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[Opportunities to Reduce the Ocean Transportation Costs of P.L. 480 Commodities]. B-95832. September 7, 1977. 9 pp. + 2 appendices (3 pp.).

Report to Secretary, Department of Agriculture; by Henry Eschwege, Director, Community and Economic Development Div.

Issue Area: Transportation Systems and Policies: National Policies and Programs (2406).
Contact: Community and Economic Development Div.
Budget Function: Commerce and Transportation: Water Transportation (406).
Organization Concerned: Maritime Administration; Commodity Credit Corp.
Congressional Relevance: House Committee on Agriculture; Senate Committee on Agriculture, Nutrition, and Forestry.
Authority: Cargo Preference Act of 1954 (P.L. 84-664). Agricultural Trade Development and Assistance Act of 1954 (P.L. 84-480).

The Cargo Preference Act of 1954 requires that at least 50 percent of the tonnage shipped under U.S. Government-financed programs be carried on privately-owned U.S. flag vessels. A review of the Maritime Administration's regulation and monitoring of the U.S. Cargo Preference Laws involved the examination of the Department of Agriculture's compliance with this requirement for ocean shipments made under title I of the Agricultural Trade Development and Assistance Act of 1954. Findings/Conclusions: Generally, the Department of Agriculture was complying with the cargo preference requirement, and U.S. flag vessels were carrying at least 50 percent of the tonnage shipped under title I of the program. However, ocean freight differential payments, which totaled about $42 million in fiscal year 1976, could be reduced if greater consideration were given to a country's total commodity requirements when allocating shipments among U.S. flag and foreign flag vessels. Further savings appeared possible if, in addition to considering a particular country's requirements, consideration were also given to an entire geographic region's requirements. When freight rates for two or more purchase authorizations are available simultaneously, the Department should approve U.S. flag vessels for shipments involving the lower ocean freight rates and foreign flag vessels for shipments involving the higher ocean freight rates. Recommendations: The Secretary of Agriculture should direct the Office of the General Sales Manager to modify current procedures to consider a country's total commodity requirements in the shipment allocation process. The revised procedure should emphasize shipping commodities with the lowest ocean freight differential on U.S. flag vessels, whenever feasible, to meet the cargo preference requirement. The Offices of the General Sales Manager and Audit should expeditiously

group countries by geographic areas to meet cargo preference requirements. If feasible, the geographic commodity requirements should be made an integral part of the shipment allocation procedure. (Author/SW)

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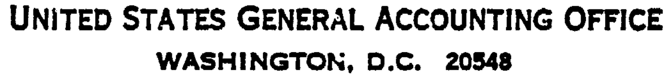

UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

COMMUNITY AND ECONOMIC
DEVELOPMENT DIVISION

SEP 7 1977

B-95832

The Honorable
The Secretary of Agriculture

Dear Mr. Secretary:

We are reviewing the Maritime Administration's regulation and monitoring of the U.S. Cargo Preference Laws. One of these laws--the Cargo Preference Act of 1954 (Public Law 664)--requires that at least 50 percent of the tonnage shipped under U.S. Government-financed programs be carried on privately owned U.S.-flag vessels. As part of our overall review, we examined the Department of Agriculture's compliance with this requirement for ocean shipments made under title I of the Agricultural Trade Development and Assistance Act of 1954 (Public Law 480). Ocean freight differential (OFD) payments reimburse foreign purchasers for their increased cost when more costly U.S.-flag vessels are used.

Generally, we found that the Department is complying with the cargo preference requirement and that U.S.-flag vessels are carrying at least 50 percent of the tonnage shipped under title I of the Public Law 480 program. However, we found that OFD payments, which totaled about $42 million in fiscal year 1976, can be reduced if greater consideration is given to a country's total commodity requirements when allocating shipments among U.S.-flag and foreign-flag vessels. Further savings appear possible if, in addition to considering a particular country's requirements, consideration is also given to an entire geographic region's requirements. This letter discusses this matter in further detail.

Our review was made primarily at the Department's Office of the General Sales Manager. We interviewed responsible officials and examined commodity and related shipping records for fiscal year 1976.

