



United States General Accounting Office
Washington, D.C. 20548

September 30, 2003

The Honorable Christopher Shays, Chairman
The Honorable Dennis J. Kucinich, Ranking Minority Member
Subcommittee on National Security, Emerging Threats, and
International Relations
Committee on Government Reform
House of Representatives

Subject: *Foreign Assistance: USAID's Operating Expense Account Does Not Fully Reflect the Cost of Delivering Foreign Assistance*

Humanitarian and economic development assistance has long been an important component of U.S. global security strategy. Since 1962, the U.S. Agency for International Development (USAID) has managed more than \$273 billion in such assistance. In fiscal year 2003, USAID estimates that it will obligate about \$13 billion for assistance programs in almost 160 countries. In recent years, demands on USAID's budget and workforce have increased as the agency strives to meet emerging requirements, such as reconstruction efforts in Afghanistan and Iraq and increased funding for health programs. However, USAID officials have expressed concern that funds provided for its administrative or operating expenses have not kept pace with the agency's requirements.

Since 1976, Congress has included a separate appropriation to consolidate USAID's operating expenses into a single budget item. Congress intended that USAID pay for the administrative costs of delivering foreign assistance (its "cost of doing business") from an operating expense account separate from its humanitarian and development assistance program funds.¹ These operating expenses are costs incurred primarily for the benefit of the United States rather than the foreign assistance recipient. In accordance with congressional guidance,² USAID reports all expenses related to U.S. direct-hire staff as operating expenses³ and, based on its guidance on what constitutes the cost of doing business, other operating expenses—from rent to office utilities and supplies. In fiscal year 2003, USAID estimates

¹S. Rept. 94-704.

²H. Rept. 95-701 and S. Rept. 95-1194.

³USAID's Automated Directives System, Functional Series 600, chapter 601 (Funding Source Policy).

that it will obligate \$668 million for its operating expenses. At your request, we examined (1) trends in USAID's operating expenses since 1995 and (2) whether charges to USAID's operating expense account reflect the agency's actual cost of doing business.

To accomplish our objectives, we interviewed cognizant officials in USAID's regional bureaus and its bureaus for management and policy and program coordination. In connection with other work, we also conducted fieldwork at seven overseas missions. We reviewed budget and workforce data generated by USAID missions and headquarters offices from fiscal years 1995 to 2003. We present our analysis in obligations because this information was readily available in USAID's annual congressional budget justifications. We converted the obligations data into constant year 2003 dollars to adjust for inflation and better reflect the agency's purchasing power over the period.

Results in Brief

According to data USAID reported, over fiscal years 1995 to 2003, USAID's total obligated operating expenses have ranged from a low of \$595.7 million in 1998 to a high of \$654.8 million in 1995, and USAID estimates total obligations in 2003 will be about \$668 million (in constant 2003 dollars).

- The largest administrative category in USAID's operating expense account is salaries and related support for U.S. direct-hire staff. Obligations for these expenses account for 43 percent (\$277.7 million) of USAID's estimated operating expenses for fiscal year 2003. However, funds obligated for direct-hire personnel declined during fiscal years 1995 through 2001—from \$302.5 million to \$249.2 million—primarily due to declining levels of direct-hire staff during this period. But, in fiscal years 2002 and 2003, U.S. direct-hire personnel costs have increased over 11 percent. USAID expects these costs to continue rising as it continues its recent hiring efforts.
- Three other administrative categories—other staff costs, information technology, and rent—account for about 33 percent (\$216.5 million) of USAID's estimated operating expenses for fiscal year 2003. Although these expenses varied from year to year, the net change in total from fiscal year 1995 was a decline of less than 1 percent.
- Between fiscal years 1995 and 2002, operating expense obligations as a percentage of program obligations remained fairly level—averaging about 8.5 percent. However, in fiscal year 2003, the operating expenses

to program funds ratio dropped to 5 percent due to large amounts of supplemental funding.⁴

