a survey of 29 implementing partners that monetized either through U.S. Agency for International Development (USAID) or and U.S. Department of Agriculture (USDA) between fiscal years 2008 and 2010, and we received a 100 percent response rate. Of the 29 implementing partners, 6 monetized through USAID only, 13 monetized through USDA only, and 10 monetized through both agencies. The tables that follow summarize selected results of the implementing partners' responses to our survey.

Table 11: Distribution of Implementing Partners Who Monetized in Consortiums versus Monetizing Only Their Own Food Aid

In general, do you only monetize your organization's own food aid?		Do you coordinate with other implementing partners in a monetization consortium?		
		No	**Yes**	**Total**
Yes	10	3	1	**14**
No	0	1	14	**15**
Total	**10**	**4**	**15**	**29**

Source: GAO analysis.

Figure 12: Number of Implementing Partners Indicating that the Following Factors Hindered Them to At Least Some Degree When Conducting Monetization



Source: GAO analysis.

Table 12: Ways in Which USAID and USDA Provided Support to Implementing Partners During Monetization

	USAID implementing partners (n=16)		USDA implementing partners (n=23)	
	Yes	No	Yes	No
Technical assistance (beyond the BEST) with market analysis	4	12	10	12
Facilitating contacts within host government	8	8	10	12
Facilitating business contacts in country	2	14	7	15
Workshops for conducting monitoring and evaluation of the monetization process	2	14	5	17
Telling implementing partners when to monetize	2	14	5	17
Telling implementing partners when not to monetize	6	10	4	18
Other	2	4	3	5

Source: GAO analysis.

Table 13: Formats in Which Implementing Partners Collected and Reported Monetization Information to USAID and USDA

	USAID implementing partners (n=16)		USDA implementing partners (n=23)	
	Yes	No	Yes	No
Quarterly reports	6	9	14	7
Annual results reports	15	0	11	9
Pipeline and resource estimate proposal reports	15	0	1	18
End of project report	14	1	17	4
Cost recovery reports	13	2	7	13
Assessment of post-monetization market impact	5	10	2	17
Logistics and monetization reports	5	10	0	22
Other	3	5	6	4

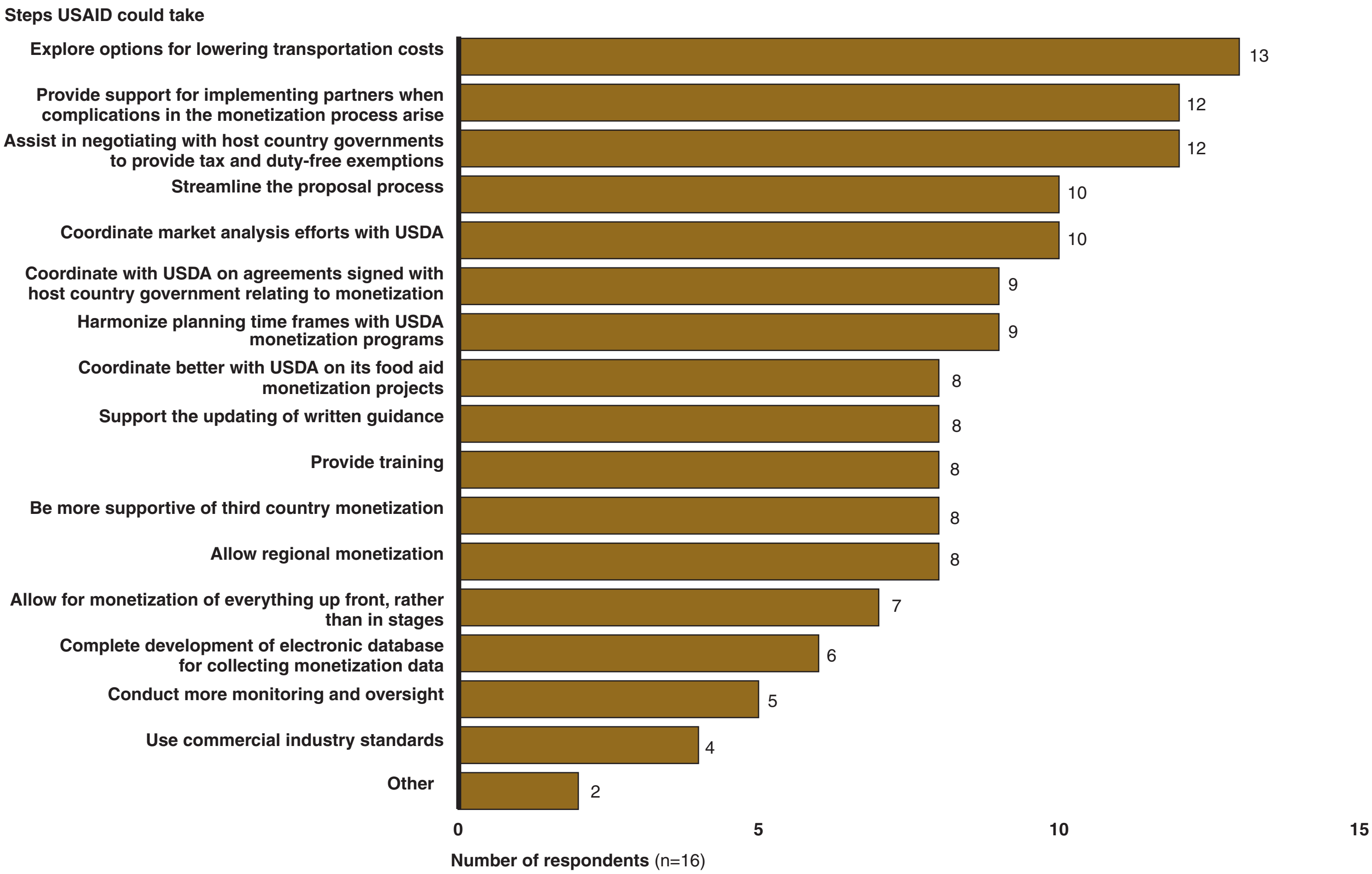
Source: GAO analysis.

