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REPORT BY THE

Comptroller General

OF THE UNITED STATES

More Can Be Done To Improve The Department Of Agriculture's Commodity Donation Program

Better management of the Department of Agriculture's \$1 billion commodity donation program is needed. Schools, programs to feed the elderly and the needy, and other recipients often receive the wrong quantities and kinds of food. Also, food is delivered at times when it cannot be effectively used.

Some argue that use of a cash or letter-of-credit voucher system would be more effective than commodity donations, but GAO believes that it has not been shown that these alternative approaches would solve all the program's ills.

GAO recommends improvements in the administration of the commodity donation program and suggests that pilot testing of the alternative systems, as provided in a December 1980 law, should provide needed data on their advantages and disadvantages.



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COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON D.C. 20548

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The Honorable Thad Cochran, Chairman
The Honorable Thomas F. Eagleton,
Ranking Minority Member
Subcommittee on Agriculture, Rural
Development, and Related Agencies
Committee on Appropriations
United States Senate

This report is in response to Senator Eagleton's September 4, 1979, request to review several issues relating to the Department of Agriculture's commodity donation program. This report examines major aspects of the program and identifies certain areas in which the Department could improve overall program administration and thereby improve program effectiveness.

The report primarily discusses overall program administration; effectiveness of Department purchases made to remove temporary market surpluses; Federal and State program monitoring; and delivery aspects of the program. This report also addresses proposed alternatives to the current commodity program.

As arranged with Senator Eagleton's office, we are sending copies of this report to the Director, Office of Management and Budget; the Secretary of Agriculture; and other interested committees and Members of Congress.

A handwritten signature in cursive script that reads "Milton J. Jordan".

Acting Comptroller General
of the United States

D I G E S T

In fiscal year 1980 State and local programs to feed students, the elderly, needy families, and others received about \$969 million worth of food through the Department of Agriculture's commodity donation program. About 90 percent of the donated food was for the school lunch program. The Food and Nutrition Service administers the commodity donation program. Two other Agriculture agencies provide the commodities to be distributed:

--The Food Safety and Quality Service buys surplus commodities from regular market channels in quantities sufficient to maintain predetermined levels of assistance. (In a June 1981 reorganization, this activity was transferred to the Agricultural Marketing Service.)

--The Agricultural Stabilization and Conservation Service buys commodities under price-support authority and donates a portion to eligible programs.

Agriculture needs to improve its program management so that program participants receive the appropriate quantities and kinds of food at times when it can be effectively used.

NEED FOR BETTER IDENTIFICATION
OF COMMODITY NEEDS

The Department has not fully and accurately determined users' commodity needs. As a result, school districts and other users receive commodities (1) with limited appeal, (2) too late to be effectively used, and (3) exceeding actual needs.

Further, States order commodities without determining user needs or preferences. For example, the California distributing agency ordered tomato products to fill the State's fiscal year 1979 entitlement without surveying school districts to determine need. Because the agency

overestimated user demand, it accumulated about \$337,000 more in tomato products than could be used in 1 year. (See p. 24.)

GAO recognizes the difficulty of balancing the program objective of purchasing commodities for surplus removal and price support with the objective of purchasing commodities that user agencies prefer and need. However, GAO believes improvements can be made in the way the Department determines which commodities are needed by user agencies.

In a January 1977 report GAO pointed out that the Food and Nutrition Service's regional offices were not ensuring that local school districts' needs were considered and accurately reflected in State-prepared commodity preference reports and that the food preference reports did not provide a means to identify actual quantities needed to meet the local schools' needs. Problems similar to those identified in GAO's 1977 report still exist.

The Service has discontinued the traditional method of obtaining information on school district needs--the school food preference report--in favor of State food distribution advisory councils. Although these groups are expected to be operational sometime in fiscal year 1981, the Service has provided only minimal guidance or direction on how district commodity-need data is to be collected, analyzed, and used in formulating future Department commodity purchase plans. (See p. 15.)

Department efforts to remedy the problems identified in GAO's 1977 report have been inconsistent. (See pp. 13 to 15.)

DELIVERY OF COMMODITIES NEEDS IMPROVEMENT

To effectively use the donated commodities, users must receive them when needed. At times, however,

- commodities were received so late that they could not effectively be used before the end of the school year;
- commodities were delivered without advance notice, causing distributing agencies and recipients to incur increased costs for storage, handling, and spoilage; and

--recipients had to purchase food items locally which they would normally receive through the program. (See pp. 45 to 51.)

The Department allows States to restrict the mode of transportation to truck or rail only. Such inflexibility can result in excessive transportation charges. Also, Service regional offices and States were not doing all they could to assure that the most economical and efficient delivery methods were used. (See pp. 55 and 56.)

Further, the Department procured most commodities, except poultry and grain products, on a free-on-board (FOB) origin basis. Other Government agencies, such as the Veterans Administration, procure these same types of commodities with like origin and delivery points on an FOB-destination basis at a savings. GAO believes the Department should consider increased use of FOB-destination procurement. (See pp. 56 to 60.)

CASH, COMMODITIES, OR LETTER OF CREDIT?

It has been suggested that the commodity donation program be replaced with a cash or letter-of-credit voucher system. This would allow recipient agencies to purchase desired food items locally using cash or credit vouchers provided by the Department. Proponents of these alternative systems believe that procuring all food and commodities locally would probably be the most effective way to solve the problems associated with the current commodity program. (See p. 61.)

Those opposed to the alternative systems say that opportunities to circumvent the system and the potential for fraud and abuse would be far greater than under the current program. Some believe that because of the quantities procured, federally donated commodities offer more for the money. There is also concern that a voucher system would reduce the Department's ability to quickly respond to temporary market surplus conditions by removing these commodities from market channels. State and local officials had mixed views concerning this issue. (See pp. 69 and 70.)

Two Federal feeding programs currently provide the option of receiving cash, commodities, or a combination of both--the elderly feeding program

(25 distributing agencies chose to receive all cash for fiscal year 1979) and the Child Care Food Program. Kansas is the only State operating its school lunch program on a cash in lieu of commodities basis. (See pp. 61 to 63.)

The commodity donation program needs improvement to better respond to users' commodity needs. However, GAO believes it has not been proven that a cash or letter-of-credit voucher system would solve all the program's ills. (See p. 70.)

Public Law 96-528, enacted December 15, 1980, includes provisions for pilot testing of cash payments and commodity letters of credit at 60 school districts for 3 years. GAO agrees that such testing, in conjunction with the data available from the Kansas experience, should provide the Congress with needed data on the pros and cons of the alternative systems. (See pp. 69 and 70.)

RECOMMENDATIONS

The Secretary of Agriculture should take a number of actions addressing (1) the impact of the Department's purchases to remove temporary market surpluses and to help stabilize farm prices, (2) the gathering of school food preference data, (3) State distributing agency methods for ordering commodities, (4) State procedures for distributing commodities, and (5) a formal program monitoring system. (See pp. 12, 21, and 42 to 44.)

Also, to improve the delivery of commodities and overall program efficiency, the Secretary should take measures regarding improved documentation on vendor commodity shipments, the need for more flexibility in the way States can take delivery of commodities, and more efficient procurement practices relating to the transport of commodities. (See p. 60.)

AGENCY COMMENTS

The Department's comments primarily clarified and corrected information presented in a draft of this report. (See app. IV.) These comments, which have been incorporated where appropriate, did not affect GAO's conclusions and recommendations.

In the letter transmitting its comments, the Department said that it is difficult to totally balance the seemingly conflicting objectives of the donation program to purchase commodities for surplus removal and price-support purposes with the need to meet recipient agencies' preferences and needs. The Department's comments directed at better reflecting the relationships of these objectives are incorporated where appropriate.

The Department also asked GAO to review the data and methodology used to estimate excess inventory amounts of commodities and suggested an alternative way to present the data. The Department did not question the fact that excess inventories exist, only the dimension of the problem. The Department's suggested method could provide additional insight into the dimension of the problem; however, GAO believes the method it used is sound and not misleading. (See p. 23 and app. IV.)

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ABBREVIATIONS

ASCS	Agricultural Stabilization and Conservation Service
CCC	Commodity Credit Corporation
FNS	Food and Nutrition Service
FOB	Free-on-board
FSQS	Food Safety and Quality Service
GAO	General Accounting Office
OIG	Office of Inspector General
OMB	Office of Management and Budget
SFD	State food distribution
USDA	U.S. Department of Agriculture
VA	Veterans Administration
WIC	Women, infants, and children

CHAPTER 1

INTRODUCTION

Through the commodity donation program, the U.S. Department of Agriculture (USDA) donates food to various eligible program outlets, such as the school lunch and breakfast programs, commodity and special supplemental food programs, nutrition programs for the elderly, needy family programs (primarily Indian families on reservations), charitable institutions, and summer camps.

PROGRAM OPERATIONS

Commodities donated through the program are purchased under price-support (sec. 416 of the Agricultural Act of 1949, as amended--7 U.S.C. 1431) and surplus-removal legislation (sec. 32 of the act of August 24, 1935, as amended--7 U.S.C. 612c) and funneled through State agencies, called distributing agencies. USDA buys commodities preferred by States, generally under section 6 of the National School Lunch Act (42 U.S.C. 1755), specifically for schools participating in the National School Lunch Program.

The types of foods and amounts purchased may fluctuate in relation to marketing conditions. USDA, however, has authority to acquire certain foods for those feeding programs which, by law, must receive a minimum annual level of assistance. The amount of commodities supplied to schools is based on the number of meals served and a set rate of payment. The rate of payment is adjusted each fiscal year to reflect changes in a computed price index for food used in schools and institutions.

For the National School Lunch Program, each State is eligible to receive annually an amount of commodities valued at a specified rate per lunch. When not enough commodities are available from USDA purchases or stocks, section 6(b) of the National School Lunch Act authorizes a cash payment to make up the difference. Such a payment--called cash-out--is determined by subtracting the value of the commodities received from the total value (number of lunches served times annual rate per lunch) of a State's entitlement. During the period July 1, 1980, through June 30, 1981, the rate per lunch was to be 15.5 cents. However, section 202(a) of Public Law 96-499 (enacted Dec. 5, 1980) reduced this amount by 2 cents. This reduction was effective January 1, 1981. Thus, for the period January through June 1981, the rate of assistance was to be 13.5 cents. No less than 75 percent of the mandated per-lunch reimbursement must be commodities. The last time a cash-out occurred was in fiscal year 1978 when \$74 million in cash was provided to States.

Appendix I includes additional information on program legislation, program operations, and the feeding programs.

PROGRAM ADMINISTRATION

USDA's Food and Nutrition Service (FNS) administers the commodity donation program aided by two other USDA agencies, the Food Safety and Quality Service (FSQS) ^{1/} and the Agricultural Stabilization and Conservation Service (ASCS). ASCS purchases price-supported items; these types of commodities are generally provided through Commodity Credit Corporation (CCC) stocks. FSQS buys all commodities other than section 416 price-supported items. The agencies' procurement procedures are discussed in appendix I. Purchase plans are submitted by the Assistant Secretary for Food and Consumer Services for approval by CCC's Board of Directors. The Assistant Secretary is responsible for authorizing revisions to the plans and for notifying the Board of significant changes to the plan. The Board can also authorize changes to the purchase plan if market conditions change. FNS is responsible for identifying school districts' commodity needs and has veto power on purchases; that is, FNS will not accept commodity items or quantities that schools cannot use without waste.

Section 14 of the National School Lunch Act requires USDA to solicit the views of local school districts and nonprofit schools participating in the school lunch and breakfast programs with respect to the type of commodity assistance needed and to consider these views in purchasing and distributing the commodities. Until the early part of fiscal year 1979, the vehicle for obtaining this data was the annual school food preference report. It consisted of a standard format listing commodities that USDA expected to purchase for the upcoming year. The use of the preference report was discontinued, however, because of the need for a new report format which could be sent to school districts through school food distribution (SFD) advisory councils.

Section 6(e) of Public Law 95-166 (42 U.S.C. 1762a, Nov. 10, 1977) requires that each State education agency receiving food assistance establish an SFD advisory council. According to USDA regulations (7 CFR 210, Jan. 4, 1980), each council is to be composed of representatives from schools that participate in the National School Lunch Program plus the chiefs of the State education and State distributing agencies acting as advisory, nonvoting members.

The regulations also require that each council meet at least once a year and report to the State education agency no later than January 15 of each year, beginning in 1981, its recommendations regarding the manner of selecting and distributing commodity

^{1/}In a June 17, 1981, reorganization, FSQS was renamed the Food Safety and Inspection Service and its commodity distribution program activities were transferred to USDA's Agricultural Marketing Service.

assistance for the next school year. The education agency is required to report the council's recommendations to FNS no later than February 15 of each year, beginning in 1981.

The regulations originally required each council to collect the food preference data through a survey of all State school authorities using a standard FNS format. However, this requirement was amended in December 1980 to allow the council to determine both the method and the scope of the survey used to obtain the preference data required. In addition, the council may use any format that it determines to be most appropriate for gathering the food preference information. FNS has prepared a sample report format and has sent the States general guidelines on the data collection procedures.

States have the option of using FNS' format, using selected portions of it, or developing their own. However, much of the information requested on the new preference form is not required. FNS requires States to rate the acceptability of certain commodities, but it only recommends that States report quantity data from users. Nevertheless, USDA believes that the councils will be in a better position to explain FNS' reporting needs to the school districts and to elaborate on the data solicited, so that State distributing agencies and USDA will receive more and better information than before.

COMMODITY DISTRIBUTION COSTS

Each year USDA spends several hundred million dollars to purchase and distribute commodities to the child nutrition programs, principally school lunch, and to other feeding programs. The school lunch program receives by far the largest amount of donated commodities each year. In fiscal years 1979 and 1980, about 90 percent of the value of all foods donated went to schools. About 4.4 billion lunches were served to school children in fiscal year 1979--an average monthly participation of about 27 million. 1/

The following table shows the costs of commodities distributed and cash-in-lieu by program for fiscal years 1979 and 1980.

1/Average computed for months of October 1979 through May 1979 plus September 1980.

Programs(s)	Fiscal year 1979 (note a)		Fiscal year 1980 (note a)	
	Commodities	Cash	Commodities	Cash
Schools (note b)	<u>c/\$665,981,331</u>	\$ 7,500,000	<u>d/\$841,617,837</u>	\$ 8,140,000
Summer food service	1,765,030	-	1,284,422	-
Child care	682,404	17,000,000	436,590	21,496,000
Charitable institutions	40,289,532	-	64,662,034	-
Needy family	29,847,065	-	24,568,211	-
Supplemental food	16,405,931	-	21,834,370	-
Elderly feeding	<u>17,669,652</u>	<u>39,500,000</u>	<u>14,622,796</u>	<u>54,064,000</u>
Total	<u>\$772,640,945</u>	<u>\$64,000,000</u>	<u>\$969,026,260</u>	<u>\$83,700,000</u>

a/Amounts for school lunch, school breakfast, child care, and summer food service are based on school year delivery. Amounts for other programs are based on fiscal year delivery.

b/Includes school lunch and school breakfast.

c/Includes \$69,614,787 bonus. (See app. I, p. 73.)

d/Includes \$137,263,566 bonus.

The purchase of agricultural commodities and other foods and their distribution are provided for in annual purchase docket prepared by USDA. These dockets, approved usually in September or October of each year, represent the planned purchases for the upcoming year and, according to FNS, are the current best estimate by ASCS, FSQS, and FNS of the amounts that will be available and can be used without waste by participants.

The 1981 docket proposed the expenditure of the following amounts for the purchase and distribution of agricultural commodities in fiscal year 1981. All dairy products except mozzarella cheese are excluded.

<u>Program</u>	<u>Fiscal year 1981 planned purchases</u>	
	<u>Original per docket</u>	<u>Revised as of January 29, 1981 (note a)</u>
Child nutrition (note b)		
FNS--6(a) (note c)	\$ 80,000,000	\$ 80,000,000
6(e) (note d)	296,047,000	159,949,971
FSQS--sec. 32	365,400,000	365,400,000
Needy family	53,700,000	43,680,000
Supplemental food	21,339,100	23,586,000
Elderly feeding	<u>37,000,000</u>	<u>10,100,000</u>
 Total	 <u>\$853,486,100</u>	 <u>\$682,715,971</u>

a/Some revisions are usually made to reflect availability of funds and food. The most significant revisions in fiscal year 1981, however, were in section 6(e) funds and were the result of changes in the rates per meal. In the original budget the estimated rate for reimbursement of meals was much higher than the final rate of 15.5 cents; in addition, another 2-cent reduction to 13.5 cents was mandated by Public Law 96-499 (Omnibus Reconciliation Act) during the latter part of the year. Also, fewer meals were served because of the Omnibus Reconciliation Act and adjustments were made to reflect the cash/commodity option selections of the summer food service and child care programs.

b/Includes school lunch, child care, and summer food service programs.

c/Section 6(a) funds are traditionally used to purchase those foods most preferred by schools; namely, meats, poultry and poultry products, fruits, and vegetables.

d/Section 6(e) is an established level of commodity assistance to reflect changes in the USDA-computed index for food used in schools and institutions. It also places special emphasis on high-protein foods.

OBJECTIVES, SCOPE, AND METHODOLOGY

At the request of Senator Thomas F. Eagleton, Ranking Minority Member (formerly Chairman) of the Subcommittee on Agriculture, Rural Development, and Related Agencies, Senate Committee on Appropriations, we reviewed USDA's commodity donation program.

Our overall objectives were to:

--Analyze the timing, types, quantities, and prices paid for commodities.

- Evaluate how USDA assesses the impacts of such purchases on market quantities and prices.
- Evaluate USDA's methods for determining commodity needs/preferences of ultimate users and how these needs affect commodity purchases.
- Evaluate the subsequent distribution system used to get the food where it is needed.

We reviewed the commodity donation program's procurement and distribution aspects to identify areas in which USDA could improve overall program effectiveness. More specifically, we reviewed legislation, regulations, instructions, various reports and studies, and records relating to the commodity donation program. At the Federal level, we interviewed USDA officials from FNS, FSQS, and ASCS.

We made our review at FNS, FSQS, and ASCS headquarters in Washington, D.C., and at four FNS regional offices--Mid-Atlantic, Mountain Plains, Southwest, and Western. We also visited State distributing agencies in 10 States--Arizona, California, Colorado, Missouri, Montana, New Mexico, North Dakota, Pennsylvania, Tennessee, and Texas. We selected these States for a combination of reasons, including (1) congressional interest, (2) receipt of large dollar amounts of donated commodities during fiscal year 1978, and (3) geographic location. We limited our selection of States to those meeting one or more of the above criteria with one exception--we excluded any State which USDA's Office of Inspector General (OIG) had included in its nationwide audit of the commodity donation program.

In the selected States, we interviewed distributing agency officials and visited a total of 42 recipient agencies: 18 participating in the school lunch program, 10 in the nutrition program for the elderly, 5 in the needy family program, 3 in the commodity supplemental feeding program, and 6 in the charitable institutions program. The offices and agencies we visited, which were picked on a judgmental basis, are listed in appendix II.

Based on our review at the distributing and recipient agencies and our discussions with knowledgeable USDA and State officials, we believe that the findings presented in this report generally represent the conditions in most States. However, the reader is cautioned not to assume that all States or recipient agencies experience the same problems.

CHAPTER 2

THE EFFECTS OF SECTION 32

PURCHASES SHOULD BE EVALUATED

Commodity purchases with section 32 funds are intended to remove temporary surpluses of perishable products from the marketplace and help stabilize farm prices. According to USDA officials, if commodity market prices are below 100 percent of parity, 1/ a surplus is presumed to exist. USDA has done little, either before or after purchases, to determine the potential or actual impact of its commodity purchases on commodity market prices and/or quantities available. In the impact analysis statements accompanying its annual purchase dockets, USDA generally concludes that its purchases are expected to have little, if any, impact on farm prices since they represent only a minor part of national consumption.

LEGISLATIVE REQUIREMENTS OF SECTION 32 PURCHASES AND USDA IMPLEMENTING ACTIONS

Section 32 was enacted in 1935 to supplement the Agricultural Adjustment Act of 1933 and assist the agricultural recovery program by encouraging the exportation and domestic consumption of agricultural commodities. Purchases under this section are intended to remove temporary market surpluses of perishable products and to help stabilize farm prices. To accomplish this objective, section 32 specifically authorizes the Secretary of Agriculture to encourage the exportation of agricultural commodities and products by paying benefits and indemnities for losses incurred in connection with such exportation; encourage the domestic consumption of such commodities by paying benefits or indemnities or by other means, thereby diverting them from the normal channels of trade and commerce; and finance adjustments in the quantity of agricultural commodities planted or produced for market.

To finance these activities, section 32 provides that 30 percent of customs receipts collected from duties on both agricultural and nonagricultural products during each calendar year be automatically appropriated to USDA. The 30-percent factor was based on the argument that at the time section 32 was enacted, roughly 30 percent of the total population lived on farms and that section 32 would make available for the farmers' benefit a sum equivalent to their fair share of tariff receipts. From fiscal year 1936

1/Parity prices are determined monthly for many farm commodities and are based on average prices farmers received during a base period and on increases in prices paid by farmers for production and living items since the base period.

through fiscal year 1980, more than \$19 billion 1/ of section 32 funds were made available to USDA.

Before each fiscal year begins, FNS meets with the various FSQS commodity divisions to formulate annual purchase plans. The commodity divisions predict what surpluses will be available based on current inventories, harvest forecasts, market prices, and other factors. The divisions then prepare plans specifying the individual commodities to be purchased.

In an opinion dated September 13, 1967, USDA's Office of General Counsel provided the following guidance on the intent of section 32 purchases:

"In the memorandum of January 20, 1961, we discussed the use of Section 32 funds both for the removal of 'physical surpluses' and 'economic surpluses', noting that in the early programs under Section 32, the program justification was based upon the existence of a physical surplus. A physical surplus has been administratively considered as the existence of a quantity of a given commodity which exceeds normal domestic and export requirements. Section 32 purchase programs have also been justified on the basis of an economic surplus which is distinguished from a physical surplus in that an economic surplus is determined on the basis of the market price of a commodity rather than on the basis of a quantity of the commodity in excess of requirements.

"An economic surplus is considered to exist when prices of a given commodity are below a predetermined desirable level."

Thus, if the market price for a food commodity is less than 100 percent of parity, it is classified as surplus and eligible for purchase with section 32 funds. According to an FNS official, virtually all nonbasic food commodities are eligible for purchase with section 32 funds.

USDA HAS DONE LITTLE TO MEASURE EFFECTIVENESS OF SECTION 32 PURCHASES

USDA has not performed any analyses that measure the expected or actual impact of its purchases on market prices and/or the extent to which its purchases helped to alleviate the surplus conditions of those commodities purchased under section 32. As a result, USDA does not know whether section 32 purchases are having the intended effects. If USDA is to continue to spend

1/Based on actual customs receipts for fiscal years 1936-78 and estimated customs receipts for fiscal years 1979 and 1980.

large sums of section 32 funds for "surplus removal," systematic and thorough evaluations are needed. In fiscal years 1978, 1979, and 1980, USDA spent about \$877 million in section 32 funds (see app. III) for the child nutrition programs--the largest recipient of donated commodities. According to USDA, it has initiated efforts to develop a planning-decision model for surplus commodity removal programs which is expected to be available for review by the end of this year.

Impact analysis statements provide little information

USDA impact analysis statements provide little information on the anticipated effect on market prices and on available quantities of USDA commodity purchases for the school lunch and breakfast programs. Because these programs comprise the vast majority (about 90 percent) of USDA's procurement activities for congressionally mandated feeding programs, USDA confines the impact analysis statements to these programs.

The fiscal year 1979 purchase docket showed that FNS planned to spend about \$281.1 million of section 32 funds as shown below.

