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Southeast Region

Audit Report

Foreign Agricultural Service Implementation of the Trade Title of the 2002 Farm Bill and the 2002 President's Management Agenda

Report 50601-12-At
March 2007

UNITED STATES DEPARTMENT OF AGRICULTURE

OFFICE OF INSPECTOR GENERAL

Washington, D.C. 20250

March 28, 2007

REPLY TO
ATTN OF: 50601-12-At

TO: Michael W. Yost
Administrator
Foreign Agricultural Service

ATTN: Robert D. Green
Acting Director
Compliance, Security and Emergency Planning Division
Office of Administrative Operations

FROM: Robert W. Young /s/
Assistant Inspector General
for Audit

SUBJECT: Foreign Agricultural Service (FAS) – Implementation of the Trade Title of the 2002 Farm Bill and the 2002 President's Management Agenda

This report presents the results of our audit of the FAS' Implementation of the Trade Title of the 2002 Farm Bill and the 2002 President's Management Agenda. Your March 5, 2007, written response to the official draft report is included in its entirety as exhibit B, with excerpts and the Office of Inspector General (OIG) position incorporated into the Findings and Recommendations section of the report, where applicable.

We are unable to accept management decision on any of the report's recommendations. We can accept management decision once we have been provided the information as outlined in the report sections, OIG Position.

In accordance with Departmental Regulation 1720-1, please furnish a reply within 60 days describing the corrective actions taken or planned, including timeframes, to address the recommendations for which a management decision has not been reached. Please note that the regulation requires management decisions to be reached on all recommendations within a maximum of 6 months from report issuance.

Executive Summary

Foreign Agricultural Service Implementation of the Trade Title of the 2002 Farm Bill and the 2002 President's Management Agenda (Audit Report No. 50601-12-At)

Results in Brief

The 2002 Farm Bill and the *2002 President's Management Agenda* established a number of new goals and requirements for the Foreign Agricultural Service (FAS), the agency charged with coordinating the U.S. Department of Agriculture's (USDA) international activities. The Office of Inspector General (OIG) initiated this review to determine the status of FAS' efforts to implement the 2002 Farm Bill amendments relating to the agency's food aid and trade programs and to evaluate FAS' efforts to address problems identified in food aid programs by the *President's Management Agenda*.

The 2002 Farm Bill's Section on Trade contained 13 provisions affecting FAS' programs, including export credit guarantees, market development, export enhancement, food aid development, technical barriers to trade, and trade-related programs in other titles of the Bill. FAS documented the timely completion of 10 of the 13 requirements by April 2003, only 1 year after the bill passed (see exhibit A). However, we found that additional work is necessary to comply with three of the bill's requirements, as follows:

- FAS has not developed a business process to ensure that the Global Market Strategy requirements of the Farm Bill – to coordinate the Department's resources and programs with those of other Departments, to identify opportunities for agricultural exports, and to remove trade barriers – are being met on a global level. Instead, agency managers have followed a strategy of supporting agricultural industry trade group partners (referred to as "participants") in implementing their individual marketing strategies. Although FAS has implemented processes to review and evaluate the marketing strategies submitted by individual program participants, the agency has not implemented a business process to integrate these into a focused global strategy that would allow FAS to identify and react to changing trends in global markets. Between 1990 and 2005, the dollar value of U.S. exports rose by 39 percent; however, during this same period, the nation's market share of global agricultural exports declined by 32 percent. At the same time, those of other exporting nations such as China, Japan, and the European Union (EU) increased significantly.

- Although FAS officials believe they had met the Farm Bill requirement of targeting 35 percent of their export credit guarantees to processed and high-value products by fiscal year (FY) 2003, we found that the lack of a single standardized definition to distinguish these from unprocessed commodities resulted in the inconsistent classifications of products that received similar degrees of processing. Also, in some instances, existing guidance was not applied in a consistent manner to determine whether commodities should be classified as high-value, processed, or bulk.

- FAS also did not provide Congress with required annual reports on its support of high-value and processed products through the Foreign Market Development (FMD) Cooperator Program. As a result, there is reduced assurance that Congress' mandate to promote the export of high-value and processed products is actually being fulfilled.

The *President's Management Agenda*, also issued in 2002, cited several problems in the implementation of the country's food aid programs, including program duplication between FAS and the U.S. Agency for International Development (USAID), waste of donated food supplies, and excessive administrative and transportation costs. For FY 2004, the Office of Management and Budget (OMB) evaluated FAS' and USAID's food aid programs, concluding that FAS' strategic planning and performance measures were inadequate. OMB concluded that coordination between the two agencies was needed on program performance measures, as well as on criteria for program evaluation and monitoring and determining eligibility for program participation. The *Government Performance and Results Act* (GPRA) requires agencies to set goals for program performance and to report accomplishments in relation to those goals.

Since that time, FAS has improved its planning in the food aid programs. Agency officials developed listings of priority countries for both the Food for Progress and Food for Education Programs and began providing these to private voluntary organizations (PVO)[1]. FAS has also begun working more closely with USAID, USDA's Economic Research Service, and other organizations as recommended in the agenda to develop better outcome-oriented performance measures, as well as an interagency Food Aid Information System to promote better coordination and reporting for its food aid programs. Finally, FAS now monitors food aid proposals from PVOs to ensure that these do not overlap with those of USAID. OMB repeated its review of FAS' food aid programs as part of the FY 2006 budget process and upgraded FAS' rating from inadequate to moderately effective. An FAS official stated that the agency's implementation of a new performance measure – the Food Aid Targeting Effectiveness Ratio, which measures FAS' success in eliminating "food gaps" in targeted, needy countries — was largely responsible for the improved rating.

However, this single performance measure does not assess FAS' progress in meeting the goals of its varied programs, and the agency needs to continue to

[1] A PVO is a non-profit organization that operates food aid grant programs for USDA and other Departments in recipient countries.

work toward developing outcome-based performance measures to reflect its accomplishments agencywide. Although both FAS and USAID have been making efforts in this area, FAS officials stated that it is difficult to design performance measures that can assess program outcomes such as changes in the nutritional levels of program recipients. FAS is also in the process of developing an automated system to accumulate, summarize, and report program performance data that the performance measures would evaluate. Until performance measures and tracking systems are fully implemented, the agency's reports under GPRA cannot provide meaningful assessments of FAS' progress in achieving USDA's strategic goals for its international activities.

Recommendations in Brief

We recommend that FAS develop and implement business processes to integrate the strategic information the agency currently possesses, including the reviews and analyses now being performed of program participants' marketing strategies, as a basis for formulating marketing strategies at a worldwide level. We also recommend that FAS, in consultation with Congress, analyze its overall marketing approach and revise its strategic goals and export strategies as necessary to increase U.S. competitiveness in world export markets.

We recommend that FAS review and clarify definitions to be used defining which commodities should be classified as bulk or standard, high value, or processed for purposes of export credit guarantees and other programs. In addition, we recommend that FAS ensure that its progress in supporting high-value and processed products through its FMD Cooperator Program is timely reported to Congress as required in the Farm Bill.

Finally, we recommend that FAS complete and adopt uniform outcome-based performance measures to assess whether its programs are achieving the objectives established in their authorizing legislation, and to implement its planned process for accumulating, summarizing, and reporting performance data under GPRA.

We are not making recommendations related to biotechnology trade issues as part of this audit. Findings and recommendations, if applicable, will be reported under OIG Audit No. 50601-14-Te, "USDA's Role in the Export of Genetically Engineered Agricultural Commodities".

Agency Response

In their response to the official draft report dated March 5, 2007, FAS officials expressed general disagreement with the conclusions contained in Finding 1 of the report and with portions of Finding 2.

They cited a cost-benefit study commissioned by FAS, which concluded that by 2008 the market development programs would enable U.S. agricultural exports to reach $74.5 billion, versus $70.8 billion without the programs. Officials noted that since the study, USDA had raised its FY 2007 export forecast to a record $77 billion.

They also questioned OIG's use of World Trade Organization (WTO) data in comparing the U.S. agricultural market share to that of our trade competitors, referring to this as an "apples to oranges" comparison.

Officials referred to OIG's use of EU export values in comparison with those of the United States as an "egregious error" because these figures included intra-trade among EU member nations. They also stated that the EU had "nearly doubled its size during the 21-year span identified by OIG, adding results from major agricultural producers/exporters such as Poland and Austria to its agricultural exports." They further cited "market access barriers" as a significant problem for U.S. exports and market share, as well as other factors such as the emergence of new export competitors such as Brazil which could "overshadow the real growth success that U.S. agricultural exports have enjoyed even as the global export market expanded."

FAS' response cited several "misunderstandings or misrepresentations" in OIG's description of the Unified Export Strategies (UES), in particular OIG's statements regarding the degree to which funding decisions are documented. FAS contends that "all allocation determinations are based on both analytical reviews and a competitive performance-based formula across divisions and industry groups." They also stated that while OIG acknowledged FAS' efforts to encourage more strategic planning on the part of its program participants, the report "suggested that this concept was not being used uniformly across divisions nor was there a specific process to ensure that the idea was being applied in a consistent fashion."

The response further cited Finding 2 of the report as "a final example of misleading statements and conclusions." FAS stated that "…in speculating that FAS' compliance with the Farm Bill's mandate that 35 percent of credit guarantees should be directed toward high-value and processed products, OIG failed to properly reflect the realities of how credit guarantee allocations are made, and failed to follow guidance that it requested from USDA's Office of General Counsel."

In addition to these "general comments," FAS officials responded individually to each of the report's recommendations. These responses are detailed in the "Agency Response" section following each recommendation.

OIG Position

WTO data for 2005 was not available until December 2006. OIG has updated all analyses in this report to reflect the most current world trade data available. OIG does not question FAS' position that the dollar value of U.S.

exports has risen during the period between 1990 and 2005. The U.S. dollar exports are discussed in the report, and reflected in the table “U.S. Exports and Share of Global Agricultural Markets” contained in Finding 1. Congress, however, has expressed its intent beginning with the 1996 Farm Bill that an increase in the nation’s market share of global agricultural exports is also a goal, along with the dollar value of exports. In using export dollars as the only benchmark, FAS officials have not presented a balanced assessment of U.S. exports in the global market.

OIG is also aware of the cost-benefit study cited by FAS officials and its conclusions that FAS’ export programs benefit both U.S. exports and the agricultural sector as a whole. Our audit did not question these conclusions, but instead questioned, in light of the continuing decline of the U.S. global market share, whether FAS’ current strategic planning efforts should be reassessed to ensure that export opportunities and trade barriers are effectively identified and addressed on a global basis. The cost-benefit study did not address this issue.

FAS officials criticized OIG’s use of statistical data provided by the WTO on exports and world market shares. However, FAS adjusted its statistics to exclude coffee, rubber, cocoa, and tea because these are not produced in the United States. This adjustment ignores the fact that many other countries do not export products produced by the United States. Regardless of the data used, both the WTO and FAS statistics reflect the same trend of steadily declining U.S. market share, even though the rate of decline is somewhat less pronounced in FAS’ analysis (which reflects a drop of about 20 percent between 1990 and 2005). The use of FAS’ analysis rather than that of the WTO would not have materially affected our conclusions. Documentation provided to us by FAS describes the U.S. market share as the lowest in 30 years, due to “<u>over reliance on slow growth commodities, mature markets, and rising competition</u>.” (emphasis added)

FAS officials have also stated that our comparison of the U.S. market share to that of the EU is invalid because of the increase in EU member nations and the intra-trade between those member nations. However, the largest increase in member nations did not occur until 2004, when 10 countries joined the 15 that were already in place. To address FAS’ concern that our comparison with the EU was invalid, our report presents an analysis for the period 2000 - 2003 (WTO data for the EU was not available prior to 2000). EU exports increased by 33 percent during this period while U.S. exports, by comparison, rose only 7 percent. Regarding FAS’ concern with intra-trade between EU member nations, it must be noted that the U.S.’ own statistics reflect trade with nations with whom we have regional Free Trade Agreements. These nations include Canada, Mexico, Guatemala, Honduras, El Salvador, the Dominican Republic, Costa Rica, and Nicaragua.

FAS cited various factors that tend to overshadow the real growth success of U.S. exports, such as export subsidies, sanitary and phytosanitary issues, and outbreaks of bovine spongiform encephalopathy (BSE) and avian influenza. However, the United States is not the only country affected by these problems. The EU was dramatically impacted by BSE before the United States; avian influenza has become a global problem. Sanitary and phytosanitary issues have replaced trade tariffs as the "new trade issues" for many countries following the Uruguay Round and recent free trade agreements. It should be noted that the 2002 Farm Bill states that one of the three objectives of a global marketing strategy is to identify and address barriers to trade. Some of these barriers, such as tariffs, cannot be addressed by working through program participants but must instead be dealt with on a government-to-government basis.