Table 14: Implementing Partners' Assessment of the Quality of Coordination between USAID and USDA on Monetization in Country

	All implementing partners (n=29)
Very poor	3
Poor	8
Fair	8
Good	5
Very good	0

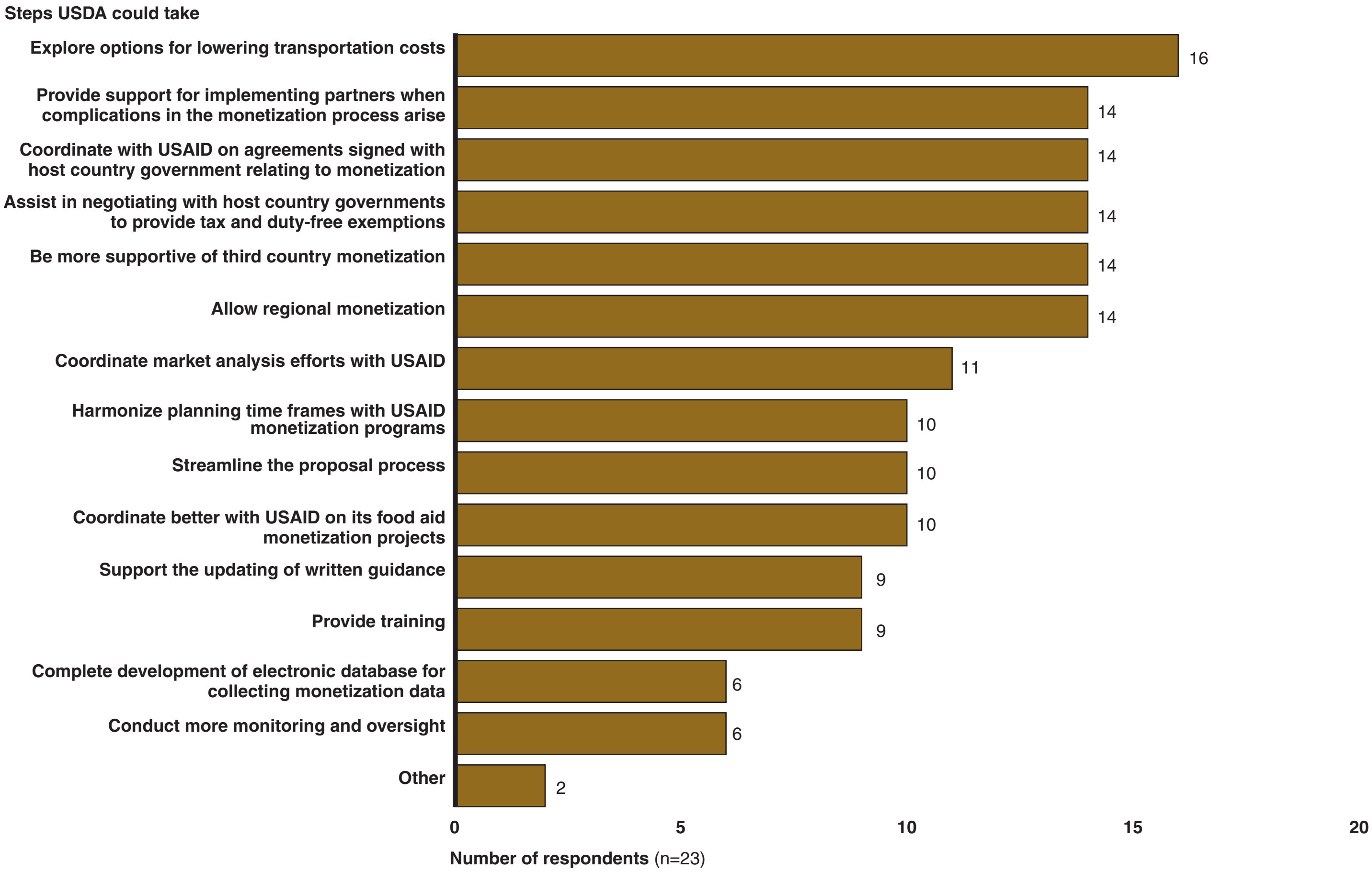
Source: GAO analysis.