<u>Commodity type</u>	<u>Planned purchases with section 32 funds</u>
	(millions)
Meats	\$ 55.2
Poultry	56.6
Fruits	75.5
Vegetables	<u>93.8</u>
Total	<u>\$281.1</u>

However, the fiscal year 1979 impact analysis statement did not show the anticipated impact of such purchases on market prices and/or quantities available. Although the impact analysis contained some general statements about overall commodity purchases resulting from the child nutrition programs, it did not attempt to explain the effects of section 32 purchases. For example, it contained the following statements on planned poultry and vegetable purchases.

Poultry--"Planned purchases of broilers under the Docket Proposal constitute about 0.75 percent of projected marketings and are therefore expected to have little effect on market demand or price. The proposed Docket purchases of turkey and turkey products, however, constitute about 3 percent of projected marketings and may therefore strengthen producer incomes and enhance prices at both the farm and retail levels."

Vegetables--"USDA vegetable purchases, however, are not expected to significantly influence prices given total production."

In a letter to the CCC Board of Directors, USDA's Director of Economics, Policy Analysis, and Budget said that although he had signed the fiscal year 1979 impact analysis statement, he believed that among other things, subsequent analyses should be more precise with respect to the impact of purchases on commodity prices because all too frequently it was asserted that there would be no significant impact. Nevertheless, USDA's fiscal year 1980 impact statement contained language similar to that shown in the 1979 statement. For example:

Poultry--"Of all planned USDA purchases, planned purchases of turkeys and light-type fowl under the Docket Mix are expected to have the most significant impact on producers' income and are expected to help stabilize the prices of these commodities the most. The USDA planned purchases of turkeys under the Docket Mix would constitute 5 percent of the market during the period of purchase; planned purchases of light-type fowl would constitute 20 percent. Since light-type fowl command the least return on the market, USDA planned purchases would help supplement the incomes of egg producers who are expected to face the most pronounced decline in price for their product. The USDA planned purchases of broilers under the Docket Mix would constitute less than 1 percent of the market during the period of purchase and are, hence, not expected to significantly affect producers' income or prices."

Vegetables--"Supplies of almost all vegetables to be purchased by USDA are expected to fall below last year's output, the exceptions are sweet potatoes and tomatoes. * * * USDA purchases of tomato products will help California producers the most, as their indicated harvest will constitute 86 percent of the total U.S. crop. Their indicated harvest is 19 percent above last year's. Sweet potato purchases will assist North Carolina and Louisiana producers the most, since their combined indicated production constitutes 54 percent of the market."

As shown above, the 1980 impact analysis statement did contain some general reference to the expected impact of section 32 purchases. However, the overall goals USDA expected to achieve were not specified in sufficient detail to have allowed it to measure the effect of its purchases on market prices or commodity availability.

Actual impact has not been analyzed

Although USDA prepares annual summaries detailing section 32 purchases, it has not performed any analyses to determine the actual impact of the section 32 purchases on the agricultural community. Without such post-purchase analyses or assessments, USDA is not in a position to know whether different purchase strategies could have had a more significant impact. For example, in fiscal year 1979 USDA purchased \$60.6 million worth of egg mix, turkey rolls, whole turkeys, and canned boned poultry with section 32 funds. Yet the annual summary detailing the purchases did not contain any information on how these purchases affected the marketplace or whether a different mix of these products would have been more or less desirable or beneficial.

USDA officials told us that they believe their section 32 purchases help stabilize farm income and prices but they were not aware of the extent of any impact.

USDA STUDY WILL RESPOND TO SENATE RESOLUTION 90

On June 20, 1979, the Senate passed a resolution (S. Res. 90) which asked the Secretary of Agriculture to address 11 issues directly related to the operation of three USDA school nutrition programs (school lunch, school breakfast, and special milk). Among the issues was the programs' contribution to the agricultural economy, including commodity-by-commodity and regional analyses. The resolution required that the Secretary provide the Congress with a progress report by January 31, 1980, and a final report by March 31, 1981. However, as of May 5, 1981, a final report had not been issued.

In its January 30, 1980, progress report, USDA said that the program's impact on the agricultural economy would be assessed by doing the following:

"This study will include a commodity-by-commodity analysis of impacts on the agricultural economy as well as an analysis of impacts across regions of the country. The impact of net product movements associated with the school feeding programs will be estimated. Data relating to specific commodities for participating schools, meal preparations, portion sizes, and menu cycle data will be collected from a nationally representative sample. This data will be used in regression models to determine the types and amounts of commodities used in school feeding programs. Estimates of gross product movements required to supply school children with food if there were no school feeding programs will be derived from regression models using the Nationwide Food

Consumption Survey of 1977-78. Net differences in commodity use associated with the school feeding programs will be determined by comparing the results of these two procedures. Impact by region will also be estimated using an approach based upon historical commercial production of each commodity."

USDA officials involved in the study told us that it will attempt to estimate the effect of the National School Lunch Program in terms of quantities bought but will not attempt to measure the effectiveness of USDA's surplus-removal purchases.

CONCLUSIONS

USDA has spent about \$877 million of section 32 funds in the direct purchase of commodities for the child nutrition programs in fiscal years 1978, 1979, and 1980. However, it has done little to document (1) how it expected these purchases to affect market prices and commodity availability or (2) the actual effects of these purchases. Determining the potential and actual impacts of its purchases on the commodity markets would put USDA in a better position to determine if its purchase strategies needed revision.

RECOMMENDATION TO THE SECRETARY OF AGRICULTURE

We recommend that the Secretary of Agriculture evaluate the potential and actual effects of USDA's section 32 commodity purchases on the market prices and quantities available.

CHAPTER 3

NEED CONTINUES FOR BETTER IDENTIFICATION OF USER NEEDS

In a January 1977 report on the school lunch program, ^{1/} we said that although FNS recognized the need for local school district input in commodity purchase decisions,

- its regional offices had not emphasized to the States the importance of obtaining data on commodity needs from school districts;
- the regional offices had not followed up to ensure that district needs were identified and subsequently considered in the State-prepared commodity preference reports;
- because State officials usually prepared the reports with only limited input from the districts, the reports did not always reflect district needs; and
- the reports did not provide a means for showing the quantities of commodities required to meet district needs.

Although FNS has tried to determine user needs and preferences of those districts receiving commodities for the school lunch program, it has had only limited success. In addition, State distributing agencies order section 6 and section 32 commodities without determining user needs or preferences. As a result, USDA has purchased and States have accepted and offered some commodities that the users do not prefer or that exceed their needs.

PAST PROBLEMS WITH SCHOOL PREFERENCE DATA

In our January 1977 report, we said that FNS regional offices were not ensuring that local school districts' needs were considered and accurately reflected in State-prepared commodity preference reports and that the preference reports did not provide a means to identify actual quantities needed to meet local schools' needs. USDA has tried to remedy some of the problems we had reported, but these efforts have been somewhat inconsistent, and similar problems continue to exist.

For the 1977-78 school year, FNS asked the States to survey all participating school districts for their commodity preferences and desired servings for each of three categories of commodities--protein foods, fruits and fruit juices, and vegetable products. These surveys were to be returned to the FNS regional offices by

^{1/}"The Impact of Federal Commodity Donations on the School Lunch Program" (CED-77-32, Jan. 31, 1977).

May 15, 1977. However, this survey data may not have been representative because

--some States did not distribute surveys to all school districts and

--a substantial number of districts that received surveys did not complete them.

After the 1977-78 school year survey, FNS devised a new survey form. For each commodity listed the form provided space for the school districts to show (1) the total number of days they would like to serve the food, (2) the total quantity of each food they would like to receive, (3) their rating of the commodity using "H" for highly acceptable, "A" for acceptable, and "U" for unacceptable, and (4) any other pertinent remarks concerning such matters as packaging and shipping.

According to USDA, the 1978-79 school food preference survey was to be sent to each State no later than April 1, 1978. This would assure that school preference data would be available for use in preparing the fiscal year 1979 commodity purchase plan. However, the Office of Management and Budget (OMB) would not approve USDA's approach of surveying all districts because OMB questioned the report's utility and its effect on overall program direction. Subsequently, USDA developed and OMB approved a statistical sampling method of surveying school districts. USDA required that consolidated State reports of district preferences be sent to FNS regional offices no later than October 30, 1978. As a result, USDA had to use preference data gathered for the 1977-78 school year in developing its fiscal year 1979 purchase plan.

As was the case with the 1977-78 survey, the 1978-79 survey data was suspect because

--some States did not distribute surveys to the required number of school districts,

--the overall response rate was too low to assure statistical reliability,

--directions for filling out the survey were unclear and interpreted in several ways, and

--some States provided inconsistent acceptability data.

The FNS program reporting staff was responsible for receiving and compiling the composite State reports. Because it did not believe the reports contained complete or reliable data, FNS did not summarize or use the quantity data received or make statistical analyses or projections of the preference data that some State had summarized.

SFD ADVISORY COUNCILS--A NEW APPROACH
FOR GATHERING PREFERENCE DATA

FNS has discontinued the traditional method of obtaining school district needs--a preference report prepared by school districts--in favor of SFD advisory councils to be operational sometime in fiscal year 1981. However, as of December 1980, FNS had provided only general instructions to these councils on how district commodity-need data is to be collected, analyzed, and used in formulating future USDA commodity purchase plans.

USDA regulations (7 CFR 210) provide that each council is to report to the State education agency, no later than January 15 of each year, beginning in 1981, recommendations regarding the selection and distribution of commodities for the next school year. The State education agency is required to report the council's recommendations to FNS before February 15 of each year, beginning in 1981.

As set forth in USDA regulations, each council's responsibilities include providing the State education agency with information to be obtained by surveying all school food authorities on the most desired foods, the least desired foods, and recommendations for new products. The council is also to advise the State on the amounts of each food item desired, types of packaging and package size, shipping schedules, and recommendations for changes in donated food specifications.

FNS had developed guidelines and a revised reporting form to be used by the councils when obtaining school districts' commodity preference and needs data. However, due to difficulties during the first year of operation, FNS has amended the requirements to allow the councils to determine both the scope and method of obtaining the preference data required. FNS has eliminated the requirement to survey all school food authorities and will allow each council to survey as many school food authorities in the State as it considers essential. Councils are not required to gather information on actual quantities. In addition, the council may now use whatever format it determines to be best for gathering school food preference data. Advisory councils will have the option of gathering data by using the FNS format in its entirety, using selected segments of it, or developing their own formats.

STATES DO NOT ALWAYS CONSIDER USER NEEDS
WHEN ORDERING DONATED COMMODITIES

States place orders with FNS for donated commodities purchased with sections 6 and 32 funds. To know the quantities of any commodity that can be effectively and efficiently used by their recipient agencies, the respective State distributing agency must obtain user needs. However, in many cases the States we visited were ordering commodities based on their judgment with no direct input from users on quantities needed or preferred. Because State distributing agencies ordered commodities without

direct input, some users (1) had refused significant amounts of commodities which were counted against the amount of commodity assistance to which they were entitled or (2) had accumulated commodity inventories which far exceeded their needs.

FNS periodically surveys State distributing agencies to determine quantities of sections 6 and 32 commodities desired by the States for the schools and the elderly feeding program. The FNS regional offices administer the surveys either by telephone or memorandum and ask the States for quantities desired. In six of the seven States we visited, State officials responded to these surveys without obtaining input from the respective users and could not always support how they arrived at the estimated needs. For example:

- The Governor's Committee on Aging is responsible for estimating needs of the elderly feeding programs in Texas. To do this, a method of estimating needs was devised in 1977 based on an employee's experience in menu planning and knowledge of the average number of times a food would be used in a month. However, this method does not consider need data of individual feeding projects or ending inventories.
- Pennsylvania does not ask for school input for commodities that are well accepted. The responsible State official told us that in determining the quantity to be ordered, he reviews commodity rejection files and appropriate State field review reports, considers the commodity's previous fiscal year activity, and adds his own experience and judgment to make the final decision. For three selected commodities, the State could not show us any detailed analyses to support the quantities it had ordered for the 1980-81 school year.
- California does not solicit user needs when ordering sections 6 and 32 commodities. The responsible State official told us that historical usage and inventory levels are used to determine quantities to be ordered. However, there was no documentation to show how these factors were considered in placing orders.

Some school districts refuse certain commodities

Program regulations (7 CFR 250.4(h)) allow any school food authority participating in food service programs under the National School Lunch Act to refuse commodities offered for use in lunches, and school districts do refuse some commodities.

- One Montana district we visited refused its entire 1978-79 school year allocations of dry pinto beans (preparation is difficult in large quantities and the children do not like them because the bean embryos look like worms), corn meal

(kitchen personnel at the preparation sites refused to use it), and canned poultry and beef (labor intensive to prepare in palatable form--veins, fat, and gristle must be removed--and even with this effort, children do not like it). In addition, our review of seven commodity shipments the State received during the 1978-79 school year showed that from less than 1 percent to 47 percent of the commodities shipped to the distributing agency were refused by school districts to which they were initially allocated. The highest percentages of refusals involved all-purpose flour (47 percent); butter (23 percent); and frozen, cooked turkey rolls (15 percent).

--For the 1979-80 school year, one California school district we visited refused the following percentages of commodities offered to it.

<u>Commodity</u>	<u>Percent refused</u>
Catsup	68
Cranberry sauce	72
Potato flakes	63
Canned tomatoes	61
Vegetarian beans	59

The district refused the catsup, cranberry sauce, and canned tomatoes because they exceeded its needs, the vegetarian beans because they cannot be prepared in a variety of ways and are not well accepted by the students, and the potato flakes because the students did not like the taste. Part of the high refusal percentages for four of the five commodities (excluding cranberry sauce) can also be attributed to their being offered to the district late in the school year. A second California school district we visited refused 75 percent of the canned poultry, 76 percent of the canned tomatoes, and 81 percent of the vegetarian beans it was offered for the 1979-80 school year because they exceeded its needs.

--One Pennsylvania school district we visited refused 50 percent of the canned peas; 60 percent of the canned apple juice; 89 percent of the canned tomato paste; and 100 percent of the frozen, cut-up chicken that was offered in fiscal year 1980.

--As of January 1980 one Missouri school district we visited had rejected from 82 to 97 percent of the quantities offered for eight different commodities for the 1979-80 school year because, based on past history, the district could not use them.

Inventories that exceed needs are occurring

State distributing agencies do not always consider user needs when ordering federally donated commodities. Because of this and other factors, some users and State distributing agencies had accumulated inventories of commodities that far exceeded their needs. Our review of inventories maintained by the 42 agencies we visited and 15 other agencies for which we were able to obtain records showed (1) inventories valued at about \$2.7 million that exceeded 12-month needs of commodity recipients under the child nutrition, elderly feeding, commodity supplemental, and charitable institution programs and (2) inventories valued at about \$1.4 million that exceeded a 3-month need plus user-desired safety levels for commodity recipients under the needy family program.

Although several factors contributed to the excessive inventory levels, the main factor, in our opinion, was the failure to determine actual user needs. These factors as well as the negative effects on users of the excessive inventories are discussed in chapter 4.

THE IMPACT OF USER NEEDS AND PREFERENCES IN ANNUAL PURCHASE PLANS IS NOT DOCUMENTED

Because USDA has never adequately determined user needs and preferences, it does not know whether annual purchase plans represent the users' desires and needs. In addition, the role of user needs and preferences in preparing the annual purchase plans is not documented.

In deciding which commodities and quantities to be purchased, FNS prepares an annual purchase docket. The docket contains three alternate purchase plans: (1) a school preference mix which is based primarily on school preferences, (2) a surplus and CCC commodity mix which is weighted heavily toward CCC-type commodities such as dairy products, grains, and vegetable oil products, and (3) a docket mix based on school preferences, use of surplus and CCC commodities, and response to past program purchases. Recommendations for those commodities to be purchased under the docket mix are then made and approved by the CCC Board of Directors. The purchase plans from year to year are similar; the following table shows the school preference, surplus and CCC commodity, and docket mixes for fiscal year 1980.

<u>Commodity</u>	School preference <u>mix</u>	Surplus and CCC commodity <u>mix</u>	Docket <u>mix</u>
	----- (millions) -----		
FSQS-type commodities:			
Meat	\$187	\$ 28	\$130.6
Poultry	76	190	153.8
Fruit	119	38	68.5
Vegetables	<u>87</u>	<u>50</u>	<u>111.1</u>
Total	<u>469</u>	<u>306</u>	<u>464.0</u>
CCC-type commodities:			
Dairy products	160	222	162.0
Grains	29	79	29.8
Peanut and oil products	<u>36</u>	<u>87</u>	<u>38.2</u>
Total	<u>225</u>	<u>388</u>	<u>230.0</u>
Total	<u>\$694</u>	<u>\$694</u>	<u>\$694.0</u>

The validity of the figures used in the purchase mixes shown in the purchase docket is difficult to determine because the calculations used in determining the dollar figures are not documented. In addition, FNS officials told us that the availability of commodities, current and estimated future market prices, availability of funds, user preferences, and previous years' purchases are all factors affecting how much will be spent on which commodities. However, no detailed analysis showing the weight given these factors or how these factors contributed to the amounts shown in the purchase docket had been prepared.

Accompanying the purchase dockets are impact analyses of the effects of commodity purchases on the applicable commodity markets and prices. However, these analyses did not provide information on how the dollar figures in the docket were arrived at. For example, the fiscal year 1980 impact analysis contained the following justification for the \$111.1 million purchase of vegetables.

"Planned purchases would total \$111.1 million with emphasis on potato and tomato products, corn, peas, green beans, dry beans, and vegetarian beans. Planned purchases would be 18 percent more than last year's plan."

Neither the impact analysis nor the purchase docket contained any justification for the recommended docket purchase of vegetables that was \$24.1 million more than the school preference mix and \$61.1 million more than the surplus mix. (See above table.)

A similar unexplained difference occurred for vegetables in fiscal year 1979. In addition, the purchase docket for fiscal year 1979 recommended purchasing \$5.5 million worth of peanut products more than the school preference mix and \$56.4 million less than the surplus and CCC commodity mix. Again, neither the impact analysis nor the purchase docket explained the reason for the difference.

CONCLUSIONS

USDA has recognized the need to obtain information from school districts on their commodity needs and preferences. Following the issuance of our 1977 report, it made two efforts to do so. However, the information it received was fragmentary and inaccurate. As a result, USDA had no assurance that the information represented the real needs and preferences of the recipients.

Many problems encountered in using donated commodities could be resolved if States determined recipient agencies' needs and preferences and reported them to FNS. Until this is done, users will continue to be offered commodities that are (1) in amounts exceeding their needs, (2) not in the desired form or size, or (3) difficult to use in some food preparation systems.

Accurate identification of users' preferences and their use by State distributing agencies when ordering commodities for their various recipients could

- increase Federal assistance to users that have refused large quantities of some commodities in the past and

- reduce the quantities of commodities on hand in State and user warehouses and, consequently, reduce storage, handling, and administrative costs.

USDA plans to gather future preference data for school districts by means of the SFD advisory councils. It is critical that these councils be given specific guidelines for gathering and summarizing such data. USDA also needs to assure that the councils follow the guidelines.

We question whether allowing the councils to determine both the scope and method of obtaining the required preference data and to use individually designed reporting formats will result in a full and accurate reflection of school district preferences.

In addition to fully and accurately determining school district needs and preferences, USDA should document the extent such needs and preferences are used in preparing the annual purchase plans.

RECOMMENDATIONS TO THE
SECRETARY OF AGRICULTURE

We recommend that the Secretary of Agriculture:

- Establish specific procedures and a required reporting format to ensure that school districts' views on commodity preferences and needs are fully, accurately, and uniformly reflected in reports sent to State educational agencies by the State food distribution advisory councils.
- Specifically show in the annual purchase plan how user needs and preferences affect the amount of funds that may be spent on commodity purchases. Included should be analyses showing the weights given such factors as commodity availability, market prices, and fund availability.
- Require State distributing agencies to order commodities for recipient agencies based on demonstrated use and need rather than judgment and personal opinion.

CHAPTER 4

FEDERAL AND STATE PROGRAM MONITORING

NEEDS IMPROVEMENT

A good Federal and State monitoring program is necessary to detect and prevent operational problems in the commodity donation program. FNS' headquarters policy and direction, its regional office oversight, and State monitoring of commodity program operations have not been adequate. As a result, excess inventories of commodities have been allowed to accumulate, some recipient agencies are not adequately controlling commodity receipt and distribution, and the accounting control over commodities used in reprocessing contracts continues to be inadequate. We believe improvements are needed in program monitoring if the program is to be operated effectively and economically.

An effective monitoring system is essential to FNS and State distributing agencies if they are to adequately control the receipt, distribution, and inventories of donated commodities. If FNS had an effective system for monitoring States and if the States had adequately monitored their recipient agencies, they could have identified the problems disclosed by our review. Effective monitoring would have enabled FNS or the State distributing agencies to

- identify the existence of excess inventories,
- identify the factors causing the accumulation of excess inventories, and
- take necessary actions to eliminate the factors causing the problem.

Eliminating the factors causing excess inventories will eventually resolve the problem and its negative effects.

SOME DISTRIBUTING AND RECIPIENT AGENCIES HAVE ACCUMULATED INVENTORIES EXCEEDING NEEDS

We reviewed inventory and usage records at 12 State distributing agencies and 42 recipient agencies comparing commodity usage with ending inventory balances. Commodities exceeding needs and valued at more than \$4.1 million had accumulated at some recipient agencies and in two State distributing agencies' warehouses. The following table shows the value of the excess inventories by program.

<u>Program</u>	<u>Value of excess inventories</u>
State distributing agencies:	
Various programs	\$1,971,000
Recipient agencies:	
Needy family	1,457,600
Elderly feeding	506,900
School lunch	198,500
Charitable institutions	<u>2,500</u>
Total	<u>\$4,136,500</u>

Using average monthly commodity-use figures, we converted ending inventory quantities into the number of years' supply on hand and found numerous instances where the quantities on hand exceeded those needed for 2 years or more, as illustrated by the following examples.

--The California distributing agency's warehouse contained a 9.3-year supply of raisins, a 6.6-year supply of all-purpose flour, a 3.2-year supply of whole wheat flour, and a 2.4-year supply of rolled wheat.

--Five Texas projects participating in the elderly feeding program had accumulated a 6.2-year supply of applesauce, a 5.2-year supply of nonfat dry milk, and a 2.3-year supply of tomato paste.

--Missouri's elderly feeding program had accumulated a 4.4-year supply of tomato paste, a 2.3-year supply of dehydrated potato flakes, and a 2.2-year supply of vegetarian beans.

Reasons for the accumulation
of excess commodity inventories

State distributing agencies' failure to fully consider user needs and preferences in determining quantities needed is the primary reason excess commodities exist at the recipient agency level and in some State distributing agency warehouses. However, this is not the sole reason. In some cases agencies have acquired commodities intending to convert them into more desirable end products. When they are not converted, they accumulate as excess inventory. In addition, some recipient agencies perpetuate excess commodity inventories by continuing to accept commodities when they already have quantities exceeding their needs.

User needs not considered in
ordering and allocating commodities

State distributing agencies did not fully consider user needs and preferences in determining the quantity of commodities needed. Too often distributing agencies ordered commodities on a judgmental basis without considering the users' usage history or existing inventories. For example, the California distributing agency ordered tomato products to fill the State's fiscal year 1979 entitlement without surveying school districts to determine need. Because the agency overestimated user demand, it accumulated about \$337,000 worth of tomato products that exceeded 1 year's needs.

