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An Analysis of the Commodity Import Program in Vietnam and Proposals for Changes in Administrative Controls

I. Introductory Matter

A. Scope of This Paper

This paper will attempt to determine the major forms of abuses which can be associated with the Commodity Import Program in Vietnam; to analyze the motivation which activates importers and the mechanics by which these abuses are accomplished; to distinguish, if possible, these abuses from abuses which may characterize commodity import programs in countries other than Vietnam; and, finally, to suggest specific changes in the conceptual framework and in the management, operation, and regulatory mechanics of the program which, on the basis of the analysis, appear best designed to prevent, to dissuade, and to overcome these abuses.

B. Commercial as Distinguished from Public Policy Abuses

Abuses associated with the CIP may, for analytical convenience, be distinguished as "commercial" or "public policy" abuses. Commercial abuses are those defects in the sale transaction which result in a commercially tainted transaction: the importer does not get what he ordered from the supplier; he gets too few units or defective units; the importer is charged a higher price than the price which the supplier would charge if he were not shipping to Vietnam; the supplier makes a kickback to the importer; or -- in one of its many varieties -- the importer and the supplier go through a mock sales transaction in order to achieve for the importer an exchange of his local currency into AID dollars. These are, in effect, typical Regulation 1 concerns.

The term "public abuses" can be applied to public relations and public-policy concerns with the Program which are not strictly commercial in nature. The non-commercial abuses concern AID rather than the mercantile parties. Foremost in this category is the abuse which relates to the procurement under AID financing of an item which AID has declared "ineligible." For public relations reasons, the Program as a whole may be discredited if the wrong item enters Vietnam under AID financing even if that item is earnestly desired by the importer and even if the importer can realize, upon domestic resale, a handsome profit in satisfying local demand for that product. General examples of such ineligible items are luxury goods, fripperies, salacious material, and items which satisfy highly specialized or unusual tastes. Another major public concern for AID is the US-Government balance of payments interest associated with the operation of the Program. The balance of payments concern - i.e., minimizing US dollar outflow - like the ineligible item problem, strikes at the domestic and at the Congressional image projected in the United States for the Program.

In the following sections of this paper an attempt will be made to consider in some detail the mechanics of each of the commercial abuses. In this regard, abuses will be analyzed in terms of those which fall peculiarly within the sphere of the importer; those which fall peculiarly within the sphere of the commodity supplier; those which fall within the sphere of other participants in a CIP transaction (ocean carriers and banks); and, of course, in the largest category of all, those which require a degree of concert of action between two or more of the parties participating in the movement of AID-financed goods to Vietnam. An attempt will be made to set the abuses into an overall, explanatory theory which, in general terms, rationalizes the conduct of the mercantile parties and analyzes the vulnerability of the Program to exploitation by them. This exploitation has as its objective forms of private gain which are not congruent with the realization of Program objectives as those objectives are, or should properly be, contemplated by AID. It is best therefore to begin with an articulation of this general theory.

II. The Vulnerability of the Program to Exploitation: The Use of "Strangers" to Carry out Program Objectives

The conceptual underpinning for mechanics of the CIP is derived entirely from the theoretical basis and the assumptions which AID propounded in developing commodity import programs for countries other than Vietnam. The flowering of this intellectual effort is represented by the approach to commodity financing and by the control mechanisms, such as they are, set forth in AID Regulation 1. It is, in effect, the only approach which AID has ever used since the inception of the Foreign Aid Program.

The theoretical assumption from which AID proceeds is that it is only a banker; that an importer in an aid-recipient country, chosen by his government, should be able to choose any supplier who can supply him with the goods which he desires; that this supplier -- a stranger to AID -- will be sufficiently motivated by pressures which the marketplace imposes upon him (i.e., competitive forces and business integrity) to honor the sales commitment which he has undertaken to the importer; that in the expectation that the supplier will in fact perform his sales undertakings properly, AID may pay him in return for his promise that he has performed and his representation that he has abided by certain AID rules; that to collect these promises and undertakings it is sufficient if AID uses the services of commercial banks which collect the pieces of paper on which the promises are printed and which, in exchange, for these pieces of paper pay out A.I.D.'s funds; that to carry the goods it is sufficient if the commodity supplier makes his own freight arrangements and brings the goods to the chosen carrier who will give the commodity supplier the requisite piece of paper -- the bill of lading -- which will permit the supplier to be paid by the bank; and that the commodity supplier should be paid for securing, in whatever fashion he deems appropriate, those special or necessary services in connection with his sales undertaking which insure his proper performance: he will secure the proper inspection of his goods; he will properly pack and store and insure the goods and will properly accomplish all those other things which a supplier of good repute and of good standing, acting in good faith, and subject to the discipline of the marketplace, can be expected to perform.

In short, AID pays money to the commodity supplier, not chosen by AID, who is a stranger to AID. That stranger gets paid by another stranger to AID -- the U. S. bank. The commodity supplier moves his goods to Vietnam by yet another stranger -- the ocean carrier. At every stage in the transaction, when an inspector must be secured, when a freight forwarder must be chosen, when an insurer must be procured, the strangers who receive AID money deal with other strangers of their own choosing. At every stage AID collects only promises. It pays out its funds in return for broadly worded, vaguely phrased promises from strangers who are not in the slightest put off by the need to make promises in order to collect cash-in-hand (sometimes in large amounts) and who are eager to play "catch me if you can" with respect to their promises.

It is the premise of the balance of this paper that because AID at every critical stage of the sales transaction deals with strangers which choose each other as participants in commodity transactions, the Program is vulnerable to exploitation. It is a corollary of this vulnerability observation that the normal market forces which AID depends upon to motivate and, indeed, to coerce these strangers into acting properly (i.e., into honoring their sales commitments to importers and their promises to AID) are woefully inadequate; as a general matter these normal market forces cannot be expected to work, and, as a specific matter with respect to Vietnam, they do not work and will not work.

This observation is central to the analysis presented by this paper. It will be illustrated in detail at each level of discussion. The marketplace assumption which underlies AID's commercial-regulatory mechanics for financing commodity imports into Vietnam will be tested in considering the abuses which lie in the sphere of the importer and those which lie in the sphere of the supplier. After this examination, the suggestions for remedial changes in the Program will once again belabor the point that marketplace mechanisms have failed AID in carrying out the CIP: accordingly, alternative control mechanisms which deserve consideration must proceed from the contrary assumption that marketplace discipline does not adequately protect AID's interests in AID-financed sales to Vietnam.

The most extended and most detailed analysis of the vulnerability of the Program should begin at the beginning of the import cycle--i.e., with the allocation to an importer by the Government of Vietnam of the use of A.I.D. dollar credits for the import of goods into Vietnam. When the importer has a license approved by the Government of Vietnam he becomes master of an asset. How A.I.D. expects him to use that asset and how he may in fact be motivated to use it in the marketplace contrary to A.I.D. expectations is the subject of the next section of this paper.

III. Abuses in the Sphere of the Importer

A. The Importer's Motivation: the Economic Axiom Does Not Apply to Vietnamese Importers

The marketplace assumption which underlies the commodity import program posits that the Vietnamese importer is really no different than an importer in a developed country; and since classic economic analysis has known for 200 years what it is that the merchant in any developed country really wants, it is assumed that A.I.D. also knows what the importer in Vietnam really wants. Two hundred years ago Adam Smith first stated the single axiom which underlies all (or nearly all) free enterprise thought: with the expenditure of each unit of money, the merchant dealing in goods seeks to maximize his profits by securing for himself the largest number of the best goods at the cheapest price which he can obtain for the money which he has to spend. The merchant seeks to buy cheap and resell at the best price; he maximizes his profit by maximizing the difference between his purchase price and his resale price. The merchant accumulates wealth by maximizing this spread between purchase and sales prices.

It is in the nature of an axiom that one does not argue with it; one accepts it on faith. The axiom and theories built on it no doubt do apply to commercial sales between U.S. merchants and between U.S. merchants and merchants in developed countries. It is likely that this body of economic thought also has great relevance for A.I.D.-financed sales to certain cooperating countries. It is, however, the purpose of this section to demonstrate that this body of thought exercises less relevance in connection with the motivations which guide Vietnamese importers in using A.I.D. dollar credits.

The axiom bears less relevance to the Vietnamese merchant because the assumptions which underlie the axiom are not present in Vietnam. One or more of these assumptions may also be lacking in certain other A.I.D. countries. But the situation in Vietnam is so extreme that, unlike other aid-recipient countries in which one or two of the assumptions underlying the axiom do not apply, all the assumptions in Vietnam are different. Specifically:

1. <u>The "Tomorrow" Assumption Which Underlies the Axiom is Missing in Vietnam</u>

   A merchant who is in foremost degree interested in buying the most of the best goods at the cheapest price so that he can resell these goods and thereby maximize his profit envisages a stable economy at least for a period long enough for him to sell the goods and enjoy the resulting profits. Such a merchant can see himself in the particular, business-activity future. The Indian importer who goes through an import procurement can see himself getting the goods several weeks or several months after concluding the sale with the foreign seller. He can see himself storing the goods, selling them, realizing a profit; he projects how he will use the profit, whether to spend the income upon himself or to re-invest the funds and to repeat the buying-and-reselling cycle. The Indian, the Brazilian, the Iranian importer does not perform his commercial activity under the shadow and at all times in the fear that there will be no commercial tomorrow either for him or for the economic class to which he belongs.