Figure 13: Number of Implementing Partners Indicating that the Following Steps, if Taken by USAID, Could Greatly or Very Greatly Improve the Monetization Process



Source: GAO analysis.

Figure 14: Number of Implementing Partners Indicating that the Following Steps, if Taken by USDA, Could Greatly or Very Greatly Improve the Monetization Process



Source: GAO analysis.

Table 15: Types of Market Analysis Examined by Implementing Partners Prior to Monetization

	USAID-only implementing partners (n=6)	USDA-only implementing partners (n=13)	USAID and USDA implementing partners (n=10)	All implementing partners (n=29)
Their organization's market analysis	5	11	10	26
Third party contractor's assessment	4	11	6	21
Agricultural attaché reports	3	10	7	20
Usual marketing requirement (UMR)	4	7	8	19

	USAID-only implementing partners (n=6)	USDA-only implementing partners (n=13)	USAID and USDA implementing partners (n=10)	All implementing partners (n=29)
BEST market analysis done by Fintrac	5	4	9	18
FEWSNET reports	3	8	6	17
USDA's Production, Supply, and Distribution (PSD) online database	3	5	6	14
Other	0	3	2	5

Source: GAO analysis.

Table 16: The Number of Implementing Partners Reporting that the Market Analysis on Which Commodities to Monetize was Sufficient

Type of analysis	USAID-only implementing partners (n=6)	USDA-only implementing partners (n=13)	USAID and USDA implementing partners (n=10)	All implementing partners (n=29)
BEST	5	4	8	17
UMR	4	7	4	15

Source: GAO analysis.

Table 17: The Number of Implementing Partners Reporting that the Market Analysis on How Much to Monetize was Sufficient

Type of analysis	USAID-only implementing partners (n=6)	USDA-only implementing partners (n=13)	USAID and USDA implementing partners (n=10)	All implementing partners (n=29)
BEST	3	2	8	13
UMR	3	7	4	14

Source: GAO analysis.

Table 18: The Number of Implementing Partners Reporting that the Market Analysis on When to Monetize was Sufficient

Type of analysis	USAID-only implementing partners (n=6)	USDA-only implementing partners (n=13)	USAID and USDA implementing partners (n=10)	All implementing partners (n=29)
BEST	2	3	5	10
UMR	0	5	0	5

Source: GAO analysis.

Table 19: Methods Used by Implementing Partners to Calculate Cost Recovery

	USAID-only implementing partners(n=6)	USDA-only implementing partners (n=13)	USAID and USDA implementing partners (n=10)	All implementing partners (n=29)
Follow guidance provided by USAID	6	1	9	16
Follow guidance provided by USDA	0	5	3	8
Follow their own calculation	2	8	2	12
Other	0	3	0	3

Source: GAO analysis.

Table 20: Methods Used by Implementing Partners to Calculate Fair Market Price

	USAID-only implementing partners (n=6)	USDA-only implementing partners (n=13)	USAID and USDA implementing partners (n=10)	All implementing partners (n=29)
Follow guidance provided by USAID	4	1	6	11
Follow guidance provided by USDA	0	5	3	8
Follow their own calculation	3	9	8	20
Use Import parity price as an estimation	3	3	5	11
Other	1	1	1	3

Source: GAO analysis.