Similarly, State agencies on aging did not always adequately solicit needs from recipient agencies participating in the elderly feeding program. For example, the Texas State Agency on Aging ordered commodities based on estimates of the number of meals to be served and how often each commodity would be served by the recipient agencies statewide. For fiscal year 1979 the agency nutritionist estimated serving frequency on the basis of her judgment of the average number of times a given food would be used in a month. The State followed the same procedure in estimating fiscal year 1980 needs. Before ordering, the State became aware that some commodities on hand exceeded needs and did not order those commodities for fiscal year 1980. However, the State failed to identify other commodities where supply exceeded 1 year's needs. For example, we found supplies of canned boned poultry and applesauce exceeding 1 year's needs, yet the State ordered 3,820 cases of canned boned poultry and 1,735 cases of applesauce. Five recipient agencies we reviewed had inventories of canned boned poultry that ranged from a 1.3-year to a 3.5-year supply and inventories of applesauce that ranged from a 2.8-year to a 13.8-year supply.

State distributing agencies' failure to adequately consider user needs in allocating donated commodities also contributed to some recipient agencies' accumulating excess inventories. For example, the Texas distributing agency allocates sections 6 and 32 commodities to school districts on the basis of the average daily number of meals served, without considering the individual districts' actual commodity needs. Under Texas procedures, districts can refuse all or part of a commodity allocation, but the procedures require school districts to refuse allocations before they know the actual quantities allocated by the State. Before the start of each school year, the State sends each school district a list of the commodities it might expect and asks district officials if they want to take either (1) their entire allocation, (2) a portion of their allocation, or (3) more than their allocation.

One Texas school food service director told us that it was very difficult to realistically refuse any part of an allocation without knowing which commodities the district would receive or in what quantity. She also said that the district would accept

its entire allocation of all commodities offered during school year 1979-80. As of March 31, 1980, the district had accepted all commodity allocations with the result that some commodities exceeded its needs. For example, as of March 31, 1980, the district had received 1,047 cases of tomato products--a 2.3-year supply of catsup, a 2-year supply of tomato paste, a 1.9-year supply of tomato juice, and a 1.4-year supply of canned tomatoes. In addition, the district had accepted 292 cases of frozen mixed vegetables, which represented a 12.2-year supply, and 260 cases of vegetarian beans, representing a 3.9-year supply.

Acceptance of commodities already in excess

Few State distributing agencies have adequate procedures for preventing recipient agencies from accepting commodities exceeding actual needs. As illustrated by the following examples, some recipient agencies perpetuated excess commodity inventories by accepting commodity allocations when existing inventories already exceeded 1 year's needs.

--In October 1979 a Montana school district accepted 177 cases of peanut butter (a 13-month supply) although it had a 14-month supply in inventory.

--In November 1979 another Montana school district accepted 194 cases of canned boned poultry (a 26-month supply) although it had a 27-month supply in inventory. In October 1979 the district accepted 113 cases of peanut granules (a 20-month supply) although it had a 17-month supply on hand.

In California, recipient agencies are allowed to refuse commodities allocated to them, but the State agency has no means of preventing the recipient agencies from accepting commodities exceeding their needs. One school district accepted a large allocation of tomato products despite having over a year's supply of tomato products in inventory.

Stockpiling of commodities to fulfill processing contracts

In the spring of 1978, the California distributing agency accumulated a large inventory of nonfat dry milk with the intent of contracting to have it processed into mozzarella cheese. Shortly after California stockpiled the nonfat dry milk, USDA began to process the commodity into mozzarella cheese nationally and offer it to the States. California subsequently discontinued its processing contract and was left with excess nonfat dry milk. As of March 31, 1980, the State still had a 1.4-year supply of the commodity valued at about \$2.6 million. However, the State was continuing its efforts to reduce its nonfat dry milk inventory by contracting to have it processed into cheddar and Monterey Jack cheese.

Effects of excess inventories

Excess inventories of donated commodities adversely affected some State distributing and recipient agencies. Excess commodity inventories result in storage cost increases, greater potential for infestation and spoilage, and difficulty in effectively utilizing commodities.

Excess commodities can cause increased storage costs whether the State and recipient agencies have their own storage facilities or contract for commercial facilities. Some recipient agencies owned and operated their storage facilities. However, most had limited storage facilities--particularly freezer storage. When inventories of donated commodities and purchased food items exceed available storage capacity, recipients must contract with commercial facilities for additional space.

When excess commodities accumulate and cannot be used within a reasonable time, the State or recipient agency incurs unnecessary storage costs. We did not attempt to estimate the total amount of additional storage costs incurred by program participants. However, the commercial rates charged certain recipient agencies indicated that the costs incurred could be substantial. For example, storage rates charged two recipient agencies in Texas ranged from 23 cents to 98 cents per hundredweight per month.

Stored commodities are also susceptible to rodent and insect infestation. When excess commodities are stored, the potential for loss increases because of the greater quantities involved and the long storage periods before the commodities may be used. According to USDA, this may also be due to the States' failure to enforce a first-in, first-out usage pattern. During the 10-month period July 1979 through April 1980, California lost commodities valued at an estimated \$204,600 because of rodent infestation at a commercial warehouse. Several of the commodities lost were in excess supply. For example, the State had a 6.6-year supply of all-purpose flour in its April 1980 inventory. During the period November 1979 through April 1980, rodents infested about 10 percent of the flour valued at about \$7,600.

Excess commodities are also more susceptible to spoilage because they are likely to be stored for a period exceeding recommended maximum shelf life. We found several examples of commodities in inventory at various locations which had been stored beyond USDA's recommended maximum storage period for such products. The following table illustrates this point.

<u>Commodity</u>	<u>Location</u>	<u>Age of commodity</u>	Recommended maximum storage period (<u>note a</u>) (months)
Print butter	Texas elderly feeding projects	25 to 27	6
Canned butter	Navajo and Papago Indian Reservations	17 to 19	6
Canned meats	Papago Indian Reservation	16 to 19	6 to 7
Corn syrup	Tennessee commodity supplemental food program	24 or more	12
Egg mix	Papago Indian Reservation	23	12
Frozen ground beef	Texas elderly feeding project	10 to 15	6 to 7

a/Recommended maximum storage period taken from amendment 6 of USDA's Commodity Inspection and Maintenance Regulation, dated July 2, 1979.

Because a food item has been in inventory beyond the maximum recommended storage period does not necessarily mean the product is unfit for consumption; however, such commodities should be given priority over newer stocks and used as soon as possible.

We noted that commercial storage facilities had the capability to properly control the storage temperature. However, some recipient agency warehouse facilities did not have the means to cool storage facilities during the summer months and had limited freezer storage.

Some recipient agencies in the elderly feeding program that received the bulk of their entitlement in commodities could not effectively use their full per-meal commodity allowance of 38.5 cents because they used a portion of their entitlement for commodities that exceeded their needs. For example, a recipient agency in Texas used an average of 5 cases of applesauce monthly, but during the 12-month period ending June 30, 1979, it received at least 750 cases of applesauce. Those commodities which cannot be effectively used prevent a recipient agency from using its maximum commodity allowance per meal. In fiscal year 1979 this recipient agency used only about 25 cents per meal, or about 13.5 cents less than the maximum allowed. Similarly, another Texas recipient agency used only about 27 cents per meal, or about three-fourths of the maximum per-meal allowance, because of inventories exceeding its needs.

ACCOUNTING CONTROLS ARE INADEQUATE

Program regulations (7 CFR 250.6(q)) provide that distributing agencies require subdistributing and recipient agencies to maintain accurate and complete records on the receipt, disposal,

and inventory of donated foods. We found instances of a general disregard by some recipient agencies for the regulatory requirements as evidenced by (1) inaccurate or inadequate reporting of commodities used or distributed and (2) failure to take periodic physical inventories or properly reconcile the physical counts with inventory book balances.

Inaccurate reporting of commodities used or distributed

We reviewed the records of 18 agencies participating in the elderly feeding, needy family, and supplemental food programs and found that 10 could not accurately account for donated commodities distributed or on hand.

At one recipient agency in Texas, we found numerous instances where commodity gains or losses shown on the monthly inventory reports submitted to the State could not be explained. For example:

- The July 1978 beginning inventory of processed cheese was reported as 268 cases. None were received during the month, but nine cases were used. The reported ending inventory was 289 cases--30 cases more than could be explained.
- The September 1978 beginning inventory of sliced peaches was 258 cases. An additional 225 cases were received during the month, making 483 cases available for use. Only 22 cases were reported as used during the month, leaving an ending inventory of 461 cases. The monthly report for September showed no ending inventory, but the October 1978 beginning inventory showed 226 cases--235 less than the records indicated.
- The September 1978 ending inventory of frozen ground beef was reported as 302 boxes. The October 1978 beginning inventory showed 273 boxes--a loss of 29 boxes.

At a Missouri recipient agency, we could not verify the reported ending inventory by adding amounts received to the beginning inventory and subtracting amounts used. Also, in many instances the reports indicated use of commodities that the feeding site did not have in inventory. An agency official could not explain the reason for these discrepancies.

Our review of the needy family programs in Montana and North Dakota showed that commodity distribution records at the reservations we visited could easily be falsified and were totally unacceptable as accounting records. For example, distribution of donated commodities to eligible recipients on Montana Indian reservations are recorded on a food distribution and receipt record. In reviewing the procedures followed by issuing clerks on two Indian reservations when recording commodity disbursements, we noted several procedures which did not

provide adequate control over disbursements and could result in a misappropriation of funds.

<u>Procedure</u>	<u>Indian reservation</u>	
	<u>Blackfeet</u>	<u>Flathead</u>
Amounts of commodities disbursed were changed without being initialed by a responsible individual	X	X
The issue column for a commodity was left blank when that commodity was out of stock	X	X
The issue column for a commodity was left blank when a recipient refused his/her allocation of the commodity	X	
Recipients signed the food distribution and receipt form before quantity figures were entered		X
When check-out personnel found that a recipient had not taken any of a commodity that was shown as issued on the distribution and receipt record, the quantity figure was not changed	X	

Similarly, recordkeeping problems in the supplemental food programs in Colorado and Tennessee caused their records to be unacceptable. In Colorado:

--A warehouseman preposted recipients' distribution records with the maximum allowable amounts of food. If a recipient refused any items, a warehouseman circled the maximum allowable quantity of the commodity on the distribution record to indicate a refusal, and returned the unwanted items to inventory. Potentially, a warehouseman could intentionally not indicate the refused commodity and later misappropriate the item.

--Unused columns on the distribution records were left blank.

--Recipients often removed commodities from their food packages and left them at the warehouse without telling anyone. Warehouse personnel returned these items to inventory but did not adjust quantities distributed because they could not identify such refusals with a particular recipient. Instead, warehouse personnel reported the items as inventory gains supported by inventory adjustment reports. Potentially, it would be easy not to report such inventory gains and misappropriate the food.

In Tennessee the quantity of commodities actually distributed could be less than the distribution records showed. A clerk prepared the individual distribution card based on the maximum allowable quantities adjusted for any quantities the recipient did not wish to accept. The recipient then signed the distribution card and proceeded to pick up the commodities. Recipients could still refuse commodities at this point and many did. However, warehouse personnel made no adjustments to the quantities distributed per the recipients' distribution records. Instead, they tried to keep a tally which could be reconciled to the monthly inventory records, but the tally sheets were not maintained after the monthly inventory report was prepared. This system failed to provide an accurate record of food distributions to recipients and increased the potential for misappropriation of commodities because no documentation existed to show that commodities had been properly issued.

Physical and perpetual inventory problems

Of 15 elderly feeding and needy family recipient agencies we visited, 4 elderly feeding agencies and 2 needy family agencies did not maintain perpetual inventory records, take physical inventories, or explain differences between physical inventory and book totals.

At one Texas recipient agency participating in the elderly feeding program, the January 1979 beginning inventories for 25 commodities varied substantially from reported ending inventories as of December 31, 1978. The project director told us that the variances occurred because of commodity transfers between projects or physical inventory adjustments. However, she could provide no documentation explaining these variances.

<u>Commodity</u>	<u>Reported inventories</u>		<u>Variance</u>
	<u>Ending 12/31/78</u>	<u>Beginning 1/1/79</u>	
Canned pears	28	244	+216
Flour	3	136	+133
Turkey roll	123	174	+ 51
Peanut butter	56	87	+ 31
Sliced peaches	157	181	+ 24
Rice	13	31	+ 18
Shortening	104	116	+ 12
Canned poultry	48	57	+ 9
Canned peas	159	163	+ 4
Apple juice	7	11	+ 4
French fries	23	25	+ 2
Potato rounds	95	97	+ 2
Tomato paste	49	51	+ 2
Catsup	23	25	+ 2
Canned corn	382	383	+ 1
Margarine	124	125	+ 1
Cranberry sauce	100	21	- 79
Process cheese	197	134	- 63
Nonfat dry milk	92	39	- 53
Frozen ground beef	488	458	- 30
Apricots	49	38	- 11
Canned tomatoes	102	94	- 8
Orange juice	58	54	- 4
Applesauce	91	87	- 4
Butter	59	58	- 1
Total			<u><u>765</u></u>

We estimated the value of the 765 cases at \$12,900.

Another Texas recipient agency participating in the elderly feeding program had not maintained any perpetual inventory records from August 1979 through January 1980. Therefore, we estimated the quantities we believed the agency should have been accountable for as of January 31, 1980. We determined monthly use of commodities for July 1978 through August 1979 and projected that use to the months of September 1979 through January 1980. By subtracting this projected use from the agency's reported ending inventory as of August 31, 1979, we obtained an estimate of quantities the agency should have had on hand. We compared these figures with the physical inventory counts taken in January 1980 and found substantial variances. For example,

--The reported ending inventory of applesauce on August 31, 1979, was 748 cases. Monthly use before September 1979 was about 14 cases. Projecting this monthly use from September 1979 through January 1980, we estimated that the inventory should have been reduced by about 70 cases to about 678 cases. However, the physical inventory as of January 1980 showed only 113 cases on hand. That left

a 565-case variance which the project director could not account for.

--The August 31, 1979, inventory of shortening was reported as 227 cases. Subtracting projected use of 8 cases during the period September 1979 through January 1980 left a balance of 219 cases. However, the physical inventory at January 31, 1980, showed only 128 cases--a variance of 91 cases. The project director said that the caterer had begun baking pies and cakes and she believed this should account for an increase in usage, but not to the extent of 91 cases over 5 months. Our analysis showed that the most shortening used in any month between July 1978 and August 1979 was 7 cases in August 1979 and that the caterer had been making its own pastries at that time.

Similar inventory control problems existed at two area agencies on aging in Pennsylvania. The State agency on aging requires its recipient agencies to take and reconcile monthly physical inventories with perpetual inventory balances. Two recipient agencies we reviewed were not complying with the State requirement. One agency director told us she did not always take a monthly physical inventory. She said that when she does not take a physical inventory, she submits her inventory report showing the physical inventory balances to be the same as the perpetual book inventory balances. She also said that when a physical inventory is taken, she does not reconcile any differences between the physical count and the reported book balance. For example, of the 23 commodities inventoried on May 27, 1980, 22 showed a difference between the physical and perpetual inventories. The other area agency did not maintain perpetual inventory records, nor did it take the required physical inventories.

At one Indian reservation in Montana, numerous discrepancies existed between the commodity totals shown on the perpetual inventory records and those determined by physical inventories for the months of October 1979 through February 1980. The following table shows that during the 5-month period, the recipient agency had to adjust anywhere from 79 to 100 percent of the perpetual inventory balances because of the monthly physical inventories.

<u>Month</u>	<u>Number of commodities</u>		<u>Percent</u>
	<u>Having a month-ending balance</u>	<u>Whose perpetual inventory balance required adjustment</u>	
October 1979	27	27	100
November 1979	28	28	100
December 1979	32	29	91
January 1980	31	30	97
February 1980	33	26	79

Most of these inventory adjustments involved cases in which the physical inventory disclosed more of a commodity on hand than was shown on the perpetual inventory record. As shown by the following examples, the differences were not always adequately explained.

--The October 1979 inventory report showed a shortage of 37 cans of applesauce. In an attachment, the issuing clerk reported that 3 cans had been damaged and destroyed, but there was no explanation of what happened to the other 34 cans.

--The December 1979 monthly report showed a shortage of 147 cans of evaporated milk. The issuing clerk reported in an attachment that he could not find or account for the 147 cans. He speculated that the only way the shortage could have occurred was if the cans were issued but not recorded.

Another reservation in Montana rarely reported any differences between perpetual inventory balances and those obtained by taking physical inventory. For the 5-month period October 1979 through February 1980, this reservation's issuing clerk had twice reported insignificant differences between perpetual inventory balances and physical inventory balances on two different commodities. He told us that several years ago a USDA auditor told him that he should not have any difference between his perpetual inventory balances and physical inventory balances. Accordingly, the clerk did not report such differences on the monthly inventory report, except when they occurred because some commodities had been damaged.

PROBLEMS IDENTIFIED WHEN STATES CONTRACT TO PROCESS FEDERALLY DONATED COMMODITIES

Both we and USDA's Office of Inspector General have identified problems associated with the accounting controls over the processing of federally donated commodities into different end products for distribution to program users.

In a February 1979 report, the OIG said that the food distribution program was not being administered in a manner that assured that the processors were properly using donated foods or that recipient agencies were receiving maximum benefits from them. The OIG found among other things that some processors (1) were not submitting required monthly performance reports, (2) were using their own ingredients in anticipation of receiving USDA-donated commodities, and (3) had accumulated inventories of donated commodities exceeding their needs. Also, the OIG found that distributing agencies had no assurance that independent distributors of processed end products were giving recipient agencies price reductions or credit for the value of donated commodities used in the end products.

The OIG also reported that FNS headquarters had furnished little guidance to its regional offices regarding processing contracts and the regional offices had done little to monitor processing activities. The OIG concluded that this lack of guidance and supervision contributed to a nearly complete breakdown in accountability over the receipt, use, and disposition of donated foods.

The OIG recommended that FNS strengthen its regulations governing the processing of donated commodities. In response, FNS drafted new regulations which were published as proposed rules on June 24, 1980. Among other things, the proposed rules would (1) require FNS approval of contractual provisions before approval by the distributing agency, (2) strengthen procedures to assure that inventories of donated foods placed with processors were properly accounted for, and (3) establish refined procedures to assure that processors were passing on price reductions or credits to recipient agencies for the value of donated commodities used in the processed products purchased. As of May 8, 1981, the regulations governing the processing of donated commodities had not been finalized.

In commenting on a draft of this report (see app. IV), USDA said that while accountability over the receipt, use, and disposition of donated foods was found lacking in many instances cited in the OIG report, it should not be assumed that the audit findings pertain to all States with processing contracts. It said that many States (1) require companies to submit monthly performance reports and compare company figures with recipient agencies' receipts, (2) check performance report figures against price and yield schedules which are submitted as an integral part of the processing contract, and (3) require performance, supply, and surety bonds to protect the value of the donated foods.

Our review of State records and interviews with State officials responsible for processing-contract administration in California, Missouri, Montana, Pennsylvania, and Texas showed that problems similar to those identified by the OIG still existed to varying degrees in some distributing agencies. For example:

- Some participating processors in Missouri and Texas did not submit required monthly performance reports or submitted them late.
- Some participating processors in California and Texas operated with negative inventory balances, indicating that they used their own ingredients in anticipation of receiving USDA-donated commodities. In California we noted that small negative inventory balances were not unusual. In Texas we found three processors showing negative inventory balances.
- One participating processor in Texas had accumulated inventories of donated commodities exceeding its needs.

- The California and Texas distributing agencies entered into processing contracts with little or no guidance in initiating and administering contracts.
- The Texas distributing agency had no assurance that recipient agencies were receiving price reductions or credits for the value of donated commodities contained in the processed end products received.
- The California, Montana, Pennsylvania, and Texas distributing agencies received little technical assistance from their respective FNS regional offices in initiating and administering processing contracts.

FNS' OVERALL PROGRAM MONITORING IS INADEQUATE

Program regulations (7 CFR 250.2) state that FNS has overall responsibility for administering the commodity donation program. This includes evaluating distributing agencies' performance and compliance with program regulations. In an April 6, 1977, memorandum to FNS regional offices, FNS headquarters emphasized that management evaluation is a continuing regional office responsibility which must be performed annually for each distributing agency. However, at the time we made our review, FNS headquarters had not issued any procedures, guidelines, or requirements governing the completion or scope of the reviews.

Of the four FNS regional offices we visited, three did not always review State distributing agency operations on an annual basis. For example, during the 5 years preceding fiscal year 1979, the Southwest regional office had not made annual reviews of any of its State distributing agencies. Additionally, the Mid-Atlantic regional office reviewed only 5 of the 10 State distributing agencies in its region in fiscal year 1979.

Similarly, an OIG draft report stated that FNS regional offices were not always reviewing State distributing agencies annually. The OIG found 16 State distributing agencies that had not had an annual review from April 1977 through April 1980, including all 10 States in FNS' Mountain Plains region. The OIG reported that an additional 29 State distributing agencies had not been reviewed for 1 or more years during the same period.

We found also that when annual evaluations were made, FNS did not always identify significant problems. For example, the Southwest regional office's annual evaluation of the Oklahoma distributing agency did not identify the existence of some commodities which exceeded 1 year's needs. Our comparison of ending inventories with the average monthly use rate showed that nine commodities were in excess supply. For example, the State had a 253-month supply of canned sweet potatoes and a 159-month supply of canned pears.

Similarly, the OIG reported that the annual evaluations that had been made had not identified significant management weaknesses subsequently found by OIG auditors.

FNS DOES NOT ADEQUATELY MONITOR
INVENTORY LEVELS OF DONATED COMMODITIES

FNS does not have an effective system for monitoring inventory levels. The monthly inventory reports FNS receives from the States are intended to help FNS officials control inventory levels. Yet they are sometimes incomplete or inaccurate and often untimely. In addition, the reports show only inventories in State-owned or -leased storage facilities and are not broken down by eligible program recipient, such as the school lunch or elderly feeding programs. Although problems exist with the inventory reports, FNS could still use the reports to analyze some State inventory levels. For example, our analysis of such reports on commodity inventories in Oklahoma identified almost \$500,000 in excess inventories.

Required reports often late,
inaccurate, and incomplete

FNS instructions require State distributing agencies to report monthly to the appropriate FNS regional office the receipt and distribution of donated commodities using FNS Form 155 (Receipt and Distribution of Donated Commodities). When properly completed, this report shows by commodity the (1) beginning monthly inventory, (2) monthly receipts, (3) quantities available for distribution, (4) quantities distributed, and (5) ending monthly inventory. The instructions also require the States to submit the report no later than 15 calendar days after the end of the reporting month.

Our review of inventory reports submitted by State distributing agencies for the 6-month period ended March 31, 1979, showed that many States had failed to submit timely reports. During the period, 35 States and/or Territories had failed to submit the required reports within the required time frames for any month. One State submitted reports as much as 195 days late, and one State had not submitted a monthly report for 16 months. Additionally, 10 States and 2 Territories submitted reports at least 30 days late during 3 or more months, and no State reported on schedule for all 6 months included in our review.

Failure to submit required reports on time was not the only problem involving the monthly inventory reports. An FNS headquarters official told us that several States' reports had not been properly completed or had contained arithmetical errors. He said that some States failed to report beginning or ending inventories and some reported neither of the two. He cited Alaska as one example of a State that submits neither beginning nor ending inventories. In addition, we found that the Pennsylvania, Virginia,

and District of Columbia distributing agencies did not complete the beginning and ending inventory sections.

Limited monitoring of inventory levels by FNS regional offices

Promptly upon receiving the monthly reports from the State distributing agencies, each FNS regional office is required to

- review each report, checking accuracy, verifying shipments with reported receipts, and monitoring inventories;
- ensure that commodities were distributed only to eligible outlets; and
- notify FNS headquarters immediately of all discrepancies or improper activity reported on the form.