It is a paramount feature of the war in Vietnam that the outcome of the struggle may well determine the form in which commercial activity will be conducted; it may determine the identity of the merchants who will conduct that commercial activity; and it may determine what commercial activity will be permitted and who shall be able to make a profit. If the Communist forces win the battle in Vietnam, there can be little doubt that the Vietnamese merchant class which has to date dominated the commercial scene will be eliminated or reduced in number, but surely drastically affected. Each importer now active in Vietnam is surely aware of the consequences which might engulf him personally, the consequences which might engulf his business and his industry, should the war take a sudden turn. In short, the Vietnamese merchant, unlike merchants in developed countries and those in other A.I.D. countries, does not necessarily see a tomorrow for himself in a stable economy in a stable society and may not even see a tomorrow for his type of business activity. If there is necessarily no tomorrow for him, why should he, in fore-most degree, be concerned with buying goods at the cheapest price and reselling them, all this to take place over an extended period of time?

The tomorrow assumption, from among the several which underly the basic economic axiom, is the most important and deserves amplification. When the merchant may have in his country no personal or business tomorrow, the motivation which drives the merchant can only be to assure for himself, as best he can, a personal or business tomorrow elsewhere. That tomorrow must envisage a partial or a full life outside Vietnam. The merchant must do what he can--and this must be his primary motivation--to reserve for himself a back door to survival. He must have in his pocket an airplane ticket out of the country; and he must have somewhere to go. Before the last minute, his family and much of his assets must be out of the country.

In sum, the merchant must have a place in France, Hong Kong, Thailand, or elsewhere to run to if he is to save himself. And if he is to plan intelligently, he will have a home and a bank account outside of Vietnam to provide for this eventuality.

If this is the necessary motivation which results from a no-tomorrow assumption, how is it borne out by the facts? One would expect Vietnamese merchants to have foreign passports in their possession or other exit documents which would permit them to leave Vietnam in the event that military events take a sudden turn for the worse; one would expect that large numbers of less optimistic merchants would have their families already safely abroad. But, most importantly, one would expect every prudent merchant to provide for the ultimate eventuality by accumulating hard currency funds: only such funds can help him in the day of emergency.

The no-tomorrow assumption, if correct, leads an importer to maximize his accumulation of hard currency in a country with the weakest of currencies. Using A.I.D. import credits in their entirety to import goods and then, in accordance with the classical axiom, to resell those goods in the local market for local currency will not achieve for the merchant any accumulation of hard currency. The importer must therefore find ways in which he can transform his local currency (i.e., transform his control over the dollar credit) into a hard currency balance over which he has exclusive control.

2. <u>The "Usability-of-Funds" Assumption Which Underlies the Axiom is not Present in Vietnam</u>

A merchant wishes to acquire the largest number of the best goods at the cheapest price only if the form of the profit which he realizes is meaningful to him.

A local currency profit on the sale of goods by a Vietnamese merchant has some usefulness to the Vietnamese merchant. It does not, however, have the same kind of complete usefulness which is necessarily an assumption of the economic axiom. The axiom does not consider the limited usefulness of certain types of currency. On the contrary, the assumption which underlies the axiom is that the money accumulation which the merchant seeks to maximize is a form of currency which will buy for its owner anything that money can buy; it is for this very reason that the merchant seeks to maximize his holding of money. When the economic axiom is employed in the United States to support a system of economic planning and analysis, it is not necessary to challenge this assumption. Clearly a dollar will buy for its owner whatever money can buy. But for the Vietnamese holder of local currency a piaster will not buy whatever money can buy. It will not, for example, buy everything that a dollar will buy.

There are several other currencies like the dollar--the hard currencies of the world--which will buy anything in the world. There are other currencies which are not quite as hard. These semi-hard currencies are acceptable in the marketplace, perhaps at a substantial discount, but nevertheless acceptable. Such currencies are, for example, the Korean currency, the currency of many Latin American countries, possibly also the currency of Pakistan and perhaps even that of India. But the currency of Vietnam is particularly undesirable in the financial centers of the world. Because of the war, Vietnam has almost no exports. Merchants in other countries have no incentive to accumulate piasters with which to pay for Vietnamese exports. Secondly, the Vietnamese currency is subject to very wide swings in exchange value and the official exchange rate is highly artificial. Moreover, in the event that military activities in Vietnam suddenly break away from the existing pattern, the entire sub-structure which underlies the currency may quickly change or evaporate. For these reasons (which can of course, if necessary, be further amplified), Vietnamese currency will buy outside of Vietnam almost nothing. The Vietnamese holder of local currency will find therefore that the range of products in the world not available in Vietnam cannot be obtained even with limitless amounts of local currency even if the Vietnamese merchant is willing to take a substantial discount on his money from the official rate. In sum, the money which the merchant acquires from his economic activity can satisfy only a portion of the broad spectrum of his needs. Only dollars will satisfy the entire spectrum of his needs and, most importantly, his most pressing need--that of preparing for the eventuality of a tomorrow outside of Vietnam.

Even apart from the no-tomorrow assumption, the merchant of wealth can acquire a luxury appliance, an automobile, a foreign trip or a foreign education for his children only with hard currency. Even brilliant economic activity which results in buying the largest number of the best goods at the cheapest price and reselling them at the highest prices in the local marketplace, will not realize the hard currency which the merchant must accumulate to satisfy these needs.

3. The Multiplicity of Rates of Exchange Between Local Currency and Dollars is Contrary to the Assumption Which Underlies the Economic Axiom That There is Only One Rate of Exchange

The economic axiom presumes that the merchant wishes to buy and sell because that is what he must do with goods in order to maximize his profits. Under the economic axiom no thought is given to the possibility that the buyer of goods can make his profit in the transaction through an activity not directly related to handling the goods. In the import situation, the economic axiom necessarily assumes one rate of exchange: The importer takes his currency, exchanges it in the marketplace or through his central government for the currency which the seller must receive for his goods; thereafter, the importer follows the normal marketplace motivation to acquire the goods and to resell them. The situation changes dramatically when there are two or more rates of exchange and when these rates of exchange vary widely. When the official exchange rate is less than the unofficial exchange rate by a wide margin, an importer who gains control over the right to import goods may be able to realize a profit even without securing the largest number of the best goods at the cheapest price. If the spread in the exchange rates is large, he may be able to earn a profit without ever getting the goods; if the spread is not so large he will make a profit on the transaction even if he deals in poor quality goods, or if he acquires fewer goods for the expenditure of each unit of money. What is important is to maximize his profit by playing the exchange-rate game. Merely acquiring control over a $10,000 import asset--the right to import $10,000 worth of goods--for an equivalent in local currency at the official rate puts the importer in a favorable currency conversion position: after all, the goods which he will acquire will, of course, be valued in the local market at the unofficial exchange rate and this will be true whatever he imports.

The thought which underlies this observation will be further developed in describing the basic mechanism for the conversion of local currency into dollars.

4. Conclusion: Three Major Assumptions Which Underlie the Economic Axiom are not Present in Vietnam

Three major assumptions which underly the economic axiom are not present with reference to economic activity by Vietnamese importers. The most important of these assumptions concerns the no-tomorrow observation which is peculiar to Vietnam. The second assumption is that profits realized in a certain currency must be useful for a wide range of economic activity; in fact however the local currency in Vietnam is a particularly weak currency useful for only limited undertakings. In this regard, the mistaken premise behind the second assumption is not peculiar to Vietnam; but the range of usefulness of Vietnamese currency is probably more limited than that of most other A.I.D. countries. The lack of the third assumption -- the "one-exchange-rate" assumption -- finds a parallel in certain other A.I.D. countries which also have wide spreads between official and unofficial rates.

As a fair generalization it may be said that the assumptions which underlie the economic axiom that an importer seeks with the expenditure of each unit of his funds to obtain the largest number of the best goods at the cheapest price so that he can maximize his profits by reselling do not apply in Vietnam and that what the Vietnamese importer truly wants, if not exclusively then at least in measureable part, is to accumulate for himself dollar balances. What the importer really wants when he acquires control over an A.I.D. credit is to transform as much of that credit as he can into a cash transfer for his own benefit. The importer must deal with import licenses and with dollar credits because this is one way-- and there are no doubt also other ways--for him to realize his dollar accumulation objective. The abuses which he makes of his control over the dollar credit are designed therefore to achieve his dollar accumulation goal.

B. Transformation of Import Credits Into Private Cash Balances

The importer can transform an import credit into a cash balance through legal or illegal methods. Both types of activity must, in a larger sense, be listed as abuses. Both types of abuses are, in a larger sense, efforts to defraud A.I.D. and/or the GVN.

Abuses of a legal nature will generally realize for the importer only a partial transformation of the credit into a cash balance. Illegal abuses within the sphere of the importer will generally (but not always) require the cooperation--of an active or passive nature--of the commodity supplier or some other participant in the sale transaction. Illegal abuses may render for the importer a relatively large and perhaps even a complete transformation of the import credit into a dollar cash balance.

1. The General Theory

For the transformation from import credit to cash balance to take place there must be a spread between the value of the import credit (generally, the "price") and the actual cost of the goods (and related services) to the person receiving the price; i.e., the importer can only get dollars out of the credit to the extent that the commodity supplier has dollars to give after subtracting the cost of the goods (and related services) from the price received. In mathematical terms the simple principle may be illustrated as follows: If the supplier receives $100 for his goods and the goods cost him $80.00, the supplier has $20.00 left over. He has therefore $20.00 which he may pay out as a "commission"; which he may kick back to the importer; or which he may otherwise dispose of in a manner which will gain for the importer his objective. If the commodity supplier receives $100 and the goods cost him only $10.00, the supplier has $90.00 with which arrangements suitable to the importer can be made. The importer therefore must always deal in goods in which there is something left over for him; he will preferably deal with goods in which there is a great deal left over for him.

