U.S. AGENCY FOR
INTERNATIONAL
DEVELOPMENT

March 29, 2000

MEMORANDUM

TO: BHR/FFP Director, William T. Oliver

FROM: IG/A/PA Director, Dianne L. Rawl Dianne L Rawl

SUBJECT: Audit of USAID's P. L. 480 Title II Monetization Programs (Audit Report No. 9-000-00-002-P)

This memorandum is our report on the subject audit. In preparing this report, we considered your written comments pertaining to our draft report and have included them as Appendix II.

This report includes two procedural recommendations. Based on your written comments we consider both Recommendation Nos. 1 and 2 to have received a management decision.

I appreciate the cooperation and courtesies your office extended to the members of our audit team during this audit.

Background

Despite budgetary constraints, the United States remains the world's major provider of international food assistance. In 1998, the United States provided 3.5 million metric tons, valued at $1.22 billion, to 67 developing and re-industrializing countries. Of this, USAID provided 1.92 million metric tons of food assistance, valued at almost $889 million, to 54 countries for emergency and non-emergency activities through Title II of the Agricultural Trade Development and Assistance Act of 1954, commonly known as Public Law (P. L.) 480.[1]

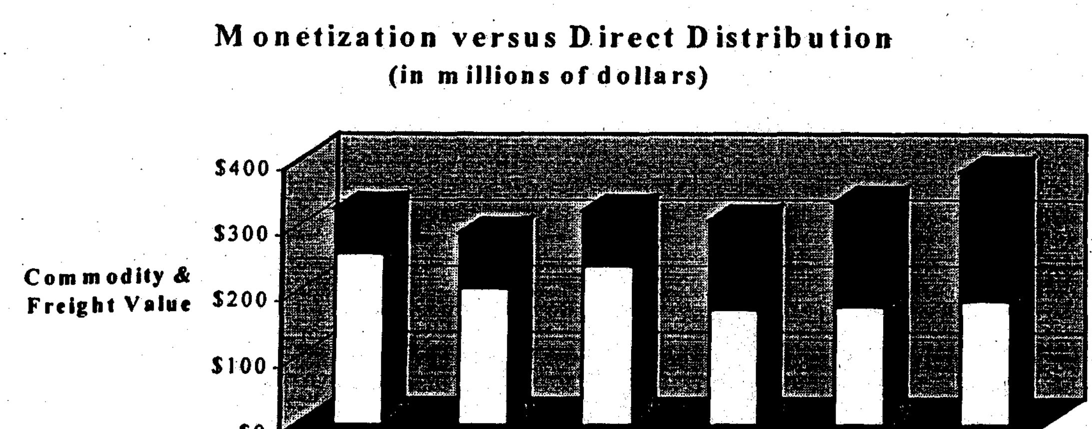
USAID provides P. L. 480 Title II agricultural commodities for non-emergency development assistance through private voluntary organizations and cooperatives acting as Cooperating Sponsors. Cooperating Sponsors may either distribute the commodities directly to recipients or sell the commodities to generate foreign currency to support local

[1] Other U.S. international food assistance programs were administered by the U.S. Department of Agriculture.

development programs. This selling of U.S. agricultural commodities by Cooperating Sponsors (turning food assistance into program funds) is referred to as monetization. The USAID office responsible for the management of P. L. 480 Title II monetization is the Office of Food for Peace (FFP) within the Bureau for Humanitarian Response.

Title II monetization began in 1986 in response to repeated requests by Cooperating Sponsors for additional funding to cover foreign currency costs associated with P. L. 480 food distribution programs. In recognition of these needs, Congress mandated that USAID permit Cooperating Sponsors to monetize annually at least five percent[2] of the total value of Title II non-emergency commodities. Initially, monetization proceeds were to be used exclusively for the logistical costs of feeding programs. Since then, the use of monetization proceeds has grown dramatically to become a critical resource for Cooperating Sponsors to implement a wide variety of developmental activities.

As a percentage of the dollar value of total non-emergency Title II commodities[3], monetization has increased from less than 25 percent in 1994 to just over 50 percent in 1999. In 1994, USAID approved monetization requests for commodities valued at approximately $71 million (over 200,000 metric tons). Five years later, USAID approved monetization requests for approximately $197 million (over 560,000 metric tons) of commodities—an increase of about 180 percent in both dollar value and tonnage.