FAS was also concerned that OIG did not understand the UES review process. OIG carefully considered the UES review process and discussed it in detail with FAS division staff who conduct the reviews. The process was also discussed with an Assistant Deputy Administrator with the Office of Trade Programs. Although these officials provided evidence of reviews at the division level, they could not provide documentation of the process that occurs at higher levels, where the final funding decisions are made. Our description of the planning process is based on the information and documentation provided to us by FAS during the audit.

In our discussions on the issue of strategic planning, we acknowledge the difficulties faced by FAS in dealing with trade barriers such as tariffs and BSE. We also acknowledge the very real and substantive efforts that FAS has made to address these concerns, as evidenced by the recent reorganization and the various processes such as UES and the Country Strategy Statements that the agency has implemented. However, both FAS and WTO analyses make it clear that despite these efforts, the U.S. market share of global agricultural exports has been in decline since the mid-1980s. Congress has made its intent clear, beginning with the 1996 Farm Bill, that any FAS marketing strategy must consider market share, as well as the dollar amount of annual exports, in measuring the overall success of its export programs.

Regarding FAS' objections to our finding on high-value and processed products (Finding 2), FAS officials may have misunderstood our position on this issue. As noted in the OIG Position section under Recommendation 3, we did not question FAS' method of allocating funds in its export credit programs, other than to point out that the agency must comply with the requirements of the 2002 Farm Bill. Rather, we raised the concern that FAS officials have not applied clear or consistent definitions of high-value and processed products within the export credit programs. As noted in our report, FAS gave different classifications to products requiring similar degrees of processing to be marketable (e.g., cotton and corn). Meanwhile, dissimilar commodities (breeding swine and potatoes) were both classified as bulk products in one year but as high-value products in another year. In their response to Recommendation 3, FAS officials agreed with the need for clearer definitions.

Based on FAS' specific responses to our recommendations, we have not yet reached management decision on any of the report recommendations. Management decisions can be reached when FAS provides the information specified in the report sections OIG Position. FAS' response is included in its entirety as exhibit B of the report.

Abbreviations Used in This Report

AMS	Aggregate Measurements of Support
APHIS	Animal and Plant Health Inspection Service
BRS	Biotechnology Regulatory Services
BSE	Bovine Spongiform Encephalopathy
CCC	Commodity Credit Corporation
CSS	Country Strategy Statements
EEP	Export Enhancement Program
ERS	Economic Research Service
EU	European Union
Farm Bill	Title III of the Agricultural Trade and Aid Section of the Farm Security and Rural Investment Act of 2002
FAIS	Food Aid Information System
FAS	Foreign Agricultural Service
FFE	Food for Education
FFP	Food for Progress
FMD	Foreign Market Development
FY	Fiscal Year
GMS	Global Market Strategy
GPRA	Government Performance and Results Act of 1993
OGC	Office of the General Counsel
OIG	Office of Inspector General
OMB	Office of Management and Budget
PART	Program Assessment Rating Tool
P.L.	Public Law
PVO	Private Voluntary Organization
SPS	Sanitary and Phytosanitary
TASC	Technical Assistance for Specialty Crops
UES	Unified Export Strategies
USAID	U.S. Agency for International Development
USDA	U.S. Department of Agriculture
U.S.C.	United States Code
WTO	World Trade Organization

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Background and Objectives

Background

The Foreign Agricultural Service (FAS) is the lead agency for the U.S. Department of Agriculture's (USDA) international activities. Operating on a global basis, FAS supports three of USDA's strategic objectives: (1) expand and maintain international export opportunities for U.S. agriculture, (2) support international economic development and trade capacity building, and (3) improve the global sanitary and phytosanitary (SPS) system to facilitate agricultural trade. FAS enhances economic opportunities for America's agricultural producers through trade agreement negotiations and monitoring, the Foreign Market Development (FMD) Cooperator Program, and the Export Credit Guarantee programs. The agency supports economic development and trade capacity building in foreign countries through food aid, technical assistance, and training. Working with other countries and with international organizations, FAS encourages the development of transparent and science-based regulatory systems that avoid restricting trade while at the same time protecting animal and plant health.

FAS conducts its activities and programs through its offices in Washington, D.C., at 80 overseas posts, and 16 agricultural trade offices. Those posts represent U.S. agricultural interests and provide reporting on agricultural policies, production, and trade for about 160 countries. FAS agricultural trade offices are located in key foreign trading centers and assist U.S. exporters, trade groups, and State export marketing officials in their trade promotion efforts. FAS has over 900 employees. For fiscal year (FY) 2005, FAS' total program level for its international programs and activities, including salaries and expenses, was $5.4 billion. The same level of expenditure is estimated for 2006.

FY 2002 Farm Bill Section on Trade

The Farm Bill[2] was designed to develop and expand commercial outlets for U.S. commodities and to provide international food assistance. The bill affected key provisions of the following FAS programs: export credit guarantees, market development, export enhancement, food aid and development, technical barriers to trade, and trade-related programs in other titles of the bill. In addition, the bill established four new programs:

1. McGovern-Dole International Food for Education (FFE) and Child Nutrition;

2. Biotechnology and Agricultural Trade;

[2] Title III, Trade, *Farm Security and Rural Investment Act of 2002* (Public Law (P.L.) 107-171).

3. Technical Assistance for Specialty Crops (TASC); and

4. Online Exporter Assistance Initiative.

2002 President's Management Agenda

In FY 2002, the President issued a management agenda designed to improve Government performance. One of its goals was to reform the Government's food aid programs to ensure that overseas food donation programs targeted food aid to the genuinely hungry and avoided waste and adverse impacts. The agenda cited several problems, including:

- program duplication between USDA and the U.S. Agency for International Development (USAID);
- waste of Commodity Credit Corporation (CCC) donated food supplies; and
- excessive administration and transportation costs.

The agenda also included the integration of performance and budget information as a government-wide management priority. Thus, for FY 2004, the Office of Management and Budget (OMB) used its Program Assessment Rating Tool (PART) to evaluate Federal programs during the budget formulation process. The 2004 PART review concluded that FAS' strategic planning and performance measures for the food aid programs were inadequate. It recommended that USDA develop performance measures that link to long-term outcome goals, as well as to the agency's strategic goals and budget. In addition, the review affirmed the need for USDA and USAID to coordinate on program performance measures, evaluation, monitoring, and eligibility criteria. By 2006, OMB had conducted PART reviews of 793 Federal agency programs, including USDA food aid programs implemented by FAS, to assess each agency's program purpose and design, strategic planning, program management, and results. The FY 2006 PART review upgraded FAS' rating to moderately effective because, in part, of the agency's work on a Food Aid Targeting Effectiveness Ratio.

Objectives

The Office of Inspector General (OIG) evaluated FAS' efforts to: (1) implement the 2002 Farm Bill amendments to existing food aid and trade programs and establish newly authorized programs and (2) work with USAID and other Departments and agencies to address problems identified in food aid programs by the *FY 2002 President's Management Agenda* and FY 2004 OMB PART review.

The Animal and Plant Health Inspection Service (APHIS) Trade Support Team and Biotechnology Regulatory Services (BRS) staffs routinely interact with FAS providing analysis, communication, and representational and liaison services. Because of its technical expertise, APHIS plays an important role in the global agricultural arena. Thus, we also evaluated the involvement of APHIS officials in food aid issues and in the implementation of the 2002 Farm Bill requirements relating to technical and biotechnology programs. This report contains no findings or recommendations related to APHIS activities. OIG is conducting a separate review of FAS' delegated responsibilities for international trade in biotech commodities.

Exhibit A contains the results of our current evaluation.

See the Scope and Methodology section at the end of this report for details of our audit methodology.

Findings and Recommendations

FAS has made considerable progress towards implementing the requirements of the 2002 Farm Bill, providing evidence to document its timely completion of 10 of the 13 requirements within a year of its passage (see exhibit A). FAS has also taken steps to improve its strategic planning and performance measures for its food aid programs as recommended by the *President's Management Agenda* and the OMB PART reviews. To focus more attention on the world's most needy countries, FAS prepared priority lists of needy countries for its FFE and Food for Progress (FFP) programs and provided the lists to private voluntary organizations (PVO) during its annual food aid planning conferences in 2005 and 2006. The agency is working more closely with USAID, USDA's Economic Research Service (ERS), and other organizations, as recommended in the agenda, to develop better outcome-oriented performance measures for its food aid programs. FAS is also coordinating with USAID on an interagency Food Aid Information System (FAIS) with common data elements for better program coordination and reporting.

However, we found that FAS still needs to take steps to fulfill the remaining requirements of the Farm Bill. Specifically, FAS needs to:

- implement a business process to analyze and prioritize its various country and participant-oriented strategies into a comprehensive plan for achieving the agency's strategic goals;

- seek clarification of the definitions of bulk/standard, high-value, and processed products so that agency officials can accurately determine if export credit guarantees for high-value and processed products meet the 35-percent goal outlined by Congress; and

- develop and implement outcome-based performance measures to assess FAS' accomplishments toward achieving the objectives established by its authorizing legislation, and complete and implement a system to accumulate and report data that will allow the agency and Congress to assess agency progress in meeting program goals.

Finding 1 FAS' Emphasis on Industry Trade Group Partners' Trade Strategies May Not Be Effective in Improving U.S. Competitiveness in World Export Markets

Although the 2002 Farm Bill required FAS to prepare a Global Market Strategy (GMS) to increase the nation's agricultural exports and facilitate coordination with other agencies and Departments, the agency has not developed a business process to fully accomplish this. FAS officials have implemented systems that allow them to access and provide program support for the export strategies of individual agricultural program participants and have begun requiring their foreign posts to provide standardized export strategies for selected countries. FAS officials do not believe that a central planning process or a formal GMS is necessary. It is not clear, though, how this focus on strategies for individual countries and program participants can provide effective coordination with other Departments or ensure that export opportunities and trade barriers are effectively identified and addressed on a global basis. Although the dollar value of U.S. exports rose by 39 percent between 1990 and 2005, larger export gains by foreign competitors have eroded the U.S.' market share of global exports by 32 percent over the same period. We question whether FAS' current strategic trade approach will be effective in addressing the Department's legislative requirement of developing an export promotion strategy whose goals are to increase both the nation's dollar exports and its global market share. Although agency officials have implemented various measures to encourage strategic planning by program participants and to evaluate their export strategies, FAS also needs to develop comprehensive strategies that can be implemented on a worldwide basis if these goals are to be reached or even to prevent the U.S. share of world agricultural markets from suffering further decline.

In 2002, Congress passed legislation aimed at improving American agricultural producers' competitive position in the global marketplace. The 2002 Farm Bill required that FAS prepare a long-range agricultural trade strategy that would identify opportunities for increasing agricultural exports to overseas markets; ensure that the Department's resources, programs, and policies are coordinated with those of other agencies; and remove barriers to overseas trade. The Bill required FAS to consult with congressional committees on the strategy in November of 2002 and every 2 years thereafter.[3]

The 2002 legislation built on the policies of the 1996 Farm Bill,[4] which established an "Agricultural Export Promotion Strategy" to take into account the new market opportunities for agricultural products resulting from the

[3] 2002 Farm Bill, Section 3206, "GMS."
[4] P.L. 104-127, *Federal Agriculture Improvement and Reform Act of 1996*.

North American Free Trade Agreement, the Uruguay Round Agreements, and increasing membership in the World Trade Organization (WTO). The goal of the strategy was to increase the value of U.S. agricultural exports each year at a faster rate than the rate of increase in the value of overall world export trade in agricultural products. This would be accomplished by encouraging the maintenance, development, and expansion of export markets for U.S. agricultural commodities and related products. The Secretary was required to annually identify as priorities those markets (1) in which imports of agricultural products showed the greatest potential for increase and (2) in which, with the assistance of Federal export promotion programs, exports of U.S. agricultural products showed the greatest potential for increase[5]. The requirements of the 1996 Farm Bill led FAS to establish, in its FY 2001 through 2005 strategic plan, a measurable goal (subsequently rescinded by agency officials, as discussed below) to recapture by 2010 the 22 percent of world market share that the United States had held in 1984. In its 2003 through 2007 plan, however, FAS dropped this goal and instead focused only on the dollar value of the nation's agricultural exports as a measure of the success of its export promotion programs.