2. Legal Abuses

a. Credit Transformation into a Cash "Commission"

Until January, 1967, it was completely lawful for the importer to buy goods with respect to which the supplier paid a healthy commission. Since the importer could choose the supplier and could choose the commodity he wished to purchase, the importer, who was properly motivated, would simply choose a supplier willing to pay the kind of commission which the importer insisted upon receiving. Whether the supplier chose to report or not to report the payment on A.I.D. forms was of relatively minor significance since the payment of a commission was itself completely lawful both under A.I.D. regulations and American and Vietnamese law. The importer would simply designate his competitor, his friend or relative, or himself (under another name) as the sales agent to receive the commission. In this manner the importer could buy goods with respect to which a commission was earned and paid in dollars.

Normally, this commission would of course be paid outside of Vietnam; but even if it were paid in Vietnam, the importer was usually able to gain complete control over the dollar amount. The commission moreover actually cost the importer nothing, since the spread between the official and the unofficial rate (somewhere in the neighborhood of 30% or more) generally covered the entire amount of the commission. Thus, if the importer put up $70 worth of local currency to acquire a $100 credit and if the importer received a $30 commission, it would follow that the importer received goods worth $70 in local currency plus a $30 cash commission. By this calculation, the importer was ahead of the game in collecting dollars if he merely received goods valued at the dollar equivalent of the local currency which he paid to get those dollars.

The commission route to dollar accumulation had one major variation. Instead of getting a commission for securing the sale, the importer might receive a "service payment" for performing--either allegedly or in fact--certain services on behalf of the supplier: he might promote the supplier's product; he might distribute free samples; he might "survey" the goods; he might erect the machinery or honor the supplier's warranty; he might, in fact, do nothing and collect the service payment. The service route, moreover, had the virtue of not even being reportable on the A.I.D. forms.

A.I.D. recognized the possibility that the commission route was being used to transform import credits into cash balances and in January 1967 added new provisions to §201.65 of Regulation 1 to regulate dollar commission payments more strictly. These rules seek to prevent payment of commissions with dollar funds and to assure that commissions will be paid only in local currency. Closing the commission loophole has, however, merely caused importers to shift to other related schemes. There is little doubt that although the rules have discouraged U.S. suppliers from paying dollar commissions to importers in Vietnam, they have failed to alter the pattern of cash flow which importers require. This conclusion is made necessary by the following observations:

(1) When A.I.D. audited closely transactions covered by letters of credit issued prior to January 1967 it was common to find a commission payment moving to a local agent in or outside of Vietnam. Such commission payments would frequently amount to sums in excess of 20% of the purchase price financed by A.I.D. Moreover, commissions or service payments were frequently paid even if the amounts were not reported on A.I.D. forms. On such forms the average commission on sales to Vietnam approximated 6%.

(2) Since the new rules were promulgated, A.I.D. forms executed by A.I.D. suppliers indicate commission payments totalling less than 1% of the total amount financed by A.I.D.

These observations justify the conclusion that importers are now using other techniques to achieve their aims; or, in the alternative, importers are choosing suppliers who are willing to make payments as commissions or service payments without reporting them at all to A.I.D.

b. The Importer as Supplier

An importer can earn a dollar profit on a sale transaction if he can arrange the sale under A.I.D. sponsorship in such a manner that he or his representative receives A.I.D. funds as the A.I.D.-financed supplier selling the goods to the A.I.D.-financed importer. Thus: the importer has a U.S. company or a firm outside of Vietnam buy U.S.-made goods from a seller in the U.S. at a price of, say, $10 per unit. The purchasing firm then acts as a secondary supplier by reselling the goods to the Vietnamese importer at, say, $100 per unit. As a result, the secondary supplier, controlled by the importer, has realized a profit of $90 on the transaction. In the process, and quite incidentally, the importer has also acquired goods worth $10 per unit. The importer is only marginally interested in the goods. He is content to receive in local currency whatever he can get for the goods for which he has paid $10 per unit (in fact, for which he has paid nothing, assuming a currency exchange differential between official and unofficial rates). Most significantly, he has in the process of controlling the right to import goods accumulated $90 in cash.

The extent to which this practice prevails is unknown. But there are some interesting indicators which are relevant in gauging the probable extent of this practice. It is a feature of the Commodity Import Program in Vietnam that in an unusual number of export sales from the United States secondary suppliers receive the AID funds. Producers-suppliers probably appear in the minority of cases. Secondary suppliers are especially prevalent on import sales by private importers, whereas producer-suppliers can most frequently be found on sales to GVN entities. Moreover, it is not unusual to find a non-US company participating in US-source sales. Thus, the Hong Kong seller may receive AID funds for selling US-source goods. Of indeterminate importance (but no doubt great relevance) is the fact that AID does not even know, on the basis of the documents which it collects, whether a non-US company has in fact received a portion of the profit on the transaction. For example: Importer A contracts with Hong Kong firm B which A controls or has set up for this purpose. The contract between A and B provides for a unit price of $100. B contracts with C, a US seller of the goods, at $50 per unit and arranges with A to have the letter of credit opened in favor of C in the United States for the full $100. C then ships the goods directly to Vietnam, collects the $100 under the letter of credit and credits B with the $50 to which B is entitled under his contract with C. The documents which C submits to the bank note C as the supplier and do not note the involvement of B. Under this scheme, B has collected $50 (and, at that, free from US taxes); C is listed as the supplier of record; and A has achieved his objective of transforming 50% of the AID credit into dollars and in the process also acquiring some local currency for himself (from the re-sale of the goods) with which he can renew the cash transformation cycle.

This technique for cash transformation lies peculiarly in the sphere of the importer. It is no doubt being practiced by sophisticated importers. And it is, at present, lawful under AID regulations.

3. Illegal Abuses in the Exclusive Sphere of the Importer.

The importer can by his own efforts achieve partial or complete cash transformation by first buying marketplace goods in the United States and reselling them for dollars (rather than, as A.I.D. expects, for local currency) either before or after the goods reach Vietnam.

a. Sale Before Goods Reach Vietnam.

As soon as the commodity supplier secures a bill of lading from an ocean carrier, he can rush to the bank to get paid under his letter of credit. The supplier's right to get paid is not in any way conditioned upon the arrival in Vietnam of the goods. The commercial documents pass through the U.S. bank to the commercial bank in Vietnam which has opened the credit at the request of the importer and which is financing (in whole or in part) the local-currency obligation of the importer. The commercial bank retains the bill of lading until the importer satisfies his local-currency debt to it. When the importer satisfies his local-currency obligation, the commercial bank releases the bill of lading. After that, the commercial bank is no longer interested in the transaction.

Under these circumstances, it is possible for an importer who has in his possession the bill of lading document to direct the vesselowner to discharge the goods at a port other than a port in Vietnam. Especially where the importer (or his representative) is the time charterer of the vessel, it is the importer who with his left hand issues the bill of lading to his right hand: it is the importer who, as owner of the goods, is presenting the bill of lading to himself as charterer of the vessel.

It is interesting in this regard to speculate what might happen if the importer takes custody and full legal title to the goods FOB inland point of origin in the United States. In such a case it is conceivable that the A.I.D.-financed goods might never leave the United States. The A.I.D. requirement that a bill of lading should be produced as a condition for payment is not an insuperable obstacle. Thus: the importer obtains $10,000 of A.I.D. financing for the shipment of roto rooters to Vietnam. He obtains another $10,000 from GVN free foreign exchange for another shipment of roto rooters. The importer obtains one bill of lading covering $10,000 of roto rooters to Vietnam and submits that bill of lading in the A.I.D.-financed transaction. The second batch of $10,000 is resold in the United States. In the process the importer has imported $10,000 worth of the product under GVN financing and has transformed 100% of the A.I.D.-financed product into a cash accumulation for his benefit.

b. Sale of Goods for Dollars After the Goods Reach Vietnam.

To transform into dollars goods which arrive in Vietnam, the importer must re-direct or re-export the commodities. The importer can arrange--even for goods on liner vessels--to have cargo left on board after the vessel reaches Vietnam. The vessel will not unload at Saigon and will instead proceed, at the request of the importer, possibly to Singapore or elsewhere and there unload its cargo. Under other schemes the importer may take possession of the cargo at Saigon and subsequently re-export the goods by sea via another vessel; or he may move the goods by land outside Vietnam. In each such case, by selling A.I.D.-financed goods outside of Vietnam, he will achieve a cash transformation.

4. Illegal Abuses Which Require the Participation of the Commodity Supplier.

a. Amplification of the General Theory.

The importer must find a commodity supplier who is willing to divert to him part of the profit realized on the sale. In the best of all possible cases the commodity supplier will spend nothing (or as close to nothing as possible) for the goods. The supplier will in such a case have 100% (or as close as 100% as he can reach) of the price realized on the sale to divert to the importer. Ideally, the commodity supplier chosen by the importer will supply nothing (empty boxes); on a sliding scale of preferences, the commodity supplier will supply items which have a low acquisition cost; e.g., patented products which cost little to make, but which can be sold at high prices; steel secondaries which can be acquired from steel mills, on occasion for nothing, and otherwise at very little cost; specialty products (e.g., sea water, rust inhibitor), brand name items, or complex industrial tools or equipment with limited markets--products which are not widely sold and which can therefore accommodate high prices.