Table 21: Number of Implementing Partners Who Included Other Costs When Calculating their Organization's Cost Recovery

	All implementing partners (n=29)
Import fees or duties on monetized commodities	13
Transaction fees paid to the host country government	9
Hiring local host country staff specifically to conduct monetization	8
Additional U.S. staff	6
Outside contractors to do market assessments	5
Other	4

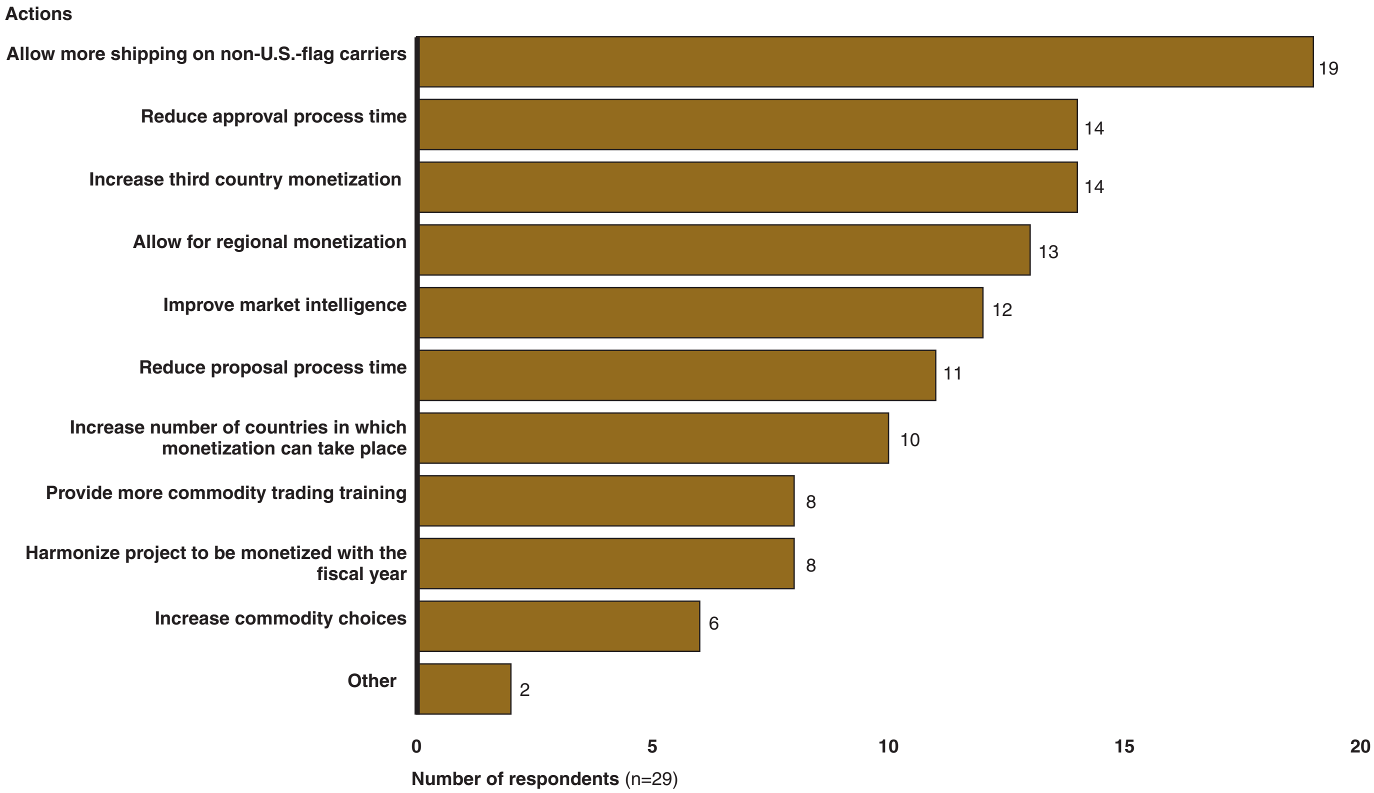
Source: GAO analysis.

Table 22: Implementing Sponsors' Views of How Often Monetization Transactions Experience Delays

	All implementing partners (n=29)
Very Often	1
Often	11
Sometimes	15
Rarely	2
Never	0

Source: GAO analysis.