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(06551)

BACKGROUND

Title I, Public Law 480, authorizes the President to enter into agreements with eligible countries and foreign private trade entities for the sale of U.S. agricultural commodities. Primary responsibility for administering title I of Public Law 480 has been given to the Secretary of Agriculture. The Commodity Credit Corporation, a wholly owned Government corporation, is authorized to finance the sale and exportation of the commodities purchased. The financial agreements are favorable to the foreign purchaser and provide for repayment over extended periods--ranging from 20 to 40 years--and at interest rates as low as 2 percent.

Since Government financing is involved, Public Law 664 requires that at least 50 percent of the tonnage of commodities purchased by the foreign buyer must be transported by privately owned U.S.-flag vessels. The Commodity Credit Corporation is authorized, however, by Public Law 480, to reimburse foreign purchasers for ocean freight charges to the extent that such charges are higher than those charged by foreign-flag vessels.

In most instances the use of U.S.-flag vessels costs more than that of foreign-flag vessels. The difference in rates between a foreign-flag and a more costly U.S.-flag vessel is referred to as ocean freight differential. OFD always represents the increased transportation charges associated with the use of a U.S-flag vessel. It can be either high or low depending on the degree of variance that exists between foreign-flag and U.S.-flag shipping rates.

To reduce the amount of OFD paid, the Department's Office of Audit in July 1975 recommended establishing a target of 50.1-percent tonnage allocation to U.S.-flag vessels in complying with the Cargo Preference Act of 1954. The 50.1 target would meet the requirement of cargo preference legislation and keep OFD payments to a minimum. In February 1976 the 50.1 target was adopted.

Procedures employed by the Department in allocating cargo among foreign- and U.S.-flag vessels

Annually, the Department enters into sales agreements with eligible foreign countries setting forth the commodities to be sold, the quantities involved, and the terms of sale. During the period that the sales agreement is in force, the

importing country applies for one or more purchase authorizations for a specific commodity and tonnage. Once a purchase authorization is approved, the importing country will procure the commodity directly from a U.S. supplier and solicit bids for ocean transportation. The Department--specifically, the Office of the General Sales Manager--must approve the vessels to be used before any shipments are made.

The Office of the General Sales Manager, to insure compliance with the cargo preference requirement, considers each purchase authorization individually and allocates the tonnage as evenly as possible among available foreign-flag and U.S.-flag vessels. For example, a 20,000-long ton shipment of rice purchased by India would be allocated as follows: 10,000 long tons shipped on a foreign-flag vessel and 10,000 long tons shipped on a U.S.-flag vessel. OFD would be paid on the tonnage transported by the U.S.-flag vessel. The purchase authorization of 20,000 long tons might represent only a small portion of the purchasing country's total requirement.

OPPORTUNITY TO REDUCE OFD BY CONSIDERING TOTAL COUNTRY AND GEOGRAPHIC AREA PUBLIC LAW 480 PURCHASES

The procedures the Office of the General Sales Manager employs do not adequately attempt to minimize the OFD involved on the movement of commodity cargoes by U.S.-flag vessels. Presently, the emphasis is on insuring that at least 50 percent of the tonnage of each purchase authorization is placed on a U.S.-flag vessel regardless of the OFD rate involved.

During our review we found that if the Office of the General Sales Manager applied 50-percent cargo preference on the basis of a country's or a geographic area's total purchases rather than on the basis of each individual purchase authorization, flexibility would be increased in the ocean transportation approval process and opportunities to reduce OFD payments would exist. U.S.-flag carriage of Public Law 480 commodities could be approved for those commodities where the OFD is lowest. Foreign-flag vessels could be approved for those commodities having a higher OFD.

Opportunities for savings by considering total country purchases in allocating shipments

The following examples illustrate the OFD savings that could be achieved if greater consideration were given to a

country's total commodity shipments rather than allocating shipments on each individual purchase authorization. In these examples, we compared OFD for actual shipments with OFD that would have resulted if the procedures discussed above had been followed.

For our examples we determined that appropriate U.S.-flag or foreign-flag vessels were available on the dates necessary to carry the required tonnage from the scheduled port. We also took the most conservative approach by insuring that total tonnage carried by U.S.-flag vessels remained the same and that U.S.-flag revenue remained at least 50 percent of the total freight revenue. Concerning total revenue to U.S.-flag carriers, our examples showed that whether total revenue increased or decreased under our procedures varied on a case-by-case basis. All of the relevant information used in our examples was available to the Office of the General Sales Manager at the time of its allocation of shipments.