In the most flagrant case the supplier will sell nothing. To achieve this result--i.e., to realize 100% cash transformation--it may be necessary for the supplier to secure the participation of other parties in the scheme. As a formal prerequisite, the supplier must secure an ocean bill of lading which indicates the passage of custody of the goods to ocean carrier. There is a tendency within A.I.D. to regard the bill of lading as something tangible, formidable--something reliable. It is assumed that the ocean carrier acts as a quasi-public utility: an ocean carrier would not issue a bill of lading unless its representatives first examined the goods to determine their identity; unless the carrier weighed the goods, measured them, or counted them to determine that the description in terms of weight and number noted on the bill of lading accorded with the facts.. It is assumed that the carrier will undertake these activities because that is what a carrier is supposed to do, that a carrier acts to protect itself against possible claims by the importer who will show up at the port of destination with the original bill of lading and demand possession of the goods in the quantity or weight noted on the bill. In sum, A.I.D. places maximum reliance on the integrity and in the protective features which it associates with the ocean transportation document which the commodity supplier must submit to the U.S. bank to receive payment with A.I.D. funds. These assumptions are erroneous.

The commodity supplier is not required to deal with a U.S.-flag carrier if A.I.D. is not financing the ocean freight. And with respect to foreign-flag carriers and especially foreign-flag tramps, it is not an insurmountable difficulty to obtain a bill of lading for non-existent or short-shipped or miscounted goods. If the commodity supplier time-charters a vessel for one trip it is completely possible for the commodity supplier, acting as the carrier, to issue to himself a bill of lading. This bill of lading will be submitted to the bank, which will forward it to the Vietnamese bank, which will, in turn, hand it over to the importer. Of course, the importer will make no claim against the vessel when the vessel arrives (if it arrives), because the importer is, after all, the prime mover in the cash transformation undertaking.

But it is not necessary for the commodity supplier chosen by the importer to deal with a foreign-flag vessel. The commodity supplier can charter a U.S.-flag tramp and have bills of lading issued to him for short-shipped items or empty boxes. Moreover, it is possible to achieve the same objective even with a recognized U.S.-flag liner vessel. It is common knowledge (and common practice) that a liner vessel will in fact issue bills of lading which do not in fact represent faithfully the statements contained on the face of the document, if the shipper of the goods executes in favor of the vessel an indemnity undertaking which protects the vessel from harmful consequences which may result from this falsification. 1/ When the importer and the commodity supplier are acting in concert, the vessel has little cause for fear and has every reason to accept the indemnity undertaking--especially if it is paid a handsome fee for its participation in the undertaking.

It is possible under this analysis for a commodity supplier to secure a bill of lading and to get paid from the U.S. bank without shipping anything. But the commodity supplier need not be so bold. He may secure a bill of lading covering the full contract amount, but, in fact, ship only part of the amount called for by his contract. Carriers are, after all, not at all loathe to issue bills of lading which state 1,000 tons of X, "shipper's count," or "shipper's weight"; or 1,000 packages "said to contain . . . ." When the carrier issues such a bill of lading in connection with an A.I.D. shipment, it is not unlikely that it has obtained an indemnity undertaking from the shipper. But A.I.D. never learns of the indemnity agreement, since the indemnity letter is not a document which is submitted by the commodity supplier to the paying bank as a condition for receiving payment.

To recapitulate: A.I.D. believes that it is difficult for a commodity supplier to secure from an ocean carrier a bill of lading which

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1/ See, e.g., in this regard, Hellenic Lines v Louis Dreyfus Corp., 1967 A.M.C. 213 (2d Cir. 1967); Walls, Ship's Business and Cargo Loss and Damage, pp. 40-41 (1963).

misrepresents the facts; it is in fact not difficult to secure a patently false bill of lading from a chartered vessel; it is, in addition, relatively easy to secure from a liner vessel a bill of lading which does not accord with the facts, provided the shipper is willing to execute a letter of indemnity. A.I.D. has mistakenly placed maximum reliance on the bill of lading.

Although no careful study of this problem has been made from A.I.D. records, a quick check on collected bills of lading on shipments to Vietnam will show many with notations "said to contain" or "shipper's count" or "shipper's weight". In addition, in each and every case of detected short-shipment a clean on-board bill of lading was processed which covered the full contract amount. The best evidence which would support these observations would be a comparison between Run 13 tonnage tabulations on shipments to Vietnam with Vietnamese import arrival statistics (maintained, hopefully, by GVN customs authorities) segregating tonnages by A.I.D. and non-A.I.D. financing. In such a comparison, it is likely that a wide discrepancy between tonnage shipped and tonnage arrived would emerge.

There is a tendency within A.I.D. to assume that abuses involving short-shipment or non-shipment of goods covered by clean bills of lading would be detected either by the opening commercial bank or by customs authorities in Vietnam. This is not the case. The commercial bank is only interested in securing from the importer an amount in local currency equivalent to the counterpart deposit obligation of the bank. Once it has collected the local currency from the importer, the bank is not itself interested in the goods as such. Of course, the bank looks to the goods as security for the undertaking of the importer to make the local currency payment; until he makes that payment the bank will not release the goods to him. But the importer who is seeking a cash transformation will pay the bank the full amount which he owes, secure the bill of lading, and collect his shipment--or his non-shipment. Furthermore, there is no connection between the ability of the supplier to get paid and customs arrival statistics. The bank will release the bill of lading and will make its counterpart deposit into the special counterpart suspense account without regard to any advice from Vietnamese customs authorities that the named goods have or have not arrived or even that the vessel which is supposed to carry the goods has or has not arrived. And, of course, should arrival of the goods ever become an issue between the importer and the Vietnamese customs authorities, the importer seeking to attain a cash transformation would find a way to arrange matters with the customs people to his satisfaction and to theirs.

b. Examples of Illegal Cash Transformations Requiring the Participation of a Commodity Supplier.

Complete cash transformation can be achieved by sending no goods; partial cash transformation can be achieved by short-shipment. On a sliding scale the same objectives, in varying degrees, can be achieved by overpricing the goods and diverting part of the difference between price and cost to the importer. The routing of funds to the importer can take various forms. In the rankest situation, the supplier will simply send the money to the importer or to the importer's representative or to the importer's foreign bank account. Under A.I.D. rules such a payment is considered a kickback and will justify an A.I.D. claim against the supplier. At the other end of the spectrum, a supplier can, if he so chooses--and it is really not necessary to be terribly secretive about these payments since the ability of A.I.D. to detect them is quite limited--arrange for the payment to take place in quite a sophisticated manner. He can for example use the proceeds to make an alleged collateral purchase from the importer (e.g., he can buy the importer's stamp collection). The supplier can lose a wager to the importer. The supplier can simply play poker with the importer's New York representative. But it is hardly necessary to be so subtle.

The attractiveness and ease of diverting large sums--which in turn depends upon a wide margin between price paid with A.I.D. funds and cost to the commodity supplier--is enhanced by a series of A.I.D. regulations which raise the price above levels which would otherwise obtain. A.I.D.'s peculiar source/origin rules, which are justified on balance of payments grounds, surely operate to raise prices on many items. If the item procured has a very limited or a unique source in the U.S., these rules will justify a high price, which, because of the limited or otherwise non-existent U.S.-domestic or commercial U.S.-export market, cannot be tested effectively under any of A.I.D.'s traditional price-ceiling formulations. Source/origin rules coupled with certain other A.I.D. rules suggest interesting patterns: e.g., A.I.D. generously allows sole-source waivers; and A.I.D. rules allow goods shipped from free ports or bonded warehouses to be considered U.S.-source goods if identical goods were shipped from the U.S. to the free port or bonded warehouse. The latter rule accommodates the following combination: Importer A in Vietnam arranges through Firm B, a participating U.S. supplier, for the purchase of 3,000 tons of U.S.-source caustic soda. B imports 3,000 tons of caustic soda from Japan into Hong Kong. B then secures a bill of lading covering the shipment of 3,000 tons of caustic soda from the United States to Hong Kong. This bill of lading might cover a real shipment, but it might also cover a phony shipment, e.g., a shipment of something other than caustic soda labelled "caustic soda". After all, B consignes the goods to himself under a straight bill of lading. Since shipper and consignee are identical, the carrier has no concern (even apart from letter of indemnity arrangements) that the consignee will complain against the carrier that the goods which he, as shipper, has placed in the custody of the carrier are not in fact that which he said they were. B sells the goods - whatever they are-- which he has shipped to Hong Kong from the United States. He sells these goods in Hong Kong or for re-shipment to any country other than Vietnam. By so doing, B has acquired a bill of lading showing the movement of 3,000 tons of caustic soda from the United States to Hong Kong. B then takes the 3,000 tons imported from Japan, ships them to Vietnam and, armed with his bill of lading covering the movement from the U.S. to Hong Kong, gets paid the contract price for U.S.-source caustic soda. By substituting the Japanese goods under the umbrella of the source/origin rules the supplier has been able to charge a high price while delivering to the importer exactly what the importer has ordered. In the process the importer has gotten his commodity and has accomplished a substantial cash transformation. The high price for the goods is made possible by the source/origin rules. Substitution of Japanese for U.S. goods is made particularly easy by granting special status to Hong Kong and Singapore. It is an A.I.D. fiction that a bill of lading showing the import of goods into Hong Kong from the United States is a basis with safeguards which assure that goods leaving Hong Kong are U.S.-source goods.

The bonded warehouse situation, which A.I.D. treats in the same way as free port areas, is no better. After all, what is a bonded warehouse? A bonded warehouse will usually remain under private control. The substitution of goods within the bonded warehouse will generally be a simple matter.

Although there is little empirical data to show large scale substitution of goods at Hong Kong, A.I.D. has stumbled upon the substitution of goods within the free trade zone area in Staten Island, New York. If suppliers are engaging in such desparate and illegal acts in a free trade area within the U.S.--which is after all subject to some control and which can be investigated by A.I.D. personnel with relative ease--how much more likely is it that manipulation of documents and goods is taking place in Hong Kong and Singapore and in bonded warehouses at various points in the world.