Figure 15: Number of Implementing Partners Indicating that the Following Actions Would Greatly Improve or Very Greatly Improve Cost Recovery Rates



Source: GAO analysis.

Appendix VII: Comments from the U.S. Agency for International Development

Note: GAO received USAID's letter on June 14, 2011.

USAID
FROM THE AMERICAN PEOPLE

Thomas Melito
Director, International Affairs and Trade
U.S. Government Accountability Office
Washington, DC 20548

Dear Mr. Melito:

I am pleased to provide the U.S. Agency for International Development's formal response to the GAO draft report entitled "International Food Assistance: Funding Development through the Purchase, Shipment and Sale of U.S. Commodities is Inefficient and Can Cause Adverse Market Impacts " (GAO-11-636).

The enclosed USAID comments are provided for incorporation with this letter as an appendix to the final report.

Thank you for the opportunity to respond to the GAO draft report and for the courtesies extended by your staff in the conduct of this audit review.

Sincerely,

Sean C. Carroll
Chief Operating Officer
U.S. Agency for International Development

Enclosure: a/s

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USAID COMMENTS ON GAO DRAFT REPORT No. GAO-11-636

To improve the extent to which monetization proceeds cover commodity and other associated costs and the agencies' ability to meet requirements to ensure that monetization does not cause adverse market and trade impacts:

Recommendation 1: We recommend that the Administrator of USAID and the Secretary of Agriculture jointly develop an agreed-upon benchmark or indicator to determine "reasonable market price" for sales of US food aid for monetization.

Management Comments: Section 403 of the Food for Peace states that the "Sales of agricultural commodities…shall be made at a reasonable market price in the economy where the agricultural commodity is to be sold…." To date, USAID has not utilized a specific cost recovery barometer. USAID will work with USDA to explore options of setting a benchmark or indicator for the sales of U.S. food aid monetization.

Recommendation 2: We recommend that the Administrator of USAID and the Secretary of Agriculture monitor food aid sales transactions to ensure that the benchmark set to achieve "reasonable market price" in the country where they are being sold is achieved as required by law.

Management Comments: USAID has regional and country-based food aid monitoring & evaluation specialists who review all aspects of USAID food aid programs including monetizations sales.

Recommendation 3: We recommend that the Administrator of USAID and the Secretary of Agriculture improve market assessments and coordinate to develop them in countries where both USAID and USDA may monetize.

Management Comments: To improve market assessments and conduct independent market analyses, USAID established the Bellmon Estimation for Title II (BEST) Project. Standard methodological approaches have been designed and applied for assessing the potential impacts of monetized food aid. This project is well accepted by USAID food aid implementing partners. The information collected by the BEST Project is posted on the USAID public website and is accessible to all interested parties. Additionally, USAID is also in the process of updating our *Field Monetization Manual* which includes market assessment guidance.

Recommendation 4: We recommend that the Administrator of USAID and the Secretary of Agriculture conduct market impact evaluations after monetization transactions have taken place to determine whether they caused adverse market impacts.

Management Comments: USAID food aid implementing partners are requested to stay abreast of the conditions of the markets in which they monetize food aid. Implementing partners are required to provide considerable information in their proposals related to the local, national and regional markets, especially for those markets that could be affected by the proposed

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monetization programs. USAID will explore possible cost-effective ways to conduct post-sale market impact evaluations with our partners.

Appendix VIII: Comments from the U.S. Department of Agriculture

Note: GAO comments supplementing those in the report text appear at the end of this appendix.

USDA

United States Department of Agriculture

Farm and Foreign Agricultural Services

1400 Independence Ave, SW
Stop 1034
Washington, DC
20250-1034

JUN 1 0 2011

Mr. Thomas Melito
Director, International Affairs and Trade Team
United States Government Accountability Office
441G Street, N.W.
Washington, D.C. 20548

Dear Mr. Melito:

The U.S. Department of Agriculture (USDA) appreciates this opportunity to respond to the Government Accountability Office (GAO) draft report "Funding Development through the Purchase, Shipment, and Sale of Commodities is Inefficient and Can Cause Adverse Market Impacts" (GAO-11-636). The report provides valuable insights regarding the monetization of U.S. commodities for development projects in the Food for Progress and Food for Peace programs. Many of the recommendations are consistent with our understanding of monetization and will be useful in ongoing efforts to generate cash development resources and improve program management.

General Comments

This GAO report and recommendations will help USDA improve overall program management. The Department will be able to manage, monitor, and evaluate the monetization process better, particularly by focusing resources on achieving higher prices for the monetized commodities, and by better coordinating our resources with those of the U.S. Agency for International Development (USAID).