None of the four FNS regional offices we visited (Mid-Atlantic, Mountain Plains, Southwest, and Western) used the monthly reports to effectively monitor inventory levels. An official at the Western regional office told us that he did not interpret the inventory monitoring requirement to mean that the region should review the monthly report to control inventory levels. It was not until March 1980 that Western region officials, on their own initiative, began analyzing the reported section 416 commodity inventory levels to determine if distributing agencies had more than a 6-month supply of commodities on hand. Regional officials told us that the lack of inventory data by specific programs limited their analyses of inventory levels to statewide totals only.

In July 1980 Western region officials took their first formal action to resolve excess inventory levels based on their analyses of the monthly inventory reports. They told the California distributing agency to consider redonating quantities of rice, whole wheat flour, rolled oats, corn meal, bulgar, and rolled wheat.

Similarly, the Southwest regional office began only in February 1980 to analyze inventory levels in terms of the number of servings of each commodity on hand. However, the region had not yet used its analyses to identify excessive or short inventory levels.

The Mid-Atlantic regional office reportedly used the FNS-155 monthly report to control State inventory levels. However, we found that the Pennsylvania, Virginia, and District of Columbia distributing agencies did not complete the beginning and ending inventory sections of the report, indicating that the region had no means of controlling those distributing agencies' inventories. The region permitted the Pennsylvania distributing agency to submit its monthly reports without beginning or ending inventories because the State claimed to distribute commodities to recipient agencies as they are received, leaving no State inventory bal-

ances. However, we found that Pennsylvania had commodities on hand at the beginning and end of a month which had not been distributed to a recipient agency.

As discussed on page 37, the regional offices are also responsible for notifying FNS headquarters of errors or discrepancies in the inventory reports. However, the regions generally had not assumed that responsibility. To further complicate matters, FNS headquarters had no formalized followup procedures to encourage prompt and accurate reporting at the regional office level. The regional offices generally initiated followups with the States on reporting problems only after headquarters prompted them to do so, as the following examples illustrate.

--One State submitted its June 1979 report showing that it distributed certain commodities when, in fact, it had only moved the commodities from one warehouse to another. It was not until December 1979, after prompting from FNS headquarters, that the regional office notified the State that the transfer of commodities from one warehouse to another did not constitute a distribution and asked the State to resubmit the June report and to correct any errors affecting subsequent reports.

--Another State had not submitted a monthly inventory report during the 16-month period September 1978 through December 1979. Prompted by a November 1979 memorandum from FNS headquarters, the regional office notified the State of the report delinquency and asked it to report on a more timely basis in the future. In February 1980 the State submitted its first inventory report since August 1978, covering the month of September 1978.

Headquarters use of inventory reports is limited

Using the monthly inventory reports submitted by the States through the FNS regional offices, FNS headquarters prepares a consolidated monthly report entitled "Monthly Distribution of Donated Commodities." This report shows for each State and Territory the monthly commodity distribution made to eligible users, total distribution (weight and dollar value), and ending inventories on hand at State warehouses. No written instructions exist on how the headquarters report should be prepared or what it is to be used for.

An FNS official told us that the reason for requiring the States to submit the monthly inventory reports was to have a management tool FNS could use to monitor inventories. However, two problems limit the reporting form's usefulness. First, the report requires only that inventories at State-owned and -leased warehouses be reported; commodity inventories at recipient agencies are not reported. Second, FNS instructions do not require

States to report beginning and ending inventories by eligible program, such as the school lunch or elderly feeding programs.

In addition, we found that because of delays and difficulties in compiling the consolidated report, it is usually not issued until several months after the month to which it applies. FNS officials told us that no time frames are specified for issuing the consolidated inventory report. As shown by the following table, our analysis of five consolidated reports showed that none were prepared in a timely manner.

<u>Month for which report prepared</u>	<u>Date report prepared</u>	<u>Months late</u>
Feb. 1979	June 1979	4
Mar. 1979	Sept. 1979	6
Apr. 1979	Feb. 1980	10
May 1979	Apr. 1980 (note a)	11
June 1979	Mar. 1980 (note a)	9

a/The May report was prepared after the June report because of problems with some May data which had to be corrected.

FNS officials said that the consolidated inventory report could be of some use if it were issued timely. For example, during the Cuban refugee situation, USDA was interested in determining how much inventory was on hand at the State level in view of the possibility of distributing commodities to the refugees. However, such information was not available because a reasonably current consolidated report had not yet been prepared.

Although the monthly inventory reports are not submitted in a timely manner, are sometimes inaccurate or incomplete, and show only commodity inventories in State-owned or -leased facilities, FNS could be using them to monitor inventory levels for those States which own or lease storage facilities. For example, we reviewed reports submitted by Oklahoma and Louisiana for a 12-month period ending February 29, 1980, to determine whether the States had accumulated inventories exceeding their 1-year needs. Using data submitted by the States, we computed each State's monthly distribution rate. By dividing this average monthly distribution rate into the ending inventory on February 29, 1980, we determined the number of months' supply of each commodity in inventory. We considered commodities to be in excess supply when the supply in ending inventory was more than 12 months. We reviewed 16 commodities in Louisiana and found none exceeding a 12-month supply. For Oklahoma we reviewed 34 commodities and found 9 exceeding 1 year's needs. The following table shows the commodities we found to be in excess and the number of months by which the inventory exceeded 1 year's needs.

<u>Commodity</u>	<u>Number of months' supply</u>		<u>Value</u>
	<u>In inventory</u>	<u>Exceeding 1 year's needs</u>	
Canned orange juice	29	17	\$ 17,800
Canned apple juice	36	24	21,000
Canned green beans	13	1	6,000
Canned corn	20	8	30,200
Canned peaches	14	2	17,500
Peanut granules	14	2	5,400
Canned pears	159	147	208,000
Canned sweet potatoes (syrup packed)	253	241	100,300
Tomato catsup	32	20	89,300
Total			<u>\$495,500</u>

STATES' MONITORING OF RECIPIENT
AGENCIES IS INADEQUATE

In the absence of a formalized monitoring plan, States vary in the extent of monitoring they do to ensure accountability over the commodity donation programs for which they are responsible. Generally, the large numbers of recipient agencies, coupled with the lack of State staffs to make the reviews, limit the States' monitoring to only a small percentage of the recipient agencies each year. Additionally, the monitoring that is done is generally not in sufficient detail to identify (1) excess inventories, (2) reasons why such inventories have accumulated, or (3) inadequate controls over the receipt, distribution, and inventories of donated commodities. The shortcomings in the State agencies' monitoring are illustrated by the following examples.

--Before calendar year 1980 California performed only limited monitoring of recipient agencies. Some school districts had not been monitored for 10 years or more. Beginning in 1980 the State initiated a program for monitoring recipient agency inventory levels. This program consisted of (1) field reviews, during which visits were made to user locations to review various aspects of their operations, including whether reasonable quantities of commodities had been ordered, and (2) desk audits of user orders to assure that they were not overordering. The State planned to make field reviews on 100 of its 1,000 school districts during calendar year 1980, but as of July 8, 1980, they had made only 41.

--In January 1980 Texas' Agency on Aging was not monitoring recipient agencies participating in the elderly feeding program. A nutritionist who had been employed by the State to monitor the recipient agencies left the agency in the late summer of 1979 and was not replaced. Although the State requires recipient agencies to submit monthly

inventory reports, some had not always done so. Also, the State did not follow up with those failing to submit the reports. A State official told us that since the nutritionist left, they have had no one to file the monthly reports, much less follow up with projects not submitting the required reports. We noted that reports received after the nutritionist left were piled up in no particular order. Because the State did not monitor the recipient agencies, some had accumulated excess inventories.

--FNS Handbook 501 governing the administration of food distribution on Indian reservations requires distributing agencies to monitor and review local operations at least semiannually. The handbook also requires the distributing agency to employ sufficient staff to, among other things, review local agency operations. The Montana distributing agency had two staff members whose primary duties were to review local agency operations, but they spent most of their time administering the various food distribution programs for which the State was responsible. A State official told us that the State legislature had denied requests for more full-time employees. Similarly, the North Dakota distributing agency had done little monitoring of local agencies because it did not have enough staff. As in Montana, the State legislature denied requests for a full-time employee to do the monitoring. In both States inadequate controls existed over the receipt, distribution, and inventories of donated commodities.

CONCLUSIONS

As discussed in chapter 3, the commodity donation program could be more effective if the State distributing agencies did a better job of determining the types and quantities of commodities actually needed by the recipient agencies. Adoption of our recommendations in chapter 3 should minimize situations in which agencies are offered commodities in amounts exceeding their needs. In addition, other matters need the Secretary of Agriculture's attention if the program is to operate effectively.

A State's method of allocating commodities to recipient agencies can contribute to the accumulation of inventories exceeding needs. The existing method needs to be changed. Allocating commodities based on the number of meals served by a recipient agency does not consider the actual commodity needs of individual recipient agencies. Instead, State distributing agencies should distribute commodities based on needs data gathered from individual recipient agencies. This should minimize the chance of offering users larger quantities than they can effectively use within a reasonable time.

Some recipient agencies continued to accept commodities when their inventories on hand exceeded quantities to meet their needs for a reasonable time. Procedures are needed to reduce the

likelihood of this happening in the future. To minimize this problem, USDA should require recipient agencies to maintain and report to the State distributing agencies data showing beginning inventory, commodities received during the month, commodities used during the month, ending inventory, and the value of commodities used per prepared meal. The State could monitor this data and adjust quantities allocated to prevent the accumulation of excess commodity inventories.

For the commodity donation program to operate effectively, FNS and State distributing agencies must have a system for monitoring inventory levels and controls. No formalized plan existed setting forth how FNS or the States should go about analyzing inventory levels and controls, how the analyses should be used, or who should be responsible for such analyses. Such a plan is necessary if inventory monitoring is to be effective.

To accurately assess any State's commodity inventory levels, FNS should require States to report not only inventory levels on hand at State storage facilities but also those at storage facilities used by recipient agencies. It is also important for FNS to identify inventory levels by program to ensure that donated commodities are being effectively used. If implemented, both changes would enable FNS to effectively monitor State commodity inventories.

An integral part of any monitoring system is accurate and timely information. The States' failure to submit timely reports, coupled with the submission of some inaccurate reports, has severely limited the usefulness of any monitoring done by FNS.

In our opinion, an effective monitoring system would enable FNS and the State distributing agencies to (1) better determine needs, (2) identify States or recipient agencies having excess inventories of certain commodities or inadequate supplies to meet recipient agency needs, (3) identify reasons for short or excess inventories, and (4) help ensure that recipient agencies have adequate controls over the receipt, distribution, and inventories of donated commodities.

RECOMMENDATIONS TO THE SECRETARY OF AGRICULTURE

We recommend that to minimize situations in which State distributing and recipient agencies accumulate commodity inventories exceeding their needs and to improve overall effectiveness of the commodity donation program, the Secretary of Agriculture revise appropriate program regulations to require FNS to develop a formal monitoring system setting forth data to be maintained by State distributing and recipient agencies, how the data should be analyzed, and who is responsible for the analyses.

We recommend also that to provide for better accountability of donated commodities by recipient agencies, the Secretary require that all recipient agencies

- maintain perpetual book inventories;
- take periodic physical inventories and submit the results to the State along with copies of the source documents used;
- explain any differences between physical inventory counts and perpetual inventory balances; and
- develop and report monthly to State distributing agencies data showing, at a minimum, (1) beginning inventory, (2) commodities received during the month, (3) commodities used during the month, (4) ending inventory, and (5) the value of commodities used per meal prepared.

Further, we recommend that the Secretary direct FNS to develop a monitoring plan to be followed by State distributing agencies in monitoring commodity inventory levels at recipient agencies. The plan should require that, at a minimum, the State agencies

- analyze monthly inventory reports submitted by the recipient agencies to identify excess and/or low inventory levels, poor inventory controls, and ineffective use of commodities;
- identify causes of the problems, recommend positive action to alleviate them, and follow up to determine that corrective action is taken; and
- visit a specified number of recipient agencies each year to take a physical inventory and review inventory control procedures.

We recommend also that the Secretary direct FNS to fully evaluate commodity inventory levels at the State distributing agencies by developing a monitoring plan that

- requires States to continue to report commodity inventory levels monthly but to include inventories at the recipient agency levels as well as inventory levels in State-owned or -leased storage facilities, and to report inventory levels by program;
- identifies the monitoring responsibilities of FNS headquarters and its regional offices;

- specifies how those involved in monitoring should analyze the State inventory data and establishes reasonable time frames for completing the analyses; and
- specifies actions to be taken when FNS identifies problems with untimely, inaccurate, or incomplete reporting, excessive inventories, or lack of adequate inventory controls.

We recommend that to further enhance the effectiveness of the commodity donation program, the Secretary direct FNS to require that States develop procedures for distributing commodities to recipient agencies based on reported needs rather than allocating commodities based on the number of meals served.

USDA COMMENTS

In commenting on a draft of this report (see app. IV), USDA cited actions taken and proposed to increase the effectiveness of FNS and States' monitoring activities. USDA said that a more formalized system of management evaluation had been developed for use by FNS regional offices and State distributing agencies and new regulations requiring the management evaluation system were in process. According to USDA, emphasis will be on maintaining constant communication between the regional offices and State distributing agencies regarding problems, corrective action, followup, and overall program improvement.

Further, USDA said that (1) FNS' Washington staff is now assisting regional offices in making reviews of State distributing agencies and will obtain and evaluate management evaluation reports, (2) each regional office has been provided an evaluation schedule for fiscal year 1981 calling for reviews of each State distributing agency, and (3) 'five critical areas have been identified for emphasis by FNS regional offices' evaluations. These are processing activities, warehousing and food storage practices, use of revolving funds, elderly feeding programs, and the food distribution program on Indian reservations.

CHAPTER 5

DELIVERY ASPECTS OF THE COMMODITY

DONATION PROGRAM CAN BE IMPROVED

To effectively use donated commodities, recipient agencies must receive them when needed. The commodity donation program's effectiveness has been diminished because, at times, commodities are

- received so late in the school year that they cannot prudently be used before year's end,
- shipped after required shipping periods, and
- received without advance notice of delivery.

As a result, users may have to (1) purchase commodities locally when prices are not favorable and (2) incur increased storage and handling costs.

To encourage vendors to ship within required shipping periods, USDA has established monetary penalties that are assessed daily beyond the end of the missed shipping period. However, vendors that do not ship within required shipping periods can have their penalty assessments reduced. USDA needs to improve its handling of penalty reduction cases because too frequently, USDA personnel either do not sufficiently review the validity of the vendors' reasons for requesting penalty reductions or do not document their reviews.

Certain commodities, such as poultry and grain products, are procured on a free-on-board (FOB) destination basis, while most other products are bought on an FOB-origin basis. Other Government agencies, such as the Veterans Administration (VA), procure these same types of commodities with like origin and delivery points on an FOB-destination basis at considerable savings. USDA should consider the increased use of FOB-destination procurement.

In addition, USDA shipping instructions to deliver commodities to State distributing agencies or food processors can result in excessive transportation charges. The States and FNS regional offices are not doing all they could to assure that the most economical and efficient delivery methods are selected.

DELIVERY PROBLEMS LIMIT PROGRAM EFFECTIVENESS

Because the commodity donation program's effectiveness has been limited by shipping and delivery problems,

- distributing and recipient agencies have incurred increased storage and handling costs,

- distributing agencies have incurred charges for detaining rail freight cars beyond the allowable time for unloading,
- recipient agencies have had to purchase food items locally which they normally receive through commodity donation, and
- the probability of spoilage increases.

These problems and their effects are discussed in the following sections.

Late receipt

According to distributing agencies in Missouri, Montana, and Pennsylvania, donated commodities for school programs must be received no later than the end of March to be used effectively. The California distributing agency said that commodities were needed by March 1 to assure their use by school districts in the same year. All four distributing agencies had received commodities well past the times they believed recipients could effectively use them. For example:

- During the 1978-79 school year, Missouri received from 40 to 51 percent of its commodity entitlements of frozen cut-up chicken, vegetarian beans, roasted peanuts, catsup, and canned tomatoes after March 31, 1979. The State also received its entire 1978-79 school year entitlement of mozzarella cheese in April and May 1979. The receipt of commodities in April and May can require school districts to incur commodity storage costs over the summer months. For example, a school district official estimated that the district had to store about 7,550 cases of commodities in commercial storage over the summer because they had been received in April and May 1979. We estimated that the district incurred at least \$2,950 in additional storage costs.
- Between March and July 1979, the California distributing agency received at least 25 percent of its commodity entitlements for 34 different commodities. These commodities were valued at \$15.4 million. Late shipments caused some school districts to refuse otherwise acceptable commodities. For example, one food service director told us that the State's February 1980 offering came too late in the year for the district to work the commodities into its menu plan. As a result, the district refused commodities valued at \$105,100 even though it could have used the turkey rolls valued at \$15,900 and the whole turkeys valued at \$20,300 if it had known earlier that these commodities were available.

--In May 1978 Montana received 1,750 cases of frozen turkey rolls and 1,120 cases of canned orange juice. We estimated that the State paid about \$2,300 to store these commodities over the summer. On May 9, 1979, Montana received 1,200 cases of canned orange juice. Although the distributing agency shipped the orange juice to schools on May 10, 11, and 14, it is doubtful that the schools were able to make effective use of it before the school year ended.

--From April 1 to June 30, 1979, Pennsylvania received 15.6 million pounds of donated food. This was 20 percent of the total amount received for the 12-month period July 1978 to June 1979. For nonfat dry milk, pineapple juice, rice, spaghetti, and vegetable shortening, the State received 100 percent of its commodity entitlement after March 31, 1979.

Receipt of commodities late in the school year cannot be attributed solely to FNS purchasing and shipping practices. Some shipments were received late because vendors did not ship within the agreed shipping period. Other shipments were received late because the States ordered commodities for shipment in April and May. Still other shipments were received late because of transportation problems beyond FNS' control.

Missed shipping periods and long delivery times

USDA purchase contracts for the commodity donation program require that the commodities be shipped within a specified period, usually 2 weeks. In many cases, vendors had not shipped commodities within required shipping periods; in one instance, shipping periods were missed by an average of 69 days.

The method used to move commodities from the vendor to the State distributing agencies and, ultimately, to the recipient agencies can further hinder commodity availability. For example, USDA told us (see app. IV) that in many cases distribution programs use rail cars as "traveling warehouses" where part of the commodity is unloaded and the car then moves to another location. According to USDA, this delays a commodity reaching its final destination. In addition, USDA said that many railroads have either closed sections of unprofitable track or reduced the frequency of switching so that commodities spend greater amounts of time in transit.

For almost half of the 1978-79 school year shipments we reviewed, the vendors did not timely ship commodities to Missouri, Montana, and Texas.

<u>State</u>	<u>Number of shipments</u>		<u>Percent</u>
	<u>Reviewed (note a)</u>	<u>Not made within required shipping period</u>	
Missouri	419	171	41
Montana	91	34	37
Texas	<u>593</u>	<u>296</u>	50
Total	<u>1,103</u>	<u>501</u>	45

a/For Missouri and Montana, we reviewed only commodity shipments for the school lunch program for which shipping information was available. For Texas, we reviewed the shipments for five commodities which we selected based on discussions with a State official.

Some examples of commodities consistently not being shipped until past the end of the required shipping periods are as follows.

<u>Commodity</u>	<u>Number of late shipments</u>		<u>Average days late</u>	
	<u>Missouri</u>	<u>Texas</u>	<u>Missouri</u>	<u>Texas</u>
Mozzarella cheese	8	37	60	69
Butter	10	84	58	11
French fries	28	121	27	18

Vendors not shipping commodities within required shipping periods were also a major concern in Pennsylvania and California. The Pennsylvania distributing agency reviewed its commodity orders for the period July 1, 1979, through January 31, 1980, and found that 444, or 41 percent, of the 1,072 shipments for which sufficient information was available were not made within the required shipping period. Our review of 110 commodity shipments for 13 selected commodities received by California after March 1, 1980, showed that 37, or 34 percent, were shipped after the required shipping period.

When vendors did not ship within required shipping periods, they needed from 1 to 161 days past the end of the shipping period to ship their commodities. The following table shows the percentage of shipments that were not shipped until at least 21 days after the required shipping period.

<u>State</u>	<u>Late shipments</u>	<u>Number of shipments at least 21 days late</u>	<u>Percent</u>
California	37	6	16
Missouri	171	66	39
Montana	34	9	26
Pennsylvania	444	169	38
Texas	<u>296</u>	<u>101</u>	34
Total	<u>982</u>	<u>351</u>	36

The vendors' shipping shortcomings and the distributing agencies' delivery uncertainties tend to disrupt the normal distribution of commodities and adversely affect commodity recipients. For example:

- In 1978 Missouri requisitioned sweet potatoes for the first half of November. Limited preference data at the distributing agency showed this commodity was not a highly preferred item. According to a State official, schools like to serve sweet potatoes at Thanksgiving and Christmas and rely on the donation program to fill their needs. However, the vendor did not ship any portion of the commodity until mid-December 1978, and Missouri received it in January and February 1979. Missouri also requested a shipment of butter during the first half of January 1979. However, no butter was shipped before February 8, and much of the butter was not received until April. A State official told us that in both instances school districts had to use their own funds to purchase items that USDA usually supplied.
- In mid-March 1980 California received shipments of pork because vendors had missed the required shipping period and the commodity had been delayed in transit. A State official told us that these late deliveries resulted in (1) poor public relations with school district officials because about half the State's school districts did not receive pork in the 1979-80 school year and (2) excess storage costs of about \$16,100 from March to July 1980.
- State officials in Montana, Pennsylvania, and Texas also said that late shipments of donated commodities caused school districts to purchase similar or like items to satisfy menu requirements. Timely shipment and delivery would have allowed school districts to make better use of their own funds to purchase needed non-USDA food items.

No advance notice of shipments

Distributing agencies also experienced difficulty in receiving advance notice of shipments from vendors. State officials claim that when advance notice is received, they can distribute commodities sooner because they can prepare in advance for unloading, storing, and shipping. When advance notice is not received, States incur unnecessary storage and handling costs and risk spoilage of perishable commodities.

ASCS instructions require that vendors notify either the ASCS Kansas City Commodity Office and/or the State when they ship a commodity. Vendors shipping by rail are to complete a preprinted notice of shipment indicating, among other things, the rail car number and the date shipped. They forward the information to the Kansas City Commodity Office which, in turn, forwards it to the State distributing agencies. Vendors shipping by truck are to notify both the Kansas City Commodity Office and the distributing agency as far in advance of delivery as possible. In addition, the Commodity Office maintains a 24-hour telephone system for processors and/or shippers to call in advance notice of shipment. According to USDA (see app. IV), this system has improved the advance notice of shipment process.

For most commodity shipments in Missouri and Montana, the distributing agencies had received advance notice. However, the following table shows that for 22 percent of their shipments, advance notice was received late or not at all.

<u>State</u>	<u>Shipments</u>		
	<u>Reviewed</u>	<u>Received with late or no advance notification</u>	<u>Percent</u>
Missouri (note a)	96	15	16
Montana (note b)	92	26	28
Total	<u>188</u>	<u>41</u>	22

a/Includes all shipments of applesauce, ground beef, frozen corn, and french fries for school year 1978-79.

b/Includes all commodity shipments for school year 1978-79, for which data on notice of shipment was available.

The Texas distributing agency also received 40 shipments in November and December 1979 without proper notice.

The following examples illustrate the effects of States not receiving advance notice of shipments.

--During the 1977-78 school year, Missouri distributed commodities carside, which required that recipient agencies be present to pick up their allocated shares when the commodities arrived. Without advance notice of shipment, the

State could not notify recipients to pick up their commodities until after the rail car arrived. At times the State incurred charges for holding rail cars beyond the time allowed for unloading so that recipients could be given adequate time to arrange for pickup.