A higher price than would otherwise obtain is achieved when the source/origin rules are coupled with waivers of the small business advertising requirements. It is fairly easy for a Vietnamese importer to select a cooperative supplier even if the proposed procurement is advertised. It is even more simple if the procurement is not advertised. In this context, it is surprising to note the percentage of goods moving in the CIP for which no OSB announcement has taken place.

5. Conclusion: Abuses Within the sphere of the Importer Can Be Achieved with Relative Ease under Present Procurement Procedures.

The importer can achieve partial cash transformation through a disguised commission routed to himself or by acting directly or indirectly as his own supplier. The importer can achieve major cash transformation by acting in concert with a compliant supplier. To accommodate a large cash diversion there must be a wide margin between price paid with A.I.D. funds and cost to the commodity supplier. Consistent with the assumption that such patterns are in fact being followed in the observation that large numbers of secondary suppliers are furnishing goods for the CIP; importers seem to favor off-shore suppliers for U.S.-source goods; and the types of commodities which A.I.D. has been financing to Vietnam lend themselves well to cash transformation schemes (high cost items such as patented drugs, and specialty products such as battery additives and steel secondaries which have very low acquisition costs for commodity sellers but relatively high A.I.D.-financed prices). Commodity suppliers can divert funds to importers with relative ease. The reliance A.I.D. has placed in the truthfulness of bill-of-lading information is misplaced, and A.I.D. source/origin rules coupled with other specialized limitations justify higher prices which suppliers can charge and, hence, a wider margin between cost and price which would otherwise exist. More importantly, the marketplace motivation which A.I.D. assumes will guide the importer to secure the largest quantity of the best goods at the cheapest price does not in primary part motivate the Vinetnamese importer; on the contrary, the importer is motivated to transform the largest portion possible of the A.I.D. commodity credit into a private cash balance over which he exercises exclusive control.

IV. Abuses by the Supplier

The size and nature of the commodity import program in Vietnam no doubt attract certain suppliers into the market who are concerned solely with their own profit and who are not interested in routing any part of their profit to Vietnamese importers. As a theoretical matter this is quite probable. But there is room to doubt that any large number of suppliers abuse the CIP while duping the importers who have chosen them. A supplier cannot by his own volition secure a CIP sale. It is the importer who alone chooses the supplier. On an analytical and pragmatic basis, it may be assumed that in most cases of short-shipment, overpriced commodities, shipment of worthless products, or the shipment of no products, the supplier has in fact acted in accordance with an understanding concluded with the importer. This conclusion should hold true especially for repeat suppliers. The repeat specialty pharmaceutical suppliers can only be getting large orders from Vietnamese importers if the importers believe that it is in their interest to procure these high-priced but low-cost items. The importer of Higgins battery additive was interested in the product only because he achieved a cash transformation thereby; Higgins could not have penetrated the market on the merit of his product alone. These observations of course carry over to suppliers of steel secondaries and to suppliers who short-ship or overprice other commodities.

It is the irony of A.I.D. rules that A.I.D. can proceed only against suppliers; yet the supplier can be changed at will by the importer, who can move from one supplier to another until from among the 200 million Americans and countless numbers of non-Americans he can find those who will be cooperative.

V. Abuses by the Ocean Carrier

The only assurance which A.I.D. has that goods--any goods--have been sent or that goods in the required quantity or weight have been sent, is the existence of a bill of lading which states that fact. This bill of lading is issued by a stranger to A.I.D., the carrier, who is chosen by another stranger to A.I.D., the commodity supplier, who, in turn, is chosen by the importer whose motivation is to transform the A.I.D. credit into a cash balance. The bill of lading does not in fact constitute sufficient proof of anything in the CIP context. The ocean carrier is too often a passive participant in the manipulations designed to abuse the CIP. For his passive participation the ocean carrier no doubt secures proper remuneration.

There are several methods by which the carrier participates actively rather than passively. One such method is so subtle and sophisticated that it deserves special mention. This is the dispatch-rebate abuse. The goods which the supplier sells are standard-item goods, for which ~~which~~ there is a known competitive price. The commodity supplier charters a ship to move the goods. The charter rate covers the movement of the goods to Vietnam plus ten days free time at port of loading to load the goods. There is also free time at port of discharge. All modern charters provide for demurrage if the shipper or the consignee exceeds the allowed free time. These charters also provide for rewards, designated "dispatch earnings", if the free time in the charter is not completely used. Thus, for example, the shipper may receive $1500 per day for each day which he saves the vessel by loading in a period less than the complete ten days. The commodity supplier loads the goods not in ten days, but in one day and earns nine times $1500. This sum is then rebated to the importer.

Another sophisticated variation is to run free time together between port of loading and port of discharge so that there are twenty days in sum total to load and unload. The shipper loads in one day, the importer unloads in nine days, and the importer receives from the carrier ten days dispatch money at $1500 a day.

These devices--submitted only as examples of abuses and not the gamut of abuses--are more sophisticated than the crude but far more prevalent direct rebate to the consignee by a representative of the ocean carrier. It is a widely prevalent practice in the ocean transporation business for a carrier to rebate sums to consignees in order to secure cargo. The rule is universally honored by foreign-flag carriers.

In addition to participating in the abuses by others of the program, ocean carriers have been notorious in abusing the program for their own profit. There is little doubt that freight rates in Vietnam have risen to commercially unjustifiable levels. For example: Under the base-port system for freight ratemaking, the base freight consists of a rate covering movement from a range of U.S. ports to one or more major ports in a region. Service to all other ports in the region is calculated as the sum of the base rate plus a differential. In all other trade routes in the world the base port rate will be the rate between U.S. ports and the ports in the region which accommodate large tonnage. With respect, however, to shipments to the region which includes Vietnam, we find that Vietnam--which accommodates very substantial tonnage--is not a base port. Instead, although carriers designate other ports in the region such as Manila or Singapore as base ports, they charge an extra differential for carrying goods to Vietnam. Properly, Vietnam should be a base port as much or more so than any other port in the region. Secondly, carriers applied war risk surcharges which exceeded the cost of war risk insurance. Carriers assessed congestion surcharges even after congestion subsided or disappeared. Charter freight rates to Vietnam far exceed freight rates to commercial ports in the same region. And why not? It is after all only A.I.D. and U.S.-Government money which is being used, and ocean carriers which fly the U.S. flag have a monopoly on securing freight financed by the U.S. Government. There is little doubt that on a cost vs. price comparison freight rates to Vietnam have been excessive. When a monopolist charges what the traffic will bear, the victim-consumer must bear a great deal.

Ocean carriers have been reluctant to make payment for lost or damaged goods after the discharge of goods in Vietnam. The pilferage rate at the port of Saigon is one of the highest in the world. Yet A.I.D. has secured almost no recoveries against ocean carriers for these losses, or for losses in transit, or for short-landings. On shipments to Vietnam there has moreover beeen a surprisingly high incidence of general average declarations and general average assessments.

A.I.D. follows exactly the same procurement procedure with respect to ocean shipping which it follows with respect to commodity suppliers: A.I.D. pays first and asks questions later. With respect to commodity suppliers, A.I.D. at least demands a Supplier's Certificate which controls certain elements of the sale transaction. Although that Certificate is frequently uninforceable, there is at least some effort at control over commodity supply transactions, even if only on a post-facto basis. With regard to transportation, the carrier writes his own bill of lading which entitles him to pre-paid freight in return for no meaningful undertaking by him. The Supplier's Certificate which the carrier signs is irrelevant to ocean transporation services. Yet in this area alone A.I.D. spends approximately $38 million per year on ocean transportation to Vietnam.

VI. Abuses by the Banks

It is the banks, strangers to A.I.D., which pay the commodity suppliers, other strangers to A.I.D., who ship the goods with still other strangers to A.I.D. Just as the commodity supplier and the ocean carrier may have interests antithetical to A.I.D., the paying bank may have contrary interests as well. When the bank makes payment to an A.I.D.-financed supplier, A.I.D. expects the bank to protect A.I.D.'s interests. To this end, A.I.D. issues a letter of commitment which states in some detail what the bank is to do in terms of collecting various pieces of paper. A.I.D.'s suspension/debarment and prior review controls depend for their effectiveness upon conscientious implementation by the banks. The banks, in addition, collect the Supplier's Certificates, the Form 283's, the Form 285's, inspection certificates, and a variety of specialized supplier certifications. The bank, A.I.D. likes to believe, acts as the enforcement mechanism at the documents collection level--the white-collar strong arm of A.I.D. But the bank is asked to make payments to commercial suppliers, and these suppliers are the bank's customers. What then is a bank to do when its responsibility to A.I.D. conflicts with its relationship with its customer, the commodity supplier? The banks have neatly avoided the core of the issue by pushing A.I.D. into the position of relieving the bank entirely from all responsibility for collecting properly executed Supplier's Certificates. The bank will make payment against a signed but otherwise blank Supplier's Certificate. The bank will not check any document other than the invoice and the bill of lading, and with respect to the bill of lading, the bank will do no more than determine that there is a bill of lading.

The conflict of loyalty reaches it peak when the bank lends the commodity supplier--the letter of credit beneficiary--a sum of money secured by the letter of credit. Usually, in such cases, the bank loan must be repaid by the commodity supplier when the letter of credit is negotiated by the supplier upon the submission of the documents required by the credit. These short-term loans bring very handsome interest rates for the bank; this is what bankers mean when they say that letter-of-credit business is not itself profitable, but that the commercial business which it stimulates is. What then is a bank to do when the letter of credit is about to expire and the commodity supplier submits non-conforming documents to the bank for payment? If the bank fails to pay the commodity supplier, it endangers repayment of its own loan. But if it does pay the supplier (i.e., if it sets off the amount which the supplier owes to it under the loan against the letter-of-credit amount and payshim the difference), does it not breach its duty to A.I.D.?