	1994	1995	1996	1997	1998	1999
■ Monetization	$71	$86	$86	$137	$160	$197
□ Direct Distribution	$256	$204	$238	$172	$177	$186

[2] Amendments to P. L. 480 increased the minimum percentage of the aggregate value of non-emergency Title II commodities to be made available annually for monetization by Cooperating Sponsors from 5 percent to 10 percent in 1988 and 15 percent in 1996.

[3] The statistics in this paragraph refer only to Title II commodities provided to private voluntary organizations and cooperatives and do not include commodities provided for World Food Program activities.

FFP's *Monetization Field Manual* outlines policy and operational procedures that Cooperative Sponsors must use to design, implement, manage, and evaluate programs that use monetization proceeds. According to the field manual, Cooperating Sponsors should plan the actual process of monetization to meet three objectives, while also striving to "do no harm" to local producers' incentives, fragile local food markets, and low-income consumers. The three objectives for Title II monetization are:

- to generate the maximum feasible amount of foreign currency funds for Title II food security activities;
- to enhance household access to food, at least in the short run; and
- to encourage, where appropriate, the development of competitive food marketing systems.

To help ensure that Cooperating Sponsors accomplish the first objective, FFP established a "cost recovery benchmark" below which commodities may not be sold without a waiver by FFP.

Audit Objective

This audit began as a survey of issues related to USAID's management of P. L. 480 Title II monetization activities. We gathered information about USAID's worldwide monetization activities from 1994 through 1999 and talked to officials from several Cooperating Sponsors, FFP, and the U.S. Department of Agriculture (USDA) about current monetization issues, concerns, and trends. We also observed the monetization activities of five Cooperating Sponsors in two countries—Kenya and Uganda.

Several controversial issues surrounding the often-complex process of turning food into money surfaced during the audit. Central to discussions of monetization was the issue of cost recovery—the extent to which expenses incurred by the U.S. Government in procuring, transporting, and selling P. L. 480 Title II commodities are offset by the revenues realized when the commodities are ultimately sold. Sales that do not recoup purchase, shipping, and sales costs have attracted the attention of the U.S. General Accounting Office, Congress, and others. According to FFP, Congressional interest in determining whether U.S. farmers and taxpayers are deriving full benefits from this form of Title II food aid is increasing. We, therefore, decided to focus our audit efforts on the important issue of cost recovery. Accordingly, we designed our audit to answer the following question:

What level of cost recovery are USAID's Cooperating Sponsors achieving on sales of agricultural commodities under Public Law 480 Title II monetization programs?

To answer this question we reviewed records of monetization programs for 15 Cooperating Sponsors in 21 countries. We performed field visits to Kenya and Uganda where we reviewed, in detail, the planning, approval, implementation, monitoring, and results reporting of five Cooperating Sponsors. Our audit universe consisted of the worldwide fiscal year 1998 monetization activities of USAID-funded Cooperating Sponsor development programs, not including the World Food Program.

Appendix I contains a complete discussion of the scope and methodology for this audit.

Audit Findings

What level of cost recovery are USAID's Cooperating Sponsors achieving on sales of agricultural commodities under Public Law 480 Title II monetization programs?

We were generally unable to determine or confirm the actual level of cost recovery achieved by Cooperating Sponsors because FFP's guidance did not require that Cooperating Sponsors collect and report all the information needed to calculate actual cost recovery. Furthermore, even if cost information had been made available, FFP did not have a management information system designed to track, analyze, or report the actual costs of monetization.

FFP did take certain measures to help ensure the efficiency of P. L. 480 monetization transactions. For example, FFP established a cost recovery benchmark to act as a measure of accountability and to prevent sales that might otherwise be carried out with little regard for obtaining a 'fair market price.' When a Cooperating Sponsor did not expect to meet or exceed the cost recovery benchmark, it was required to submit a written waiver request for approval to the Director of FFP. Also, if two or more Cooperating Sponsors intended to conduct monetization activities in the same country, FFP strongly encouraged them to participate in a joint 'umbrella' monetization in order to minimize marketing costs, avoid duplication of effort, and strengthen the ability of Cooperating Sponsors to negotiate more competitively in the market. FFP also required Cooperating Sponsors to obtain a performance bond, equal to at least 10 percent of the expected sales price, to guarantee payment to the Cooperating Sponsor in the event the buyer of the Title II commodities failed to perform in accordance with the sales agreement. Finally, under certain situations, FFP might approve monetization in a third country if Cooperating Sponsors demonstrated that commodity sales in the country in which they had their development activities were impracticable.