--A Montana State official said that advance notices of shipments allow them to maximize shipments to schools and minimize storage and handling costs. On March 26, 1979, the State received a shipment of macaroni without any advance notice. According to a State official, if the State had known in advance approximately when the shipment would arrive, it could have delayed an impending shipment of commodities to schools. However, it distributed the other foods and temporarily stored the macaroni in a warehouse at a \$266 storage and handling cost.

--A Texas distributing agency official said that failure to receive an advance notice of shipment presents problems for the two State distribution facilities with no freezer storage. When frozen commodities are expected, the State notifies the recipient agencies when to be on location to unload their portions. If vendors fail to notify the State of an impending shipment, it does not know when to expect delivery. If the shipment arrives by rail, the State may have to pay demurrage on the refrigerated car until all users are notified and the car unloaded. According to a State official, shipments received by truck present another problem. Trucks are unloaded immediately, and the State has to arrange quickly for temporary storage or risk spoilage of perishables.

PRACTICES FOR REDUCING ASSESSED PENALTIES FOR LATE SHIPMENTS NEED STRENGTHENING

As an incentive for vendors to ship commodities within required shipping periods, USDA established that shipments made beyond required shipping periods are subject to monetary penalties (10 cents per hundredweight per day effective July 1980 ^{1/}) which are deducted from contract proceeds due the vendor. Vendors may appeal their assessed penalties for late shipments and the penalties may be reduced.

USDA procedures state that the vendor shall not be liable for liquidated damages due to causes beyond the control and without the fault or negligence of the vendor. The vendor is required to furnish documents to substantiate the inability to perform. According to USDA officials, inability to supply timely transportation

^{1/}Before July 1980, the penalty rate was 5 cents per hundredweight per day.

is considered a justifiable cause to excuse liquidated damages, providing acceptable documentation is provided.

During fiscal year 1979 USDA refunded \$686,500, or about 31 percent, of the \$2.2 million in penalties assessed against vendors who failed to ship commodities within shipping periods specified in their contracts. As of May 31, 1980, USDA had refunded about \$224,119 of the \$1.2 million in assessed penalties for fiscal year 1980.

Because USDA personnel are either not sufficiently reviewing the appeals or not adequately documenting their reviews, or both, USDA does not have assurances that all reductions in assessed penalties are justified. This problem results from several factors, namely (1) low priority placed on vendor appeal verifications by management, (2) lack of emphasis on obtaining detailed support for late shipment justifications, (3) lack of ASCS guidance on what constitutes a thorough review of vendors' claims, and (4) lack of supervisory review of the work performed in approving vendors' appeals.

Procedures for handling vendor appeals

The Processed Products Branch of the Inventory Management Division of ASCS' Kansas City Commodity Office is authorized to grant penalty assessment reductions on items FSQS procures where a transportation or weather problem is cited as the reason for late shipment. For other problems, the vendor's appeal is handled by FSQS' contracting division in Washington, D.C. For ASCS-procured items, the responsible ASCS purchasing units at the Kansas City Commodity Office resolve all vendor appeals for reduced penalties.

Commodity Office procedures specify that when a vendor appeals assessed charges for late shipment, the claim be assigned to a marketing specialist who is to perform a prompt, thorough review and subsequently determine either to disapprove or approve all or part of the vendor's claim. The Commodity Office's procedures also provide a means (the Report of Late Shipment and NLT 1/Date Determination) by which personnel, such as marketing specialists, can properly document and review a vendor's appeal. Depending on the ASCS unit handling the appeal, the Commodity Office's Traffic Management Division may be asked to contact the carriers to certify the rail or truck equipment shortages.

Insufficient review and inadequate documentation of vendor appeals

To evaluate the adequacy of ASCS' review of vendor appeals, we reviewed 16 late shipment appeals in which \$201,000 of the

1/NLT stands for no later than.

assessed \$287,000 in penalties was refunded to the vendors. In many of these cases, the ASCS specialists either had not followed up to the extent necessary to make a satisfactory decision on penalty reductions or had not adequately documented their efforts, or both. For example:

--In 8 of the 16 cases, the specialists had not determined that the commodities had been ready for shipment by the original contract shipping dates.

--In five cases, no evidence existed that the specialists had verified with the carriers the vendors' claims that lack of available transportation prevented timely fulfillment of the contracts. In three other cases, the specialists had initially followed up with the carriers but later granted additional reduced penalties without subsequent followup.

--In 12 cases, no evidence existed that the specialists had determined when the vendors had requested the necessary transportation.

The following examples illustrate these cases.

1. Vendor A contracted to deliver 110,000 cases of canned applesauce within six 2-week shipping periods beginning November 1, 1978, and ending February 28, 1979. Because the vendor did not ship the required quantities in the designated shipping periods, ASCS penalized the vendor about \$36,500. However, the entire penalty amount was refunded because the vendor claimed that the carrier was unable to provide necessary rail cars.

On a December 14, 1978, Report of Late Shipment and NLT Date Determination prepared by ASCS, "Rail cars late" was the reason shown for the missed shipping periods. The file did not contain any written documentation from the carrier explaining why the necessary rail cars could not be provided to the vendor.

ASCS procedures provide an example of how to maintain a chronological listing of contacts with vendors and carriers regarding late shipments and the results of such contacts; however, no such listing was prepared in this case.

We found no evidence that ASCS had reviewed USDA Certificate of Quality and Condition reports, which are required prior to each shipment, for the canned applesauce delivered under this contract. However, some of the applesauce was not inspected until well past the end of the last required shipping period. For example, one certificate report showed that a total of 2,750 cases of applesauce had been inspected on December 19, 1978, January 8, 1979, and January 12, 1979, well beyond the required shipping date of December 15, 1978. An ASCS official agreed that the use of these reports in conjunction with the required shipping periods could indicate that the vendor was experiencing production problems.

2. Vendor B contracted to deliver 386,000 pounds of plain macaroni by October 15, 1978, and another 166,500 pounds by October 30, 1978. ASCS penalized the vendor \$3,023 because it did not ship the required quantities on time. However, the entire penalty was refunded because of the vendor's claim of a railcar shortage during the times of the required shipping dates. Reports of Late Shipment and NLT Date Determination contained no evidence that ASCS followed up with the carrier to verify that a shortage existed. In addition, the contract file contained no information on (1) when the vendor ordered the rail cars, (2) the number of cars ordered, or (3) the number of rail cars the vendor shipped commercially during the period it was to fulfill its USDA contract.

Our review of commodity inspection certificates showed that USDA had not inspected 140,100 pounds of macaroni until January and February 1979. Again, in our opinion, this indicates that the vendor might have experienced production problems. As in the above example, however, ASCS had not prepared a chronological listing of contacts, including the results of such contacts, between the vendor and carrier.

An ASCS official agreed that in this case the supporting documentation did not justify the reduced penalty. In a November 29, 1978, letter to the vendor, ASCS said that in the future the vendor would be required to supply ASCS with the (1) date cars were ordered, including number of cars ordered, (2) date cars were received, including number of cars received, (3) date cars were to be loaded, (4) date cars actually were loaded, and (5) number of cars shipped commercially during the period.

ASCS officials generally agreed that improvements were needed in reviewing and documenting the legitimacy of vendor appeals on late shipment penalties. They attributed the lack of adequate documentation and followup to insufficient personnel and time to obtain necessary documentation from carriers and vendors. Low priority is placed on late shipment followup because during the regular program year, emphasis is placed on processing shipping orders. In addition, the officials believed that (1) as a result of their day-to-day contacts with vendors and carriers, the employees working on the penalty appeal cases had a general knowledge of vendor and rail transportation problems and (2) they probably relied on that knowledge to decide whether or not to approve a vendor's appeal.

The above reasons may have contributed to the lack of documentation regarding USDA's analyses of vendors' reasons for not shipping within required shipping periods.

In commenting on our draft report (see app. IV), USDA said that as recently as June 20, 1980, all ASCS food suppliers had been notified of the problems and hardships that late shipments cause recipients. The suppliers were also reminded of contract provisions requiring compliance with deliveries and ASCS options available to deal with those who fail to perform. USDA also

pointed to the July 1980 raise in penalty rates (see p. 51) as further evidence of its commitment for having shipments made timely. ASCS officials had varying opinions, however, of the potential effectiveness that the increased rate would have in actually reducing late shipments.

FNS DELIVERY REQUIREMENTS CAN
INCREASE USDA TRANSPORTATION COSTS

FNS shipping instructions to deliver commodities to State distributing agencies can result in unnecessarily high USDA transportation costs because some States require "rail car only" delivery and do not give the opportunity to ship by truck while others require "truck only." This prohibits USDA from providing maximum flexibility regarding the mode of transportation. FNS has required that its regional offices stress to distributing agencies that greater flexibility be adopted in the way they accept delivery on some commodities. In addition, the distributing agencies are now to provide written justification to the appropriate FNS regional office whenever they desire rail-only deliveries.

FNS instructions allow shipments by either railroad or truck so that the transportation mode selected will result in the lowest transportation costs. However, distributing agencies may restrict the method of shipment when necessary to their program operations. If the distributing agency selects a specific transportation mode, an explanation of the need for the restriction must be made and be approved by the FNS regional office.

Between June 13, 1977, and February 4, 1980, at least 152 requests had been submitted to the Kansas City Commodity Office for truck-only delivery into certain locations. On its own initiative, the Commodity Office determined that for at least 25 of these requests (16 percent), the States could have accepted rail shipment. In 8 of these 25 cases, the States eventually agreed to accept the rail services even though they had primarily indicated truck-only delivery. Five examples follow in which ASCS determined that railroad transportation was available. Because the State distributing agencies designated truck-only delivery, this method of transportation eventually was used.

<u>Commodity</u>	<u>Destination</u>	<u>Estimated savings if sent by railroad</u>
Beans, dry--in tomato sauce	South Dakota	\$1,902
Tomatoes	South Dakota	1,207
Peanut butter	South Dakota	1,193
Dry milk	Michigan	300
Peaches	New Jersey	<u>1,788</u>
Total		<u>\$6,390</u>

ASCS officials said they had notified FNS regional offices of the potential cost savings, but because they received no replies to their wires, the shipments were made by truck.

At our request, Commodity Office personnel developed the following additional examples of cases in which USDA may have needlessly paid more in transportation costs because States requested truck-only shipments. In all six cases, ASCS records showed that railroad transportation was available.

<u>Commodity(s)</u>	<u>Origin</u>	<u>Desti- nation</u>	<u>Estimated savings if sent by railroad</u>
Nonfat dry milk	Texas	Florida	\$ 187
Nonfat dry milk	Pennsylvania	New York	54
Tomato paste	California	New York	1,686
Fruit cocktail, dry beans, applesauce	Kansas	Minnesota	607
Dry beans, rolled oats, apple juice	Kansas	Minnesota	493
Canned chicken, dry beans, pears, egg mix	Kansas	Kansas	<u>253</u>
Total			<u>\$3,280</u>

In June 1980 FNS sent a memorandum to its regions which stressed that States be encouraged to adopt greater flexibility in the way they take delivery on certain commodities. Also, the FNS regions were asked to have all their States update their destination data sheets. The memorandum added that the distributing agencies were to provide written justification for continued use of "rail only" deliveries. The regions were to advise headquarters within 3 weeks on State distributing agencies which changed to "rail or truck" delivery.

INCREASED USE OF FOB-DESTINATION CONTRACTS
IN PURCHASING COMMODITIES IS FEASIBLE

Commodities for the various donation programs are either purchased at a price which includes transportation costs of delivery to domestic destinations (FOB-destination contracts) or USDA takes title to the commodity at the contractor's warehouse or plant and specifies the method of shipment (FOB-origin contracts). Fruits, vegetables, and dairy products have been purchased on an FOB-origin basis with no consideration as to whether they could be procured more economically on a destination basis. USDA could save transportation costs by purchasing some of these commodities on a destination basis.

Past studies of FOB-origin versus
FOB-destination purchases

At various times in the past, USDA has considered changing some commodity purchases from an FOB-origin to an FOB-destination basis.

In January 1972 the Director of the Minneapolis ASCS Commodity Office recommended that some types of nonfat dry milk be purchased on an FOB-destination basis. In May 1972 this proposal was dropped because of widespread dairy industry opposition. Industry officials opposed the change, citing labor problems, lowered profit margins, and penalties to producers with prior commercial commitments.

In a November 1979 memo, the Kansas City Commodity Office Director suggested to the ASCS Deputy Administrator, Commodity Operations, that mozzarella cheese be procured on an FOB-destination basis. The Director said that this change would solve bid evaluation problems, increase efficiency in contract awards and payments, and permit offerors to compete with their own transportation equipment or arrangements. The Director also said that the Commodity Office had surveyed nine regular mozzarella cheese suppliers and found that seven either had indicated a preference for the destination basis or had no preference one way or another.

ASCS sometimes bought mozzarella cheese on an FOB-destination basis. Kansas City Commodity Office officials told us that this practice has probably resulted in lower transportation costs of an additional \$1.12 to \$3.15 per hundredweight. The following examples show ASCS' cost savings when it has, in effect, purchased mozzarella cheese on a destination rather than an origin basis.

<u>Origin</u>	<u>Destination</u>	<u>Quantity (pounds)</u>	<u>Delivered cost</u>		<u>Savings</u>
			<u>FOB origin</u>	<u>FOB desti- nation</u>	
Newman Grove, NE	Salina, KS	40,000	\$24,660	\$23,400	\$1,260
Hebron, NE	Salina, KS	40,000	24,800	24,000	800
Green Bay, WI	Springfield, IL	40,000	24,171	23,700	471
Total					<u>\$2,531</u>

During February and April 1981, USDA purchased about 4.65 million pounds of mozzarella cheese on an FOB-destination basis. An ASCS official told us that because of weak dairy prices, USDA was not able to assess the cost savings of these purchases.

Cost savings afforded by
FOB-destination purchases

The Veterans Administration buys some of the same commodities for its hospitals that USDA buys for its commodity donation

program. Deliveries are made every 2 weeks for a 2- to 3-month period to warehouses located in Bell, California; Hines, Illinois; and Summerville, New Jersey. According to a VA official, VA buys canned fruits and vegetables on an FOB-destination basis because

- the contractor retains responsibility for the commodity until delivery;
- VA does not need a traffic department to evaluate freight rates;
- procurement can be carried out with fewer personnel; and
- contractors, if necessary, can combine agency shipments with commercial deliveries and make stops at warehouses as applicable.

To determine if it would be financially advantageous for USDA to purchase some fruits and/or vegetables on an FOB-destination basis, we selected and compared USDA and VA delivered costs (purchase price plus transportation costs) for 10 shipments made between July 1979 and March 1980. To make the comparisons, we selected actual shipments of the same commodities made from the same origin to the same general destination within the same time period. We obtained the delivered costs of the VA commodities from VA. From USDA, we obtained the freight rates in effect when the shipments were made, applied them to the quantities involved, and added in the commodity purchase price to arrive at a figure that could be compared with VA's delivered cost. Any known cost differences caused by product specifications were also considered. A responsible FSQS official concurred in our approach.

As shown in the following table, the comparison showed that for 7 of the 10 shipments, USDA could have saved a total of \$6,810 in transportation costs had the commodities been purchased on an FOB-destination basis.

<u>Shipment</u>	<u>Commodity</u> (note a)	<u>Origin</u>	<u>Destination</u>	<u>Savings</u> (note b)
1	Peaches	Modesto, CA	New Jersey	\$ 613
2	Peaches	Modesto, CA	Los Angeles	488
3	Peaches	Modesto, CA	New Jersey	1,587
4	Peaches	Modesto, CA	Los Angeles	1,415
5	Tomatoes	Modesto, CA	Chicago	2,131
6	Tomatoes	Modesto, CA	New Jersey	235
7	Applesauce	Belgium, WI	Chicago	341
Total				<u>\$6,810</u>

a/Canned goods.

b/If bought on FOB-destination basis.

For the remaining three shipments, USDA transportation costs would have been increased by \$3,403 had FOB-destination contracts been used, as shown in the following table.

<u>Shipment</u>	<u>Commodity</u> (note a)	<u>Origin</u>	<u>Destination</u>	<u>Additional</u> <u>cost</u> (note b)
8	Peaches	Sunnyside, WA	New Jersey	\$1,343
9	Green beans	Salem/Staton, OR	Los Angeles	1,370
10	Applesauce	Winchester, VA	New Jersey	<u>690</u>
Total				<u>\$3,403</u>

a/Canned goods.

b/If bought on FOB-destination basis.

We contacted seven regular suppliers of fruits and vegetables to USDA under the commodity donation program. All seven said they would sell fruits and/or vegetables to USDA on an FOB-destination basis if that was the way USDA wanted to purchase the commodities. Four of the seven suppliers said that they were then selling commodities to other Federal agencies (VA and the Defense Logistics Agency) on an FOB-destination basis. Although specific cost figures were not provided, two said that transportation costs (total commodity costs for USDA) could increase if they sold to USDA on an FOB-destination basis; five said they would probably remain the same. In June 1980 FSQS headquarters officials told us that they were going to try FOB-destination procurements for the needy family program.

CONCLUSIONS

The donated commodity program's efficiency would be improved if food items were delivered to recipients in time for use before the end of the school year, vendors shipped contracted quantities within required shipping periods, and States received advance notice before shipments were received. These improvements would provide better program efficiency because recipient agencies would not have to repeatedly serve some food items to use inventories by the end of the school year, they would be in a better position to purchase commodities locally when prices may be more favorable, and their storage and handling costs would be reduced.

ASCS needs to strengthen its practices and procedures for deciding when to reduce penalties assessed for vendors' failure to ship commodities within designated shipping periods. When a vendor appeals an assessed penalty, ASCS needs to verify that the reasons cited are valid, adequately document its verification efforts, and pursue all leads to assure that factors other than those cited by the vendor did not prevent contract performance.

ASCS procedures provide for vendors to notify either the Kansas City Commodity Office or the State distributing agencies when they ship a commodity, and in most cases State distributing agencies are receiving advance notifications of shipment. However, ASCS needs to stress to all vendors the importance of notifying States when commodities have been shipped.

FNS regional offices need to improve their monitoring of State distributing agency requests for truck deliveries into their States. These special requests can and in some cases did result in unjustified additional transportation costs for ASCS. In June 1980 FNS requested that all States update their delivery requirements and that the FNS regional offices work with their States to assure that they allow for greater flexibility in choosing the methods by which they will accept commodity deliveries.

USDA needs to consider increased use of FOB-destination procurement. Although poultry and grain products are already procured on a destination basis, other products are procured on an FOB-origin basis with no consideration being given to destination procurement. Other Government agencies procure these same types of commodities on an FOB-destination basis at a savings. All seven vendors we interviewed indicated that they would be willing to sell on a destination basis.

RECOMMENDATIONS TO THE SECRETARY OF AGRICULTURE

We recommend that to improve delivery aspects of the commodity donation program and overall program efficiency, the Secretary of Agriculture:

- Revise USDA procedures to require that shippers provide specific written documentation regarding their inability to supply needed transportation and dates when the vendor requested transportation.
- Emphasize to ASCS the need to completely review vendor appeal cases and to sufficiently document its actions.
- Monitor FNS regional office efforts in getting States to adopt greater flexibility in the way they take delivery on commodities and, if necessary, require States to annually update their delivery capabilities.
- Monitor the FOB-destination procurement of fruits and vegetables for the needy family program and, where cost-justified, expand such procurement of fruits and vegetables to other programs receiving donated commodities.

CHAPTER 6

CASH, COMMODITIES, OR LETTER OF CREDIT?

Because of the shortcomings in USDA's commodity donation program, some have suggested replacing it with a cash or letter-of-credit system. The cash or letter-of-credit system would allow individual users to purchase desired food items locally with cash or credit vouchers provided by USDA.

Proponents of these alternative systems believe that purchasing all commodities locally would probably be the most effective way of remedying the current commodity program's problems. Those opposed say that the Secretary's ability to aid producers during surplus periods would be diminished and that opportunities to circumvent the systems and the potential for fraud and abuse would be far greater than under the current commodity program. USDA has done little to adequately determine what revised measures could be undertaken to improve program operations. Studies done by USDA and others have fallen somewhat short of determining the real effects of a commodity donation program based on either a cash or letter-of-credit system.

PROPOSED ALTERNATIVES TO THE CURRENT SYSTEM

Two proposed alternatives to the current donation program are (1) cash in lieu of commodities and (2) commodity letters of credit.

Currently, Kansas is the only State which receives cash in lieu of commodities. ^{1/} However, under a total cash system, all States would receive cash in lieu of commodities. The amount of cash received would be based on the number of meals served multiplied by an annual rate of reimbursement price per meal. This would be adjusted annually on the basis of a price-per-meal index for food used in schools and institutions. This is basically the approach currently used in establishing State commodity entitlements. Adoption of an all-cash system would eliminate direct commodity donations by USDA. Currently, USDA supplies about 20 percent of all commodities used by the States annually. Schools also receive cash payments as reimbursements for some of their costs and at other times when insufficient commodities are available for distribution.

^{1/}Public Law 94-105 (42 U.S.C. 1765), which added section 16 to the National School Lunch Act, provides that States which had phased out their commodity programs before June 30, 1974, were eligible to receive all cash in lieu of commodities. Kansas was the only State that qualified.

Under a commodity letter-of-credit system, the States would be issued a general letter of credit for the commodity program in an amount equal to the legally mandated per-meal commodity value. During the period July 1, 1979, through June 30, 1980, this equaled 15.75 cents for each lunch served. USDA would then, on a periodic basis--probably monthly--make advance program payments to the States. These payments would be deposited in a bank or other financial institution where they would automatically be available for payment to vendors.

States could issue commodity letters of credit to school districts according to USDA guidelines. Each letter of credit could identify

- specific commodities;
- funding authority for purchase (sections 6, 32, or 416);
- quantity to be purchased, including quality or grade;
- time of purchase; and
- a dollar ceiling for the purchase.

In some projects under the special supplemental food program which was designed especially for women, infants, and children, a system like the proposed commodity letter of credit is used. In these projects, the eligible recipient is given a voucher which identifies the specific product(s) to be purchased, the quantity, a maximum price that can be paid, and the date by which the voucher must be used. The recipient gives the voucher to the grocery store as payment and the store fills in the purchase amount. The store then deposits the voucher in its bank account.

FEDERAL PROGRAMS HAVING CASH OPTION

Two Federal feeding programs provide the option of receiving cash in lieu of commodities. Beginning in fiscal year 1978, agencies participating in the elderly feeding program were given the option of receiving cash in place of donated commodities or receiving a combination of cash and commodities. In fiscal year 1980, 28 State agencies elected to receive cash, 23 chose a cash/commodities mix, and 3 chose all commodities.

The option of cash in lieu of commodities is authorized for the Child Care Food Program under section 17 of the National School Lunch Act. Under this program, meal service is provided to children in child care institutions, such as child care centers and family and group day care homes. Regulations require the State to survey the institutions to determine their preference for cash or commodities instead of making a decision itself.

USDA has studied the feasibility of a cash system for the school lunch program. However, the letter-of-credit or voucher

system has not been studied in detail. In addition, the Congress has been concerned about the issue of cash versus commodities for schools and in Public Law 95-166 (42 U.S.C. 1769, Nov. 10, 1977) directed that USDA test cash in lieu of commodities for the school lunch program using pilot projects.

CASH VERSUS COMMODITIES STUDIES

As directed by Public Law 95-166, FNS initiated a special project to collect data from eight pilot school districts and two control districts to analyze the effects on the schools' child nutrition programs when cash was substituted for donated commodities. Kansas State University, funded by the National Frozen Food Association, also made a study using data from these pilot projects. Our January 1977 report (see p. 13) also addressed this issue.