There is evidence which indicates that some of the notorious pharmaceutical suppliers to Vietnam did in fact receive loans from New York banks at the time they were submitting documents to these same banks under A.I.D. letters of credit. The classic illustration of this dual position of the bank is represented by the Aadal escapade (on a shipment to Pakistan) with Manufacturers' Hanover Trust Company on large shipments of steel. The bank paid out against bills of lading issued by the commodity supplier, acting as the ocean carrier; the bills of lading were manifestly false (there was no such vessel at New York at the time), but the bank honored them nevertheless in order to secure with A.I.D. funds repayment of large loans which it had made to the commodity supplier.

As a final matter which concerns the activities of the banks, it is important to indicate the central role which the bank plays with respect to A.I.D. suspension/debarment. When A.I.D. suspends or debars a supplier, it adds his name to the list of ineligible suppliers and forwards the name to the bank. A.I.D. expects the bank to screen out suppliers whose names appear on this list and not to make payment to them. If the bank does, however, make such a payment, it is, pursuant to Reg. 1 still entitled to reimbursement from A.I.D. (The Reg. 1 standard is that the bank must only set up a system of controls. If a payment slips through the controls, the bank is not penalized.) Moreover, these suspension/debarments have no effect at all on outstanding irrevocable letters of credit. A credit may be on the books of the bank for a year or more and A.I.D. is unable to cancel it or to interject itself into the payment process. Furthermore, it is relatively simple for a supplier whose name appears on an ineligibility list (the Reg. 8 list of ineligible suppliers or the Designated National List of the Treasury Department or the Economic Defense List of Commerce) simply to substitute (through the importer) an affiliate as a beneficiary of the letter of credit. The banks go along with such substitutions and have no desire and no responsibility to police A.I.D.'s concerns beyond the strict limits of the rather meager limitations which A.I.D. imposes upon them. The irrevocable letter of credit problem and the ability to substitute beneficiaries will limit, quite substantially, the control effectiveness of any system devised by A.I.D. which must proceed through the banking system.

VII. The Inadequacies of Regulation 1

To deal with the strangers who receive AID funds AID has developed the Regulation1 financing system. Under this system, a supplier executes a Supplier's Certificate which sets out his undertakings to AID. Subsections of this form refer back to sections in Regulation 1. One such section consists of a certification to AID that the supplier has not charged prices which exceed the limitations set forth in subpart G of the Regulation. Another section states simply that he has not violated AID's source/origin rules. Still another paragraph states that he has not made a proscribed kickback. The feature of this payment device is that it is payment to strangers against naked promises. There is no pre-qualification of suppliers; there is no quick records check against suppliers before payment is made; there is no self-operating machinery to secure factual information from suppliers. A supplier collects his money from the U. S. bank and gives AID only these rights which AID can, after the fact, derive from the Supplier's Certificate. In the best of all cases, when AID has enough evidence to prove a violation of an undertaking in the Supplier's Certificate, the supplier must still be found. If the supplier is located outside the U.S., the breach-of-contract theory for recovery of damages is, as a practical matter, of no help. Moreover, if the supplier can be found, he must be solvent. What good is a claim against Higgins when Higgins no longer has the AID funds he collected?

It is extraordinary that a person who is judgement proof, who has so few assets that no one would entrust him with a major undertaking, can secure AID-backed letters of credit which he can negotiate in return for boilerplate promises in the Supplier's Certificate. No one in the commercial world in the U.S. would ordinarily do business with this person or buy his product; but that person is eligible to receive AID letter-of-credit financing. Assuming the supplier who has received AID funds can be found and that the supplier has funds, AID can, at best, invoke the cumbersome legal machinery which the judicial route for the enforcement of legal rights requires. AID must proceed through the Department of Justice, an Agency which establishes its own priorities and which is not necessarily concerned with AID program objectives. The Department is concerned with the quality and quantity of proof; with live and competent witnesses; with a showing of economic damages; with the limitations on recovery imposed by principles of law, the hearsay rule, with mens rea ("on the basis of information and belief" - from the Supplier's Certificate); with admissibility of evidence, and the like. The rules which establish the proper standard for the supplier's conduct are themselves vague and general. These rules represent invariably, low-level compromises among staff offices, tepid acknowledgements to high-minded principles of fairness.

AID has pressed only one overpricing case to a judicial conclusion. In that case - the famous Standard Oil Case of 1958 - the Court of Appeals threw out the basic price limitation of Regulation 1. AID has pressed no source/origin case to ultimate judicial conclusion: the Department of Justice has bluntly told AID that the source/origin rules are weak and probably unenforceable. Large claims which AID has developed against European suppliers have never been pressed because the Department of Justice despairs of proceeding with a Regulation 1 theory in a foreign court.

Regulation 1 has, in sum, simply served as a convenient vehicle for processing country-refund claims. In such claims, AID does not go before a court, and as between AID and the country, AID can always point to something in the Regulation to demonstrate the "taint" in the transaction. Country-refund claims do not, however, prevent the abuses incident to AID-financed transactions. They discourage no one -- not the country, not the importer, not the supplier. Country-refund claims are an economic fiction which AID propagates: the Agency has overcome the taint in the transaction by "disassociating" itself from the transaction through the country-refund claim.

Regulation 1 was conceived and formulated at the very inception of the foreign-aid program. Its central underlying premise is that normal market mechanisms should be followed to the maximum degree possible. It was thought that mere general guidelines, such as broadly-phrased price limitations, would, when combined with normal market forces, serve to assure the propriety of AID transactions. It was thought that the banks could be trusted to assure AID's interests; that suppliers competing against each other would deliver goods at reasonable prices; that written undertakings by suppliers would be sufficient as a basis on which to make payment; and, most importantly, it was assumed that importers in AID countries would be guided by the basic economic axiom.

In Vietnam, at least, the importer is not motivated in the manner anticipated by AID; the supplier chosen by the importer will certify to anything in order to secure the AID funds; and the banks cannot satisfy the monitoring burden which AID imposes upon them.

VIII. Carry-Over Consequences into the Larger Commercial Community of Private Commercial Abuses of the CIP

In an importing community in which merchants are actively and successfully engaged in converting dollar import credits into private cash balances in the manner described in the foregoing sections of this paper, the following consequences, on a larger scale, which affect the importing community and perhaps, also other knowledgeable circles in Vietnam, can be projected:

1. A cynicism and a disregard for the stated objectives of the CIP may result from the focus by importers on poor quality goods purchased deliberately at high prices; on non-goods purchased at high prices; on diversion of goods to neighboring countries for the exchange of imports into hard currencies; and on all the other schemes which disregard the goods themselves in favor of cash transformations.

2. When certain merchants are successful in accumulating private cash balances mined out of the CIP, resentment and envy may affect other merchants who have been dealing only with the goods and who handle the goods to make a local-currency profit. The cash-transformation merchant becomes a model for others who detect within themselves a similar motivation.

3. The cash-transformation motive is strong and merchants may be desperate to achieve their aim. In addition, large sums of money may be covered by import licenses issued to these merchants. In such circumstances, it is not surprising if an escalating series of developments occurs in which one desperate act succeeds another: to secure an import license, the merchant may bribe a GVN official; to secure a large margin of cash transformation the merchant may feel impelled to use patently illegal methods as opposed to legal methods; to achieve his end quickly the merchant may deal with particularly disreputable suppliers who are willing to take risks and perform acts which legitimate merchants in good standing would not be willing to undertake. Each of the series of desperate acts may cost the importer a fee which, in turn, may require him to mine an increasing percentage out of the import credit for himself. The larger consequences, therefore, of permitting the exploitation of the CIP is a growing participation for merchants, government officials, suppliers, and middlemen in acts of corruption.

4. Within the supplying community, a cynicism and a lack of trust in the objectives of the Program develop when exporters percieve the low quality of goods supplied; the high prices being charged; the pattern by which importers choose the suppliers. Suppliers quickly learn that if they are to participate in CIP business they must do what the importer demands from them.

5. Particularly disreputable, desperate, and amoral suppliers are attracted to the Program. Front men who are not U.S. citizens, and those who are judgement-proof may be used as AID suppliers of record. It is no accident that the Gubbay's and Navarro's in the CIP maintain no residence in the U.S. and are not U.S. citizens; that Thomas Edison Higgins and Stuhr Kennedy are mental cases and judgement-proof as well, and that the Roy Greene's have criminal records. It is not surprising in this context that even the larger pharmaceutical houses which until recently were selling to Vietnam were coerced into rebating in one form or another large sums to importers as the price for securing business.

A program vulnerable to exploitation for the realization by private individuals of private goals inconsistent with AID's public goals undermines trust in the program in Vietnam and breeds cynicism and mistrust in the supplying community in the U.S.

IX. Public Abuses of the Program

Certain abuses concern only AID in the sense that they do not promote the transformation of dollar import credits into cash balances. Foremost in this regard is the problem of ineligible items and the cluster of problems concerning balance of payments considerations associated with AID-financed CIP sales.

A. The Problem of Ineligible Items

If an importer legitimately procures goods for local resale in order to accumulate a local-currency profit, it is of little concern to him whether the item which he handles does or does not, from a public relations point of view, embarrass AID with the Congress or with the American press. A legitimate importer would, ordinarily, as between industrial ball bearings and pornographic material care only which of the two items would yield for him a larger profit in return for the same expenditure of funds. Acting only as a businessman, he would be unconcerned with the U.S. moral or public relations nature of a particular item. But, of course, it makes a great deal of difference to AID whether the importer chooses to procure pornographic material or industrial ball bearings.

