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Commodity Credit Corporation's  
Export Credit Guarantee Programs

Statement of  
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Before the  
Subcommittee on Tobacco and Peanuts  
Committee on Agriculture  
House of Representatives



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Mr. Chairman and Members of the Subcommittee.

We are pleased to be here today to discuss the status of our current review of the Foreign Agricultural Service's (FAS) management of the Commodity Credit Corporation's (CCC) GSM-102 and GSM-103 export credit guarantee programs, particularly the issue of foreign and U.S. content. My statement describes actions taken by FAS officials in response to our June 1988 report<sup>1</sup> on those programs and presents the preliminary findings and observations of our current work.

#### FAS ACTIONS ON PREVIOUS RECOMMENDATIONS

Our June report noted that improvements were needed in the management of the export credit guarantee programs. We recommended that FAS (1) clarify program regulations by defining a U.S. agricultural commodity, and (2) design, develop, test, and implement internal controls, including steps to ensure the accurate accounting of outstanding guarantees, and random on-site verifications, to ensure that loan guarantees are used to obtain U.S. agricultural commodities. Since issuance of the report, FAS officials have taken some steps to improve program management but further actions are still needed.

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<sup>1</sup>INTERNATIONAL TRADE: Commodity Credit Corporation's Export Credit Guarantee Programs (GAO/NSIAD-88-194, June 10, 1988).

On September 21, 1988, FAS issued a Notice To Exporters clarifying commodity eligibility under the programs. It also included a policy change that, for the first time, generally allowed the value of exports under the programs to include up to 25 percent imported agricultural commodities. However, only the value of the U.S. portion of the agricultural commodities would receive the CCC guarantee. For example, if an agricultural export valued at \$1 million contained an imported agricultural product valued at \$250,000, or 25 percent, then CCC guarantees would apply only to the \$750,000. Although a maximum of 25 percent was set on the value of the imported commodities, the volume of the foreign amount could be substantially greater than 25 percent if the imported commodities were cheaper than the U.S. commodities. The Notice also required exporters to certify to FAS the percentage of imported commodities in each export sale.

For the approximate five-month period that this new policy was in effect, guarantees were approved for exports of mixed U.S. and foreign content for tobacco, leather, grocery items, and soft drink concentrate. Based on preliminary information we compiled, these exports represented only about \$23.7 million, including about \$19.2 million of U.S. content. In the same time period, total loan guarantees under the programs exceeded \$2 billion.

On February 15, 1989, the policy was changed. FAS announced that only commodities having 100 percent U.S. ingredients would be

eligible for program coverage and exporters must certify that none of the commodity or product value is of foreign origin. This policy precludes coverage for the export of agricultural products that contain any foreign ingredients. The February announcement also stated that FAS would be reevaluating its policy regarding foreign content. FAS officials explained to us that this meant that they are planning to evaluate the effectiveness of the credit guarantee programs under the 75-25 percent policy and they expect to complete this evaluation within 90 days.

FAS officials told us that their intentions from the time of the September announcement were to experiment with the policy for awhile, see which high value-added or processed agricultural products would be sold under the new policy, and then evaluate the effectiveness of the policy. The decision to rescind the 75-25 percent policy was made in consultation with the General Sales Manager and his staff, senior program operations officials, and the USDA Office of General Counsel over a period of several days. According to the FAS Administrator and the General Sales Manager, this decision was made solely at the FAS organizational level, without the input of higher level Departmental officials.

#### FAS FOREIGN CONTENT POLICY

The Administrator of FAS testified last October that the September 1988 announcement did not constitute a new policy and that the

backed-out value of the U.S. portion of an agricultural export had always been eligible for program coverage. Thus far our review has shown that, while there was one exception involving a U.S. value back-out in mid-1988, the general policy since the program's inception had been to provide coverage for commodities or products containing only U.S. content. Interviews with FAS officials, review of program documents, and correspondence between FAS and exporters confirm that this was the policy prior to September 21, 1988.

As early as June 1986, the issue of coverage for exports containing foreign content surfaced in FAS. A request for program coverage for the financing of grocery items made by an importer in a foreign country triggered consideration of the issue. A June 1986 FAS issue paper raised a number of concerns regarding this request, including the issue of foreign content, and stated that:

"Derivation of a 'formula' whereby 102 coverage for a given grocery item would be limited to some portion/value deemed to be clearly of U.S. agricultural origin was considered and rejected."

Beginning about March 1987, tobacco exporters asked that their products, which contain foreign origin content, be made eligible for GSM-102 or GSM-103 coverage. One of these exporters asked for coverage only on the value of the U.S. origin portion. Once

again, FAS officials declined to provide coverage, stating in correspondence to the exporter that it was the Department's policy to cover only U.S. agricultural commodities or products.

However, because of such exporter concerns and the inclusion in the Food Security Act of 1985 of support for the export of high-value added agricultural products which can include foreign content, a May 1987 issue paper from the Administrator of FAS to the Under Secretary of Agriculture for International Affairs and Commodity Programs presented two alternatives for a content policy. The first alternative was to

"Maintain current policy by continuing the requirement that all agricultural products be 100% U.S.-origin and manufactured in the United States in order to be eligible to receive GSM-102/103 financing."