Following the passage of the 2002 Farm Bill, FAS created a first draft of the GMS. As part of this, agency analysts prepared an analysis of the global marketing climate, the strengths and weaknesses of the U.S. agricultural marketing strategy for capitalizing on global market trends, and an assessment of how FAS resources should be redeployed to correct the nation's declining market share. The draft GMS identified market access issues by region and by country, and recognized the need to build emerging markets and support high-value and processed products. In November 2002, the FAS Administrator testified before Congress on FAS' efforts to complete the GMS.

In 2002 and 2003, FAS provided drafts of its GMS to program participants and stakeholders for comment. However, the participants generally opposed implementation of the GMS because it emphasized the rising third world countries in Asia and the Western Hemisphere as the most promising markets for American exports. FAS officials stated that the participants preferred to continue dealing with stable, developed markets such as the European Union (EU) and Japan rather than the developing markets that were specified in the 1996 Farm Bill. FAS was unable to complete the GMS and provide it by the next required consultation in November 2004, but officials made a second attempt to draft a GMS in February 2005. This document, which eliminated the detailed country/regional analyses and the identification of "best prospect" markets, remained in draft and was never completed.

[5] Title 7, *United States Code* (U.S.C.), Section 5603(d).

We noted that, following the FAS Administrator's testimony before Congress in November 2002, there was no record that agency officials had consulted with Congress on their implementation of the GMS as required in Section 3206 of the Farm Bill. A senior official we interviewed stated that agency officials did consult with Congress on an ongoing basis, but that there was no documentation to show the nature of the discussions or of the information provided to Congress.

FAS management officials stated that they view the GMS as an internal agency working document only, and that FAS has no plans to complete or issue it. FAS' strategy has been to support the agricultural program participants in implementing their own individual export strategies, rather than engaging in the type of "central planning" envisioned in the draft GMS. An official noted that a GMS would, once completed, be a static strategy that could not keep up with rapidly changing market situations. Officials stated that the agency's Unified Export Strategies (UES), which incorporate the strategies of the participants for their targeted markets, were dynamic and continually updated to reflect current country conditions. As such, it was their position that the UES performed the function of a GMS, and that this strategic process fulfilled the requirement of the 2002 Farm Bill. We disagree that a global strategic process would, or should, be static; since it would be linked to the processes already in place with the UES and Country Strategy Statements (CSS) described in the following paragraphs, it would adapt to changing market conditions, as they do.

Unified Export Strategies

The UES system is an online application that allows program participants – generally marketing associations for specific commodities - to annually submit their individual marketing plans and their applications for FAS program funding. FAS agricultural marketing specialists from each division within the agency's Office of Trade Programs, as well as country attachés from the foreign posts, review the participants' applications and make funding recommendations based on ranking factors that help to identify the most promising marketing proposals submitted to each division. These recommendations are channeled up through the directors of each division to the Deputy Administrator, where funding decisions are ultimately made. Although the divisions document their analyses of the UES submitted by each cooperator, the process above the division level is primarily conducted on a verbal basis. Nor are funding decisions necessarily based on a participant's UES; one division's recommendations to the Deputy Administrator on the 2006 UES submissions stated that because of the need to maintain existing funding for average and below average performers, there was no opportunity to shift funds to the higher performing participants.

FAS has, in recent years, promoted the concept of Comprehensive Industry Strategic Planning, which encourages program participants to engage in strategic planning processes when formulating their UES each year. An official we interviewed also stated that, in some instances, agricultural marketing specialists have worked with participants to evaluate the specifics of their planning process. This would include a determination of whether the participant had accurately gauged existing market conditions and identified promising future markets for their commodities. However, no specific process has been implemented to perform this function routinely throughout the various divisions, and this would not necessarily affect funding decisions.

Although we agree that the UES system facilitates the funding application process for both participants and FAS' agricultural marketing staffs, they are not routinely reviewed or analyzed above the division level. An FAS official noted also that each division is allocated a share of marketing funds before the UES are analyzed. As a result, other than the review by the Deputy Administrator, there is no process in place above the division level to analyze and compare the various marketing strategies to identify those whose support would most benefit the country's overall agricultural export levels.

Country Strategy Statements

In addition to developing the UES system, FAS officials also recognized that changing world market conditions necessitated a fundamental review of the agency's organization and functions. In 2004, therefore, agency officials began work on a reorganization plan which was approved on August 30, 2006. Under this plan, the agency has been aligned around three main functions – Policy, Program, and Operational Support. Among the benefits the reorganization is expected to achieve are (1) more effective support for negotiation and enforcement of trade agreements, (2) greater focus on technical barriers to agricultural trade, (3) better coordination of USDA issues and activities with foreign country governments, and (4) more proactive representation of U.S. agricultural interests in international organizations.

As the reorganization is phased in, the agency attachés assigned to foreign posts will be required to submit annual CSS on or about July 31 of each year for countries in each post's area of responsibility. The CSSs are intended to be forward-looking plans that connect long-term strategic issues with current activities, goals, and results. Each CSS will contain (1) a description of the country's political, economic, and trade environment; (2) an analysis of issues, trends, and impending changes within the country that impact U.S. agricultural interests; (3) an identification of market opportunities; and (4) a statement of strategy and goals – both long and short-term – that link to the USDA and FAS strategic plans. The CSSs were prepared on a test basis for 2006, with full implementation scheduled for 2007.

The CSSs provide useful strategic planning at the country level and, in conjunction with the UES, can be valuable tools in an overall strategic planning process. However, each CSS targets only a single country and we found that for 2006, only 73 CSSs were submitted by 80 foreign posts covering about 160 countries. An agency official stated that because this process was still being phased in during 2006, some countries that would otherwise be targeted for CSS were omitted. For 2007 and after, the official stated that the foreign posts should be preparing CSS for each country in which they plan "significant activities." He stated that this should, for instance, include any country with which the United States has a Free Trade Agreement. However, the decision of whether to do a CSS would still rest with the officials at the posts themselves.

The CSSs are strategic tools at the country level, but do not constitute a global strategy by themselves. A management official we interviewed stated that the CSSs are a part of the process that participants and FAS divisions will use to prepare and evaluate the UES, but agreed that there is currently no process in place to analyze and evaluate them above the level of the individual FAS divisions. Another official stated that no decisions had been made as to where these documents will be sent within FAS Headquarters after the reorganization; it was possible that they might be routed to the individual country desks. This official stated that in the future, the country desks might combine country reports to create regional trade strategies; at present, however, there is no process in place to analyze the CSSs and prioritize export opportunities and challenges on a global level, or to ensure that strategies are prepared for each country that either is, or may become, a significant trading partner with the United States.

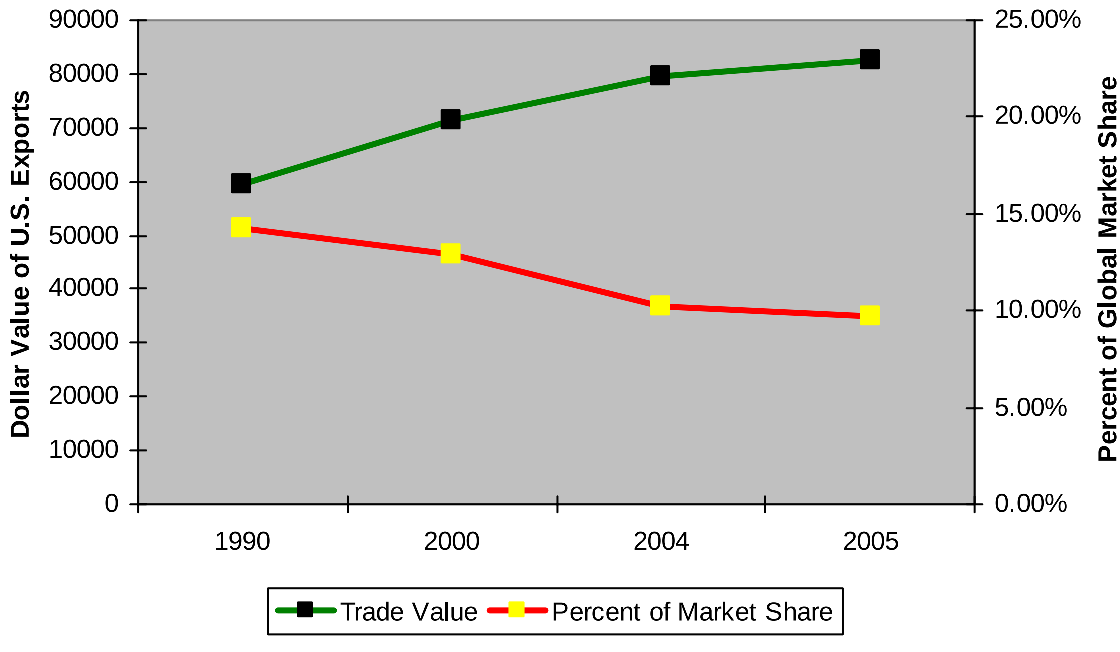
Strategic Planning Processes

The 2002 Farm Bill required that the GMS fulfills three functions. Two of these, the identification of opportunities for increasing agricultural exports and the removal of barriers to overseas trade, could potentially be addressed in part by the UES and the CSS. However, they could be an effective strategic planning tool in addressing the Farm Bill goals only if FAS can assure that trade opportunities are identified for "countries of interest," and only if a process exists to evaluate and prioritize the various country and participant strategies worldwide. Presently, no such business process exists within FAS. The third requirement (that of ensuring that the Department's resources, programs, and policies are coordinated with those of other Departments) is not addressed by the UES. Although one official stated that the foreign posts had been asked to tie their CSS planning into both the State Department and the USDA strategic planning processes, this responsibility is not centralized, but rather is dispersed between 80 foreign posts across the world.

In recent years, many foreign trading competitors have capitalized on the growing worldwide demand for agricultural products and have experienced dramatic growth in their agricultural exports. For instance, between 1990 and 2005, China's agricultural exports increased by 185 percent, while those of Japan, Canada, and Mexico increased by 82 percent, 84 percent, and 267 percent, respectively. In comparison, the dollar value of U.S. agricultural exports grew during this period by 39 percent.

Between 2000 and 2003, the EU's exports increased by 33 percent, as compared to a 7-percent increase for the United States. In 1990, the U.S. market share was 14.3 percent; by 2005, it had declined to 9.7 percent.[6] Therefore, while the dollar value of U.S. agricultural exports rose by 39 percent, from $59.4 billion in 1990 to $82.7 billion in 2005, during the same period, the nation's global market share declined by 32 percent. The following table illustrates these diverging trends.

U.S. Exports and Share of Global Agricultural Markets (Millions of Dollars and Percentages)



Subsequent to the 2001 through 2005 strategic plan, FAS officials dropped the measurable goal of recapturing the 22-percent global market share held by the United States in 1984; thereafter, the agency has used primarily the

[6] The U.S. share of world exports for 2005 was 9.7 percent according to the WTO's, *International Trade Statistics, 2005 – Trade by Sector*, 2006, Table IV.8, "Leading exporters and importers of agricultural products, 2005."

dollar value of the nation’s agricultural exports to measure the success of its export promotion programs. However, when Congress established the requirement for an Agricultural Export Promotion Strategy under the 1996 Farm Bill, it specified that this strategy would have two goals – to increase the value of U.S. agricultural exports each year, and to increase the value of U.S. agricultural exports each year at a faster rate than the rate of increase in the value of overall world export trade in agricultural products (i.e., the nation’s market share). These goals, which were to apply both to overall exports and to exports of high-value and value-added agricultural products, are incorporated into Title 7 U.S.C. Section 5603 (b).

An FAS management official stated that the agency’s goal of regaining the 1984 market share was changed because prevailing global circumstances had made this impossible. He stated that at the time Congress drafted its legislation which made increased market share a goal, the large increases in agricultural exports by our foreign competitors had not been foreseen. He stated that agency officials had not consulted with Congress on this issue, and he had not been aware that this goal was still cited in the public law. While we agree that global trends cannot always be foreseen, we also believe that a strategic planning process that consolidates and analyzes the divisional reviews and the CSS could increase FAS’ ability to identify promising markets.

With the UES and the CSS, FAS has the beginnings of a comprehensive strategy but needs to engineer a process to coordinate and prioritize them into regional and global strategic plans to increase the nation’s competitiveness as a worldwide agricultural exporter. FAS also needs to incorporate into this process any other strategic planning information that may be available in addition to the UES and the CSS. In the long term, we believe that FAS – in consultation with Congress – needs to analyze and reassess its strategic goals and marketing strategies as a whole in order to regain, to the extent possible, U.S. competitiveness in global agricultural exports.