Until fairly recently all commodity code numbering took place within the context of AID's four-digit commodity code. These codes are of course, "genus" codes and under any one four-digit number hundreds of particular items may appear. AID has recently shifted to Department of Commerce Schedule B numbers; there is now some effort to supplement Schedule B codes with several additional digits in order to bring down the relationship between number and item to a ratio which, as close as possible, approaches one to one.

Ideally, if one number matched one product (in the sense that every number represented a particular set of specifications and if any in the set of specifications were changed in any way the identifying number would also be changed), AID could identify precisely any item which it finances. With such a system of controls, the legion of commodity analysts and commodity checkers could be cut back. The license review task could be easily automated. A computer programmer could certainly put the 50,000 odd items which AID is prepared to finance all on one tape. The material on tape would be divided into several classifications. The import license application would be fed into the computer and if the item by number fell within category of eligible items, the machine would so indicate (with, for example, a green light meaning "finance"); if the item fell within the category of ineligible items a red light meaning "no financing" might go on; in a third category would be items, designated by number, which AID would finance only within certain limits (e.g., at a certain price or only in a certain quantity.)

The ideal one-to-one ratio between number and set of specifications of course exists in the form of the Federal Stock Numbering System. This suggestion for a shift to the Federal Stock Numbering System has been considered on several occasions during the past two years. The System was not adopted because the Agency did not in fact wish to adopt a control device with such formidable possibilities. The shift toward expanded Schedule B numbering probably emerged from the FSN suggestions. But until AID adopts one-to-one numbering and gets away from genus codes, it will continue to run on an unnecessarily large risk that ineligible items slip through the bureaucratic filter.

B. Balance of Payments Losses

When import credits are transformed into cash balances in favor of private importers a U.S. balance-of-payments loss occurs. To the extent that cash transformations are in significant amounts taking place, large balance-of-payments losses are also taking place. The commercial abuse of the program by private importers dovetails into a public abuse of the program in the balance-of-payments area.

In addition to the private abuse of the program which results in balance-of-payments losses, the GVN itself takes its cut on all AID shipments in much the same form that the private importer takes his cut. It is not generally appreciated that port and unloading charges in Vietnam are at present among the highest in the world. Each ship which arrives at Saigon must pay port charges (harbor dues, dockage, wharfage, pilotage fee, etc.), and, it is the carrier who must secure the stevedoring with respect to all liner shipments. It is also the liner carrier who must pay the barge owner if the goods are loaded or stored. All of these activities must be paid for in dollars. It is probably a conservative estimate to conclude that twelve to fifteen percent of the liner tariff rate to Vietnam consists of these port charges payable in dollars. In the past twelve months it is likely that over 5 million tons of cargo were discharged in Vietnam. Much of this cargo was shipped by liner vessels. It would not be difficult to arrive at an average freight rate for the liner portion of these shipments and to take an average 14 percent of that figure to determine the cash revenue taken in by the GVN from port operations. To a substantial extent this cash transformation and flow into the public treasury of dollars consists of a public transformation of AID dollar import credits into cash balances. Even with respect to charter shipments in which the consignee must arrange for discharge, there is in the form of port charges a substantial cash transformation. Assuming for purposes of simplicity an average \$5 per ton cash transformation (probably on the low side), it would follow that for the 5 million tons, a \$25 million dollar annual public cash transformation of import credits (AID and non-AID) has been taking place and with it a comensurate U.S. balance-of-payments-loss connected with import activities in Vietnam.

X. A System of Effective Controls: Alternatives to Regulation 1 Financing

The analysis in this paper has proceeded from an examination of the motivation of the importer. It has indicated in some detail how the vulnerability of the Regulation1financing system permits the importer to achieve his cash transformation objective. The Regulation 1 system regards "normal channels of private trade" as the outermost control mechanism. But where the importer's motivation is inconsistent with the basic economic maxim, the marketplace control mechanism does not work.

In the following paragraphs of this section proposals will be outlined for controlling each of the major steps in the typical AID-financed CIP sale to Vietnam. AID deals with commodity suppliers who are strangers to the Agency chosen by an importer who has an economic motivation contrary to that of AID. As a first and major step it is necessary to impose firm and self-operating controls on this stranger, the commodity supplier, which insure the non-participation in AID-financed sales of obviously disreputable, marginal, or pliant suppliers willing to perform the cash transformation task on behalf of the importer. In Paragraph A of this section a specific proposal to accomplish this objective will be outlined.

The commodity supplier receives his AID funds from another stranger, the U.S. bank. All AID substantive controls are placed in the narrow letter-of-credit funnel. AID has packed into the letter-of-credit payment device its entire system of documentary controls. These controls are inadequate, as the discussion above concerning the bank payment system has indicated, because the banks do not adequately monitor AID documents and because the banks may have dual loyalties with a paramount loyalty to the letter-of-credit beneficiary rather than to AID. In Paragraph B of this section a suggestion is set forth that AID take away the payment function from strangers and handle it directly.

Payment has been made to strangers by strangers on the basis of bills of lading issued by strangers. The bill of lading, as described above, has served as evidence of the shipment to Vietnam of specific goods in specific quantity or weight. In Paragraph C below a proposal is set forth that the function of carriage, to the extent possible, be taken away from strangers and should be performed by AID directly.

There are three major proposals for changes. Each of these proposals would transform a function which is now performed by strangers by making it an AID-controlled or an AID performed function. The commodity supplier must be controlled effectively by AID; the payment function must be performed by AID; and the carrying function must be performed by AID. Only by techniques which take the strangers out of the AID payment and procurement processes will AID be able to assure that goods of quality at reasonable export prices are shipped to and received in all cases in Vietnam.

There are other peripheral control devices which can be suggested and developed. Substantive limitations of various types could theoretically be added to existing letter-of-credit provisions and to the Supplier's Certificate. Greater surveillance of this, that, and the other thing could be undertaken. But as long as AID continues its blind faith in a marketplace process by which strangers deal with strangers and collect AID funds for their activity commercial abuses in the program will continue; public abuses of the program will take place; and disenchantment and cynicism both in Vietnam and the U.S. will be associated with the CIP.

A. Control Over Commodity Suppliers: A Proposal for the Bonding of Commodity Suppliers.

1. The Proposal

As a pre-condition for supplying goods under AID financing each supplier would be required to file with AID a bond drafted by AID and issued by a surety company. This bond would state that the supplier agrees with AID that if AID determines and so notifies the supplier that in connection with his participation in an AID-financed sale to Vietnam evidence exists that he has violated one of a stated number of specific rules, AID will draw down the amount of the bond in an amount which compensates AID entirely for the particular regulatory violation by the supplier. A supplier who disagrees with AID on the facts or disagrees with respect to the legal conclusion that he has breached an undertaking in his bond may proceed at law against the United States to recover, if he can, the amount of the AID drawdown on the bond. This bonding proposal shifts the penalty provision onto the other foot: whereas at present the supplier receives AID funds in return for promises and AID must catch the supplier in order to make itself whole, under the new proposal, AID first draws down the supplier's funds and the supplier must catch AID, if he can, to make himself whole.

2. Benefits to AID If the Proposal Is Adopted

Judgement-proof and non-commercial suppliers will not participate in the CIP program simply because they can not be bonded. Few surety companies will issue a bond for $100,000 or more to a mental case, to a new company with no export history, to a criminal, or to a company making a sleazy product. Furthermore, if a bond is ever drawn down by AID, it will be drawn down only once:

if a surety company must pay out on a bond, it will never again issue a bond to the same supplier. This is a well-known feature of the surety business. In addition, a supplier, who is aware of the powerful hold which AID under this proposal will have over his activities, will hardly be willing to play the importer's cash-transformation game if the cash transformation which the importer may achieve will come out of the supplier's hide. In effect, therefore, the willingness of suppliers to cooperate with importers in the multifarious cash-transformation schemes will disappear: the risks under the bonding system are simply too great for the supplier. Moreover, if a commercial abuse does take place, AID can immediately make itself whole at the expense of the supplier rather than at the expense of the public treasury of Vietnam.

3. A Bonding System Will Only Work If It Is Keyed to Specific Rules

Regulation 1 formulations concerning "prices generally charged" or "prevailing export market prices" cannot be cranked into a bonding control mechanism. A supplier must be held with respect to the requirements for which he is bonded to specific rules and any ambiguities in those rules will be intepreted against AID. The rules to which the bonds are keyed must state, for example, that the supplier has not charged "more than the maximum price stated by AID in Circular Announcement X;" or, the supplier has not charged "more than $68 per ton;" or, the supplier has not charged "more than the price which he has charged any other buyer within or outside the U. S. for the identical commodity within the past three months." Of course, this specificity requires close AID attention to commodity prices. It may be necessary to fix by way of ceiling prices the price for major AID-financed items moving to Vietnam. Such price limitations must be clear, certain, and not readily subject to dispute. AID could certainly say in an OSB announcement that "until further notice steel secondaries in the reject, waster, or waste-waster categories will be financed at no price which exceeds X dollar per ton." This is the kind of specificity to which the bonding requirement could be geared.

The bond would also permit an AID drawdown in the event a kickback were made to the importer; in the event source/origin rules were violated, goods short-shipped, or the wrong goods shipped; or if the goods turned out to be of a particularly poor quality, or in poor condition, or completely non-efficacious.