In the report, GAO uses the spread between the final monetization sales price and USDA's total costs as a means to measure efficiency. This definition of efficiency is clearly intuitive and easily calculated to provide useful information for program administrators.

See comment.

However, there are additional benefits not captured by this definition of efficiency. In addition to the economic benefits of development projects funded by monetization, these sales can encourage commercial markets for agricultural products and enhance the sophistication of participants in the market. This is an especially important outcome in countries that receive funding from the Food for Progress program. In fact, many countries in the Former Soviet Union and Africa received this market-building benefit as they were taking steps toward private enterprise.

Participants in USDA monetizations also often benefit from the sales process itself. Unlike cash grants and food aid distributions, monetizations are market-mediated, encourage the development of private sector institutions, and can stimulate the emergence of a competitive domestic food distribution channel. USDA is aware of many instances where the monetization of a U.S. product helped developing country traders enter into new markets and use more sophisticated trading instruments such as letters of credit, credit insurance, and other risk management tools.

Mr. Thomas Melito
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Two examples provide insight into the benefits of monetization. In Kenya, a U.S.-based private voluntary organization monetized wheat in 2005 that provided funds for an agricultural development project. Follow-on commercial sales of wheat were recorded in both 2010 and 2011. Millers in Kenya reported that they became familiar with the quality of imported wheat through food aid monetizations and grew to understand its superior milling characteristics. A second example is from Afghanistan, where soybean oil was provided through a 2006 government-to-government agreement. Afghan buyers of U.S. soybean oil participated in an open auction managed by a professional monetization agency. These auctions exposed Afghan traders to a competitive bidding process, in which that they had no previous experience. This ancillary benefit, while certainly difficult to calculate, was not captured in the GAO report.

Costs of Monetization

The Department has been actively exploring ways to reduce the cost of food aid shipments, including those designated for monetization. One example is a food aid agreement with the Government of the Philippines (GOP) that required the GOP to pay for the cost of ocean transportation. Through this, the Food for Progress program realized approximately $1.3 million in freight savings. USDA also reviews commodity selections and specifications to make sure that commodities fit the market and mesh with the traditional standards in the market. During the procurement process, USDA looks for shipments that can be combined so that volume discounts can be obtained. USDA's implementing organizations regularly re-tender for ocean freight when the offers are considered to be high or when ship availability is an issue.

Joint Development of an Agreed upon Benchmark to Determine a Reasonable Market Price

As recommended in the report, USDA will work with USAID to develop improved benchmarks for reasonable local market prices. Setting ranges for reasonable local market prices is challenging given the lack of market information in many recipient countries. Under current practices, implementing organizations regularly survey the local market and establish price ranges. The use of public tenders and establishment of floor prices provide safeguards which limit disruptions to local production and markets.

In this report, GAO uses the Import Parity Price (IPP) to identify the extent to which a monetization transaction is a normal commercial transaction in a market setting. The use of IPP is relevant when comparing like products to each other; for example, comparing locally produced rice in Nigeria to rice imported from Liberia, on similar terms of delivery, quantity, and quality.

However, this methodology has limitations when comparing a product shipped from the United States to one locally produced or imported from a nearby market. The quality of the product from the United States will usually be higher and would command a premium

Mr. Thomas Melito
Page 3

price in a developed market. Obtaining that price premium in less developed markets is difficult.

In its grant agreements, USDA requires sales contracts and financing arrangements to be in place before a commodity can be purchased in the United States. These requirements reduce credit and contractual risks. While this benefits implementing organizations, it is accomplished by having the buyer absorb additional price risk during the time between the execution of the sales contract and financing, and the actual delivery of the commodity. Buyers often offer reduced prices to compensate for this greater price risk.

Monitor Food Aid Sales Transactions to Ensure that the Reasonable Market Price is Achieved

Regarding the monitoring of food aid sales transactions, USDA will work with its network of attachés and enhance its reporting system to improve the monitoring of market prices. Since January 2010, USDA has hired four new staff members in order to devote more resources to reviewing project reports and conducting site visits. USDA has also tripled the number of site visits to monetization projects since 2009, and has established a target of assessing each project in the field at least once every two years. USDA also has developed a field monitoring guide for staff in order to standardize the results of monitoring trips. USDA will work to establish a systematic process for choosing which projects to visit, and will finalize its monitoring guidance.