Recommendation 1

Develop and implement processes to integrate the strategic information contained in the UES and in the CSS documents, as well as the analyses now performed within the divisions of FAS’ Office of Trade Programs, and to use these as a basis for formulating marketing strategies at a worldwide level.

Agency Response.

In their response, FAS officials stated that Congress and the Secretary have specified that the FAS Administrator and agency managers have the authority and prerogative to determine the methods by which the agency fulfills its mission. They stated that FAS' practices and procedures related to market development are consistent with FAS and USDA strategic goals. They cited a number of these practices, including the UES and the attendant process by which participants' applications are evaluated, as well as their efforts to encourage participants to increase their strategic planning.

The officials noted that FAS has recently completed a comprehensive reorganization that shifts resources to address critical needs in the area of market access, trade negotiation and capacity building. As part of this reorganization, FAS has established a new Office of Country and Regional Affairs that is coordinating a comprehensive strategic plan based on the new CSS that will cover not only marketing but also the other critical areas of market access, trade negotiation, capacity building, reporting and analysis. Officials concluded that FAS will continue all these efforts already underway to enhance coordination among and between industry partners, FAS overseas offices and the Washington office staff, and other appropriate agencies to expand market access and export opportunities for exporters of U.S. food and agricultural products.

OIG Position.

Although OIG recognizes the value of the CSS and the other processes cited by FAS officials, we maintain our position that these do not entirely fulfill the functions of a GMS as outlined in the 2002 Farm Bill. Moreover, despite these existing processes, FAS' own statistics as well as those of the WTO show a continued, long-term decline in the nation's market share of global agricultural exports. Documentation provided to us by FAS describes the U.S. market share as the lowest in 30 years, due to "<u>over reliance on slow growth commodities, mature markets, and rising competition</u>." (emphasis added) All of these are factors that a strategic planning process should address. As a result, we question whether agency officials' stated plan of continuing the efforts already underway will be effective in reversing this long-term trend. To reach management decision, FAS needs to provide us either with a plan, including timeframes, to implement the recommendation, or an alternative action that would address the issue of declining market share.

Recommendation 2

Perform a long-term analysis of FAS' strategic goals and global marketing approach, including consultations with Congress and other Federal agencies, to determine what strategies are needed to increase U.S. competitiveness in global agricultural exports. Based on the results of this analysis, develop and implement export strategies as needed.

Agency Response.

FAS officials stated that the agency maintains a constant state of consultation with Congress on virtually every aspect of the agency's operations, including its mandate to support the export of U.S. food and agricultural products. They also noted FAS' working relationships with other agencies, including the Office of the U.S. Trade Representative, the Department of State, the USAID, and the Department of Commerce, as well as the regulatory agencies in USDA that support FAS' efforts to address foreign market access issues.

They noted that FAS has continued to review its overall strategic plan and make adjustments as needed, citing the recent FAS reorganization as evidence of this. They stated that there already is an effort underway to integrate more fully FAS and industry market development efforts that goes beyond marketing strategies to include comprehensive strategic planning on market access, trade negotiation, capacity building, reporting, and analysis.

OIG Position.

In our discussions with agency officials prior to the exit conference, they stated that no decisions had yet been made as to how the various planning processes, such as the UES and CSS, would be utilized above the division level following the reorganization. The agency's plans as described above – for a comprehensive strategic planning process that includes market access, trade negotiation, capacity building, reporting, and analysis may address our recommendation, but only if the agency's plans also address how these planning documents will be used on a comprehensive, global basis. To reach management decision, FAS needs to provide us with a detailed plan for implementing a strategic planning process on a global basis, as well as timeframes for its implementation. The response should also specify when agency officials will communicate these plans to Congress.

Finding 2 — FAS Needs To Implement Consistent Definitions of High-Value and Processed Products In Its Export Credit Programs

Although FAS officials reported that they had achieved the 2002 Farm Bill's mandate to direct at least 35 percent of the agency's export credit dollars to high-value and processed products, we found that this determination was based on product classifications that were inconsistent or were not based on existing definitions. We attributed this to the fact that neither the 1996 nor the 2002 Farm Bills contained specific guidance as to what constituted a high-value or processed product, as opposed to standard or bulk commodities. Depending on which definitions are used, the actual percentage of export credit dollars that supported high-value and processed products in FY 2003 – which FAS reported as 35 percent – may have actually been as high as 59 percent or as low as 24 percent. As a result, there is reduced assurance that Congress' intent to target these products is actually being met.

The 1996 Farm Bill established an "Agricultural Export Promotion Strategy" to encourage the maintenance, development, and expansion of export markets for U.S. agricultural commodities and related products. That strategy required that FAS increase credit guarantees for exports of American processed and high-value commodities to 35 percent of the total amount of credit guarantees issued for a given fiscal year. At the latest, FAS was required to meet this target by FY 2000. The 2002 Farm Bill again required the 35-percent benchmark and required that it be maintained through 2007.

FAS officials did not actively monitor compliance with the 35-percent requirement, but the computations that they provided at our request for FY 2003 showed that the requirement had been met. However, we noted that two commodities, rice and cotton, were included in the category of high-value and processed products despite the fact that both of these commodities are classified along with wheat, soybeans, and other coarse grains, as bulk agricultural products in FAS' Bulk, Intermediate, and Consumer-Oriented reports. Had these been classified as bulk commodities in FAS' computations, the percentage of export credit funds supporting high-value/processed products would drop to 22 percent.

FAS officials maintained that both cotton and rice should be considered processed (although not high-value) products because they cannot be marketed without some degree of processing after harvest. Cotton, for instance, must be "ginned" to remove the seeds and then baled. Rice is not edible until the hulls are removed from the grains. We noted, however, that under this definition other agricultural commodities – such as corn – could also be considered as "processed."[7] However, in FAS' computations, corn was classified as an unprocessed commodity for FY 2003. We noted also that in its October 2005 announcement of the commodities eligible for export credit guarantees, FAS included cotton, rice, and corn as "standard" rather than high-value or processed agricultural products.

ERS' website contained the following discussion regarding the classification of agricultural products:

> *Food trade is often categorized based on the level of processing:*
>
> - *Traditional bulk commodities such as wheat, rice, and corn;*
> - *Horticultural products such as fresh fruits and vegetables;*
> - *Semi-processed products such as flour and oils; and*
> - *Processed food products such as pasta and prepared meats.*
>
> *Horticultural, semi-processed, and processed products are considered high-value products. Unlike bulk commodities, high-value products are often ready to eat and are generally more perishable by nature. These characteristics make high-value products subject to greater quality and safety scrutiny compared with bulk agricultural commodities.*

We requested that the Office of the General Counsel (OGC) research the legislative history for a legal definition of high-value and processed products. OGC found that there was relevant statutory language regarding export credit guarantees in Section 709 of the FREEDOM Support Act of 1992.[8] The House Conference Report accompanying the Act provided the following definitions:

> *The committee of conference intends that the term '**high-value agricultural product'** means an agricultural commodity the value of which, on a per-unit or equivalent volume basis, is substantially higher than the value of bulk or raw agricultural commodities, such as grains or oilseeds. The term includes, but is not limited to fresh, chilled, or frozen meats, fish (without regard to whether such fish are harvested in aquacultural operations), dairy cattle, fruits and vegetables, eggs, breeder stock, plant seeds, and tobacco. (1992 U.S. Code Cong. and Adm. News, p. 2813).*
>
> *The committee of conference intends that the term '**processed agricultural product**' means a product derived from a bulk or raw*

[7] Corn is removed from the husks and separated from the cob by machine during harvest. The corn must then be machine dried to reduce its moisture content before it is ready for export.
[8] P.L. 102-511, *Freedom for Russia and Emerging Eurasian Democracies and Open Markets Support Act of 1992* (FREEDOM Support Act). Section 709(a)(2) of that act first added sub-section 202(k) to the currently applicable *Agricultural Trade Act of 1978*, as amended.

agricultural commodity which, as a result of the application of human labor, the use of machines, or other factors involved in a manufacturing process, is increased in value and made more appropriate for human consumption or use. Such term includes, but is not limited to livestock products, poultry products, fish products (without regard to whether such fish are harvested in aquacultural operations), dairy products, peanut products, wheat flour, milled rice, refined sugar, vegetable oil, processed baby foods, and prepared, preserved, canned and other processed food products.

OGC concluded that rice, because it is specifically mentioned in the 1992 report, should be regarded as a processed product, and we concurred based on the above citations. Including rice in FAS' 2003 computation would increase the percentage of export credit guarantees supporting high-value/processed products from 22 to 24 percent. The OGC opinion also noted that cotton, while not specifically mentioned, does require the "application of human labor" and "the use of machines" to make it saleable after harvest, and thus also fits the definition of a processed product. While this is true, other commodities such as corn also require a degree of processing, and yet are classified as "standard" commodities by FAS.

Depending on how such products are classified, they could greatly affect the percentage of export credit guarantees that are reflected as supporting high-value and processed products in any given year. OIG reviewed FAS' calculations for the 35-percent target for FYs 2003 through 2005. We found that FAS had not included breeding cattle and swine in its calculations for high-value products for FY 2003, even though these were specifically referenced as such in the conference report accompanying the 1992 legislation. Nor were fish or plant seeds classified as high-value products in FAS' computations for FY 2005. Breeding swine and potatoes were classified as bulk commodities by FAS in FY 2003, but as processed or high-value commodities in FY 2005. Depending on how each of these various commodities was classified between the high-value/processed and standard/bulk categories, the percentage of export credit dollars for these years could have been reflected as high as 59 percent or as low as 24 percent.

The 2002 Farm Bill also supported the export of processed and value-added products through the FMD. This program, which uses CCC funds to aid in the creation and expansion of long-term export markets for U.S. agricultural products, received funding totaling $34.5 million per year for FY 2002 through 2007. The Bill required FAS to submit an annual report to Congress describing the amount of funding being provided, the types of programs funded, the value-added products targeted, and the foreign markets developed for those products. However, we found that no reports were submitted to Congress following the initial report provided to Congress in April 2003. An

FAS management official stated that the official responsible for the report had been reassigned, and the reports had been overlooked subsequent to this. FAS needs to ensure that these reports are timely prepared and submitted so that Congress can evaluate the agency's use of the appropriated FMD funds.

Congress recognized the growing importance of high-value and processed products and sought to support U.S. exports of these products through its 1996 and 2002 Farm Bill legislation, including the Export Credit Guarantee Program. However, without clear and consistent definitions of what constitutes a high-value or processed product, there is reduced assurance that FAS' export guarantees will in fact meet Congress' intent. As noted by FAS officials, these definitions would not directly affect the allocation of export credit guarantees as long as there are available funds in excess of those applied for and approved. However, even in years where excess funds are available, FAS should monitor export credit trends for the high-value and processed products. A disproportionately small percentage of high-value and processed products supported by export credit guarantees could reveal a need for additional outreach efforts by FAS to attract such commodities for its export credit guarantee program.

Recommendation 3

In consultation with the Department and Congress, review and clarify definitions to be used defining which commodities should be classified as bulk or standard, high value, or processed for purposes of export credit guarantees and other programs.

Agency Response.

FAS officials stated that, beginning in 1999, the agency began moving away from programming individual commodity allocations under the credit guarantee programs, and now provides that country or regional allocations are, in most cases, available to the entire General Sales Manager list of eligible commodities. They believed that by not differentiating programming, this process is consistent with Section 202 (k)(2) of the *Agricultural Trade Act of 1978*, which stipulates that the 35-percent mandate applies only if it would not require a reduction in the total amount of guarantees issued. Targeting specific sectors in order to conclusively reach a 35-percent threshold runs the risk of violating this provision of law and thwarting support for all agricultural exports. They believed that the OGC memorandum to OIG, dated August 29, 2006, further established that the commodities used by FAS to calculate compliance are correct and that there should be no question that compliance was achieved. After review of OGC's determination, they did not believe that consultation with Congress is needed since OGC's research had found specific relevant legislative history in the House Conference Report that accompanied the FREEDOM Support Act.

However, FAS officials agreed that there is need for clarification in definitions across programs lines and will endeavor to review and clarify them within the Department.

OIG Position.

Contrary to FAS' response, our finding did not question the manner in which the agency currently manages its allocations under the commodity export programs, nor are we recommending that agency officials reduce their allocations of export credit funds for bulk and standard commodities to achieve a 35-percent allocation for high-value and processed commodities. However, regardless of the process by which funds are allocated, agency officials are still responsible for meeting the requirement of the 2002 Farm Bil, and thus would have to target 35 percent of their export credit funds to high-value and processed products if sufficient funding applications for these are received.