Although FFP established policies and procedures to help ensure the efficiency of P. L. 480 Title II monetization transactions, it did not collect or use actual cost data to measure the effectiveness of those policies and procedures.

USAID Needs to Capture Actual Cost Data
in Order to Calculate Actual Cost Recovery

To help ensure that U.S. taxpayers receive full value for their food assistance dollar, USAID policy requires that Cooperating Sponsors strive to achieve at least full cost recovery with each monetization transaction. However, FFP's guidance did not require that Cooperating Sponsors collect or report all the cost information needed to accurately measure actual cost recovery. Without measuring actual cost recovery, USAID was not able to assess the efficiency of its P. L. 480 monetization programs or take appropriate action to address the causes of any inefficiencies

Accordingly, we recommend that FFP develop procedures to ensure that it obtains all the information needed to accurately calculate cost recovery of all P. L. 480 Title II monetization transactions.

> **Recommendation No. 1: We recommend that the Director of USAID's Office of Food for Peace develop guidelines and procedures to require that full information on actual costs is obtained and used to calculate the actual level of cost recovery for each Public Law 480 Title II monetization sales transaction.**

According to FFP's *Monetization Field Manual*, one of the primary objectives for selling P. L. 480 commodities is "to generate the maximum feasible amount of foreign currency funds" because net sales revenue will fund approved food security activities. In order to help maximize the net revenue generated by monetization, USAID requires that Cooperating Sponsors strive to achieve at least full cost recovery with each and every monetization transaction they conduct. However, because USAID recognizes that full cost recovery is not always achievable, it has established a benchmark sales price (cost recovery benchmark) below which commodities may not be sold without a waiver by FFP.

FFP's *Monetization Field Manual* defines the cost recovery benchmark as the greater of:

- 100 percent of the Free Alongside Ship (FAS) price quotation, which is an approximate value for a specific commodity which includes all costs of transportation and delivery of the goods to the dock; or

- 80 percent of the Commodity and Freight (C&F) value which includes the FAS price quotation provided by FFP at the time the commodities are called forward, the foreign flag shipping rate[4], port clearing and handling costs and duties, estimated transport

[4] Because the Merchant Marine Act of 1936, as amended, requires that 75 percent of Title II food assistance be shipped on U.S. flag vessels, USAID has allowed Cooperating Sponsors to use the estimated costs of shipping commodities on less expensive foreign flag vessels for both budgeting and reporting purposes.

costs to move the commodity to the point of sale, and expenses associated with marketing the commodity.

In its field manual, FFP requires Cooperating Sponsors to calculate, at a minimum of four points in time, the extent to which their monetization sales revenues are expected to achieve, or have achieved, cost recovery in accordance with the cost recovery benchmark defined above. The Cooperating Sponsor's first calculation is to be included in its program proposal,[5] the second is to be completed at the time of the call forward[6], the third is submitted to USAID 30 days after the sale, and the fourth is included in the Cooperating Sponsor's annual results report. The earliest calculation is necessarily based on the Cooperating Sponsor's best estimates of costs and sales prices. However, as planned events transpire, Cooperating Sponsors are expected to replace some, but not all, of these estimates with actual cost data.

Calculation at the Time of Proposal - Because Cooperating Sponsors prepare their proposals well before actual costs are known, benchmark price calculations at the proposal stage should be based on best available estimates. A major element of this calculation is a price "indication," which is the estimated cost of commodities delivered to a U.S. port. Additional costs to be included are estimated ocean freight and inland transport costs for landlocked countries; estimated internal transport costs to the point of sale; and estimated duty, handling, port clearing, and marketing costs. A preliminary cost recovery estimate should then be calculated by expressing estimated sales revenue (plus projected interest to be earned) as a percentage of total estimated costs.

Calculation at the Time of the Call Forward – To obtain FFP approval of a call forward for the delivery of commodities, a Cooperating Sponsor must recalculate the cost recovery benchmark by replacing the price "indication" in its initial calculation with a FAS price quotation. The Cooperating Sponsor must also reconfirm that the expected sales price will meet or exceed the benchmark sales price.