As noted by GAO, USDA will complete its Food Aid Information System (FAIS) by the end of this fiscal year. This system will enable USDA to manage its food assistance programs and coordinate interactions with food assistance program participants. Future program participants will be required to submit all required reports through FAIS. FAIS will allow USDA track reported results against the requirements in the grant agreements. With FAIS and additional staff, USDA will be able to monitor program implementation and engage more quickly with implementing organizations.

Improve Market Assessments and Coordinate to Develop Them in Countries Where Both USDA and USAID May Monetize

USDA will work with USAID to ensure that coordinated monetization objectives are achieved. USDA is impressed by the quality and overall depth of analysis provided by the Bellmon Estimation for Title II (BEST) project, funded by USAID. We will continue to encourage USDA program participants to review the BEST studies where applicable. Further, USDA will conduct an ad-hoc analysis of its own to identify opportunities to improve cost recovery. We will focus additional resources for monitoring and evaluation on coordination with USAID on monetization.

Mr. Thomas Melito
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Conduct Market Impact Evaluations after Monetization Transactions Have Taken Place

USDA and USAID will explore options for market impact evaluations. Currently, USDA requires all participants to describe in detail the outcomes of their monetization transactions in twice-a-year mandatory reporting. Further, USDA revised its regulations in 2008 to require mid-term and final evaluations of its programs. USDA will consider adding market impact requirements to its policy guidance for these evaluations. Currently USDA is administering a pilot project on Local and Regional Procurement, which requires extensive tracking of market impacts. Lessons learned from that pilot and the upcoming third-party evaluation will be incorporated into the Food for Progress program where appropriate.

USDA again thanks GAO for its review of monetization and appreciates many of its finding and recommendations. All GAO comments and recommendations will be taken into account as USDA works to finalize all needed policies and procedures.

Sincerely,

Michael T. Scuse
Acting Under Secretary
Farm and Foreign Agricultural Services

The following are GAO's comments on the U.S. Department of Agriculture letter dated June 10, 2011.

GAO Comment

The U.S. Department of Agriculture noted some advantages in addition to the economic benefits of development projects funded by monetization, such as encouraging commercial markets for agricultural products and other market-building benefits. However, the potential for adverse market impacts, such as artificially suppressing the price of a commodity due to excessive monetization, could work against the agricultural development goals for which the funding was originally provided.

Appendix IX: Comments from the U.S. Department of Transportation

Note: GAO comments supplementing those in the report text appear at the end of this appendix.

U.S. Department of Transportation
Office of the Secretary of Transportation

JUN 1 4 2011

1200 New Jersey Avenue, SE
Washington, DC 20590

Mr. Thomas Melito
Director, International Affairs and Trade
U.S. Government Accountability Office
441 G Street, N.W.
Washington, D.C. 20548

Dear Mr. Melito,

See comment 1.

While the Department of Transportation and its Maritime Administration (MARAD) appreciates GAO's efforts over the years to bring a more business-like approach to ocean shipping for the Nation's food aid programs, we have significant concerns regarding the nature and basis of findings pertaining to ocean shipping in the current draft report. The GAO report offers a Matter for Congressional Consideration that is potentially detrimental to the U.S. maritime industry,[1] without offering a complete analytical perspective on the impact of the recommended action. Before offering such a far-reaching recommendation to the Congress, one would expect to see an analysis of the potential outcomes of the action on U.S.-flag carriers and the sustainability of the U.S. fleet, along with an overall quantitative analytical assessment of the potential costs and benefits of the action. Such analysis is not apparent in the draft report.

See comment 2.

The GAO draft report does not adequately recognize that food aid shipping agencies are reimbursed the cost differential between U.S.- and foreign-flag carriers. MARAD reimburses the additional cost of using U.S.-flag vessels to USAID and USDA through Ocean Freight Differential and excess freight payments, so these agencies are not financially affected by cargo preference requirements. Based on MARAD's analysis of the transportation costs for the P.L. 480 Title II food aid program, which includes an adjustment for the amount reimbursed by MARAD, we believe the costs identified in the GAO draft report are significantly overstated.

See comment 3.

Between fiscal year (FY) 2005 and 2009, transportation costs ranged from a low of 8.0 percent

[1] The GAO draft report suggests eliminating the 3-year waiting period imposed on foreign vessels that acquire US-flag registry before they are eligible to transport U.S. food aid cargos.

in FY 2008 to a high of 10.8 percent during FY 2005. These values are considerably less than the 33 percent asserted in the report.