Shipment of wheat flour, rice, and soybean oil to Guinea

In April 1976 the Department signed an agreement with the Government of Guinea for the sale of wheat flour, rice, and soybean oil. On May 14, 1976, vessel approvals were issued for each of these commodities with tonnage allocations--under the Department's normal practices--distributed equally among U.S.-flag and foreign-flag vessels. The OFD was $21.41 per long ton for the wheat flour and $90.16 per long ton for the soybean oil. There was no OFD for the rice. The average OFD rate paid was $17.82 and the total OFD paid was $173,008.

A less costly allocation of these commodities among U.S.- and foreign-flag vessels would have been to place 100 percent of the rice, 2 percent of the wheat flour, and none of the soybean oil on U.S.-flag vessels. This allocation still would have met the cargo preference requirements while lowering the average OFD rate to $0.29. Total cost to the U.S. Government would have been $2,826--a savings of $170,182. (See p. 10, for a detailed breakout of these shipments.) Total revenue to U.S.-flag carriers would have decreased by about $179,000.

Shipments of wheat, rice, and soybean oil to Bangladesh

In September 1975 the Department signed an agreement with the Government of Bangladesh for the sale of wheat, rice, and soybean oil. Between October 3 and December 11, 1975, vessels were approved to ship these commodities on four purchase authorizations. Tonnage allocations for each purchase authorization were distributed equally; i.e., approximately 50 percent of each commodity was carried by U.S.- and foreign-flag vessels, respectively.

Several of the purchase authorizations for Bangladesh were approved during the same month and had overlapping delivery dates. The OFD for soybean oil was $13.26 per long ton, for rice it was between $30.85 and $47.45 per long ton, and for wheat it ranged between $31.00 and $49.68 per long ton. By allocating each purchase authorization equally among U.S.- and foreign-flag carriers, the average OFD rate for the above-listed shipments was $35.84 and the total OFD expense amounted to $7,364,771.

We believe that in reviewing the ocean transportation rates for the above-listed commodities the Department should have taken advantage of the relatively low OFD for soybean oil by shipping all of it on U.S.-flag vessels. For instance, if 100 percent of the soybean oil, 100 percent of the rice, and 32 percent of the wheat (the 32 percent with the lowest OFD rate) had been shipped on U.S.-flag vessels, the average OFD rate would have been $35.39; the total OFD expense would have been $7,273,729--a savings of $91,042. The 50-percent cargo preference requirement still would be met. (See p. 11, for a detailed breakout of this analysis.) Total revenue to U.S.-flag carriers would have increased by about $1.4 million.

Further opportunities for savings by considering total geographic area purchases in allocating shipments

In addition to the savings in OFD possible by considering a country's total commodity requirements, further savings could be achieved if allocations were based on a geographic rather than country-by-country basis. This procedure is consistent with the Cargo Preference Act of 1954 which states that there be "* * * a fair and reasonable participation of U.S.-flag vessels in such cargoes by geographic areas."

During our review we found that consideration of the total commodity shipments to be made to a geographic area when allocating ocean transportation could result in substantial reductions in OFD payments, as demonstrated by the following.

Agreements for the sale of agricultural commodities were signed between the Department and the Governments of Pakistan and Bangladesh in August and September 1975, respectively. These agreements called for the sale of wheat to Pakistan and the sale of wheat, rice, and soybean oil to Bangladesh. Vessel approvals were issued for the shipment of these commodities between August 21 and December 11, 1975.

Using the Department's current procedure of allocating ocean transportation between U.S.-flag and foreign-flag carriers on a purchase authorization basis, the total OFD paid for transporting these commodities was $10,682,301. The average OFD rate per ton was $30.51.

By grouping Pakistan and Bangladesh into the same geographic area, mixing commodities, and allocating tonnage so that U.S.-flag vessels were used when the OFD rate was lowest, we were able to reallocate the shipments among U.S.-flag and foreign-flag carriers and significantly reduce the OFD. Using this procedure we arrived at an average OFD rate of $27.96 and a total OFD of $9,791,297. This is a reduction of $891,004 from the amount the Department actually paid. (See p. 12 for a detailed breakout of this analysis.) As with our previous two examples, we assured ourselves that the appropriate vessels were available during the necessary periods and that the U.S.-flag operators would have received at least 50 percent of the total revenue paid. Total tonnage shipped on U.S.-flag vessels remained the same.