Calculation After the Sale – Within 30 days after the commodity sale, Cooperating Sponsors must report in writing to the appropriate USAID Mission the actual sales price in comparison to the cost recovery benchmark. FFP's *Monetization Field Manual* includes a standardized format, called a monetization profile, for reporting this information. In the event that Cooperating Sponsors fail to achieve cost recovery, the USAID Mission should report the circumstances back to FFP.

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[5] To obtain commodities for monetization, as part of its Development Activity Proposal (DAP), a Cooperating Sponsor must submit a monetization plan that compares sales proceeds to monetization costs. If sales proceeds are expected to be less than the cost recovery benchmark, defined above, the difference must be justified on the basis of food security impacts.

[6] A "call forward" is a request initiated by a Cooperating Sponsor for the delivery of a quantity of food commodities to a particular country program for use over a specified period of time.

Calculation for the Annual Results Report - Cooperating Sponsors should also include a report of monetization in their Annual Results Report. FFP's guidelines for preparing the fiscal year 1998 Annual Results Report instructed Sponsors to include a final comparison of actual sales revenues to the cost recovery benchmark for each monetization transaction. According to those guidelines, the applicable benchmark for Cooperating Sponsor proposals approved after January 1, 1998, was the same as that defined in FFP's *Monetization Field Manual.*

In order to determine the level of cost recovery USAID's Cooperating Sponsors were achieving on sales of agricultural commodities under P. L. 480 Title II monetization programs, we reviewed Annual Results Reports submitted by 15 Cooperating Sponsors for 69 monetization programs in 21 countries for fiscal year 1998. However, we were unable to determine from those reports the actual level of cost recovery because USAID's guidance did not require Cooperating Sponsors to collect and report all the information needed to calculate actual cost recovery. For example, USAID's guidance required Cooperating Sponsors to continue using the FAS price quotation, as well as estimated ocean transport costs (rather than actual transport costs), to calculate cost recovery. Thus, according to FFP's guidelines, the most significant components of any cost recovery calculation or comparison—commodity prices and ocean transportation costs—were to be based on estimated rather than actual costs.

Although the remaining elements of cost recovery calculations (e.g., internal transport to the point of sale, duty, handling, port clearing, and marketing costs) were usually minor when compared to commodity and ocean freight costs, they could, occasionally and unpredictably, be substantial. Because FFP guidelines were unclear as to which costs should be reported, or how they were to be calculated as part of the cost recovery benchmark, we found that Cooperating Sponsors often used different and sometimes flawed methodologies when reporting cost recovery calculations in their Annual Results Reports. This precluded useful analyses and comparisons. Further, we found that much of the cost data necessary to calculate actual cost recovery was simply missing from these reports. For example:

- For the 69 monetization programs included in the Annual Results Reports we reviewed, costs other than commodity and ocean freight costs were reported for only 20 programs.
- Several Cooperating Sponsors reported cost data without specifying whether the costs were actual or estimated.
- Others simply reported that they had met the cost recovery benchmark without presenting any detailed cost information.
- Still others did not report on cost recovery at all.

After exhaustive efforts to obtain missing or unclear cost information directly from Cooperating Sponsors, particularly for those monetization programs we visited in Kenya and Uganda, we concluded that Cooperating Sponsors had generally not collected the required data or could not easily isolate or retrieve the desired data from their records. This condition was caused, in part, because FFP's guidance did not require that Cooperating Sponsors collect and report all the information needed to calculate actual cost recovery. As a result, USAID managers (as well as other interested parties[7]) were unable to analyze the efficiency of monetization processes by determining the actual level of cost recovery achieved by Cooperating Sponsors through their monetization of P. L. 480 Title II commodities.

FFP officials believed that it would be easy for Cooperating Sponsors to provide actual commodity and transportation cost data because this information appeared on the bills of lading they received for each commodity shipment. The Commodity Credit Corporation (CCC) of the U.S. Department of Agriculture (USDA) is another source of this information. The CCC is authorized under P. L. 480 to pay for the acquisition and transportation of Title II commodities. We contacted CCC to determine whether they could provide actual costs to USAID or Cooperating Sponsors. CCC officials provided us a copy of a new report designed to show actual commodity and ocean freight costs for all food aid shipments. CCC officials said they were currently testing the report's accuracy. USAID officials said they would contact CCC to determine how they could access the information in the new CCC database.