USAID's operating expense account does not fully reflect the agency's cost of doing business primarily because the agency pays for some administrative activities done by contractors and other nondirect-hire staff with program funds. As we noted in our recent report,⁵ USAID's overseas missions have increasingly relied on personal services contractors—foreign national personal services contractors make up about 60 percent of its workforce—to manage USAID's development activities due to declining numbers of U.S. direct-hire staff. Nondirect-hire staff may be paid with either program or operating expense funds. Many of these staff perform administrative duties that directly benefit the United States, and it is often difficult to distinguish between the administrative duties they perform and those done by U.S. direct-hire personnel. In four missions we visited, some foreign national personal services contractors were financial and procurement analysts, secretaries, and drivers. Although these analysts and support staff performed primarily administrative tasks for USAID's benefit, some were assigned to specific technical teams, and their salaries and support costs were paid from program funds because USAID considered their services directly allocable to these activities and did not report them as operating expenses. According to USAID officials, based on data recently collected from its missions, USAID estimates that about \$350 million in program funds will be used to pay for nondirect-hire staff performing both administrative and technical support functions in fiscal year 2003. As a result, the operating expense account and other funds authorized for operating expenses do not fully reflect the cost of delivering foreign assistance.

To help provide increased visibility over USAID's operating expenses and a more realistic accounting of the agency's cost of doing business, we recommend that the USAID Administrator identify all administrative costs that primarily benefit the United States—whether paid for with operating expense funds or program funds—and report this information to the

⁴Primarily, funding provided for relief and reconstruction activities in Iraq and the global initiative to fight human immunodeficiency virus/acquired immune deficiency syndrome.

⁵U.S. General Accounting Office, *Foreign Assistance: Strategic Workforce Planning Can Help USAID Address Current and Future Challenges*, GAO-03-946 (Washington, D.C.: Aug. 22, 2003).

Congress in its annual budget requests for operating expense account appropriations.

In commenting on a draft of this report, USAID fully agreed with our recommendation. USAID also stated that it is well aware of the issues raised and is taking corrective actions to fundamentally restructure financing for the administration of foreign assistance to reflect the full cost of assistance delivery and match resources with changing circumstances.

Background

Until the mid-1970s, about two-thirds of USAID's operating expenses were funded from appropriations to program accounts, and the rest were funded from a separate administrative expenses account.⁶ In 1975, the House Appropriations Committee noted that when USAID was first established, a large percentage of direct-hire employees implemented assistance projects as technical specialists, and their salaries and support were paid from program funds because they were considered to be working primarily for the benefit of the recipient country.⁷ USAID staff working for the benefit of both the recipient country and the U.S. government were also paid from program funds, while the remaining staff—whose activities were primarily in the interest of the United States—were paid from the administrative expense account. The Committee noted that this distinction became blurred as USAID delegated more program implementation responsibilities to third parties and its direct-hire staff took on more of a monitoring role. The Committee concluded that operating expense activities paid from program funds did not really differ from those paid from the administrative expenses account and suggested the creation of a separate account that would reflect all operating expenses.

In 1976, Congress began providing a line-item appropriation for operating expenses separate from USAID's humanitarian and economic development assistance programs.⁸ The accompanying Senate report noted that USAID's cost of doing business would be better managed if these funds were

⁶The administration's budget request for fiscal year 1975 identified 11 separate funding accounts from which administrative expenses would be funded.

⁷H. Rept. 94-53.

⁸P.L. 94-330.

separately appropriated.⁹ Congress authorized USAID's separate operating expense account the following year.¹⁰

USAID's criteria for determining the expenses to be paid from operating expense funds are based on guidance it has received from Congress as well as its assessment of who benefits from a particular activity. A 1977 congressional report stated that "operating costs include not only the traditional 'administrative expenses,' but also the substantial cost of support and management of programs and projects (such as technical planning and management of specific projects, contracting, procurement of commodities, engineering services, and handling of trainees from abroad)."¹¹ Congressional reports in the late 1970s directed USAID to fund the costs of all full-time staff in permanent positions from the operating expense account.¹²

We also note that since 1976 Congress has approved funding sources other than USAID's operating expense account appropriation to pay USAID's operating expenses. For example, in fiscal year 2003, USAID's estimated appropriations for operating expenses are about 86 percent (\$572.2 million) of the agency's total estimated obligations, and other sources comprise the remaining 14 percent (\$95.8 million). Other congressional sources of operating expense funds have included specific uses of program funds and specific amounts in supplemental appropriations for humanitarian and reconstruction assistance—\$21 million for fiscal year 2003.