The Department's Office of Audit in a July 1975 report made a similar observation and recommended that in complying with the Cargo Preference Act of 1954, the Department allocate tonnage on the basis of the total fiscal year program by geographic area, if feasible, rather than purchase authorization or country program. Since that time there has been continuing correspondence between the Office of Audit and the Office of the General Sales Manager. The above recommendation remained unimplemented as of August 1977.

COMMENTS OF DEPARTMENT OFFICIALS

In discussions with us and in replying to the Office of Audit report, Department officials stressed that they could not determine what the ocean freight differential for a particular commodity would be until offers were received from shipping agents. They stated that it is difficult, therefore, to judge what commodities should be shipped on U.S.-flag vessels to meet the 50-percent cargo preference requirement at lowest cost. We were told that the current procedure of allocating cargo on a purchase authorization basis, equally among U.S.- and foreign-flag vessels, results in an easily administered policy. Nevertheless, these officials generally believed that the procedures we used in our total country examples are feasible. However, they were more apprehensive concerning our procedures for allocating shipments on a geographic basis.

The subject of ocean freight differentials is, admittedly, both complex and dynamic. OFDs do vary by time, commodity, and country, and the Department has not developed a historical data bank to identify shipping rate trends which would be needed in projecting future differential rates. Despite these limitations, we believe that immediate reductions in OFD could be achieved--while still meeting the 50-percent cargo preference requirement--for a number of reasons. Among these are:

--Historically, commodity shipments to certain countries are known to be different. For example, OFD rates for wheat shipments to Pakistan have historically been less than OFD rates for wheat shipments to Bangladesh.

--Frequently, different commodity shipments are approved at the same time. Consequently, OFD rates are known and are available for comparison and decisionmaking purposes, as demonstrated in our examples.

--We believe that operating personnel have the knowledge to implement our proposal. Department officials stated that when an attractive rate is available for a particular purchase authorization and they know more of the same commodity will be shipped to the country that year, they will ship more than 50 percent on U.S.-flag vessels in order to save money. For subsequent purchase authorizations, foreign-flag tonnage is increased to enable the Department to meet the 50-50 percent tonnage allocation.

CONCLUSIONS

We recognize that actual OFD rates are not always available to the Department. However, when freight rates for two or more purchase authorizations are available simultaneously, the Department should approve U.S.-flag vessels for shipments involving the lower OFD rates and foreign-flag vessels for shipments involving the higher OFD rates. In addition, although the Department's present procedure is easily administered, it would seem that the potential savings as demonstrated in this letter would justify the additional effort required to maintain a data base for OFD trends and on allocations made on a country and/or geographic basis.

In the examples cited, which represent only a small part of the total OFD paid, the Department could have saved over $1 million in fiscal year 1976 by combining different commodities and countries in the same geographic area and using the lower OFDs. In our examples we allocated the same tonnage to U.S.-flag vessels as was actually shipped on them. Furthermore, U.S.-flag revenue would have remained at least 50 percent of the total ocean freight payments.

RECOMMENDATIONS

We recommend that the Secretary of Agriculture direct the Office of the General Sales Manager to modify current procedures to consider a country's total commodity requirements in the shipment allocation process. The revised procedure should emphasize shipping commodities with the lowest OFD on U.S.-flag vessels, whenever feasible, to meet the cargo preference requirement. In addition, we recommend that the Secretary of Agriculture direct the Offices of the General Sales Manager and Audit to expeditiously resolve the issue of grouping countries by geographic areas to meet cargo preference requirements. If determined to be feasible, the geographic commodity requirements should then be made an integral part of the shipment allocation procedure.

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Section 236 of the Legislative Reorganization Act of 1970 requires the head of a Federal agency to submit a written statement on actions taken on our recommendations to the House Committee on Government Operations and the Senate Committee on Governmental Affairs not later than 60 days after the date of the report, and to the House and Senate

Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of the report.