USAID Needs a System to Track and
<u>Report on Actual Costs of Monetization</u>

Even if FFP did obtain complete cost information, it would not be able to systematically track, analyze, or report the actual cost recovery of monetization programs because it does not have a management information system designed to do so. Such a system would enable FFP to produce reports necessary to evaluate the efficiency of monetization programs. Consequently, we recommend that FFP develop such a system.

> <u>Recommendation No. 2:</u> **We recommend that the Director of USAID's Office of Food for Peace develop a management information system to track and report actual cost recovery data in order to evaluate the efficiency of Public Law 480 Title II monetization programs.**

USAID does not have a management information system to track actual costs and evaluate the efficiency of their monetization programs. Although FFP does maintain a P. L. 480

[7] During our audit, the Office of Management and Budget (OMB) initiated a limited review of P. L. 480 Title II monetization programs and had similar difficulty extracting actual and complete cost information from Cooperating Sponsors. According to OMB, due to the lack of reliable data, FFP was unable to answer some questions from Congress in FY98 concerning the number of Title II monetizations which were concluded at, above, or below the benchmark price.

commodity delivery tracking system, it is used as a delivery planning tool, not a cost recovery management information system. Further, based on our audit, we found that FFP's delivery tracking system included many errors and was missing much information. For example, FFP budgeted a total of $160 million for procuring and transporting 473,380 metric tons of P. L. 480 Title II commodities to be monetized during FY98. From FFP's delivery tracking system we could identify only 152,610 metric tons costing $42.8 million relating to the budgeted shipments.

Because FFP does not have a system to track actual costs of monetized commodities, USAID management is unable to systematically calculate or report on actual cost recoveries, or respond to requests for monetization information. Based on our audit, we concluded that, because USAID does not capture or report actual costs of its monetization program, USAID managers, as well as other interested parties, are not able to assess the efficiency of the monetization program in terms of cost recovery.

Management Comments and Our Evaluation

In response to our draft audit report, FFP management provided written comments (attached as Appendix II) which indicated management's acceptance of both audit recommendations. Further, the management comments stated that FFP staff had already initiated corrective actions expected to close both recommendations by the end of the fiscal year. In addition, management included some technical comments which resulted in some minor changes to this final audit report.

Scope and Methodology

Scope

We performed this audit in accordance with generally accepted government auditing standards. As noted in this report, we were unable to satisfy the audit objective completely due to data limitations. Nevertheless, we believe that the data and evidence we were able to obtain provided sufficient evidence to support our conclusions and subsequent recommendations.

This audit began with a survey of USAID's P. L. 480 Title II monetization activities worldwide. We gathered information from USAID's Office of Food for Peace (FFP), within the Bureau for Humanitarian Response, about monetization activities worldwide from 1994 through 1999. In addition, we talked to several Cooperating Sponsors, FFP officials, and external parties about USAID's monetization activities worldwide and related issues, concerns, and trends. We also performed field visits to review monetization activities in two countries—Kenya and Uganda. We examined the planning, approval, implementation and monitoring of the Kenya and Uganda programs for fiscal year 1999, and the result reporting for their fiscal year 1998 programs.

Based on our survey work, we determined that an audit of monetization activities would be most effective if focused on the cost of monetizing commodities. Therefore, we designed our audit to determine the level of cost recovery USAID was achieving on sales of agricultural commodities under its P. L. 480 Title II monetization program. Our audit universe consisted of the worldwide fiscal year 1998 monetization activities, excluding those of the World Food Program. Based on FFP records, these activities consisted of 75 monetization programs for 15 Cooperating Sponsors in 21 countries with 473,380 metric tons of commodities valued at over $160 million. Due to the lack of records for six programs, we were only able to review Annual Results Reports for 69 of the 75 monetization programs approved for fiscal year 1998.

Methodology

To answer the audit objective, we gathered information about USAID's monetization programs, including any laws, policies, and regulations that impact the program. We also talked to various USAID personnel, Office of Management and Budget (OMB) officials, U.S. Department of Agriculture (USDA) officials, as well as other individuals outside of the government with interest in USAID's monetization programs.