USDA study

In response to USDA's notice in the Federal Register for school districts interested in participating in the study, 37 districts volunteered. Eight school districts (Oakland, California; Boise, Idaho; Riceville, Iowa; Jonesboro, Arkansas; Chipley, Florida; St. Louis, Missouri; Williamsville, New York; and Dayton, Ohio) were selected as pilot projects. These districts received donated commodities for the 1977-78 school year and cash for the 1978-79 school year. In addition, a control unit of two school districts--one in Hutchinson, Kansas, and another in Greeley, Colorado--was selected and data collected for the same period. The study's primary objective was to compare the monthly and total costs of preparing and serving a school lunch for the period reviewed. For each lunch served during the 1978-79 school year that met USDA's type A meal requirements, the pilot school districts received 13.75 cents rather than an equal value of commodities.

Study methodology

In each pilot district, all schools were removed from the commodity distribution program and placed on a cash basis for 1 year beginning July 1, 1978. The effects of the cash system on local school food authority costs (food, labor, and other) and on the types, amounts, and quality of food were examined. Other costs included rent, utilities, and equipment. The impacts on USDA and State administrative expenses were also reviewed from data obtained from FNS, ASCS, and FSQS and from the two control States--Kansas, which had been on a cash system since 1975, and Colorado, which according to USDA was a commodity State with school food service program characteristics similar to those of Kansas.

Data collection and analysis

Data was collected on the local school districts' food, labor, and other costs; the quality of the food bought; the types

and amounts of food used; and State and USDA administrative expenses. USDA compared October 1977 cash and commodity purchasing patterns with the corresponding data for October 1978--a 1-month period. The October 1978 data was adjusted to reflect the effects of inflation. According to USDA, most information was collected at the school district level using questionnaires. At selected schools in each pilot and control school district, data on food, labor, and other costs was collected. Plate-waste data was also collected using a sample of students.

USDA obtained Department and State administrative expense data through interviews with Washington and regional office staffs and with officials in the Colorado and Kansas State agencies.

Results

USDA found that food costs for six of the eight districts decreased under cash-in-lieu while in the other two districts, food costs increased. Changes also occurred in the two control districts. In Kansas, which was on a cash system in both 1977 and 1978, USDA found that food costs increased 1.75 cents per meal. In the control district in Colorado, which was on commodities both years, per-meal food costs decreased 1.69 cents.

In five of the eight pilot districts, USDA found that labor costs increased; in the remaining three districts, labor costs decreased. USDA suggested in its report that a reduction in food costs under a cash system may result in increased labor costs in some cases (due to increased staffing devoted to procurement and related areas). However, USDA pointed out that the data was not conclusive as to whether or how much labor costs might increase under a cash system.

In five of the eight pilot districts, USDA reported that other costs changed by less than 1.5 cents per meal between the 1977 and 1978 observations. In the remaining three districts, other costs increased between 2.86 and 5.37 cents per meal. According to the study, if the effect of inflation were removed, it is possible that decreases would have been observed. However, USDA pointed out that no definite conclusions could be drawn about the cash system's effect on other costs.

Administrative cost savings identified in control district

USDA's report, "A Study of Cash in Lieu of Commodities in School Food Service Programs," compared administrative costs in only the two control districts (Kansas and Colorado) and concluded that in Colorado it was likely that most of the costs relating to food distribution overhead could be avoided. The report suggested that an all-cash system, not a partial system, might reduce overall Colorado State administrative expenses by almost 30 percent. USDA indicated, however, that the Colorado results may not be relevant for other States because other States differ

from Colorado in a number of respects, including the nature of State and local responsibilities and the number and characteristics of participating schools and students.

Federal expenses

According to USDA's findings, adopting a cash system would reduce FNS, FSQS, and ASCS administrative expenses by a total of about \$37.5 million.

For FNS, the main impact of a cash system would be the elimination of certain transportation and storage costs generated in transferring commodities from warehouses to schools. According to USDA, FNS spends about \$39 million annually for commodity shipping costs for all of its child nutrition programs. These include the school lunch, school breakfast, summer feeding, and child care programs. A total cash system would eliminate shipping costs for the two school programs, resulting in a net savings of \$35 million to \$36 million, or about 90 percent of all shipping costs associated with the child nutrition programs.

Additional savings would accrue to FNS because fewer employees would be required to administer a cash system. Staff reductions would be possible both in Washington and in the regions. According to the report, the Washington commodity allocation and distribution staff could be reduced by 15 to 30 percent, or 4 to 10 full-time equivalent positions. This would amount to an annual savings of between \$150,000 and \$275,000. The report concluded that a shift to cash would conceivably result in similar staff reductions in the regional offices. In that case, USDA concluded that another \$150,000 to \$275,000 could be saved annually, resulting in a total staffing cost savings of \$300,000 to \$550,000 annually.

The report said that these savings would be offset by staff increases in other parts of FNS to administer a cash program. However, it said that the increases would be very minor because the necessary structure already exists to manage current cash reimbursements.

Overall, the net FNS savings were estimated to be about \$36 million annually. USDA concluded, however, that as in the case of State expenses, the savings would be much smaller under a partial cash system.

Under a total cash system, FSQS and ASCS would continue their activities in price-support and surplus-removal functions under the sections 32 and 416 programs. But according to USDA, they would no longer purchase, transport, and store section 6 commodities. USDA estimated that the reduction in personnel and other costs associated with eliminating section 6 purchases would amount to about \$1.5 million annually.

Food quality

The study also sought to gather data on the quality of food States purchased locally versus commodities purchased and donated by USDA. A panel of FSQS officials analyzed 21 types of food generally purchased in the commodity program. Commodity graders visited 18 (9 cash and 9 commodity) locations and determined each product's grade, condition, weight, and compliance with specific requirements. The following are two examples of what the panel found.

--Beef products: Samples of ground beef were compared. The fat content was similar (22 percent) for both locally purchased and donated ground beef. Several locally purchased products contained textured vegetable protein.

--Poultry: Turkey rolls purchased locally were tested and found to be similar in fat, moisture, total protein, and salt to the donated turkey rolls tested. However, in the donated product, the amount of meat was much greater (81 percent) than in the locally purchased product (52 percent).

The major difference the FSQS panel found appeared to be in the consistency of the grade of food. More of the donated foods than the locally purchased foods were Grade A or B. However, other than grade specifications, the panel found little difference between donated commodities and locally purchased foods. USDA said that although donated products generally were of higher grade, this did not mean that they were nutritionally better. According to USDA, it is possible that school districts that switched to lower grade foods under cash may have served meals nutritionally equal to those prepared from donated commodities. Procuring lower grade foods may have enabled them to reduce costs without compromising nutritional goals.

USDA study results leave many questions unanswered

USDA's abbreviated study of only eight pilot projects and two control districts provides some data on a cash program but leaves many questions unanswered. The study's findings are based on data collected during a relatively short period from a very small sample of the Nation's schools, selected from only 37 volunteer districts. The study's limitations are clearly laid out in USDA's report. The major limitations are as follows.

--Small number of sites selected. Eight pilot projects and two control units were selected. According to USDA, "Eight is too small a sample to be statistically valid." The report pointed out that a much larger sample, possibly 50 or more sites, would be necessary to draw statistically valid conclusions for certain regions or school types.

--Self-selection bias. Sites were not randomly selected to participate in the study. Only 37 school districts applied, of which 8 were selected. According to USDA, those that applied probably were in favor of a cash system. Therefore, volunteers for the cash test most likely were those viewing a cash system as having beneficial effects.

--The short study period. The report suggested that the participating schools probably did not adjust as completely under the 1-year test situation as they would under a permanent cash system. Adjustments in staffing and basic program procedures would not have changed as completely as they would have had a permanent switch to cash taken place. In addition, USDA only compared data for a 1-month period--October 1977 with October 1978.

Based on these study limitations, extreme caution should be taken by those viewing the study as conclusive evidence on which to base a program switch to cash. Data gathered from eight volunteer school districts during a 1-month period should be viewed in perspective.

Previous USDA studies

In two 1974 studies, "Implications of Discontinuing USDA Commodity Acquisition and Domestic Distribution Activities" and "A Study of Alternatives to Commodity Distribution Programs," USDA examined alternative measures to replace the commodity donation program. Circumstances at that time were somewhat similar to the problems currently associated with the program--late deliveries, distribution of limited-appeal items, and inadequate program monitoring and supervision. The studies on replacing the commodity program with an all-cash or letter-of-credit system generally concluded that compared with continuing the commodity program, school food costs would have increased only slightly to moderately, depending on the system adopted. USDA also suggested that possible savings in commodity distribution costs would offset these increases.

Kansas State University study

Kansas State University was funded by the National Frozen Food Association and other food industry trade associations to study the costs associated with preparing and serving school lunches in all pilot school districts included in USDA's study. The University was asked to compile costs for the entire school year 1978-79 when the districts received cash in lieu of commodities and then compare those costs with those in the previous year when those districts received donated commodities. The study was completed by Dr. Donald Erickson of the University's Department of Economics in Manhattan, Kansas.

The study's conclusions were as follows.

- By projecting 1978-79 deflated food prices against actual 1977-78 food prices, the study found that on the average, the food costs for each meal served in the pilot project school districts decreased by 6.5 cents.
- With no inflation factor between the cash year and commodity year, six of the eight school districts experienced actual reductions in food costs per meal of from 1.4 cents to 6.6 cents. The average food cost reduction reported was 3.6 cents per meal.
- Large and small, urban and rural school districts reduced their food costs with cash in lieu of commodities. (A 1974 USDA study of 15 school districts had indicated that smaller school districts would do better with donated commodities than with cash while larger school districts could generally match USDA's purchasing power.)
- The food service directors in each district preferred the cash system over donated commodities because it provided them more flexibility in purchasing.

In summarizing the report, Dr. Erickson concluded that the economic consideration of cash in lieu of commodities versus donated commodities was clearly in favor of using the cash program. He also said that the cash program allowed better menu planning because of accurate delivery dates for products, better inventory control, far less storage costs, and reduced paperwork.

OUR ANALYSIS OF THE KANSAS CASH-IN-LIEU PROGRAM

In our 1977 report, 1/ we addressed the issue of cash in lieu of federally donated commodities. During that review we visited three school districts in Kansas and found that State and local school lunch program officials favored cash in lieu of commodities. According to the officials, the cash program had

- eliminated various inconveniences associated with the commodity program, such as menu limitations, late deliveries, and commodities in undesirable package sizes or in excessive quantities;
- reduced transportation, storage, and administrative costs associated with the commodity program;
- eliminated the need to deal with limited-appeal commodities previously provided under the commodity program; and

1/ See footnote, p. 13.

--allowed more food variety.

Officials from all nine districts in that earlier review in Missouri, Ohio, and Pennsylvania favored cash over commodities because they generally believed that districts can

--purchase a greater variety of foods and provide a greater menu variety;

--reduce administrative, processing, storage, and delivery costs;

--use only those commodities that work best in their systems; and

--receive their full Federal contributions which can be used to purchase more food than is now being provided.

PROPOSED TEST OF CASH SYSTEM AT SELECTED LOCATIONS

Public Law 96-528, enacted December 15, 1980, provides for a 3-year USDA study to determine whether there may be more efficient, economical, and reliable methods of operating the commodity donation program for the National School Lunch Program. The project calls for a random statistical selection of 60 school districts. School districts which participated in USDA's earlier pilot project study will have the option of participating in this study.

USDA will analyze the administrative feasibility and nutritional impact of cash payments and letters of credit. The study should also assess Federal, State, and local costs incurred by adoption of the test approaches. The study will also review the impacts on (1) Federal programs for providing adequate income to farmers, (2) the quality of food served, (3) plate waste, (4) local economies, and (5) local, regional, and national marketing of the commodities used in the school lunch program.

SCHOOL DISTRICTS ARE DIVIDED ON QUESTION OF CASH, COMMODITIES, OR LETTER OF CREDIT

During this review, we asked officials in 12 school districts in California, Missouri, Montana, and Texas whether they preferred to continue receiving federally donated commodities or to receive cash or a commodity letter of credit. Officials in eight districts told us they would prefer cash in lieu of commodities while officials in three districts told us they wanted to continue to receive commodities. One district official said he favored either cash in lieu of commodities or a commodity letter of credit rather than the current commodity program.

District officials preferring cash over commodities told us that generally they believed cash in lieu of commodities would allow the districts more flexibility because they could

- buy the food items they believe best meet the needs;
- prepare menus based on local preferences instead of gearing the menus to the donated commodities received;
- purchase more usable food items, such as precooked hamburger patties, sloppy joe mix, pizza, and burritos;
- control the quantity of food items received;
- control when commodities are purchased and delivered; and
- buy foods locally below USDA's delivered price.

Generally speaking, the district officials favoring commodities over cash believed that federally donated commodities offered more for the money. For example, a district director for school food services in Texas told us that the quality of federally donated commodities is better than what the districts can purchase locally. A district official in California told us that USDA has more buying power than the average school district and can buy more food for the dollar.

USDA COMMENTS

According to USDA (see app. IV), it is concerned about the agricultural-impact implications of an alternative system. It said that most proponents of an alternative system do not address the food donation objective of price support and surplus removal. It cited the following concerns should the alternative systems be adopted: (1) outlets for donation of CCC inventory items, (2) ability to maintain other commodity programs such as the needy family program on Indian reservations, and (3) ability to respond to disaster relief feeding needs.

CONCLUSIONS

Although some studies have been done on the effects of an all-cash program, many questions remain unanswered. The real effects of a total cash or letter-of-credit system have not been determined. The 3-year study of 60 school districts as mandated by Public Law 96-528 could go a long way in providing useful data for developing approaches to solve many problems now associated with commodity donations to the school lunch program. In light of this study, we are not making recommendations at this time.

COMMODITY DONATION PROGRAM: LEGISLATIVE BASIS,
PROGRAM OPERATIONS, AND MAJOR RECIPIENTS

LEGISLATIVE BASIS FOR THE COMMODITY PROGRAM

The commodity donation program is centered on three major pieces of legislation: section 32 of the act of August 24, 1935 (7 U.S.C. 612c), section 416 of the Agricultural Act of 1949 (7 U.S.C. 1431), and section 6 of the National School Lunch Act of 1946 (42 U.S.C. 1755).

Section 32

Purchases under this section are intended to remove temporary market surpluses of perishable foods and to help stabilize farm prices. Section 32-designated commodities are purchased by FSQS. Under section 32 legislation, USDA annually receives 30 percent of the customs receipts collected from the duties on agricultural and nonagricultural products during each calendar year. In fiscal year 1979 this amounted to about \$1.7 billion.

According to USDA, funds appropriated under section 32 must be used principally for purchasing surplus perishable, nonbasic agricultural commodities. Surplus has been defined by USDA as either physical (supplies exceeding requirements) or economic (prices below desired levels). In the case of an economic surplus, any nonbasic perishable commodity that has a market price of less than 100 percent of parity can be purchased under section 32 authority.

Section 32 items generally include commodities such as meats, fruits, and vegetables. The Secretary determines which commodities will receive assistance and the level and extent of such assistance. Major factors considered in determining those commodities that require assistance are

- existence and size of surplus,
- whether the commodities are perishable nonbasic items,
and
- potential recipients.

An economic surplus is considered to exist when the market price is less than 100 percent of parity. Theoretically, price-support programs are designed to maintain the price of a crop or production at an announced price level. Section 32 funds have been used to buy ground beef, applesauce, canned corn, canned tomatoes, whole frozen turkeys, and several other items. (See app. III.)

Sections 9 and 13 of the National School Lunch Act (42 U.S.C. 1758 and 1761, respectively) and section 8 of the Child Nutrition Act (42 U.S.C. 1777) authorize the Secretary to donate section 32 and section 416 (see below) commodities to child feeding programs. Section 14 of the National School Lunch Act (42 U.S.C. 1762a) authorizes the expenditure of funds from sections 32 and 416 to purchase agricultural commodities which are customarily acquired and donated under those sections for (1) child nutrition programs under that act and the Child Nutrition Act of 1966 and (2) elderly nutrition programs under title VII of the Older Americans Act of 1965, as amended (42 U.S.C. 3045 et seq.).

The amount of any one commodity purchased with section 32 funds is subject to several constraints: (1) the amount of the commodity usable by the various programs, (2) the amount of section 32 funds available, and (3) the requirement that not more than 25 percent of the available section 32 funds can be spent on any one commodity. In addition, commodities purchased with section 32 funds must be produced in the United States.

Purchases of some commodities are made once or twice annually at the peak of the packing season. Other commodities are purchased repeatedly, sometimes weekly, when a surplus continues.

Section 416

Commodities donated under section 416 of the Agricultural Act of 1949 are acquired under USDA's price-support program. These commodities are primarily basic nonperishable items. According to USDA, prices are supported by removing surplus commodities from the market and storing them for return to the market when conditions are more favorable. Section 416 authorizes the Secretary of Agriculture to distribute food commodities and the Commodity Credit Corporation (CCC) to pay the cost of processing commodities into a form more suitable for home or institutional use, plus the cost of packaging, transporting, handling, and other charges accruing up to the time of their delivery to the designated State or other recipient agency.

Only commodities determined by the Congress or the Secretary of Agriculture as eligible for price support may be donated under this section. These items must be in surplus, and it must be shown that such dispositions are necessary to prevent waste. Section 416 commodities include dairy products, such as cheese, butter, and milk, and other foods, such as fats and oils, rice, wheat, and other grains. According to USDA, dairy products accounted for 69 percent of section 416 donated foods in 1979.

Section 709 of the Food and Agriculture Act of 1965, as amended (7 U.S.C. 1446a-1) authorizes the Secretary of Agriculture to purchase with CCC funds dairy products for schools (other than fluid milk), domestic relief, community action, and other authorized programs when CCC dairy stocks are insufficient. This authority has been used infrequently.

In 1978 FNS began offering "bonus" section 416 commodities to States for their child nutrition programs. This meant that once a State had used all of its original entitlement of one or more of the section 416 commodities, it could order additional commodities--all the State could use without waste. In fiscal year 1979 bonus commodities valued at \$69.6 million were distributed to States.

Section 6

Section 6 of the National School Lunch Act makes funds available to USDA for direct expenditure on agricultural commodities and other foods which are distributed to schools and service institutions participating in food service programs. Emphasis is focused on high-protein foods, meat, and meat alternatives, which are preferred by schools but usually not available under the surplus-removal activities. FNS' policy has been to use section 6 funds to buy commodities States prefer. Section 6 foods have included ground beef, frozen chicken, fruits, and various vegetables.

Section 6 also establishes the mandated national average value of commodity assistance for lunches served in the National School Lunch Program and for lunches and suppers served in the Child Care Food Program at 10 cents per meal. That amount is subject to annual adjustments to reflect changes in the Index for Food Used in Schools and Institutions.

Section 6 purchases during fiscal year 1979 amounted to \$80 million. Protein foods made up the bulk of the purchases, constituting about 99 percent of the total. About \$49.5 million was used to purchase frozen chicken and \$19.5 million for frozen turkey rolls.

PROGRAM OPERATIONS

FNS is responsible for the overall administration of the program with FSQS and ASCS buying surplus commodities from regular market channels (price assistance) and other commodities to maintain programmed levels of assistance to schools, elderly feeding, and other domestic food assistance programs.

According to USDA, all purchases are coordinated with FNS to assure that the quantity, quality, and variety of commodities purchased can be used in domestic feeding programs.

Procurement procedures

FSQS in Washington, D.C., and ASCS in Kansas City, Missouri, are responsible for purchasing all commodities for the commodity donation program. FSQS purchases fruits, vegetables, meats, poultry, and egg products. ASCS purchases price-supported items, including grain and dairy products. Each agency's procurement procedures are summarized briefly as follows.

FSQS' commodity procurement branches are responsible under the general supervision of their respective division directors for recommending, managing, and supervising surplus removal purchases and diversion programs for domestic feeding programs under section 6 of the National School Lunch Act and section 32. Commodities are also purchased under legislation authorized for feeding special groups, including needy families (Indians), children in summer camps, lactating mothers, and the elderly. The branches recommend, through the division directors and the Administrator of FSQS to the Assistant Secretary for Food and Consumer Services, action to be taken regarding purchases.

FSQS and FNS jointly determine the anticipated types and quantities of sections 6 and 32 commodities to be purchased under the program. This determination is made using information obtained on commodity availability, market price, and availability of funds. To determine a commodity's availability, FSQS among other things reviews trade and market reports and talks to industry officials.

Following this, FNS determines through surveys the quantities of commodities the States desire. Matching school preferences with parity and surplus removal considerations are all taken into account in developing final purchase plans. Following approval of such plans, FSQS issues a Food Purchase Report announcing the forthcoming purchases and also mails announcement/invitations and other applicable documents to all prospective bidders, trade groups, magazines, associations, and other interested parties on agency mailing lists.

Bids are requested on an FOB-origin or -destination basis depending on the type of commodity being procured. To meet distribution needs and avoid prolonged storage, frozen meat and poultry items are generally procured on a weekly or biweekly basis from late summer to early spring. Fruits and vegetables, being seasonal products, are usually purchased once yearly following harvest, with staggered delivery periods.

Offers accepted are those considered to be the most advantageous to USDA considering price, transportation costs, and other factors. In analyzing bids, personnel compare prices offered with raw material prices quoted in USDA market news reports and list prices quoted in trade reports, magazines, and journals. Also considered for those programs operating on a continual basis is the supply/price outlook for future procurements.

Following approval of awards at the agency level, a Food Purchase Report is issued and successful bidders are notified.

ASCS distributes program announcements identifying commodities which it plans to purchase from time to time. These announcements, depending on the commodity, are mailed to all applicable vendors

and prospective bidders on ASCS mailing lists. Copies also go to trade groups, associations, carriers, and other interested parties. ASCS solicits bids on the various commodities by issuing invitations for bid. Invitations for bid on grain products are issued subsequent to the receipt of consolidated State agency orders from FNS regional offices. On dairy products, ASCS invites bids based on an FNS estimate of the need for dairy products. The invitations remain open for about 10 days. As bids are received, they are logged in and filed. Once the invitations for bids close, the bids are removed and analyzed.

Bids received for grain products are separated by commodity, checked for compliance with Government contracting requirements, logged in, and assigned official bid numbers. The bids are then prepared for computer input by bid number and price. Several different printouts are generated. One lists all bids by vendor and commodity. Another ranks all bids from lowest to highest. Finally, a special linear program is run against the data to determine the lowest bidder and to prepare an award by bidder listing.

MAJOR RECIPIENTS

Programs receiving commodities include, but are not limited to, the following.

Child nutrition programs

The National School Lunch Program is the largest child nutrition program and receives about 90 percent of the commodities USDA provides to all eligible recipients. First authorized under the National School Lunch Act of 1946 (42 U.S.C. 1751 *et seq.*), the program provides Federal assistance to help States and schools serve nutritious school lunches. Federal assistance in cash and commodities is also provided for use in preparing and serving meals to children in institutional settings. This assistance is provided through the school lunch, school breakfast, ¹/ summer food service, and child care food programs. Its purpose is to help maintain the health and proper physical development of American children. Funds are also made available for other program-related expenses, including State administrative expenses.

Funds are provided by direct appropriations and through transfer of section 32 funds. In fiscal year 1979 for the child nutrition programs, USDA provided about \$2.7 billion in cash and about \$668.4 million in commodities (including \$69.6 million in bonus commodities) or cash in lieu. In fiscal year 1980 regular

¹/As a result of the Omnibus Reconciliation Act of 1980 (94 Stat. 2599) beginning in school year 1981, USDA no longer offers commodity assistance to school breakfast programs based on the number of meals served.

cash expenditures increased to \$3.1 billion while the value of commodities supplied to all child nutrition programs (schools, summer food service, and child care) was about \$843.3 million (including \$137.3 million in bonus commodities).