We are sending copies of this report to the Director, Office of Management and Budget; the above committees; applicable legislative committees; your Director, Office of Audit; your Assistant Secretary for International Affairs and Commodity Programs; and the Assistant Secretary for Maritime Affairs, Department of Commerce.

Sincerely yours,

Henry Eschwege
Director

SHIPMENTS TO GUINEA APPROVED MAY 14, 1976

Actual Shipments and OFD

Commodity	OFD rate (note a)	U.S.-flag tonnage (long tons)	Foreign-flag tonnage (long tons)	OFD expense (note a)	Average OFD (rate per ton)
Wheat	$21.41	3,937	3,899	$ 84,291	$21.41
Soybean oil	90.16	984	984	88,717	90.16
Rice	-	4,789	4,789	-	-
Total		9,710	9,672	$173,008	b/$17.82

Reconstructed Shipments Using Our Recommended Procedures

Commodity	OFD rate (note a)	U.S.-flag tonnage (long tons)	Foreign-flag tonnage (long tons)	OFD expense (note a)	Average OFD (rate per ton)
Wheat	$21.41	132	7,704	$ 2,826	$21.41
Soybean oil	-	-	1,968	-	-
Rice	-	9,578	-	-	-
Total		9,710	9,672	$ 2,826	b/$ 0.29

a/ OFD rate and expense relate only to U.S.-flag tonnage.

b/ Average rate per ton for all U.S.-flag shipments.

SHIPMENTS TO BANGLADESH

APPROVED OCTOBER 3

TO DECEMBER 11, 1975

Actual Shipments and OFD

Commodity	OFD rate (note a)	U.S.-flag tonnage (long tons)	Foreign-flag tonnage (long tons)	OFD expense (note a)	Average OFD rate (per long ton)
Soybean oil	$13.26	8,144	8,193	$ 107,989	$13.26
Wheat	31.00-49.68	147,139	135,816	5,225,098	35.51
Rice	30.85-47.45	50,221	48,252	2,031,684	40.45
Total		205,504	192,261	$7,364,771	b/$35.84

Reconstructed Shipments Using Our Recommended Procedures

Commodity	OFD rate (note a)	U.S.-flag tonnage (long tons)	Foreign-flag tonnage (long tons)	OFD expense (note a)	Average OFD rate (per long ton)
Soybean oil	$13.26-17.53	16,337	-	$ 240,937	$14.75
Rice	30.85-49.65	98,473	-	4,126,564	41.91
Wheat	31.00-32.69	90,694	192,261	2,906,228	32.04
Total		205,504	192,261	$7,273,729	b/$35.39

a/ OFD rate and expense relate only to U.S.-flag tonnage.

b/ Average rate per ton for all U.S.-flag shipments.

SHIPMENTS TO BANGLADESH AND PAKISTAN APPROVED

AUGUST 21 TO DECEMBER 11, 1975

Actual Shipments and OFD

Country/ commodity	OFD rate (note a)	U.S.-flag tonnage (long tons)	Foreign-flag tonnage (long tons)	OFD expense (note a)	Average OFD (rate per ton)
Pakistan:					
Wheat	$17.68-28.40	144,677	125,879	$ 3,317,530	$22.93
Bangladesh:					
Soybean oil	13.26	8,144	8,193	107,989	13.26
Rice	30.85-47.45	50,221	48,252	2,031,684	40.45
Wheat	31.00-49.68	147,139	135,816	5,225,098	35.51
Total		350,181	318,140	$10,682,301	b/$30.51

Reconstructed Shipments Using Our Recommended Procedures

Country/ commodity	OFD rate (note a)	U.S.-flag tonnage (long tons)	Foreign-flag tonnage (long tons)	OFD expense (note a)	Average OFD (rate per ton)
Pakistan:					
Wheat	$17.68-34.45	270,556	-	$ 7,084,734	$26.19
Bangladesh:					
Soybean oil	13.26-17.53	16,337	-	240,937	14.75
Rice	30.85-47.45	63,288	35,185	2,465,626	38.96
Wheat	-	-	282,955	-	-
Total		350,181	318,140	$ 9,791,297	b/$27.96

a/ OFD rate and expense relate only to U.S.-flag tonnage.

b/ Average rate per ton for all U.S.-flag shipments.