We gathered and analyzed (for cost recovery) the fiscal year 1998 annual results reports of Cooperating Sponsor programs worldwide. Data was also collected on the costs of 1998 commodities from FFP, OMB, and USDA. In addition, we reviewed program documents and made site visits of the Kenya and Uganda programs implemented by five Cooperating Sponsors—Catholic Relief Services, Technoserve, World Vision, ACDI/VOCA, and Africare. We interviewed USAID officials in Washington, as well as those in Kenya and Uganda. We also interviewed selected Cooperating Sponsor personnel and other individuals inside and outside of the U.S. Government, with interests in the monetization programs, in Washington, Kenya, and Uganda.

We did not perform the audit work necessary to verify, in any detail, the results of activities as reported by USAID and/or Cooperating Sponsors. From site visits, we were able to assess that activities were generally working towards achieving planned goals and that recipients and/or Cooperating Sponsors believed that they would be successful.

Management Comments

U.S. Agency for International Development

MAR 28 2000

MEMORANDUM

TO: IG/A/PA Director, Dianne L. Rawl

FROM: BHR/FFP Director, W.T. Oliver

SUBJECT: Audit of USAID's P.L. 480 Title II Monetization Programs
BHR/FFP concurrence with IG/A/PA Draft Audit dated 2/24/00

In response to your draft audit referenced above, the Office of Food for Peace (BHR/FFP) is pleased to provide the following comments and also provide its official acceptance of the two recommendations noted therein:

TECHNICAL COMMENTS:

- Page 1., Background, First paragraph, last line: Most U.S. food assistance in FY 1999 was provided under the Section 416(b) program. The significance of Section 416(b) should be noted.
- Page 2., Second paragraph: References to monetization levels should clearly state that the statistics quoted refer solely to PVO non-emergency levels and do not include WFP non-emergency levels which is part of the base non-emergency tonnage.
- Page 1., Background, Second paragraph: All references to "local currency" should be deleted a replaced with "foreign currency".
- Page 4., Audit Findings, First paragraph: BHR/FFP feels strongly that the reference to the assertion that USAID "neither issued appropriate guidance nor enforced existing guidance…" is not entirely accurate. BHR/FFP believes that the guidance as issued was sufficient, but enforcement efforts were inconsistent.
- Page 5., first bullet at bottom of page: FAS refers to "free along side" not "free alongside ship".
- Page 6., first bullet at top of page: C&F refers to "commodity and freight" not "cost and freight".

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DISCUSSION: BHR/FFP was generally very pleased with the scope of the referenced audit and the associated findings. As stated in the draft audit, monetization has been a part of Title II programming since 1986, although the significant impact of monetization on the Title II program only manifested itself in the mid 1990's. The dramatic rise in both the value and the tonnage level of requests for monetization activities during the mid 1990's forced USAID in general, and BHR/FFP in particular, to recognize, understand, interpret, and codify an entirely new set of programmatic issues and procedures in order to ensure that the new programmatic tool was appropriately utilized. As an example, issues related to local market impact and the potential disincentive effect on of commodities on commercial sales took on new significance with the rise in monetization supported activities. Issues like cost recovery emerged as new issues altogether.

In FY 1998, after extensive consultations with the Title II cooperating sponsors, BHR/FFP finalized a revised Monetization Field Manual which made a great deal of progress in addressing the majority of the new issues that developed along with the increase in requests for Title II monetization supported activities. A major portion of the Monetization Field Manual was dedicated to the issue of "cost recovery". "Cost recovery" was defined, its importance was discussed, and procedures were established to gather cost recovery data.

As discussed in the draft audit report, the procedures established in the Monetization Field Manual to gather and record cost recovery data have not been adhered to on a consistent basis. As a result, two specific recommendations were included in the draft audit report:

Recommendation No. 1: We recommend that the Director of USAID's Office of Food for Peace develop guidelines and procedures to ensure that full information on actual costs is obtained and used to calculate the actual level of cost recovery for each monetization sales transaction.

Recommendation No. 2: We recommend that the Director of USAID's Office of Food for Peace develop a management information system to track and report actual cost recovery data in order to evaluate the efficiency of Title II monetization programs.

BHR/FFP has reviewed both draft audit recommendations and has determined that both are acceptable to the office. BHR/FFP staff has already initiated actions that will close both draft audit recommendations by the end of the fiscal year.

BHR/FFP appreciated the cooperation and flexibility of your staff during their work on this audit. We look forward to maintaining our strong relationship with your office in the future.