Child Care Food Program

Authorized by section 17 of the National School Lunch Act (42 U.S.C. 1766), this program provides meal service to children enrolled in nonresidential child care institutions, including child care centers, family day care homes, and outside-school-hour centers. The amount of funding provided is based on the number and type (free, reduced price, or full price) of meals served. Total USDA expenditures for this program for fiscal year 1980 amounted to about \$211.5 million. Except for about \$5.9 million provided States for food service equipment, the expenditures were for meals provided (about \$203.7 million) and commodities distributed (\$1.9 million).

Commodity and special supplemental food programs

The supplemental food programs--the Special Supplemental Food Program for Women, Infants, and Children (WIC) and the Commodity Supplemental Food Program--have similar objectives. They are designed to safeguard the health of pregnant, post-partum, and breast-feeding women and infants and children who are at nutritional risk because of inadequate nutrition and inadequate income.

The Commodity Supplemental Food Program was originally authorized under the Department of Agriculture and Related Agencies Appropriation Act of 1969 (Public Law 90-463, Aug. 8, 1968); the Food and Agriculture Act of 1977 (Public Law 95-113, Sept. 29, 1977) extended the program through 1981. During fiscal year 1980 only 10 States and the District of Columbia participated in the program. The number of projects ranged from a high of 23 in October 1979 to 20 in September 1980, with an average monthly participation of 102,500 persons. About \$21.8 million worth of commodities was distributed.

WIC is authorized through September 30, 1982, by section 17 of the Child Nutrition Act of 1966, as amended (42 U.S.C. 1786). The program makes funds available to local health clinics through State departments of health and to Indian groups. As of September 1980, 80 State and Indian agencies participated in the program and served an average of about 1.9 million persons each month. The average monthly benefit per person was about \$26 which, together with administrative and other expenses, amounted to a total dollar expenditure of about \$743.6 million for fiscal year 1980. Of this amount, about \$600.4 million represented food costs.

Needy family program

The Agriculture and Consumer Protection Act of 1973, as amended by Public Law 93-347 (88 Stat. 340), provides for a directly funded food distribution program for needy persons.

Agricultural commodities are provided to needy households living on or near Indian reservations and to such households in the Trust Territories of the Pacific Islands and the Commonwealth of the Northern Marianas. Cash assistance is provided to distributing agencies to help meet operating and administrative expenses. In fiscal year 1980 cash payments were made only to distributing agencies in the Pacific Trust Territories.

In the past, domestic feeding programs for families were operated with commodities acquired through section 32 surplus-removal and CCC section 416 price-support activities. During fiscal year 1974, section 4(a) of Public Law 93-86 (87 Stat. 249) provided authority to use funds from section 32 and CCC, without regard to surplus-removal or price-support conditions, to maintain traditional levels of program assistance. Public Law 93-347 (88 Stat. 340) amended this provision and authorized the use of directly appropriated funds through fiscal year 1977. Public Law 95-113 (91 Stat. 980) extended program authorization through fiscal year 1981 and directed the Secretary to improve the variety and quantity of commodities supplied to Indians.

Average monthly participation was 74,827 in fiscal year 1980. During that year commodities valued at about \$24.6 million were purchased for the needy family program, including about \$12.7 million in section 416 commodities and \$11.9 million in commodities provided under section 4(a). Some \$6.6 million was budgeted (out of fiscal year 1980 Food Stamp Program appropriations) for administrative expenses of States and Indian tribal organizations conducting distribution to households.

Elderly feeding program

Commodity support for this program is required by title III, section 311, of the Older Americans Act of 1965, as amended. USDA buys commodities for the elderly feeding program and is reimbursed by the Department of Health and Human Services. The foods are used in preparing meals which are served in senior citizens' centers and similar settings.

In fiscal year 1980 about 166 million meals were served in the elderly feeding program (about 634,000 meals each day). States have the option of receiving cash, commodities, or a combination of cash and commodities. During fiscal year 1980, 23 State agencies chose to receive a combination of cash and commodities, 28 chose cash, and 7 chose to receive commodities. Generally, the

same commodities provided to schools in fiscal year 1980 were provided to the elderly. Commodities valued at \$14.6 million and \$54.1 million in cash-in-lieu were provided for the elderly nutrition program in fiscal year 1980.

Charitable institutions and summer camps

Food is distributed to nonprofit charitable institutions and summer camps for children under section 416 price-support authority. During fiscal year 1980 commodities valued at about \$64.7 million were distributed to about 7,400 institutions serving an estimated 888,000 needy persons. About 4,600 summer camps serving about 84.4 million meals received donated foods valued at \$4.7 million in fiscal year 1980.

LOCATIONS VISITED

WASHINGTON, D.C.:

Agricultural Stabilization and Conservation Service headquarters
 Food and Nutrition Service headquarters
 Food Safety and Quality Service headquarters

ARIZONA:

Papago Indian Reservation, Sells

CALIFORNIA:

FNS Western Regional Office, San Francisco
 Department of Education, Office of Surplus Property,
 Sacramento
 San Francisco Unified School District, San Francisco
 Oakland Unified School District, Oakland
 San Juan Unified School District, Carmichael
 Sacramento Unified School District, Sacramento
 Volunteers of America, Sacramento
 Union Gospel Mission, Sacramento
 St. Anthony's Dining Room, San Francisco

COLORADO:

FNS Mountain Plains Regional Office, Denver
 Department of Social Services, Food Assistance Program Division,
 Denver
 Denver County Commodity Supplemental Feeding Program, Denver

MISSOURI:

Department of Elementary and Secondary Education, Jefferson
 City
 Department of Social Services, Division of Family Services,
 Jefferson City
 Department of Social Services, Division of Aging, Jefferson
 City
 Kansas City School District, Kansas City
 St. Louis School District, St. Louis
 Central Missouri Area Agency on Aging, Columbia
 Mid-American Regional Council Area Agency on Aging, Kansas
 City

MONTANA:

Department of Social and Rehabilitation Services, Economic
 Assistance Division, Food and Nutrition Bureau, Helena
 Office of Public Instruction, Division of School Food Services,
 Helena
 Department of Social and Rehabilitation Services, Community
 Services Division, Aging Services Bureau, Helena
 Missoula Elementary School District #1, Missoula
 Missoula High Schools, Missoula
 Arlee School, Arlee
 Helena Schools, Helena

Blackfeet Indian Reservation, Browning
Flathead Indian Reservation, St. Ignatius
Area V Area Agency on Aging, Anaconda

NEW JERSEY:

FNS Mid-Atlantic Regional Office, Robbinsville

NEW MEXICO:

Navajo Indian Reservation, Fort Wingate

NORTH DAKOTA:

Department of Public Instruction, Bismark
Fort Totten Indian Reservation

PENNSYLVANIA:

Department of General Services, Bureau of Government Donated
Food, Harrisburg
Lower Dauphin School District, Hummelstown
Diocese of Pittsburgh Schools, Pittsburgh
Pittsburgh Board of Public Education, Pittsburgh
Dauphin County Area Agency on Aging, Harrisburg
Mon Valley Area Agency on Aging, Monessen
Harrisburg State Hospital, Harrisburg
John Kane Hospital, Pittsburgh
C. Howard Marcy State Hospital, Pittsburgh

TENNESSEE:

Department of Agriculture, Commodity Distribution, Nashville
Metropolitan Health Department of Nashville and Davidson
County Tennessee, Nashville
Shelby County Commodity Supplemental Feeding Program, Memphis

TEXAS:

FNS Southwest Regional Office, Dallas
Department of Human Resources, Food Services Division, Austin
Department of Human Resources, Food Services Division, Region
IV, Fort Worth
Governor's Committee on Aging, Austin
Arlington Independent School District, Arlington
Birdville Independent School District, Fort Worth
Lewisville Independent School District, Lewisville
Grapevine-Colleyville Independent School District, Grapevine
Dallas Independent School District, Dallas
Dallas County Nutrition Project, Dallas
Tarrant County Nutrition Project, Fort Worth

SECTION 32 PURCHASES FOR THE CHILD NUTRITION PROGRAMSFISCAL YEARS 1978-80

<u>Commodity</u>	<u>Section 32 purchases</u>		
	<u>FY 1978</u>	<u>FY 1979</u>	<u>FY 1980</u>
	----- (millions) -----		
Poultry:			
Turkeys, whole	\$ 10.5	\$ 31.2	\$ 20.6
Turkey rolls	-	4.5	7.8
Canned boned poultry	16.4	16.4	18.4
Egg mix	5.3	8.5	5.1
Chicken	-	0.1	-
Meat:			
Beef	78.9	76.7	70.6
Pork	-	-	73.5
Fruit:			
Apple juice (note a)	0.7	2.5	6.8
Orange juice (note a)	(b)	0.3	-
Applesauce (note a)	7.1	2.1	13.1
Peaches (note a)	8.1	10.2	13.0
Pears (note a)	4.2	13.4	19.1
Lemon juice	0.4	-	-
Plums, purple	1.9	-	0.5
Pineapple (note a)	7.1	(b)	-
Raisins	3.4	-	10.7
Apples	-	2.2	2.9
Apricots	-	-	8.1
Vegetables:			
Tomato juice (note a)	0.6	1.3	2.4
Corn (note c)	3.0	10.1	11.4
French fries (note d)	12.4	16.9	17.3
Potato rounds	8.1	17.6	16.3
Potatoes, dehy., instant	9.5	5.7	1.3
Sweet potatoes	2.2	5.6	6.2
Beans, green (note c)	-	7.8	6.0
Peas (note c)	6.4	7.1	7.3
Vegetables, mixed	-	5.4	5.2
Tomato catsup	7.8	3.4	14.1
Tomatoes (note a)	13.0	10.9	2.5
Tomato paste	10.1	11.6	6.4
Beans, dry	-	3.4	6.2
Beans, vegetarian	-	6.7	5.6
Carrot sticks	-	-	0.1
Onions	-	-	0.1
Total	<u>\$217.1</u>	<u>\$281.6</u>	<u>\$378.6</u>

a/Canned goods.

b/Less than \$50,000.

c/Canned and frozen goods.

d/Includes frozen, deep fry, and oven varieties.



United States
Department of
Agriculture

Food and
Nutrition
Service

Washington,
D.C. 20250

APR 20 1981

Mr. Henry Eschwege, Director
United States General Accounting Office
Washington, D.C. 20548

Dear Mr. Eschwege:

Thank you for the opportunity to review and comment on your proposed report entitled "Department of Agriculture's Commodity Donation Program: Some Success, But Improvements Are Needed." The Food and Nutrition Service was designated as the lead agency to coordinate our written comments. Also, providing input was the Food Safety and Quality Service, the Agricultural Stabilization and Conservation Service and the Office of Budget, Planning and Evaluation.

Attached are our written comments. As you will see we have attempted to restrict our comments to clarifying or correcting factual information. It is difficult, as you found during your audit, to totally balance the seemingly conflicting objectives of the donation program i.e., the purchase of commodities for surplus removal and price support purposes and the donation of commodities which always meet the recipient agencies' preferences and needs. We have provided some suggested wording changes which we believe will better reflect the relationship of the objectives of our donation program.

In addition we request that you carefully review the data and methodology used to arrive at the excess inventory amounts listed in the draft audit. We are not questioning the fact that there are excess inventories, only the dimension of the problem. Perhaps a better way of illustrating the size of an inventory would be to convert them to "servings per child" and compare to the number of school days.

We look forward to your final report. If you have any questions concerning our written comments, please contact Darrel E. Gray, Food Distribution Division Director, on 447-8371.

Sincerely,

G. WILLIAM HOAGLAND
Administrator

Enclosure

[GAO NOTE: This appendix contains USDA's comments on our report. We have summarized and evaluated the comments at the end of each applicable report chapter and, in some instances, made changes to the report. Our evaluations of comments not covered at the end of the various chapters are included in this appendix, enclosed in brackets, immediately under the paragraph or set of paragraphs in which a point is raised.]

USDA COMMENTS ON GAO'S DRAFT REPORT"DEPARTMENT OF AGRICULTURE'S COMMODITY DONATION PROGRAM:SOME SUCCESS, BUT IMPROVEMENTS NEEDED" [1/]DIGEST

The total value of food distributed shown in this section (\$996.1 million) does not agree with the amounts shown in Appendix I, pages 75-78. We have therefore corrected the amounts in this section, on page 4, and in Appendix I. The amount in this section should read \$969.0 million.

[GAO COMMENT: The data provided has been incorporated in the final report. These changes did not affect our conclusions and recommendations.]

PROGRAM ADMINISTRATION

We have no recommended changes on this section.

NEED FOR BETTER IDENTIFICATION OF COMMODITY NEEDS

We have the following comments on this section.

1. The third paragraph of page i (and several other places in the report, as noted in other comments below) reflect a fundamental confusion about how the commodity distribution program works. The authors seem to be under the misconception that the food preference surveys (the FNS-35 reports) are meant to be a definitive statement of what States want, rather than simply a preliminary, exploratory survey. The authors also implicitly assume, incorrectly, that commodity purchases are supposed to be based almost exclusively on the States' preferences, rather than jointly on States' preferences and several other competing and sometimes inconsistent factors--including whether particular commodities are in surplus or need price support.

As a result of these misunderstandings, the authors misstate on page i and subsequent pages the real problem with the surveys. We agree there is a problem, but the audit report as currently written misses the point. At the start of the yearly planning cycle, FNS surveys the States to get a general overview of the kinds and amounts of commodities desired nationwide. This survey is not intended to reflect any commitment by the States that they will ultimately accept the items they put on the survey form. Nor is there meant to be any commitment by FNS that all preferences

[1/GAO NOTE: This portion of the Department's letter was retyped to facilitate showing our comments. The page numbers were changed to reflect those in the final report.]

will be satisfied. Any such commitments would be impossible at this early stage in the planning process (given that the commodity market conditions must still be considered) and would be contrary to the whole purpose of the survey--which is simply to get a rough idea of States' initial thoughts on their desires for the upcoming year.

FNS then meets with FSQS and ASCS to formulate a preliminary overall annual purchase plan. Information from the preference survey is brought together with analysis of which commodities are likely to have surpluses or need price support. The annual purchase plan attempts to balance the States' preferences with the commodity market considerations.

FNS advises the States of the type and quantity of commodities which FNS anticipates will be available, based on the contents of the annual purchase plan. The State distributing agencies then advise FNS as to the commodities they want and can order up to their fair share. Thus, the States are consulted a second time (the first being the preference survey) and then provide more precise specifications of their desires. This step is crucial to understanding the whole process, but is not understood in the draft audit report.

In order to accurately reflect the difficult balance between the dual objectives of price support and surplus removal and the "entitlement" of users (including their preferences or "needs") we suggest the following language be substituted for the first sentence in this section.

"The types of commodities purchased for donation fluctuate in relation to market conditions. In fact, the foods purchased and donated will not always be among the most desired by recipient agencies. However, the Department has not been as thorough as they could have been in fully and accurately determining users' commodity needs."

[GAO COMMENT: On page 1 we point out that the types of foods and amounts purchased may fluctuate in relation to marketing conditions. Again in appendix I (see pp. 71 and 74), we discuss the information used by USDA in determining commodity purchases. We do not assume that commodity purchases are supposed to be based exclusively on the States' preferences rather than a joint consideration of these preferences and surplus-removal or price-support activities. Instead, we believe that the food preference surveys have not been given proper consideration in determining user commodity preferences. We believe that the preference survey, with proper analysis and evaluation, can be a more effective tool in determining user commodity preferences and needs and that this

information would help in matching user needs with price-support and surplus-removal activities.]

2. On pages i and ii, we believe the example used is poor. It actually demonstrates a State agency's failure to fully consider a user's needs rather than the Department's failure. The Department relies upon a State agency to exercise prudent administration of the donation program within their State. We suggest the example either be deleted or inserted after the second paragraph on page ii, because the second paragraph speaks to the relationships between FNS, the State, and the local school districts.

[GAO COMMENT: This matter has been clarified on page ii. Nevertheless, we believe that the example illustrates the failure of both the State and USDA to effectively monitor inventory levels. As pointed out on page 36 of the report, FNS instructions require State distributing agencies to report monthly inventory levels to appropriate FNS regional offices for the purpose of monitoring inventories. The regional offices are required to identify any discrepancies and report them to headquarters immediately. (See p. 37.)]

CHAPTER 1 - COMMODITY DISTRIBUTION COSTS

As mentioned in our comments on the DIGEST Section, appropriate corrections have been made in the funding figures used throughout the report. The following, therefore, should be inserted in toto in lieu of page 4 of the draft report.

[GAO COMMENT: The updated figures, which are not reproduced in this appendix, have been incorporated into the final report.]

CHAPTER 2 - THE EFFECTS OF SECTION 32 PURCHASES SHOULD BE EVALUATED

We have the following comments on page 8 under the section titled: USDA HAS DONE LITTLE TO MEASURE EFFECTIVENESS OF SECTION 32 PURCHASES

1. The main point of this paragraph is obscured somewhat by the construction of the paragraph. We suggest the second sentence in the first paragraph be reworded as follows and inserted after the current third sentence.

"In fiscal years 1978, 1979, and 1980 USDA spent about \$877 million in Section 32 funds (See Appendix III) for the Child Nutrition Program--the largest recipient of donated commodities."

[GAO COMMENT: Paragraph revised.]

2. Further, while it is true that a systematic evaluation process may be needed, some work has been done by USDA on evaluation models. Some of the problems associated with designing a workable model to assist in making commodity purchase decisions are discussed in the enclosed article, "Commodity Distribution Programs and the Support of Farm Income," which appeared in the September 1978 issue of Agricultural-Food Policy Review. The article also contains information which underscores the Department's commitment to improving its analytical capabilities for determining the effects of food purchases on farm income.

In view of the work that has been done, we recommend that the following paragraph be added to this section:

"In the early 1970's Department officials, including those responsible for obligating Section 32 funds, initiated efforts to develop a planning-decision model for surplus commodity removal programs. A preliminary model was developed and tested. Although it was found to be conceptually strong, it was determined to be impractical for use in actual situations. The Economics and Statistics Service of USDA is continuing developmental work on a simulation model. A documentation (description) of the model is expected to be available for review by USDA personnel later this year. FSQS officials will evaluate the feasibility of the model when ESS considers it operational. If found workable, FSQS will use the model to assist in the decisionmaking process for selected commodity purchasing operations."

[GAO COMMENT: The report has been revised to point out USDA's efforts in this area. The article referred to is not reproduced herein.]

CHAPTER 3 - NEED FOR BETTER IDENTIFICATION OF USER NEEDS CONTINUE

We have the following comments pertaining to this chapter.

Clarification is needed that the food preference survey and food orders based on user needs are two separate issues. The food preference survey is not meant as an order form for specific quantities. Food preference information from the school food authorities is meant to be used as a guide to help the Department to provide, to the extent feasible, the foods that the schools desire. Once a decision has been made to purchase a certain commodity based on preference and/or surplus removal or price support considerations, the State distributing agent orders food on a food requisition form. Desired quantities based on user needs must be specified on the food requisition form.

The suggested wording given below will help clarify the distinctions in the discussions of problems.

1. Under the section, NEW APPROACHES FOR GATHERING PREFERENCE DATA, on page 15, the report has not stressed the fact that the food preference report is now required. The following language should be added.

"Under the regulations for the National School Lunch Program (7 CFR Part 210), the State Food Distribution Advisory Councils are required to survey a percentage of the school food authorities in their States. The problems of the earlier surveys, given on pages 13 and 14, arose partly because the food preference report was not required. Because of the requirement that the advisory councils obtain the information and report back to the State educational agencies, with the State educational agencies forwarding the information to FNS, the survey data should be more representative than it has been in years past. Also, in forwarding the information to FNS in the food preference reports, the State agencies are required to include the number of school food authorities that provided the required information along with other data which will make the reports truly representative of schools' food preferences in the States."

[GAO COMMENT: We do not believe that the new regulations will necessarily make the surveys any more representative of users' preferences and needs than what has been done in the past. Councils, for example, have not been advised as to the number or percentage of school food authorities to be surveyed and are permitted to devise their own methodologies for making preference surveys. (See p. 15.) Based on past experience, this could result in a great variety of methods used in gathering, analyzing, and presenting individual State data and make USDA's analysis of the data more cumbersome and difficult than it was under the previous system. We believe that all councils should use the same data-gathering methodology and reporting format.]

2. On page 15, paragraph 4, line 12, we believe that it is better to refer to "school food preference data"; "commodity needs" data is an inaccurate and misleading term. The food preference surveys are meant to inform us about preferences rather than actual quantities. We recommend you add the following language after the fourth paragraph on page 15.

"The State Food Distribution Advisory Councils implemented by USDA, as a result of P.L. 95-166, are not required to gather information on actual quantities; they are solely required to gather information on the most desired and least desired foods, and on recommendations for new products. Although USDA is encouraging the advisory councils

to give advice on the amounts of each food item desired, they are not requiring this information. The purpose of the food preference survey is to gather information which will provide an estimate of the types and amounts of foods wanted, in order to give a general idea of what to order and offer to the States."

[GAO COMMENT: We agree with these points and made changes on page 15 to reflect them.]

CHAPTER 4 - FEDERAL AND STATE PROGRAM MONITORING NEEDS IMPROVEMENT

We have the following comments on this chapter.

1. We seriously question the methodology used to arrive at the value of excess inventories on pages 23 and 24. The comparison of "commodity usage" with ending inventories can grossly overstate the excess inventories if the "commodity usage" rate is significantly understated. For example, the 9.3 year supply of raisins in California must assume an extremely low level of usage since our total purchase of raisins during school years 78-79 and 79-80 equaled only 1.4 and 4.9 servings per child per year on a national basis.

As mentioned in our covering letter, we request that you carefully analyze the data and methodology used to arrive at the excess inventory figures. We are not questioning the fact that there are excess inventories, only the dimension of the problem. The utilization rates are apparently determined by GAO based on past performances and, therefore, may result in a distortion of information. For example, if red purple plums are served only once a school year in the past, six servings would represent a six year supply. However placing them on the menu once a month--once in 22 meals--there would only be a six month supply. We suggest that a better way of illustrating the size of an inventory would be to convert them to servings per child and compare to the number of school days.

[GAO COMMENT: The usage rates we used were in fact based on past experience using the 12-month period preceding the school year reviewed. Although the alternative method suggested by USDA to determine excess inventories would provide additional insight into the dimension of the problem, we believe that historical data provides a sound basis to project future usage. Further, USDA concedes there is a problem, and our major concern is the adequacy of its actions to resolve the problem rather than the dimension of the problem.]

2. Under the section, EFFECTS OF EXCESS INVENTORIES, it should be noted that a first-in-first-out inventory control system problem may be the problem rather than excessive inventory, per se. We recommend the following sentence be inserted in the fourth

paragraph on page 26 between second and third sentence of the paragraph.

"This may be the result of excessive inventories or the failure of the States to enforce a first-in-first-out usage pattern."

[GAO COMMENT: Sentence added.]

3. Under the section, PROBLEMS IDENTIFIED WHEN STATES CONTRACT TO PROCESS FEDERALLY DONATED COMMODITIES we have the following comments.

This section repeats many of the issues raised in a 1979 OIG report. The FNS response to that audit and the corrective action that has taken place since the audit are not noted. Therefore, we recommend that the paragraphs on pages 33-35 under this heading be revised as appropriate after considering the following comments.

While the OIG audit report of processing activities concluded that there are problems in the accountability of the donated foods used for processing agreements, we do not feel there is a "complete breakdown in accountability over the receipt, use and disposition of donated foods," as mentioned in the first full paragraph of page 34. Many States involved in processing do require companies to submit monthly reports of performance and actually compare company figures with recipient agency signed receipts. Also, performance report figures are checked against price and yield schedules which are submitted as an integral part of the processing contract. Many State distributing agencies require performance, supply and surety bonds from the processors to protect the value of the donated foods from further processing. While accountability over the receipt, use and disposition of the donated foods was found to be lacking in many instances cited in the OIG audit report, we believe it should not be assumed that the audit findings pertain to all States with processing contracts.