This may not be possible if FAS officials do not use standardized definitions to differentiate high-value/processed products from bulk/standard products. As noted in our finding, even the definitions contained in the 1992 FREEDOM Support Act were inconsistently applied and in some cases, the same commodities were classified differently from year to year. It is this condition that our recommendation was intended to address. FAS officials have expressed their agreement that clearer definitions are needed. We also maintain that Congress needs to be consulted as part of this process, so that decisions can be made as to whether the 15-year old definitions in the *1992* FREEDOM Act need to be updated or amended.

To reach management decision, FAS needs to provide a further response that details their plan, including timeframes, to standardize and clarify their definitions of high-value and processed products in the export credit programs.

Recommendation 4

Institute procedures to ensure that the required reports on the FMD Cooperator Program are timely prepared and submitted to Congress.

Agency Response.

In their response, agency officials stated that they will institute procedures to ensure that the remaining required report on the Cooperator Program is timely prepared and submitted to Congress.

OIG Position.

The response indicates that only one more report to Congress is required, but the 2002 Farm Bill required annual reporting to Congress without specifying an ending date. To reach management decision, FAS needs to provide us with timeframes for when the cited procedures will be in place and also to clarify whether the procedures will call for ongoing annual reports, as specified in the 2002 Farm Bill.

Finding 3 FAS Works to Improve Its Food Aid Performance Measures and Performance Data Reporting, But Improvements Are Still Needed

Although the *2002 President's Management Agenda* highlighted the need for FAS to evaluate the success of its food aid programs in terms of their actual benefits, new outcome-based performance measures to accomplish this had not been incorporated into the agency's reporting process under the *Government Performance and Results Act of 1993* (GPRA). FAS officials attributed this to the difficulty of designing performance measures that can assess program outcomes, when these are affected by multiple factors outside the agency's control. Also, FAS has not completed developing an automated system to accumulate, summarize and report program performance data. As a result, FAS' reports under GPRA are not yet able to adequately present the agency's accomplishments regarding its programs, or demonstrate that the agency is achieving the goals established by authorizing legislation.

During the 1990s, members of Congress became increasingly concerned about waste and inefficiency in Federal programs that undermined the confidence of the American people in the Government's ability to adequately address public needs. To address these concerns, Congress passed GPRA,[9] whose purpose was to improve the management, efficiency, and effectiveness of Federal programs by establishing a system for agencies to set goals for program performance and measure results.

The *2002 President's Management Agenda* required that foreign food aid programs be subject to an analysis of their benefits, costs, and performance to determine how they are meeting their priorities, and how well they are accomplishing the Administration's primary goal of directly feeding

[9] P.L.103-62. GPRA required Federal agencies to develop strategic plans, annual performance plans, and reports; to express performance goals in an objective, quantifiable, and measurable form; and to describe the means the agency will use to verify and validate its performance data. After OMB's PART review in FY 2004, GPRA's annual performance plan was replaced by a performance budget, linking an agency's strategic goals with its related annual performance goals and with the costs of the specific activities contributing to achieving those goals.

genuinely hungry populations.[10] Thus, FAS' food aid programs have three objectives for which program performance must be measured: (1) meeting global food security challenges, (2) improving literacy and promoting education, and (3) increasing economic growth and trade capacity in developing countries.

GPRA shifted the evaluation and measurement of program performance away from *output* towards *outcome*. By stating, for instance, how many metric tons of commodities it shipped during a given year, or how many grant agreements it signed, FAS can state with relative ease its programs' *output*. Determining the *outcome* resulting from shipping quantities of food to foreign countries is more complicated because it requires that FAS report how nutritional health and literacy in those countries were improved.[11] Also, improvements in donor countries' agricultural infrastructure and economic development resulting from grant activities funded by the agency's FFP Program[12] have yet to be measured. Because such important indicators of program success are affected by many factors beyond FAS' control—including wars, international economic conditions, and natural disasters—isolating the precise outcome of foreign food aid represents a challenge. Also, finding a common performance measure for food aid programs with multiple objectives can be difficult. In addition, USDA's food donations in recent years have been relatively small compared to those administered by USAID.

In FY 2004, OMB developed the PART as a diagnostic tool to evaluate Federal programs. PART was used to review 234 Federal agency programs, including the FAS and USAID food aid programs. OMB concluded that FAS' strategic planning and performance measures for its food aid programs were inadequate and that coordination between FAS and USAID was needed on program performance measures, evaluation, monitoring, and eligibility criteria. It found that FAS needed to develop performance measures that link to the long-term outcome goals of food security, as well as the agency's strategic goals and budget. OMB repeated its PART review during the FY 2006 budget process and upgraded FAS' rating from inadequate to moderately effective based on the development of the Food Aid Targeting Effectiveness Ratio, which measures USDA food aid programs' contribution

[10] Executive Office of the President, OMB, *The President's Management Agenda, FY 2002*, Program Initiative 13, Reform of Food Aid Programs, USAID, Department of State, USDA, page 67.
[11] Section 3107 of the 2002 Farm Bill established the McGovern-Dole International FFE and Child Nutrition Program to provide commodities to carry out preschool and school food programs to improve food security, reduce hunger, and improve literacy and primary education. Other FAS food aid programs include Section 416(b) donations and P.L. 480, also known as Food For Peace. P.L. 480 has three titles, each with a specific objective and serving countries at particular levels of development. Title 1 of P.L. 480 is administered by USDA, while Titles II and III are administered by USAID.
[12] The FFP Program, authorized by the FFP Act of 1985, provided for the donation or credit sales of U.S. commodities to developing countries and emerging democracies to support democracy and the expansion of private enterprise. To date, all food aid under this program has been through donation.

to the reduction in the number of the world's hungry people by one-half by 2015[13]. ERS assisted FAS in developing the ratio.

The Food Aid Targeting Effectiveness Ratio is a long-term performance measure intended to gauge the effectiveness of USDA's food aid programs in improving food security in low-income countries. It measures the effectiveness of USDA's food aid programs in addressing the food distribution "gaps" in the most food-insecure countries. ERS calculates the ratio using its Food Security Assessment Model, which measures food security based on estimations of food gaps in 71 of the world's poorest countries. Food gaps represent the difference between projected food availability and targeted food consumption.

While the development of the Food Aid Targeting Effectiveness Ratio is a significant accomplishment by ERS and FAS to assess USDA's performance in reducing world hunger, it is a measurement of success for only one of its programs' objectives. The ratio does not, for instance, measure the achievements of the FFE Program in improving literacy and primary education in targeted countries. It also does not measure the FFP Program's success in improving countries' agricultural infrastructure, economic development, or trade capacity building. The agency needs to continue to work on new performance measures to gauge its success in achieving the objectives established by the authorizing legislation for these programs.

In addition to improving its performance measures, FAS has also been working to improve its systems for accumulating and reporting data on its food aid programs. FAS officials continue to work with their counterparts at USAID to determine how to provide more responsive information to OMB on the status and results of food aid projects. A major project of FAS' 2002 Business Process Re-Engineering study was to design an interagency FAIS with common data elements. The new system will be used by all U.S. government agencies dealing with food aid – USDA (FAS and the Farm Service Agency), USAID, and the Department of Transportation, Maritime Division. It will contain program budgets, project proposals and agreements, commodity and freight purchases, commodity shipments, and payments. FAS has already developed a Performance Management and Evaluation Module that will become part of FAIS, which contains semi-annual logistics and monetization reports from PVOs and quarterly-financial reports. Eventually, FAS plans to implement a PVO-reporting module that will capture and report on performance data throughout the food aid process.

However, these new systems are not yet completed or implemented. At the time our fieldwork ended, FAS did not have a database that was capable of

[13] In 1996, member countries held a World Food Summit in Rome. Following the summit, in September 2000, the member countries adopted the United Nations Millennium Declaration goal to reduce the number of the world's hungry people by one-half by 2015. USDA also adopted this goal for its food aid programs.

adequately tracking or accumulating performance data to be used in GPRA reports.

Before FAS will be able to provide a comprehensive overall assessment of its food aid programs' success in achieving agency goals and the objectives of the food aid programs' authorizing legislation, agency officials will need to complete the outcome-based performance measures and the database system for accumulating, summarizing and reporting the programs' performance data.

Recommendation 5

Complete and adopt uniform outcome-based performance measures to assess whether FAS' programs are achieving the objectives of their authorizing legislation.

Agency Response.

FAS officials stated that beginning in April 2007, the agency will work with cooperating FFP and McGovern-Dole Program sponsors to identify potential, practical uniform outcome-based performance measures for various types of food aid interventions. Current procedures for collecting data and reporting also will be reviewed. By May 2008, FAS will announce a list of outcome measures to be adopted. Beginning in FY 2009, these measures will be included in food aid agreements.

OIG Position.

We concur with FAS' planned corrective actions. To reach management decision, FAS needs to provide us with copies of the outcome performance measures once these are developed, along with timeframes for their implementation.

Recommendation 6

Complete and implement the planned FAIS for collecting program performance data and the PVO-reporting module to summarize and report on the food aid programs' achievements toward FFE and FFP legislative objectives and goals. If necessary, seek additional funding from Congress to accomplish this.

Agency Response.

FAS officials stated that they have made substantial progress on FAIS and hope to secure funding to start building the system in FY 2008. They also stated that they hope to have the system completed for implementation by January 2009.

OIG Position.

We concur with the proposed actions. To reach management decision, FAS needs to provide clarification as to whether the dates cited in the response are the established timeframes. We also need clarification as to whether FAS has made attempts to secure funding for completion of the FAIS, and the alternatives being considered if funding levels are less than anticipated.

Scope and Methodology

The audit work primarily focused on the activities of FAS to implement the requirements of the Trade Title of the 2002 Farm Bill and the *President's Management Agenda*. Since FAS works closely with APHIS on issues involving biotechnology and on strategies to address technical barriers to trade, we also interviewed officials of that agency. We also interviewed a senior official of USAID in charge of the Food for Peace Program, regarding USAID's and FAS' efforts to address issues identified in the *President's Management Agenda*.

Our fieldwork was conducted at FAS and APHIS Headquarters in Washington, D.C., from January to May 2004. We monitored developments impacting identified issues through September 2006.

To accomplish our audit objectives, we:

- interviewed responsible senior FAS management officials of Export Credits, Commodity Marketing Programs (now the Office of Trade Programs), International Trade Policy, and other divisions and areas;

- assessed the adequacy of internal controls, policies, and procedures used by FAS to implement the 13 requirements of the 2002 Farm Bill, and also assessed the impact of changes to both new and existing programs (see exhibit A);

- reviewed FAS' management controls over the process of monitoring food aid grants;

- reviewed FAS' efforts to create a GMS to address the new market realities of the 21st century;

- reviewed OMB's PART assessments of FAS' food aid programs and interviewed FAS and USAID officials concerning the assessments and efforts made by the two agencies to address identified issues;

- interviewed responsible officials of APHIS' Trade Support Team and BRS;

- reviewed applicable legislative history, laws, regulations, Government Accountability Office reports, prior OIG reports, and agencies' internal reviews, including the *Federal Managers' Financial Integrity Act* reports;

- examined performance measure data related to the food aid and trade programs in the agencies' annual GPRA plans; and

- interviewed officials of PVOs operating food aid programs in Guatemala, Honduras, and Tajikistan.

We conducted our audit in accordance with generally accepted government auditing standards.

Exhibit A – FAS Implementation of Requirements of FY 2002 Farm Bill

International Food and Trade Programs Reformed or Created by the 2002 Farm Bill

Program Provisions	Farm Bill Reform(s)	Audit Results	Recommendations
(1) General provisions.	Programs should encourage approval of multi-year and multi-country agreements and are expanded to include all eligible organizations, not just PVOs. Each program is to streamline, improve, and clarify the application, approval, and implementation process, and to report progress to congressional committees.	FAS awarded multi-country agreements. For FY 2005, FAS awarded one multi-year FFP agreement and instituted multi-year shipments for existing 416 (b) agreements. For FY 2006, the agency committed $17 million for multi-year agreements with a maximum of 3 years for shipments of commodities. In addition to PVOs, FAS awarded agreements to the World Food Program of the United Nations.	NONE
(2) Export Credit Guarantee programs facilitate commercial sales of U.S. agricultural products.	Extends the Export Credit Guarantee programs and annual funding through 2007. Requires the Secretary and U.S. trade representative to consult regularly with Congress on multi-lateral negotiations at WTO and the Organization for Economic Cooperation and Development. Continues requirement that not less than 35 percent of export credit guarantees issued be used to promote exports of processed or high-value agricultural products. Extends repayment terms for the Supplier Credit Guarantee program from 180 to 360 days.	The 1996 and 2002 Farm Bills did not include definitions of processed and high-value commodities. The only guidance came from a 1992 House Conference report associated with the FREEDOM Support Act that provided food aid to emerging Russian and Eurasian democracies. FAS did not consistently apply the 1992 guidance in computing Congress' 35-percent target for supporting high-value and processed products. (See Finding 2.) Export Credits had not revised the Supplier Credit Guarantee program regulations to include the 360-day repayment term due to lack of demand and appropriation funding. Also, a new WTO agreement eliminated the 360-day requirement.	We recommend that, in consultation with the Department and Congress, FAS develop clear and consistent definitions to be used in defining which commodities should be classed as bulk/standard, high value, or processed for purposes of export credit and other programs.