In addition, local currency trust funds generated by the sale of U.S. commodities, which totaled more than \$27 million at 18 overseas missions in fiscal year 2003, can be used for their operating expenses. However, the Office of Management and Budget offsets the use of trust funds from USAID's estimated operating expense account requirements. In addition, USAID regulations allow missions to charge a portion of leased office space, utilities, and maintenance costs to program accounts based on the number of program-funded personnel employed at the mission.

⁹S. Rept. 94-704.

¹⁰P.L. 95-88, Sec. 129, 22 U.S.C. 2427.

¹¹H. Rept. 95-240.

¹²H. Rept. 95-701 and S. Rept. 95-1194.

Enclosure I provides more detail on USAID's sources of funding for operating expenses in fiscal year 2003.

Trends in USAID's Operating Expenses

Over fiscal years 1995 to 2002, USAID's total obligated operating expenses in constant 2003 dollars have ranged from a low of \$595.7 million in 1998 to a high of \$654.8 million in 1995, and USAID estimates total obligations in 2003 will be about \$668 million.¹³ However, as table 1 shows, the various administrative categories have varied considerably over this period with the net changes resulting in a modest total decline of about 1.2 percent between fiscal years 1995 and 2003.

- The largest administrative category in USAID's operating expense account is salaries and related support for U.S. direct-hire staff—accounting for 43 percent of USAID's estimated operating expenses in fiscal year 2003. However, funds obligated for direct-hire personnel declined during fiscal years 1995 through 2001, primarily due to declining levels of direct-hire staff during this period. But, in fiscal years 2002 and 2003, U.S. direct-hire personnel costs have increased over 11 percent. USAID expects these costs to rise as it continues its recent hiring efforts.
- Three other administrative categories—other staff costs, information technology, and rent—accounted for about 33 percent of USAID's estimated operating expenses for fiscal year 2003. Since fiscal year 1995, rent has increased more than 10 percent while other staff costs and information technology declined 6 percent and 3.4 percent, respectively. Although these expenses varied from year to year, the net change in total from fiscal year 1995 was a decline of less than 1 percent.
- Twelve other administrative categories account for the remaining operating expenses—about 24 percent in fiscal year 2003. Several categories varied widely over this period. Most notably land and structures ranged from a high of about \$21 million in fiscal year 2000 to a low of \$241,000 in 1996. Beginning in fiscal year 2004, most funding for new buildings will be provided from a newly established Capital Investment Fund.

¹³Including a \$21 million supplemental for operating expenses that USAID has not allocated to its administrative categories.

Table 1: Table 1: Operating Expense Obligations by Administrative Category, Fiscal Years 1995-2003 (Constant 2003 dollars in thousands)