See comment 4.

See comment 5.

The draft report's analysis is also unduly focused on the number of ships rather than their carrying capacity. MARAD records show that food aid cargo tonnage was 46 percent higher in FY 2010 than in FY 2002 despite using fewer ships. As a result, reaching a conclusion based on an analysis of the number of ships alone could yield misleading results.[2] Further, the GAO draft report's argument that competition has declined is not supported by any specific analysis of cargo freight bids. Finally, any decline in the number of US flag vessels should not adversely affect shipping costs as these vessels are subject to a cost-based rate limit imposed by MARAD.

The Congress created the Cargo Preference Program and applied it to food aid shipments in a way that provides vital support to the U.S.-flag fleet and the U.S. Merchant Marine to help maintain key defense capabilities while protecting the generosity of the American people in conveying food supplies to nations in need around the world. The Department continues to believe that more complete implementation of modern transportation contracting practices, including commercial principles of shared risks, supply chain partnerships, streamlined administration methods, and expedited payment methods offers potential savings to the American taxpayer while maintaining the generous level of support this nation now offers those in need.

We appreciate the opportunity to comment on this draft report. The attachment contains additional specific and technical comments on the draft report. Please contact Christopher J. McMahon, Acting Associate Administrator for Business and Finance Development on 202-366-7018 if there are any questions.

Sincerely,

Brodi L. Fontenot
Deputy Assistant Secretary
for Administration

See comment 6.

[2] MARAD is unable to replicate GAO's analysis of the decline in the number of food aid ships. MARAD data show that there were 84 ships in 2002, and 67 in 2010, a decrease of 20 percent, not the 50 percent drop portrayed in the report.

The following are GAO's comments on the U.S. Department of Transportation letter dated June 14, 2011.

GAO Comments

1. We are making this proposed amendment on the basis of the following four factors: First, the number of vessels participating in the food aid program has declined. In a 2009 report to Congress, U.S. Agency for International Development (USAID) and U.S. Department of Agriculture (USDA) jointly stated that, due to the declining size of the U.S.-flag commercial fleet, USAID and USDA are forced to compete with the Department of Defense and other exporters for space aboard the few remaining U.S.-flag vessels, thereby limiting competition in transportation contracting and leading to higher freight rates. Second, our analysis of ocean transportation costs showed that food aid shipments on foreign-flag carriers cost the U.S. government, on average, $25 per ton less than U.S.-flag carriers. Third, although the 3-year requirement was established to provide employment opportunities to U.S. shipyards, since 2005, U.S. shipyards have built only two new U.S.-flag vessels appropriate for transporting food and the vessels have not been awarded a food aid contract. Fourth, the 3-year requirement applies only to food aid and not to defense agencies and the U.S. Export-Import Bank. The elimination of the 3-year waiting period can ease entry of new vessels into U.S. food aid programs, with the potential to increase competition among eligible U.S.-flag ships and reduce the cost of transportation.

2. We added clarifying language to describe the U.S. Department of Transportation's reimbursement to USAID and USDA for the ocean freight differential (OFD). However, the OFD represents a cost to the U.S. government. In addition, according to USAID and USDA, the OFD reimbursements for monetization are transferred to the general food aid accounts of both agencies, can be used to fund either emergency or nonemergency programs, and are likely not fully available to fund development assistance.

3. Our analysis of transportation cost was based on Kansas City Commodity Office (KCCO) data covering all monetization transactions for both agencies for fiscal years 2008 through 2010 and is thus a precise calculation of the actual cost to the U.S. government.

4. In a 2009 report to Congress, USAID and USDA jointly stated that, due to the declining size of the U.S.-flag commercial fleet, USAID and USDA are forced to compete with the Department of Defense and other exporters for space aboard the few remaining U.S.-flag vessels,

thereby limiting competition in transportation contracting and leading to higher freight rates.

5. While we did not analyze cargo freight bids, our analysis of KCCO data included more than 5,000 food aid purchase transactions for fiscal years 2007 to 2010. We included in this data the number of vessels awarded all food aid contracts, not just Title II, by fiscal year and determined that both the number of vessels and the tonnage shipped per year had declined. We also determined the actual difference in cost to the U.S. government between U.S.- and foreign-flag vessels.

6. According to KCCO data, the number of U.S.-flag vessels awarded food aid contracts in fiscal year 2002 was 134.

Appendix X: GAO Contact and Staff Acknowledgments

GAO Contact

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Staff Acknowledgments

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