Since the audit cited FNS as furnishing little guidance in the area of processing, proposed regulations governing the processing of USDA donated foods were drafted and published as proposed rules in the Federal Register on June 24, 1980. The regulations in proposed form require FNS approval of contractual provisions prior to a distributing agency's approval of any processing contracts. The proposed regulations also contain provisions which strengthen procedures to assure that inventories placed with processors are properly accounted for and establish refined procedures to assure that processors are passing on price reductions or credits to recipient agencies for the value of the donated foods used in the processed foods purchased. Also provisions for on-site monitoring of processing activities will help identify problem areas of accountability in a more expeditious manner. As of March 16, 1981, the proposed regulations for

processing (with changes resulting from the ninety-day comment period afforded the general public) went into formal clearance procedures. The target date for publication as final rule is April 1981.

The new regulations also require State agencies to develop a processing contract manual as procedural and guidance material to be provided to recipient agencies and processors. This manual must explain the workings of the processing program within the particular State.

The regulations speak to the correction of all types of problems associated with processing, such as missing or late performance reports, negative or excessive inventory balances, no guarantee of full value pass through for the donated foods, lack of guidance from FNS headquarters and the FNS Regional Offices, etc. The corrective action requirements are carefully spelled out in the regulations which as noted above are soon to be published in the Federal Register.

[GAO COMMENT: USDA's comments are recognized in the final report. (See p. 34.)]

4. Under this section, OVERALL MONITORING BY FNS IS INADEQUATE we have the following comments.

The situations noted in this section are not representative of current Food Distribution activities. Therefore, we recommend that the paragraphs under this heading be revised after considering the following comments.

There are several reasons for the decrease in monitoring activities during the time period discussed in the report. Most notably, during the years immediately following the 1972 Russian wheat deal, surplus commodities were scarce and Food Distribution activities were significantly reduced. Consequently, there was a phasedown of programs and functions related to program operations such as monitoring. Since 1977, however, every Regional Office has conducted reviews of some State distributing agencies annually. Although Mountain Plains Regional Office did not conduct reviews in 1979, monitoring efforts were conducted in fiscal years 1978 and 1980.

[GAO COMMENT: As stated in the report (see p. 35), three of the four FNS regional offices we visited were not reviewing State distributing agencies on an annual basis as required by program regulations. Because FNS has only seven regional offices and one of the criteria we used in selecting the regions was high dollar volume of donated commodities, we believe our findings demonstrate a significant overall monitoring problem irrespective of whether the problem is or is not representative of all regions. Further, if there

was cause to reduce the monitoring function because of reduced activity, appropriate revisions of the regulations should have been made.)

Further, we are not in agreement with the observation that when annual evaluations of the State agencies were made, FNS did not always identify significant problems or management weaknesses. Your example of the Southwest Regional Office's failure to identify excessive commodity inventory levels in Oklahoma does not necessarily reflect the national experience.

[GAO COMMENT: While we agree that the Oklahoma situation does not necessarily represent the national situation, we believe it illustrates a significant problem in need of attention.]

During the last year, an in-house evaluation of the Division's Management Evaluation system culminated in extensive planning over the last several months to correct deficiencies in this area. In an effort to attain more complete program accountability, a more formalized system of Management Evaluation has been developed in the form of Comprehensive Management Evaluation Guidance. This tool may be used by both FNS Regional staff and distributing agencies to identify program strengths and weaknesses and to assess the effectiveness of the distribution system. In addition to annual on-site reviews based on the guidance, the Division is encouraging the Regional Offices to treat Management Evaluation as an ongoing process throughout the fiscal year. That is, an emphasis is being placed on maintaining constant communication between the Regional Offices and State distributing agencies regarding problems, corrective action, follow-up to corrective action and overall program improvement. The Management Evaluation Guidance will be updated each fiscal year to reflect changes in the program regulations and more effective ways to perform the monitoring function. In addition to new regulations, which are currently in clearance, requiring a Management Evaluation system, the Washington staff is now assisting the Regional Offices in conducting reviews of State distributing agency operations. The Washington staff also have been organized to receive copies of Management Evaluation reports, assess them, provide feedback to the Regional Offices, and to identify nationwide trends regarding problem areas.

Each Regional Office has provided a schedule of planned FD Management Evaluations for fiscal year 1981. Reviews are planned for every State distributing agency.

In an effort to ensure that a number of the more problematic areas are addressed during fiscal year 1981 management evaluations, five critical areas have been identified by the Division for the RO's to scrutinize very closely. These areas include: processing activities, warehousing and food storage practices, use of revolving funds, Title III elderly feeding programs, and the Food Distribution Program on Indian Reservations.

[GAO COMMENT: A summary of the cited actions has been added to the final report. (See p. 44.)]

CHAPTER 5 - DELIVERY ASPECTS OF THE COMMODITY DONATION PROGRAM CAN BE IMPROVED

We have the following comments on this Chapter.

1. Under the section, DELIVERY PROBLEMS LIMIT PROGRAM EFFECTIVENESS, we notice that all of the examples listed under the sub-section Late Receipt, on pages 46 and 47, are from the 1978-79 school year or earlier. We recognize the need to continually improve our performance in this area and believe that we did make significant progress last school year. Since the research for this report was conducted during school year 1979-80 and later, we would suggest that comments be added concerning the last school year. If in fact there was a demonstrated improvement, we believe it should be acknowledged in the audit.

[GAO COMMENT: At the time of our fieldwork, the 1978-79 school year represented the latest year for which complete data on commodity shipments was available. We made our review using this data. Because like data on commodity shipments for the 1979-80 school year was not available at the time of our review, we have no basis for drawing any conclusions regarding whether improvements were made during the 1979-80 school year in reducing problems with late receipt of commodities.]

2. On page 47, in the second paragraph of the sub-section, Late Receipt, we note that all of the donated food listed (except pineapple juice) as being received late by Pennsylvania were open allocation items during school year 1979 and could have been ordered as early as July 1978. Therefore, it appears to be unjustified to conclude that all shipments after March of 1979 were indeed "late receipts" due to FNS purchasing and shipping practices.

[GAO COMMENT: Although we conclude on page 59 that the donated commodity program's efficiency would be improved if food items were delivered to recipients in time for use by the end of the school year, we are not implying that all shipments received after March were "late receipts" due solely to FNS purchasing and shipping practices. In some cases the shipments were late because vendors missed shipping periods or States ordered commodities for shipment in April or May. In other cases movement of commodities from the vendor to the State distributing agencies delayed receipt of commodities. Accordingly, we have revised page 47 of the report.]

3. We concur that timely delivery and notification of shipments are problem areas to the domestic food program. One problem with late deliveries is in how late deliveries are defined. USDA contracts are on a shipping period basis meaning shipments are late only when vendors ship the commodity after the contract shipping period expires. Many of the problems regarding delivery also revolve around a misunderstanding of the term "shipment". To many of the recipients, prior to 1980, the term "shipment" was meant to be consistent with arrival of the finished product at the destination. During the past calendar year, considerable progress has been made in arranging for the Food and Nutrition Service (FNS) to indicate exactly when the commodity is needed or must be "shipped", and when ASCS must acquire the product and arrange to have it shipped to meet the "delivered" or usage date. We suggest that GAO recommend that the terms shipping period, delivery date, and date of receipt by recipient be clarified so that all parties will have a mutual understanding of the contractual provisions and program requirements.

[GAO COMMENT: We agree that a clear definition of the various delivery terms would be beneficial. However, USDA recognizes the problem and should be able to take the needed action without our specific recommendation.]

4. Since March 1980, ASCS has been attempting to make purchases of some commodities to coordinate with the period FNS expects the commodity to arrive. The 75-day advance notice that the Kansas City Commodity Office receives on FNS requirements has helped improve USDA's ability to schedule purchases and to make timely delivery. However, some States still find it difficult to forecast their needs far enough in advance for ASCS to purchase on an arrival date basis.

As stated earlier, much improvement has been made in the last year regarding the time recipients want commodities delivered. Much of the background data for this audit necessarily covered the period dating back to 1977, and we believe many of the complaints received by users would be nonexistent today.

[GAO COMMENT: In several recent interviews with State and school district officials conducted in conjunction with a review of the school lunch program, one of the officials' major complaints expressed about the commodity donation program has been the problem of scheduling delivery of the commodities. This is not to say, however, that improvements have not been made in this area.]

5. In addition to late deliveries, considerable emphasis has been placed on the notification to recipients of when the commodity is to arrive. Again, though, the draft does not acknowledge recent changes. We suggest mention be made of the

improved system whereby processors and/or shippers notify the KCCO on a 24-hour a day phone system. This system has helped get information to recipients more timely.

Further, we recommend the scope of shipments also be noted. While we recognize that notification of shipments is a problem, it must also be recognized that with as many as 200 shipments a day from many suppliers, 100 percent compliance will be difficult if not impossible to achieve. That is not to say that improvements cannot and have not been made.

[GAO COMMENT: Our draft report stated that KCCO maintains a 24-hour telephone system for vendors to call in advance notice of shipment. KCCO officials told us that the system generally works and gives them more control over commodity shipments. We revised the report to emphasize USDA's position that use of the 24-hour telephone system has helped to get advance notification to recipients on a more timely basis. (See p. 50).

[We are not suggesting that total compliance with the requirements for advance notification of shipments would be possible. Our draft report pointed out that, generally, distributing agencies in Missouri and Montana had received advance notification of shipments. However, for 22 percent of the 188 commodity shipments we reviewed in the two States, advance notice was received late or not at all.]

6. Another area causing many of the problems which is not discussed in the draft report is the way in which the donation programs are administered. For example, rarely, if ever, do commercial food companies today employ anything other than central warehouses where their products are received in units from full truckloads to unit trains, and are unloaded and stored for eventual distribution. In many cases our distribution program employs the use of rail cars as "traveling warehouses" where part of the commodity is unloaded then moved to another location. These "stop-offs" result in delays of a commodity reaching a final destination, extra damage from improper handling when the car moves on, and increased cost by vendors and/or USDA in providing routing. In addition, as a means of reducing costs, many of the railroads have either closed sections of unprofitable track or reduced the frequency of switching so products are either stored farther from intended usage points or spend much greater amounts of time in transit. We believe some mention of these points should be made in the report.

[GAO COMMENT: In discussions with vendors having contracts with USDA and with USDA commodity distribution and marketing officials, the difference between

centralized commercial storage and distribution program delivery practices was not advanced as a reason why shipments had been delayed. However, page 47 of the report has been revised to recognize USDA's comments.]

7. We have the following comments in regard to the section, PRACTICES FOR REDUCING ASSESSED PENALTIES FOR LATE SHIPMENTS NEED STRENGTHENING. While our documentation may have been inadequate at the time of audit, we believe provisions provided in contracts to ensure compliance with program needs are adequate and have been properly applied. As stated in the audit report, we follow established ASCS procedures for handling vendor appeals. Our marketing specialists adhere to these guidelines in reducing assessed penalties for late shipments. In addition, the file can be referred to our Traffic Management Division (TMD) for verification of the justification for delay and whether or not it was due to the railroad's inability to furnish cars or service. TMD makes inquiries and investigations as necessary.

[GAO COMMENT: Our report is not intended to suggest that contract provisions pertaining to compliance with program needs are inadequate or have been improperly applied. Furthermore, we would agree that marketing specialists do adhere to guidelines in actually reducing assessed penalties on late shipments. Our main concern, as indicated in the report, is whether the cases are sufficiently reviewed and documented, as called for by the procedures, to make a sufficient determination as to whether a penalty should be reduced. Our report also recognizes the Traffic Management Division's responsibility for contacting the carriers to certify the rail or truck equipment shortage, and we found the Division had made inquiries of the carriers. However, as stated in our report, some of these inquiries were not sufficiently documented to show the carriers' actions. (See pp. 53 and 54.)]

Contractually, articles 41 and 42 of USDA-1 state that the contractor shall not be liable for liquidated damages due to causes beyond the control and without the fault or negligence of the contractor. The contractor is required to furnish documents to substantiate the inability to perform. The inability to supply timely transportation is considered a justifiable cause to excuse liquidated damages, providing acceptable documents are provided.

[GAO COMMENT: We do not intend to suggest that there are no USDA procedures for reducing liquidated damages on late shipments that are due to causes beyond the vendor's control. Consequently, we have added wording to emphasize that the vendor is required to furnish documents to substantiate its inability

to perform for reasons such as lack of timely transportation. (See p. 51.) One of the primary points emphasized on pages 52-54 of the report is that generally such documentation was not available in the case files reviewed.]

Further, although we concur that contract files should be fully documented and reviewed before refunding liquidated damages, it is not clear whether the examples cited in the audit of little or no documentation are representative or rare examples. In either case, we agree that all determinations granting or denying variances in liquidated damages should carry the background documentation or adequate cross references to ensure the validity of the determinations.

[GAO COMMENT: Our examples cited on pages 53-54 were initially selected on the basis of dollar value without regard to the extent of case file documentation. Cases were not included or excluded from the report on the basis of the amount of documentation available.]

As recently as June 20, 1980, a notice was mailed to all ASCS food suppliers notifying them of the problems and hardships late shipments cause the recipients of the food. At this time we listed the provisions of the contract requiring compliance with deliveries and the options available to the Agency for failure to perform. To further emphasize our commitment for having shipments made timely, we raised the rate of liquidated damages five cents per hundredweight per day, which, in most cases, was a doubling of the previous rate.

Therefore, we suggest the report include some discussion of the action that has been taken to strengthen the program and improve performance in this area.

[GAO COMMENT: We revised page 54 of the report to recognize the June 20, 1980, notice. The draft report had recognized the increase that was made in the penalty rate for late shipment. We have added, however, that ASCS officials had varying opinions as to the potential effectiveness of the penalty rate increase. (See p. 55.)]

8. We have the following comments concerning the section, FNS DELIVERY REQUIREMENTS CAN INCREASE USDA TRANSPORTATION COSTS. As outlined in the audit report, there have been past studies of f.o.b. origin versus f.o.b. destination purchases, and we are in general agreement with the principle of f.o.b. destination purchases. We recognize that there are advantages to purchasing on a destination basis, but not all commodities can be purchased on this basis. For example, some dairy products (evaporated milk and infant formula) are purchased on a destination basis because it

is the prevailing practice used in commercial operations. In addition, the quantities required by FNS, when they will be needed, and destinations for these products are relatively stable factors. In contrast, purchases of butter, cheese and nonfat dry milk (in bulk form) are carried out to support the price of milk. These purchases must be made on an origin basis and subsequently shipped to warehouses for storage and/or processing plants. Destinations and exact quantities are not known for these products at the time of purchase. Consequently, it is not possible nor efficient to have a uniform system for the purchase and delivery of all commodities. The criteria used to decide which type of purchase to use must be weighed carefully. Therefore, we suggest this report recommend that USDA develop criteria for determining which type of purchase method to use. Such criteria should include (a) USDA program objectives, (b) prevailing practices used in commercial operations, (c) potential costs of operating the programs, and (d) realignment of procurement resources such as manpower, space and equipment.

[GAO COMMENT: We did not intend to suggest that all commodities can be considered for purchase on an FOB-destination basis or that one uniform procurement method could be used. During our review, ASCS officials expressed their concerns regarding any attempted purchase of certain price-support-type commodities on an FOB-destination basis. However, because we limited our review to commodities purchased for the commodity donation program, we did not incorporate these comments into the report. We did note that one price-support-related item--mozzarella cheese--could be purchased on an FOB-destination basis. Although ASCS normally procured mozzarella cheese on an FOB-origin basis, it agreed to test purchase the item on an FOB-destination basis.]

[In February and April 1981 USDA purchased about 4.65 million pounds of mozzarella cheese on an FOB-destination basis. An ASCS official told us that because of weak dairy prices, USDA has not been able to assess the cost savings made possible by purchasing on the FOB-destination basis. We revised page 57 of the report to reflect this latest information.]

[We believe USDA has set forth a valid recommendation regarding development of criteria to determine the type of procurement method to be used. Since USDA recognizes the need to develop specific criteria, we see no need to make a specific recommendation on this point.]

CHAPTER 6 - CASH, COMMODITIES, OR LETTER OF CREDIT?

We appreciate GAO not making recommendations on this subject in light of the three-year mandated study. However, we believe

the chapter would be more balanced if you discussed the disadvantages of the two studies mentioned, rather than just the advantages. For example, of major concern to us is the implications for agricultural impacts. Most proponents of the alternative system do not address the food donation objective of price support and surplus removal. We recommend some treatment in the report of the following concerns should the alternative systems be adopted: outlets for donation of CCC inventory items; ability to maintain other commodity programs such as the Needy Family Program on Indian Reservations and our ability to respond to disaster relief feeding needs.

[GAO COMMENT: We believe that these points, which we have added on page 70, should be thoroughly considered before any adoption of an alternative system. However, our review was not directed at the above issues and therefore we cannot comment on them at this time.]

APPENDIX I - COMMODITY DONATION PROGRAM: LEGISLATIVE BASIS, PROGRAM OPERATIONS, AND MAJOR RECIPIENTS

We have the following corrections for insertion in this Appendix.

1. In the first paragraph on page 71, sections 32, 416 and 6 should be referred to as "three major pieces of legislation," since there is other related legislation (referred to in the GAO report) which affects the acquisition and donation of commodities. Also, the code reference for section 6 should be changed to 42 U.S.C. 1755.

[GAO COMMENT: Paragraph revised.]

2. The third sentence of the first full paragraph on page 72 should be removed and inserted after the first sentence of the fifth paragraph on this page (under Section 416). The Department does not store commodities purchased under Section 32 surplus removal activities for return to the market. Section 32 commodities are permanently diverted from the normal channels of trade.

[GAO COMMENT: Sentence revised.]

3. In the first full paragraph on page 72, please change the second sentence to read: "Section 14 of the National School Lunch Act (7 U.S.C. 1431) authorized the expenditure of funds from sections 32 and 416 to purchase, for child nutrition programs under that Act and the Child Nutrition Act of 1966, as well as for elderly nutrition programs under the Older Americans Act of 1965, agricultural commodities which are customarily acquired and donated under those sections."

[GAO COMMENT: Sentence revised.]

4. The following paragraph should be added on page 72 as the last full paragraph: "Section 709 of the Food and Agriculture Act of 1965, as amended (7 U.S.C. 1446a-1) authorizes the Secretary of Agriculture to purchase with funds of the Commodity Credit Corporation (CCC) dairy products for schools (other than fluid milk), domestic relief, community action, foreign distribution, and other authorized programs when CCC dairy stocks are insufficient. This authority has been used infrequently."

[GAO COMMENT: Paragraph added.]

5. The following paragraph should be added on page 73 after the first paragraph under Section 6: "Section 6 also establishes the mandated national average value of commodity assistance for lunches served in the National School Lunch Program and for lunches and suppers served in the Child Care Food Program at 10 cents per meal. That amount is subject to annual adjustments to reflect changes in the Index for Food Used in Schools and Institutions."

[GAO COMMENT: Paragraph added.]

6. The following text change should be substituted for the third paragraph on page 74:

"Following this, FNS determines through surveys the quantities of commodities desired by the States. Matching school preferences with parity and surplus removal considerations are all taken into account in the development of final purchase plans.

Following approval of such plans, FSQS issues a Food Purchase Report announcing the forthcoming purchases and also mails announcement/invitations and other applicable documents to all prospective bidders, trade groups, and magazines, associations, and other interested parties on agency mailing lists.

Bids are requested on an f.o.b. origin or destination basis depending on the type of commodity being procured. In order to meet distribution needs and avoid prolonged storage, procurement for frozen meat and poultry items are generally made on a weekly or biweekly basis from late summer to early spring. Fruits and vegetables, being seasonal products, are usually purchased once yearly following harvest, with staggered delivery periods.

Offers accepted are those considered to be the most advantageous to USDA considering price, transportation costs, and other factors. In analyzing bids, personnel compare prices offered with raw material prices quoted in USDA market news reports and list prices quoted in trade reports, magazines,

journals, etc. Also considered for those programs operating on a continual basis is the supply/price outlook for future procurements.

Following approval of awards at the Agency level, a Food Purchase Report is issued and successful bidders are notified."

[GAO comment: Section revised.]

7. On page 75, insert the following sentence after the first sentence in the third full paragraph: "However, as a result of the Omnibus Reconciliation Act of 1980, beginning in school year 1981, USDA no longer offers commodity assistance to school breakfast programs based on the number of meals served."

[GAO COMMENT: Sentence added as footnote.]

8. The final paragraph on page 75 under Child nutrition programs should be revised as follows to reflect FNS actual program obligation statistics for fiscal year 1980 and to include commodity information for the summer food service and child care food program: "Funds are provided by direct appropriations and through transfer of section 32 funds. In fiscal year 1979, USDA provided about \$2.7 billion to the States for child nutrition-related expenditures and about \$668.4 million 1/ in commodities or cash in lieu thereof. In fiscal year 1980 regular cash expenditure increased to \$3.1 billion, while the value of commodities or cash in lieu thereof supplied to all child nutrition programs (schools, summer food service and child care) was about \$843.3 million. 2/

[GAO COMMENT: Paragraph revised.]

9. In the second paragraph on page 76 under Commodity and Supplemental food programs, the first sentence should read: "The Commodity Supplemental Food Program was originally authorized under the Department of Agriculture and Related Agencies Appropriation Act of 1969 (Public Law 90-463); the Food and Agriculture Act of 1977 (Public Law 95-113) extended the program through fiscal year 1981." The third sentence of this section concerning Indian reservations should be deleted; in fact, only two of the twenty projects are located on reservations. Also, please revise the final two sentences to read as follows: "The number of projects ranged from a high of 23 in October 1979 to 20 in September 1980, with an average monthly participation of 102,500 persons. About \$21.8 million in commodities were distributed."

[GAO COMMENT: Paragraph revised.]

1/Includes \$69.6 in bonus commodities.

2/Includes \$137.3 in bonus commodities.

10. On page 77 please change the second full paragraph to read as follows: "Agricultural commodities are provided to needy households living on or near Indian reservations and to such households in the Trust Territory of the Pacific Islands and the Commonwealth of the Northern Marianas. Cash assistance is provided to these distributing agencies to assist them in meeting operating and administrative expenses."

[GAO COMMENT: Paragraph revised.]

11. The fourth paragraph on page 77 should be revised to read as follows: "Average monthly participation was 74,827 in fiscal year 1980. During that year, \$24.6 million in commodities were purchased for the needy family program, including about \$12.7 million in Section 416 commodities and \$11.9 million in commodities provided under section 4(a). Some \$6.6 million in administrative expenses was budgeted (out of fiscal year 1980 Food Stamp Program appropriations) for States and Indian Tribal Organizations conducting distribution to households."

[GAO COMMENT: Paragraph revised.]

12. On page 77, in the first sentence of the last paragraph, the number of meals served in fiscal year 1980 should be changed to 166 million meals, and the last sentence of that paragraph should be revised to read: "Commodities valued at \$14.6 million and \$54.1 million in cash in lieu were provided for the elderly nutrition program in fiscal year 1980."

[GAO COMMENT: Paragraph revised.]

13. The second and third sentences of the final paragraph on page 78 should read: "During fiscal year 1980, commodities valued at about \$64.7 million were distributed to some 7,400 institutions serving approximately 888,000 needy persons. Some 4,600 summer camps serving about 84.4 million meals received donated foods valued at \$4.7 million in fiscal year 1980."

[GAO COMMENT: Paragraph revised.]

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