Administrative category	Fiscal years									Percentage change 1995-2003
	1995	1996	1997	1998	1999	2000	2001	2002	2003 ^a	
U.S. direct-hire personnel costs ^b	\$302.5	\$292.3	\$268.2	\$255.1	\$255.2	\$254.3	\$249.2	\$264.5	\$277.7	-8.2
Other staff costs ^c	90.4	87.3	79.6	77.2	77.3	67.8	74.4	78.5	85.0	-6.0
Information technology ^d	68.2	56.0	47.7	60.0	61.7	64.1	83.8	78.6	65.9	-3.4
Rent ^e	59.4	55.2	54.7	56.8	59.3	57.3	61.6	62.8	65.7	10.5
Goods and services from government accounts ^f	24.7	24.3	38.0	28.5	29.0	31.7	29.4	33.5	38.2	54.6
Other USAID-contracted services ^g	19.5	14.6	19.4	32.5	38.5	20.0	21.5	21.1	22.3	14.2
Operation and maintenance	14.2	14.3	11.4	11.8	10.8	8.6	11.1	14.0	15.7	10.8
Communications and utilities	20.8	19.1	17.3	18.9	14.1	12.9	13.0	12.1	13.8	-33.5
Land and structures	0.7	0.2	9.8	1.9	12.2	21.0	3.5	4.3	13.3	1,715.1
Security	6.8	7.6	6.8	6.8	7.7	8.2	10.4	9.8	11.6	71.7
Equipment	11.8	19.5	30.0	14.4	19.4	18.3	25.3	18.3	10.1	-14.3
Transportation of goods	15.9	13.0	10.5	11.7	10.8	10.5	9.9	9.2	9.9	-37.8
Supplies and materials	11.8	8.9	9.6	10.5	10.7	11.1	10.9	10.3	8.8	-25.6
Training	5.7	5.9	5.9	8.9	5.5	7.2	10.2	7.0	8.4	47.7
Claims and indemnities	0.6	1.0	0.7	1.1	2.3	0.4	4.1	0.6	0.6	-6.4
Grants, subsidies, and contributors	1.7	1.7	2.4	0	0.2	0.4	1.5	1.2	0	-100.0
Total^h	\$654.8	\$621.0	\$612.2	\$595.7	\$614.5	\$593.9	\$619.9	\$625.8	\$647.0	-1.2

Source: GAO analysis of USAID data.

Note: USAID data are taken from its congressional budget justification documents.

^aWe did not include \$21 million provided to USAID in supplemental funding for operating expenses in fiscal year 2003 because USAID has not allocated it among the administrative categories.

^bIncludes compensation, benefits, training, and travel expenses, such as home leave, post-assignment travel, and travel expenses incurred for training.

^cUSAID funds many of its overseas non-U.S. direct-hire personnel using operating expenses because their tasks are administrative in nature, such as providing support to the executive office.

^dIncludes costs for computer equipment, systems design and analysis, maintenance, and support.

^eIncludes domestic and overseas rental payments.

^fIncludes USAID's portion of administrative costs shared by U.S. agencies with an overseas presence and paid primarily to the Department of State.

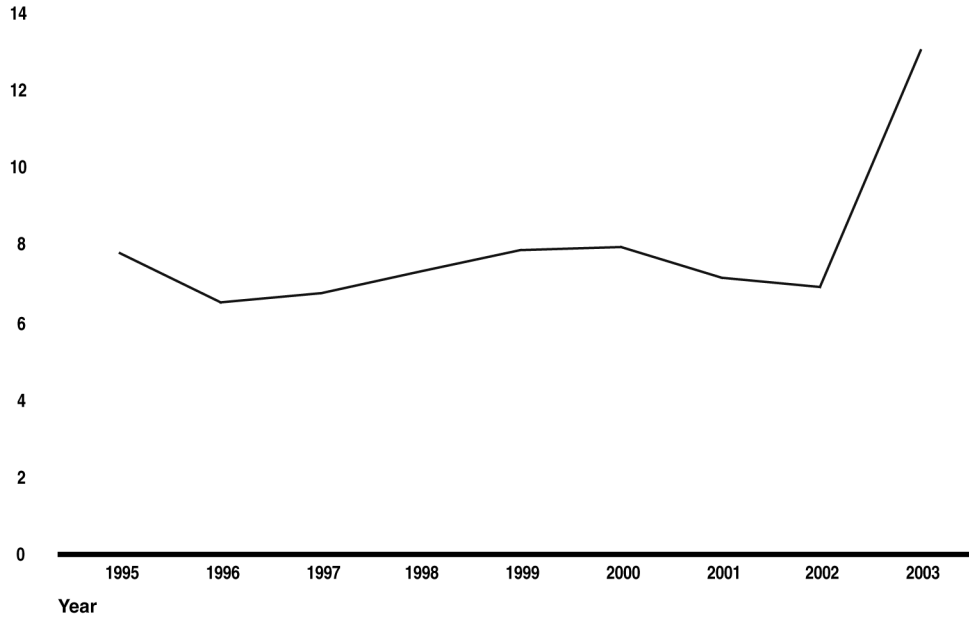
⁹Includes operation and maintenance of facilities and goods, security costs, equipment, and transportation of household goods.