The other alternative was to

"Consider an alternative strategy where we would agree to finance only the percentage of U.S. origin and manufacture in a given product."

The Administrator recommended that FAS consult with interested parties and consider their views before taking any action on changing the foreign content policy.

We discussed the issue paper with the then Undersecretary, who confirmed that the policy in place at the time was to provide coverage for 100 percent U.S. commodities. The Undersecretary remembers discussing the issue with FAS officials, but does not remember making a decision on the Administrator's recommendation. According to the FAS Administrator, no action was taken on the recommendation in the issue paper.

In October 1987, there was correspondence between a tobacco company and FAS regarding the eligibility of blended tobacco. FAS informed the tobacco company that the Department of Agriculture was reviewing the issue of foreign content. In April 1988, there was also correspondence between a representative of an infant formula exporter and FAS regarding product eligibility. The exporter of powdered infant formula sought coverage under the program for an export sale. Approximately 2 percent of the value of the sale represented foreign origin contents. FAS approved coverage for the 98 percent U.S. contents value but wrote the exporter that the exception granted should not be viewed as setting a precedent and that FAS's general policy was to provide coverage only for commodities entirely grown and processed in the United States.

Approximately one and a half years elapsed between the issue paper and the policy change of September 21, 1988 announcing the 75-25 percent policy.

## SUSPENSION AND DEBARMENT

Evidence that large quantities of foreign tobacco were shipped under the programs prior to September 1988 raises the issue of whether companies that have been found to have violated program regulations should be suspended or debarred from further participation in those programs. A number of companies identified by Agriculture's Inspector General as having exported large quantities of foreign tobacco under the programs as U.S. tobacco during fiscal years 1986 through 1988 were allowed to participate in the programs in fiscal year 1989.

Generally, firms which engage in improper business practices under these programs can be suspended or debarred from future participation. FAS has informed us that it has referred to Agriculture's General Counsel the issue of the appropriateness of bringing suspension or debarment actions against the companies currently being investigated by the U.S. Attorney in North Carolina. They do not intend to initiate such proceedings while the U.S. Attorney's investigation continues so as not to impair the U.S. Attorney's case.

We think that some of the companies involved have engaged in improper practices for which suspension or debarment proceedings would be the appropriate agency response. Agriculture should be



prepared to initiate such action when the U.S. Attorney completes his work on the case.

#### INTERNAL CONTROLS

In response to our June report recommendations concerning compliance checks to assure that loan guarantees are used to obtain U.S. agricultural commodities, an Assistant Administrator of FAS directed the compliance review staff to perform compliance checks on the export credit guarantee programs. That staff is now evaluating resource requirements necessary to do this.

The compliance review staff consists of six auditors who are currently performing compliance reviews of FAS market development programs, the Targeted Export Assistance Program and other projects that come up from time to time. They have not yet performed any compliance checks for the GSM-102 and 103 programs. The compliance review staff is too small to handle these added responsibilities and we believe that allocating more resources for compliance checks is needed.

#### FOREIGN CONTENT COMPLIANCE CHECKS

My staff has met with tobacco industry representatives. They were told that it is a routine practice for tobacco exporters to mix foreign tobacco with U.S. tobacco in filling sales orders for

unmanufactured flue-cured tobacco. They added that in many cases, this tobacco has been represented as U.S. tobacco and covered under the export credit guarantee programs.

In cooperation with the U.S. Customs Service, we checked for foreign content in seven tobacco export sales destined for countries that finance such sales under GSM programs. We physically inspected shipment containers at export terminals and warehouses in the cities of Newport News, Norfolk, and Richmond Virginia. In two cases, we identified cartons labeled as containing foreign tobacco. However, when we obtained the relevant shipping documentation, we found that these sales were not guaranteed under the programs and that the tobacco exporter was financing these sales.

In the other five cases, the sales were being financed under the export credit guarantee programs. One of the sales included foreign tobacco and was made under FAS' 75-25 percent policy, thereby guaranteeing only the value of the U.S. portion. Customs officials believe that over 80 percent of the volume of tobacco in this sale is of foreign origin.

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Our review is still ongoing and we have more work to do. Nevertheless, it is clear that the lack of internal controls

identified in our June report remains. Compliance checks have not yet been made.

The history of the foreign content issue and the fact that the last two program announcements were made by FAS without a comprehensive evaluation makes it all the more important that FAS conduct its current assessment of the foreign content question in a comprehensive and systematic manner. It should assess the impact of different options on the value and volume of U.S. agricultural exports. It should also consider whether uniform guidance for all commodities is appropriate or whether commodity specific guidance may be more desirable. For example, should coverage of high value-added commodities be governed by the same guidance as bulk commodities? FAS in completing this evaluation should also solicit and consider the views of program participants and other interested parties. Any program change resulting from this analysis should be incorporated into formal program regulations.

Mr. Chairman, this concludes my statement. I will be happy to try to respond to any questions you may have.