4. Problems Associated with the Bonding Proposal

Suppliers will not like the proposal. Why should they? All suppliers who until now have been playing the importer's game will scream. Arguments will be put forward that such a proposal violates freedom of the marketplace. Perhaps it does. Some suppliers who are not bondable will scream with particular vehemence. Arguments will be put forward that the bonding proposal strongly discriminates against small businesses. This may be true, but probably is not. The U. S. Treasury has a large number of bonding requirements which are imposed on large and small businesses in dazzling variety. If small businesses are, contrary to expectation, in some way discriminated against, efforts should be made to mitigate this consequence; but the basic proposal should not be rejected simply because the very types of people AID wishes to exclude from the program, the judgement-proof, the overly pliant and the incompetents, are in fact excluded.

There can be no doubt that under this proposal Regulation 1 must go. No bond can be geared to the sweeping generalizations in the present Regulation. In place of the detergent language of the regulation hard specific criteria must be set as the standards to which the supplier will be held. The Supplier's Certificate must go. In lieu thereof the bonding form will be submitted, either on a transaction-by-transaction basis or on a one-shot filing basis similar to the procedure which U. S. Customs uses on import transactions into the United States.

It is likely that if AID insists upon bonding for U. S. suppliers, it will be able to persuade the GVN reciprocally to bond importers. The GVN could itself issue the bonds to importers. Importers could be held to requirements which are analogous to the requirements to which suppliers are held. If for any reason an importer succeeds in achieving a cash transformation, his bond would be drawn down by the GVN; such a drawdown would itself represent a determination of further ineligibility to participate in the CIP. But only if AID insists upon bonds for U. S. suppliers, will the GVN even consider bonding importers. With dual bonding at both ends of the transaction, it would indeed be difficult to achieve commercial abuses of the program.

B. AID Payment Proposal: The Vietnam Bureau Should Itself Directly Pay Suppliers.

The strangers who pay out AID funds to the other strangers who supply the goods should be taken out of the picture. The irrevocable letter-of-credit system which prevails now on CIP shipments should be abolished. It is absurd to have an irrevocable undertaking to pay out funds when program objectives indicate it is not in the interest of the program to make the payment. It is absurd to finance pharmaceuticals after

AID has decided it does not wish to finance pharmaceuticals. It is absurd to finance shipments from Gedeon Richter, Archifar, and Chemo-Pharm after these suppliers have been suspended. It is absurd to collect promises on AID forms, yet to permit the banks to pay out AID funds without monitoring even the proper execution of the promises.

1. The Proposal

AID should itself issue payment instructions to commodity suppliers. Under these payment instructions, AID will make payment in return for the submission by the commodity supplier of AID-required documents including the bonding document. Unlike irrevocable letters of credit, payment instructions can be cancelled at any time for whatever reason. If AID makes the payment, it can insist that all promises to AID on all AID forms be properly executed. If AID has any collateral evidence (or suspicion) of fraud, it can withhold payment. Most importantly, however, payment by AID will avoid the dual-loyalty problem. AID will not issue loans to commodity suppliers secured by AID payment instructions. If AID knows that a ship is not in port, it will not accept an on-board bill of lading ostensibly issued to the shipper by the carrier.

2. Problems Associated with the Proposal

The banks will not like the proposal. Why should they? The banks have been abusing the business which AID has been giving them and have been making money in the process. At least some of the banks believe that it is they who provide foreign assistance and not AID. Commodity suppliers will also scream if the self-operating and clubby letter-of-credit system is changed into a payment-instruction system. Once a supplier has a letter-of-credit, he sits in the drivers's seat. Nothing that AID or the bank can do will affect his prospect for receiving payment. All he need do is submit the right documents and not even suspension/debarment by AID can get to him. Direct payment by AID under payment instructions will eliminate all possibility of such manipulation by suppliers.

The administrative burden of making direct payment should be manageable. AID personnel will closely examine documents initially at the stage of payment, but payment under payment instructions will in no way lessen AID's right to draw down a supplier's bond after a substantive irregularity is discovered upon post audit. Direct AID payment is especially feasible if Regulation 1 is dropped and a bonding system geared to specific rules is instituted.

C. The Carriage Proposal: To the Extent Possible AID Should Itself Carry Goods Which It Finances.

The role played by the ocean carrier in a CIP transaction has been considered at length in this paper. The critical moment which determines whether a supplier will succeed with a commercial abuse of the program occurs when he secures the bill of lading; that is the major document he needs to secure payment. It should be AID, and not strangers to AID chosen by the commodity supplier, which examines the goods as they go over the rail. It is AID which should transport the goods at cost to Vietnam and not the private carriers operating at inflated freight rates. AID should make certain that goods reach Vietnam and that if goods do not arrive in the proper amount and in the proper condition, prompt and proper compensation is made by the vessel's operator.

1. The Proposal.

AID should time-charter U.S.-flag vessels, if such are available; if such are not available, AID should secure time-chartered foreign-flag shipping, perhaps under PD-31 payment arrangements, to carry CIP cargoes to Vietnam. Time-chartering vessels will permit AID to carry goods to Vietnam at cost. Time-chartering vessels will permit AID to issue the bills of lading. It will be AID which will look at the goods as the goods move over ship's rail. If AID time-charters vessels, a bill of lading which a supplier submits, as a document required for payment will have specific, measurable, and valid meaning. AID will be able to trust a bill of lading issued by a vessel which it controls. AID will be assured that if the supplier loads damaged goods, no clean bill of lading will be issued; if the supplier loads a lesser amount or a lesser weight than that which he claims, AID is assured that the ship operator will not accept a letter of indemity in return for issuing a clean on-board bill of lading; if AID controls the vessel, there should be a complete matching between Run 13 payment and tonnage amounts, and tonnage arrival statistics in Vietnam. If AID controls the vessel, the last stranger in the sale transaction would be eliminated: AID will itself make the payment and itself control the carrier; and AID would place substantive and effective controls over the commodity supplier chosen by the importer.

2. Problems with the Proposal.

Neither commodity suppliers nor shipping companies will like the proposal. Why should they? Such a plan does not promote their interests.

AID did, at one time, time-charter two vessels for six months; this was to be the beginning of an AID chartered fleet for Vietnam. For reasons wholly unrelated to the merit of the proposal, the White House intervened and demanded that the time charter for these two ships be transferred to MSTS. It is unfortunate that the effort was thus aborted. The idea, however, is sound and should be pursued once again. On one voyage to Vietnam which AID controlled by time-charter on the S.S. American Falcon, Resources Transportation Division estimates that a net saving in freight of $400,000 was achieved. This undertaking achieved a substantial saving on freight, an important, but still rather peripheral objective compared with the other major goals which should properly concern AID in an AID-financed sale to Vietnam.

D. Other Proposals for Major Changes in the Control Mechanism for CIP Sales.

The analysis which this paper has made points to reform in three major areas: in the control of the supplier; in the elimination for the CIP of the letter of commitment/letter of credit payment procedure through the facilities of U.S. banks; and the substitution for private ocean carriers of AID time-chartered vessels. Without such fundamental changes in the mechanics of the CIP, it is difficult to see how a really tightly-controlled program insured against abuses can be run. Small modifications in existing procedures - such as the addition of further manpower to perform surveillance activities - will not accomplish this objective.

It is, of course, possible to suggest a large number of substantive changes apart from the three basic proposals; these proposals will have some, but not an overriding impact on the mechanics of the CIP and will not, of themselves, adequately protect the program from abuses.

. Listing of Other Proposals of a Minor Nature.

1. Adoption of the Federal Stock Numbering System: The Federal Stock Numbering System should be adopted to control the ineligibility problem. With its adoption, it would be considerably more difficult for suppliers to ship, say, poor quality milk while charging prices for top quality milk. Post audit would be simpler and surveillance of import license applications would be made easier.

2. Partial Pre-Payment for Suppliers: A supplier might be paid against shipment documents under his letter of credit 75% of the purchase price. Upon arrival in Vietnam, the goods would be inspected for conformity with the contract and for proper weight and number. A document would be issued by the inspection agency in Vietnam. With this document the supplier could collect from the U. S. bank the balance of his purchase price.

3. Further AID action could be taken to eliminate foreign suppliers from AID financed shipments of U.S.-source goods.

4. AID could stop financing port charges in Vietnam as component elements of freight rates.

5. AID might itself hire inspectors to inspect goods furnished by commodity suppliers under AID financing.

6. Prior review of large transactions.

Instead of placing certain suppliers on prior review for all transactions in which they participate, AID might, as a matter of policy, automatically review in advance all sales in excess of a fixed sum, perhaps $100,000. It is such sales (the large ones) which enable the transformation of sizable import credits into sizable private cash balances.

7. AID might for Vietnam issue specific price limitations in the form of a periodic price bulletin.

Even without a bonding system, AID might determine not to finance steel secondaries (and other commodity categories) beyond certain fixed price levels. Anything that gets this Agency away from the vague price rules in Regulation 1 is beneficial.

XI. Conclusions.

The motivations which control the conduct of the importer in Vietnam are not consistent with AID's aspirations and expectations for the CIP. AID's free marketplace psychology as the basis for financing goods leaves the CIP vulnerable to abuse by the importer who seeks to transform AID credits into private cash balances. Regulation 1, which expresses faith in private channels of trade and a procedure which consists of payment to strangers against promises, does not adequately safeguard AID. AID should eliminate from participation in the CIP suppliers who are not bondable; it should eliminate U.S. banks as payment agents for AID; and, to the extent possible, it should eliminate the ocean carriers who are strangers to AID. AID should demand, under penalty of forfeiture of bond, that suppliers adhere scrupulously to specific substantive limitations. AID should take on the payment function directly under payment-instructions procedures, and AID should carry its own goods to Vietnam on time-chartered vessels. Although other substantive proposals can be suggested, none are fundamental in the same sense as the three major proposals.

If the CIP structure is in danger of collapse because of abuses associated with the program, repairs should begin in the foundation of the structure and not in the attic.

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