Program Provisions	Farm Bill Reform(s)	Audit Results	Recommendations
(3) FMD helps maintain and develop foreign markets for U.S. agricultural commodities, primarily through trade associations.	Authorizes use of CCC funds to support the program and increases funding to $34.5 million. Requires continued emphasis on exporting value-added products to emerging markets. The Department is required to submit a report to Congress annually describing the amount of funds provided, the types of programs funded, the value-added products targeted, and the foreign markets developed for those products.	In April 2003, FAS submitted the first required FMD report to Congress reporting that in FY 2002, the $34.5 million in FMD funds had been allocated to 23 participants. Thirty percent, approximately $10.2 million had been used to promote value-added agricultural products around the world. The FMD funds had been used to support value-added products in numerous foreign emerging markets including China, Korea, Taiwan, Southeast Asia, the Middle East, Africa, and the Caribbean Basin. However, FAS had not submitted any more of the required reports to Congress since the April 2003 report. (See Finding 2.)	We recommended that FAS prepare and submit the required annual reports.
(4) Online Exporter Assistance Initiative. No similar provisions in 1996 Farm Bill.	USDA shall maintain a website that provides comprehensive information to assist exporters and potential exporters of U.S. agricultural commodities. No funds are authorized.	FAS has created a website identified as FAS Online to assist exporters and potential exporters of U.S. agricultural commodities. Users can find information on regulations and Federal laws that impact an export transaction. FAS officials continue to improve the website. They have added a new link, which has applicable forms and applications, and navigational features to make the website more user friendly.	NONE

Program Provisions	Farm Bill Reform(s)	Audit Results	Recommendations
(5) GMS. The 1996 Farm Bill established and "Agricultural Export Promotion Strategy" to expand export markets for U.S. agricultural commodities. The Secretary was required to annually identify priority markets with the greatest potential for increasing exports. The 2002 Farm Bill built on the 1996 bill by requiring a long-range GMS.	Mandates preparing a long-range agricultural trade strategy that identifies opportunities for growth in exports; ensures that resource programs and policies are coordinated with those of other agencies; and removes barriers to trade in overseas markets. Consultations with relevant congressional committees shall occur before November 9, 2002, and every 2 years subsequently.	FAS has not completed its GMS and submitted it to Congress as required. Rather than implementing a centralized global strategy, FAS supports the country and regional market strategies of the agency's individual program participants. (See Finding 1.)	We recommended that FAS develop and implement processes to combine all the agency's strategic planning information as a basis for formulating market strategies at a worldwide level to address the United States' declining market share of global agricultural exports.
(6) Export Enhancement Program (EEP) provides funding to U.S. exporters to help compete against subsidized prices in specific export markets.	Extends annual funding through 2007 at the current funding level of $478 million per year. Expands definition of unfair trade practices to include: (1) state trading enterprises; (2) unfair subsidies by foreign counties; (3) unjustified trade restrictions on new technologies (e.g., labeling of biotech products); (4) unjustified SPS barriers; (5) unfair rules on tariff-rate quotas; and (6) failure of a country to adhere to trade agreements.	The Department made a policy decision not to implement EEP funding except in rare cases. Although funding for the program is still available, in practice, the program has not operated since FY 2001. FAS and APHIS continue their efforts to address unjustified trade restrictions and SPS barriers and to enforce trade agreements.	NONE

Program Provisions	Farm Bill Reform(s)	Audit Results	Recommendations
(7) P.L. 480, also known as Food for Peace, includes concessional sales through Title I and donations and grants through Titles II and III. The Title II and III programs are administered by USAID.	The 1996 Farm Bill authorized Title I agreements with private entities in addition to foreign governments; modified repayment terms for Title I credit including (1) elimination of the minimum repayment period of 10 years and (2) reduction of the maximum grace period from 7 to 5 years. The 2002 Farm Bill reauthorized this program through 2007 and adds conflict prevention as a program objective.	FAS has been working in post-conflict zones since 1992 toward the U.S. Government's strategic goals of fostering regional stability, building civil society, and democratic government institutions. FAS programs focus on agricultural sector development, scientific education, and international exchanges. FAS is currently working as part of the U.S. Government's reconstruction efforts in Afghanistan, Iraq, Kosovo, Bosnia, Serbia, and Montenegro.	NONE
(8) George McGovern-Robert Dole International FFE and Nutrition Program.	Authorizes a program to provide commodities and financial and technical assistance for foreign preschool and school feeding programs. The goal is to reduce hunger and improve literacy and nutrition programs for pregnant and nursing women and for young children. Eligible recipients include governments, PVOs, cooperatives, and other entities. Provides $100 million of CCC funds to continue existing pilot projects and authorize the program in subsequent years.	In FY 2003, FAS officials approved 21 project proposals for countries in Africa, Asia, Latin America, the Middle East, Central Asia, and Eastern Europe. The sponsors of these selected proposals included PVOs and the United Nations' World Food Program. The new program replaces the Global FFE Initiative Program that began as a pilot program in FY 2001. More recently during 2006, FFE assistance was expected to reach $103 million and benefit approximately 2.4 million women and children through donations of nearly 80,000 metric tons of commodities.	NONE

Program Provisions	Farm Bill Reform(s)	Audit Results	Recommendations
(9) Technical barriers to trade. No similar provisions in the FY 1996 Farm Bill.	New programs established to remove, resolve, or mitigate SPS, and other technical barriers to trade.	As part of the new reorganization plan, FAS' Office of Scientific and Technical Affairs will include an International Regulations and Standards Division. The division will include a WTO SPS Committee and Enquiry Point Branch; a CODEX, OIE, IPPC, MEA, and ISO Branch; and a Foreign Regulations Branch. FAS staff in these branches will work toward the development of international food standards and SPS regulations, and the resolution of technical issues. The Enquiry Point Branch will handle all outgoing SPS notifications for the United States, sending them to the WTO SPS committee, and track commitments by the U.S. and foreign governments to address SPS and technical issues. FAS works closely with APHIS to address technical barriers to trade. APHIS officials also work closely with third world countries trying to establish regulatory frameworks for imports of U.S. agricultural products being donated as food aid.	NONE
(10) Biotechnology and agricultural trade program. No similar provisions in the 1996 Farm Bill.	Addresses regulatory non-tariff barriers to the export of U.S. agricultural commodities. Authorizes grants for public and private-sector projects for: (1) quick-response intervention regarding non-tariff barriers to U.S. exports involving issues of biotechnology, food safety, disease, or other SPS concerns and (2) developing protocols as part of bilateral negotiations with other countries on issues such as animal health, grain quality, and genetically modified organisms. Program is authorized at $6 million per year through 2007.	FAS and APHIS formed biotech groups, which deal specifically with biotech related issues. The FAS group has implemented several projects dealing with quick-response intervention and other biotech related issues. APHIS established BRS to be responsible for establishing a Federal regulatory framework for the biotech agricultural area. It coordinates with other Federal agencies and agricultural groups to develop protocols on biotech related issues. BRS also helps other countries with trade capacity building issues, establishment of regulations, and provides instructions for performing risk assessments. For FY 2004, OMB allocated $2 million to USDA to be dedicated to biotechnology.	We are not making recommendations related to biotechnology trade issues as part of this audit. Findings and recommendations, if applicable, will be reported under OIG Audit No. 50601-0014-Te, "USDA's Role in the Export of Genetically Engineered Agricultural Commodities".

Program Provisions	Farm Bill Reform(s)	Audit Results	Recommendations
(11) TASC - No similar provisions in the 1996 Farm Bill.	Establishes an export assistance program to address unique barriers that prohibit or threaten the export of U.S. specialty crops. Provides for public and private-sector projects and technical assistance to address time-sensitive and strategic issues of market retention, market access, and market expansion. Authorized at $2 million a year.	The FAS Marketing Operations Division officials approved 18 TASC projects in FY 2002 and 16 TASC projects in FY 2003.	NONE
(12) Trade-related programs in other titles: Uruguay Round compliance. The Uruguay Round Agreement on agriculture puts a maximum allowable level on trade-distorting domestic support programs as measured by the aggregate measurements of support (AMS). The ceiling on the U.S. AMS support has been $19.1 billon since FY 2000, and will continue to be at this level until a new WTO agreement is reached. No similar provisions were in the 1996 Farm Bill.	If the Secretary determines that AMS ceiling will be exceeded, the Secretary shall to the maximum extent practicable, adjust expenditures to avoid exceeding allowable levels. Before making any adjustments, the Secretary shall submit a report to Congress describing the adjustments to be made.	The 2002 Farm Bill required USDA to develop a mechanism called the "circuit breaker." This mechanism requires the Secretary of USDA to ensure that the United States does not exceed its WTO limits. USDA has not developed any regulations for the "circuit breaker." One official said the Department received little guidance in the Farm Bill for how they should implement this mechanism. Also, the current AMS level is significantly below the $19.1 billion support ceiling and is projected to remain below that level. Therefore, the circuit breaker mechanism has not been needed.	NONE

Program Provisions	Farm Bill Reform(s)	Audit Results	Recommendations
(13) Country-of-origin labeling.	Requires that meat, fish, produce, and peanuts be labeled with the country of origin, starting in 2004.	The FY 2004 appropriation bill delayed implementation of this program, except for fish and shellfish, until September 30, 2006. Fish and shellfish were to be implemented September 30, 2004. In November 2005, P. L. 109-97 delayed the implementation of country of origin labeling requirements until September 30, 2008.	NONE

United States Department of Agriculture

Farm and Foreign Agricultural Services

Foreign Agricultural Service

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TO: Robert W. Young
Assistant Inspector General for Audit
Office of Inspector General

FROM: Michael W. Yost
Administrator

MAR 5 2007

SUBJECT: Response to OIG Official Draft Audit Report -- "Foreign Agricultural Service Implementation of the Trade Title of the 2002 Farm Bill and the 2002 President's Management Agenda" (50601-12-At)

The Foreign Agricultural Service (FAS) appreciates this opportunity to respond to the Office of Inspector General's (OIG) draft audit report. FAS also acknowledges the effort made by OIG auditors to work with FAS officials to better understand FAS strategic objectives related to market development. However, FAS must point out several areas where misunderstandings or differences of opinion may have resulted in misleading statements and conclusions in the report.

Specifically, OIG speculates that FAS's strategic partnership with industry trade groups may not be effective in promoting U.S. agricultural exports. In reaching this conclusion, OIG relied on questionable export market share data and minimized the value of compelling economic analysis provided by FAS that demonstrated the very positive impact of the market development programs on U.S. exports.

For example, OIG was made aware of a recently completed independent cost-benefit study commissioned by FAS which found that the market development programs have proven to be very effective in supporting U.S. agricultural trade. The study calculated that by 2008 the market development programs would enable total U.S. agricultural exports to reach $74.5 billion, versus $70.8 billion without the programs, valuing the benefit at $3.8 billion (note that in the time since the cost-benefit study was completed, USDA has raised its FY 2007 export forecast to a record $77.0 billion). Furthermore, annual farm cash receipts (which were projected to average $225.7 billion over the life of the 2002 Farm Bill), were calculated to have increased by $2.2 billion due to the additional agricultural exports generated by the market development programs. The higher cash receipts, in turn, increased annual farm net cash income by $460 million, representing a $4 increase in farm income for every additional $1 increase in government spending on market development. The programs also helped generate positive welfare gains for the overall U.S. economy of roughly $800 million annually.

To support its speculation, OIG relied on an "apples to oranges" comparison of its own questionable export market share calculations to historical FAS documents. OIG calculated a sharp decline in the U.S. market share of world agricultural trade between 1984 and 2005, and contrasted that with calculated increases in the global market share of competitor exporters such as the European Union (EU), China, Canada, Mexico and Japan. Even though FAS provided OIG with more accurately comparable statistical data that demonstrated a far more modest decline in U.S. market share during this time period, OIG elected to rely upon its own data set while failing to acknowledge several important facts that would put its statements in the proper context.

The most egregious error by OIG in its calculations was using a total EU export value that includes the EU intra-trade among member nations, significantly inflating the EU market share. Also left out is the fact that the EU nearly doubled in size during the 21 year span identified by OIG, adding the results from major agricultural producers/exporters such as Poland and Austria to its export totals. The appreciation of the Euro against the U.S. dollar (which was used to calculate the World Trade Organization statistics used by OIG) sharply inflated the measure of EU exports and market share as well. In fact, one of the main findings highlighted in the independent study was that the value of the dollar is a major determinant in the level of U.S. market share, estimated to be four times more powerful than market development efforts in determining U.S. market share.

Market access barriers also have been a significant problem for U.S. exports and market share. Even though significant improvements in market access were accomplished during this period through the Uruguay Round and subsequent Free Trade Agreements like the North American Free Trade Agreement, old problems such as the continued heavy use of export subsidies by other competitors still remain, even as new problems like the use of sanitary and phytosanitary restrictions have crept up. Restrictions on genetically modified corn and soybeans and on hormone-treated beef in particular have hurt U.S. exports to many countries, particularly the world's largest import market – the EU.

Meanwhile, other factors sometimes tend to overshadow the real growth success that U.S. agricultural exports have enjoyed even as the global export market expanded. These include the emergence of new export competitors like Brazil, and outbreaks of Bovine Spongiform Encephalopathy and Avian Influenza. The changing global landscape contributed to FAS's 2001 decision to remove the target market share measurement from the agency's Strategic Plan and focus instead on increasing the dollar amount of U.S. agricultural products sold into foreign markets. In that there has been great success, as U.S. exports increased from $26 billion in 1986 to a record $69 billion in 2006, and are projected to rise even further to $77 billion in 2007.

Regarding OIG's discussion of the Unified Export Strategy (UES), FAS notes several misunderstandings or misrepresentations in this section of the OIG report as well. For example, OIG asserts that the allocation decisions at the Deputy Administrator level are primarily conducted on a verbal basis, implying that there is no formal or strategic review of the proposals at this stage. This statement is in direct contrast to the actual process used. All allocation recommendations are based on both analytical reviews and a competitive performance-based formula across divisions and industry groups (i.e., at the Deputy Administrator level). The Deputy Administrator's final allocation decisions are documented and presented in the form of a decision memo to the FAS administrator. This entire process is published annually in the Federal Register.

The OIG audit report acknowledges FAS's efforts to encourage even more strategic planning on the part of the program participants, specifically in the form of the comprehensive industry strategic planning concept. However, the report suggested that this concept was not being used uniformly across divisions nor was there a specific process to ensure that the idea was being applied in a consistent fashion. In fact, FAS again had provided copies of evaluation documents that detailed numerical ratings that were consistently applied across all divisions.

As a final example of misleading statements and conclusions in the report, in speculating that FAS's compliance with the Farm Bill's mandate that 35 percent of credit guarantees should be directed toward high-value ***and*** (emphasis added) processed products, OIG failed to properly reflect the realities of how credit guarantee allocations are made, and failed to follow the guidance that it requested from USDA's Office of General Counsel (OGC), which is attached as a part of this response. In this case, OIG's use of the word "and" is inconsistent with section 202(k)(1) of the Agricultural Trade Act of 1978, which distinguishes between the two categories as referenced in the text as high-value ***or*** (emphasis added) processed products. A full reading of the OGC determination provides several such instances where OIG may have been too eager to include in this review its own unsupported theories and opinions, causing it to stray into the policy-making process and to appear less than objective in its efforts and conclusions.

As for the six recommendations contained within the OIG report, FAS's specific response to each is provided as follows:

Recommendation 1:

Develop and implement processes to combine and integrate the strategic information contained in the UES and in the CSS documents, as well as the analyses now performed within the divisions of FAS' Office of Trade Programs, and to [sic] use these as a basis for formulating marketing strategies at a worldwide level.

FAS Response:

Congress and the Secretary of Agriculture have specified that the FAS Administrator and agency managers have the authority and prerogative to determine the methods by

which the agency fulfills its mission. In the performance of its responsibility to administer the export market development programs, FAS employs practices and procedures that are wholly consistent with FAS and USDA strategic goals. Since 1997, FAS has mandated that industry trade groups which present the broadest representation of their commodity sector submit a single UES when applying for federal funds from any of the FAS-administered foreign market development programs. These global marketing strategies are quite comprehensive, identifying target markets and proposing plans for activities that will make the most efficient and effective use of all USDA and industry matching resources available. Dedicated FAS agricultural marketing specialists thoroughly review every application, as do FAS officials serving in relevant overseas offices. The proposals also undergo an objective competitive evaluation which utilizes a consistent series of transparent criteria to measure performance such as export goals, past export values, and relative market value. This entire process is published in advance in the Federal Register; is undertaken in a uniform, time-tested manner throughout the agency; and is well documented in writing at every stage.

In addition, FAS encouraged these industry trade group partners to increase their strategic use of programs. In recent years FAS provided additional funding incentives to encourage industry partners to work more closely across all segments of their own export supply chain (growers, processors, packers, research institutions, etc.), and to collaborate with one another in specific cross-commodity projects of mutual interest. The result has been a more coordinated and effective approach to bringing U.S. goods into the global market. For example, the U.S. Grains Council, the American Soybean Association, and the U.S. Poultry and Egg Export Council recently teamed up and pooled resources in several foreign markets to implement an effective response to the outbreak of Avian Influenza.

FAS also provides a strong link in the strategic partnership that USDA maintains with the U.S. agricultural industry. FAS overseas staff share market information and provide on-the-ground support with regard to market access and other trade policy issues. FAS Washington staff work closely with regulatory agencies, the office of the U.S. Trade Representative, and the Departments of State and Commerce to support industry's foreign market development and maintenance efforts. The partnership works both ways, as the industry increasingly is providing critical support for USDA and FAS mandates in the area of capacity building overseas through Market Access Program and Foreign Market Development Cooperator Program funded activities that offer technical training and scientific exchanges.

As the OIG report notes, FAS has recently completed a comprehensive reorganization that shifts resources to address critical needs in the area of market access, trade negotiation and capacity building. As part of this reorganization, FAS has established a new Office of Country and Regional Affairs that is coordinating a comprehensive strategic plan based on the new Country Strategy Statements that will cover not only marketing but also the other critical areas of market access, trade negotiation, capacity building, reporting and analysis.

FAS will continue all these efforts already underway to enhance coordination among and between industry partners, FAS overseas offices, FAS Washington staff, and other appropriate agencies to expand market access and export opportunities for exporters of U.S. food and agricultural products.

Recommendation 2:

Perform a long-term analysis of FAS' strategic goals and global marketing approach, including consultations with Congress and other Federal agencies, to determine what strategies are needed to increase the United States' competitiveness in global agricultural exports. Based on the results of this analysis, develop and implement export strategies as needed.

FAS Response:

FAS maintains a constant state of consultation with Congress on virtually every aspect of the agency's operations, including its mandate to support the export of U.S. food and agricultural products. FAS also enjoys close working relationships with other agencies, including the Office of the U.S. Trade Representative, the Department of State, the U.S. Agency for International Development, and the Department of Commerce, as well as the regulatory agencies in USDA that play an important role in supporting FAS efforts to address foreign market access issues. All of these contacts are fully and effectively utilized in FAS's overall market development efforts.

FAS has continued to review its overall strategic plan and make adjustments as needed. The recent FAS reorganization is an example of ongoing FAS efforts to address the changing agricultural and trade environments. As noted in the response to Recommendation 1, there already is an effort underway to integrate more fully FAS and industry market development efforts that goes far beyond just marketing strategies to include comprehensive strategic planning on market access, trade negotiation, capacity building, reporting, and analysis.

Recommendation 3:

In consultation with the Department and Congress, review and clarify definitions to be used defining which commodities should be classified as bulk or standard, high value, or processed for purposes of export credit guarantees and other programs.

FAS Response:

As alluded to above, beginning in 1999 FAS began moving away from programming individual commodity allocations under the credit guarantee programs, and now provides that country or regional allocations are, in most cases, available to the entire General Sales Manager list of eligible commodities. Under this process programming is inclusive and does not differentiate between the eligible commodities, thus allowing maximum flexibility for the exporters in registering transactions. By not differentiating programming, this process is consistent with Section 202(k)(2) of the Agricultural Trade Act of 1978, which stipulates that the 35 percent mandate applies only if it would not require a reduction in the total amount of guarantees issued. Targeting specific sectors in order to conclusively reach a 35 percent threshold runs the risk of violating this provision of law, and thwarting support for all agricultural exports.

Clearly OGC's August 29, 2006, memorandum to OIG on this matter further established that the commodities used by FAS to calculate compliance are correct. As a result of this determination, there should be no question that compliance was achieved. Further, after review of OGC's determination, we do not feel that consultation with Congress is needed to review and clarify those definitions as suggested in Recommendation 3, as OGC clearly researched and found specific relevant legislative history in the House Conference Report that accompanied the FREEDOM Support Act.

However, FAS agrees that there is need for clarification in definitions across programs lines, and will endeavor to review and clarify them within the Department.

Recommendation 4:

Institute procedures to ensure that the required reports on the FMD Cooperator Program are timely prepared and submitted to Congress.

FAS Response:

FAS will institute procedures to ensure that the remaining required report on the Cooperator Program is timely prepared and submitted to Congress.

Recommendation 5:

Complete and adopt uniform outcome-based performance measures to assess whether the FFE and FFP programs are achieving the objectives of the programs' authorizing legislation, including the improvement of literacy, primary education, agricultural infrastructure, economic development, and trade capacity building.

FAS Response:

Beginning in April 2007, FAS will work with cooperating Food for Progress and McGovern-Dole Program sponsors to identify potential, practical uniform outcome-based performance measures for various types of food aid interventions. Current procedures for collecting data and reporting also will be reviewed. By May 2008, FAS will announce a list of outcome measures to be adopted. Beginning in FY 2009, these measures will be included in food aid agreements.

Recommendation 6:

Complete and implement the planned FAIS for collecting program performance data and the PVO-reported module to summarize and report on the food aid programs' achievements toward FFE and FFP legislative objectives and goals. If necessary, seek additional funding from Congress to accomplish this.

FAS Response:

FAS has made substantial progress on FAIS in the three full years since OIG's fieldwork ended. FAS hopes to secure funding to start building the system in FY 2008 and hopes to have the system completed for implementation by January 2009.

If you have any questions or concerns regarding this memorandum, or if you need additional information, please contact James Gartner, FAS's Audit Liaison, on (202) 720-0517.

Attachment

cc: Ernest Hayashi
Howard Albers

United States Department of Agriculture
AUG 29 2006

Office of the General Counsel

Washington, D.C. 20250-1400

MEMORANDUM FOR ERNEST M. HAYASHI
DIRECTOR
FARM AND FOREIGN AGRICULTURAL DIVISION
OFFICE OF INSPECTOR GENERAL

From: Ralph Linden
Assistant General Counsel
International Affairs and Commodity Programs Division

Subject: Your reference 50601-12-At
"Implementation of President's Management Agenda and Trade Title of 2002 Farm Bill - Interpretation of 2002 Farm Bill Provisions Related to Foreign Agricultural Service (FAS) Export Credit Programs"

Introduction

In connection with the above-referenced audit of your office, we have received your memorandum of August 15, 2006, requesting responses to specific questions concerning the application of certain provisions of law to activities of the Foreign Agricultural Service in its administration of the (1) Commodity Credit Corporation export credit guarantee programs and (2) Market Access Program (MAP).

In particular, you have asked the following questions in connection with the export credit guarantee programs:

"(1) Where are high-value or processed agricultural commodities defined for the purposes of 7 USC 5622? Please include the citations to the law, legislative history and/or program regulations.

(2) Should FAS include cotton and rice exports in the computation of the 35-percent goal for high value or processed agricultural product in the export credit guarantee program?"

In connection with the MAP program you have asked the following questions:

"(1) Please clarify what Congress intended by directing FAS to "give equal considerations" to proposals from old and new participating organizations, and give equal consideration to proposals submitted for activities in emerging markets and other than emerging markets. An explanation from the legislative history or further explanatory language would be appreciated.

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(2) What actions were required by FAS to comply with the program priorities intended by Congress regarding the development of new cooperators and programs in emerging markets?"

Answers with Respect to the Export Credit Guarantee Programs:

1. The primary source for the definition of high-value or processed agricultural products for purposes of 7 USC 5622(k) is House Conference Report No. 102-964 (Oct. 1, 1992) accompanying the Freedom for Russia and Emerging Eurasian Democracies and Open Markets Support Act of 1992 ("FREEDOM Support Act") (P.L. 102-511). In addition, the Secretary of Agriculture may determine an otherwise qualifying agricultural product to be a high-value product pursuant to 7 USC 5602(7) and regulations promulgated thereunder. Numerous products have received such designation and are reported as such on the FAS website.

2. The relevant legislative history explicitly contemplates inclusion of milled rice within the meaning of a processed agricultural product. Raw cotton is not traded in commercial export markets. Exported cotton must first be ginned and baled. The relevant criteria for a "processed agricultural product" is "a product derived from a bulk or raw agricultural commodity which, as a result of the application of human labor, the use of machines, or other factors involved in a manufacturing process, is increased in value and made more appropriate for human consumption or use." Consequently, for the specific purposes of section 202(k) of the Agricultural Trade Act of 1978, as amended (7 USC 5622(k)), it is certainly reasonable for FAS to characterize exported cotton as a "processed agricultural product."

Answers with Respect to the Market Access Program:

1. 7 U.S.C. 5641(c)(2) requires FAS to give "equal consideration", i.e., the same continuous and careful thought, to proposals from new participants as it gives to proposals from existing/former participants of the MAP program, to the maximum extent practicable. Similarly, the statute requires FAS, to the extent it can practicably do so, to give "equal consideration" to proposals involving activities in emerging markets as it gives to proposals involving other markets. Thus, to the extent practicable, a proposal should not enjoy greater or lesser consideration simply because of the applicant's prior participation or lack thereof in the MAP program. Similarly, to the extent practicable, a proposal should not enjoy greater review simply because it is aimed at a mature market. The conference report to the 2002 Farm Bill states with regard to this section "that proposals submitted by new program participants and programs in emerging markets shall receive consideration equal to that given to current program participants for new funds made available."

2. The only action required by FAS to comply with 7 U.S.C. 5641(c) is to give "equal consideration," i.e., equal thought, to proposals submitted to the MAP program from new cooperators and from existing/prior cooperators and "equal consideration" to proposals submitted to the MAP program involving programs in emerging markets and programs in other (i.e., more

mature) markets. 7 U.S.C. 5641(c) does not require FAS to take any other actions, such as outreach activities.

Discussion with Respect to the Export Credit Guarantee Programs:

1. Processed and high-value products under the CCC export credit guarantee programs

Your memorandum and inquiry appear to focus on the text of section 202(k)(1) of the Agricultural Trade Act of 1978, as amended (7 USC 5622 (k)(1)). As most recently amended by section 3102(b) of the Farm Security and Investment Act of 2002 ("2002 FSIA") and section 243(a)(5) of the Federal Agriculture Improvement and Reform Act of 1996 ("1996 FAIR Act"), such section 202(k) provides:

"(k) Processed and High-Value Products -

(1) In General - In issuing export credit guarantees under this section, the Commodity Credit Corporation shall, subject to paragraph (2), ensure that not less than 25 percent for each of fiscal years 1996 and 1997, 30 percent for each of fiscal years 1998 and 1999, and 35 percent for each of fiscal years 2000 through 2007, of the total amount of credit guarantees issued for a fiscal year is issued to promote the export of processed or high-value agricultural products and that the balance is issued to promote the export of bulk or raw agricultural commodities.

(2) Limitation. - The percentage requirement of paragraph (1) shall apply for a fiscal year to the extent that a reduction in the total amount of credit guarantees issued for the fiscal year is not required to meet the percentage requirement."

In your review of implementation of this provision by FAS, you concluded that FAS "had not established management controls to monitor the percentage of high-value and processed products supported by its export credit guarantee programs" in response to section 202(k). As a result, you asked FAS "to prepare a report identifying the percentages of credit guarantees that could be counted toward [the current] 35-percent target." FAS reported that it had achieved the target by 2003. FAS included rice and cotton as high-value or processed commodities for purposes of this calculation. You indicate that without rice and cotton, the relevant percentage would drop to 21.6.

Apparently, OIG and FAS disagree over the appropriateness of inclusion of rice and cotton as high-value or processed commodities for purposes of section 202(k). FAS apparently considers both eligible for inclusion, but "OIG concluded that while cooked rice or cooked rice included in other prepared food mixtures could be considered value added, milled rice must be cooked before it is ready to eat" and therefore, presumably, OIG believes that milled rice is not eligible for inclusion.

The review of OIG "has not identified a definition of high-value or processed products" for purposes of section 202(k). Your memorandum notes that the 1996 FAIR Act (section 243(c)) amended the definition of United States agricultural commodity, effectively authorizing the issuance of export credit guarantees in connection with high-value products with at least 90 percent U.S. content by weight. OIG notes that such section 243(c) did not specifically classify any particular products as high-value.

After a review of various ancillary sources, OIG has raised the two specific questions noted above.

Section 243(c) of the 1996 FAIR Act (7 USC 5602(7) specifically authorized the Secretary of Agriculture to determine when an otherwise qualifying product of an agricultural commodity is a "high-value agricultural product" (7 USC 5602(7)(B)(ii)). Such authority is replicated in program regulations applicable to (1) the CCC Export Credit guarantee Program and CCC Intermediate Export Credit Guarantee Program at 7 CFR Section 1493.20(z)(2)(ii) and (2) the Supplier Credit Guarantee Program at 7 CFR Section 1493.410(x)(2)(ii). The FAS website provides a list of agricultural products that have been determined to be high-value agricultural products pursuant to this authority (http://www.fas.usda.gov/excredits/gsmcommodities.html). Consequently, any products duly determined as high-value pursuant to this authority are presumptively high-value for purposes of section 202(k). However, neither rice nor cotton is listed among these products.

Although OIG has referred to the 1996 FAIR Act and the 2002 FSIA, the relevant statutory language concerning "processed agricultural products and high-value agricultural products" as well as a set-aside for a percentage of export credit guarantees in connection with such goods, first appeared in section 709 of the Freedom for Russia and Emerging Eurasian Democracies and Open Markets Support Act of 1992 ("FREEDOM Support Act") (P.L. 102-511). Section 709(a)(2) of that act first added sub-section 202(k) to the currently applicable Agricultural Trade Act of 1978, as amended. Although such set-aside originally applied, with respect to the export credit guarantee programs, to sales to the independent states of the former Soviet Union, the specific reference to processed and high-value agricultural products has since remained unchanged.

In a rare instance of specifically relevant legislative history, the House Conference Report (No. 102-964, Oct. 1, 1992) accompanying the FREEDOM Support Act provides:

"The committee of conference intends that the term 'processed agricultural product' means a product derived from a bulk or raw agricultural commodity which, as a result of the application of human labor, the use of machines, or other factors involved in a manufacturing process, is increased in value and made more appropriate for human consumption or use. Such term includes, but is not limited to livestock products, poultry products, fish products (without regard to whether such fish are harvested in aquacultural operations), dairy products, peanut products, wheat flour, **milled rice [emphasis added]**, refined sugar, vegetable oil, processed baby foods, and prepared, preserved, canned and other processed food products.

"The committee of conference intends that the term 'high-value agricultural product' means an agricultural commodity the value of which, on a per-unit or equivalent volume basis, is substantially higher than the value of bulk or raw agricultural commodities, such as grains or oilseeds. The term includes, but is not limited to fresh, chilled, or frozen meats, fish (without regard to whether such fish are harvested in aquacultural operations), dairy cattle, fruits and vegetables, eggs, breeder stock, plant seeds, and tobacco." (1992 U.S. Code Cong. And Adm. News, p. 2813).

Consequently, the directly relevant legislative history explicitly includes milled rice within the meaning of "processed agricultural product."

With respect to cotton, a difference exists between raw cotton and cotton in a form in which it can be exported. As OIG notes, cotton traded in export markets is both ginned and baled. As the "lowest form of cotton in the export trade," ginned and baled cotton is, OIG concludes, not a processed or high-value commodity for purposes of section 202(k).

However, the standard for classification under section 202(k) as a processed or high-value commodity is not whether the good is something other than "lowest unit of trade measured in the trade and export environment" or the "lowest form . . . in the export trade," as OIG has theorized with respect to rice and cotton, respectively. The Conference Report language accompanying the FREEDOM Support Act provides numerous contrary examples in addition to milled rice itself: fish, dairy cattle, fruits and vegetables, eggs, breeder stock, plant seeds, and tobacco. The relevant criteria for a "processed agricultural product" is "a product derived from a bulk or raw agricultural commodity which, as a result of the application of human labor, the use of machines, or other factors involved in a manufacturing process, is increased in value and made more appropriate for human consumption or use." Without question, for raw cotton to be exported and appropriate for use in export markets, the raw cotton must be ginned and baled through "human labor, the use of machines, or other factors involved in a manufacturing process." Consequently, for the specific purposes of section 202(k) of the Agricultural Trade Act of 1978, as amended, it is certainly reasonable for FAS to characterize exported cotton as a "processed agricultural product."

Discussion with Respect to the Market Access Program:

OIG has requested further clarification of Congress' "intent" in 7 U.S.C. 5641(c). In this case, the plain language of 7 U.S.C. 5641(c) provides clear direction as to FAS' responsibilities. The provision states that: "In providing any amount of funds made available under paragraph (1)(A) for any fiscal year that is in excess of the amount made available under paragraph (1)(A) for fiscal year 2001, the Secretary shall, to the maximum extent practicable, (A) give equal consideration to (i) proposals submitted by organizations that were participating organizations in prior fiscal years; and (ii) proposals submitted by eligible trade organizations that have not previously participated in the program established under this subchapter; and (B) give equal consideration to (i) proposals submitted for activities in emerging markets; and (ii) proposals submitted for activities in markets other than emerging markets."

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The language in the statute is straightforward. The word "consideration" is defined to mean "continuous and careful thought;" "a careful weighing of the reasons for or against something." See Merriam-Webster Online Dictionary. "Consideration" is synonymous with "debate, deliberation, thought." The word "practicable" is defined to mean "capable of being put into practice or of being done or accomplished: feasible". "Practicable" is synonymous with "possible". Thus, the statute's plain language directs FAS, to the maximum extent it can practicably do so, to give the same careful and continuous thought to proposals from new participants as it gives to proposals from existing participants. The statute also requires FAS to give the same level of deliberation to proposals involving emerging markets as it gives proposals involving other markets. To the extent feasible, a proposal should not receive greater or lesser review simply because of the applicant's prior participation or lack thereof in the MAP program. Similarly, to the extent possible, a proposal should not enjoy an advantage or disadvantage simply because it is aimed at a particular type of market.

This is the entire scope of 7 U.S.C. 5641(c). In the above-referenced audit, OIG has noted its concern that FAS has not conducted increased outreach to inform potential exporters of the additional MAP funds available to them. The language of the statute, however, does not authorize FAS to conduct any activity, including outreach activities, other than the consideration of proposals submitted in the regular conduct of the MAP program. If FAS were to attempt to justify outreach activities under 7 U.S.C. 5641(c), it would be OGC's opinion that FAS lacked statutory authority to do so under that provision.

While the plain language of the statute is dispositive regarding OIG's questions concerning 7 U.S.C. 5641(c), given OIG's request for further explanatory language/legislative history, OGC has researched the legislative history of the provision. Section 3103 of the 2002 Farm Bill initially originated in the House version of the farm bill and simply increased funding for the MAP program through fiscal year 2011. Subsequently, the Senate version of the bill reduced the funding levels and added the new subsection involving "Program Priorities." In the initial Senate proposal, the new subsection on program priorities required, without caveat, that for funds over $90 million, priority be given to proposals made by applicants who had never participated in MAP before or for emerging markets. In the final bill, however, this language was changed to require the Secretary to comply only "to the maximum extent practicable" and only to give "equal consideration," rather than "priority," to such proposals. In explaining this provision, the House Conference Report to the 2002 Farm Bill simply noted that "[t]he Conference substitute . . . establishes that proposals submitted by new program participants and programs in emerging markets shall receive consideration equal to that given to current program participants for new funds made available." House Conference Report No. 107-424 (May 1, 2002), p. 508, accompanying the Farm Security and Rural Investment Act of 2002 (P.L. 107-171). Thus, the legislative history confirms that section 3103 is limited simply to FAS' consideration of proposals and does not direct FAS to conduct any outreach activities.

Informational copies of this report have been distributed to:

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