^hTotals may not add due to rounding.

As shown in figures 1 and 2, between fiscal years 1995 and 2002, USAID's program obligations decreased at a faster rate than operating expense obligations, with fluctuations during this period. In constant 2003 dollars, USAID's program obligations decreased by more than 10 percent—from almost \$7.8 billion in fiscal year 1995 to about \$6.9 billion in fiscal year 2002. In fiscal year 2003, USAID's estimated program obligations increased almost 88 percent to \$13 billion because of \$4.2 billion in supplemental funds for, among other things, relief and reconstruction activities in Iraq and the global initiative to fight human immunodeficiency virus/acquired immune deficiency syndrome. However, USAID's estimated operating expense account obligations for fiscal year 2003 did not increase at a similar rate. Including \$21 million in operating expense funds provided by supplemental legislation, estimated operating expenses increased less than 7 percent.

Figure 1: Program Obligations, Fiscal Years 1995 to 2003

Constant 2003 dollars in millions

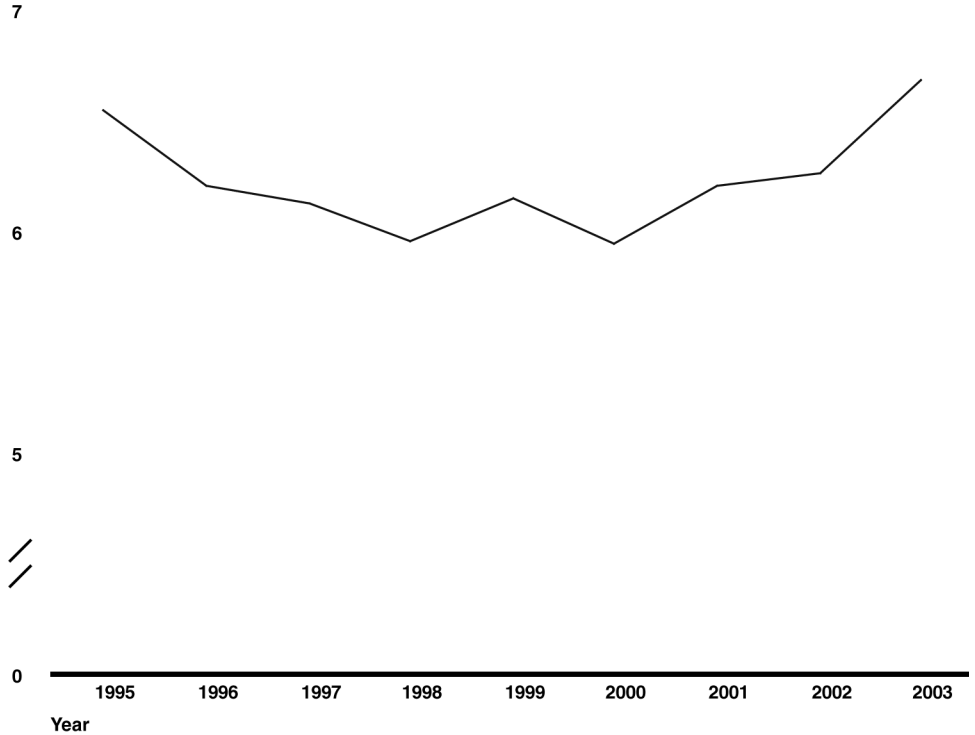


Source: GAO analysis of USAID data.

Notes: USAID data are taken from its congressional budget justification documents and the Emergency Wartime Supplemental Appropriations Act of 2003 (P.L. 108-11). Fiscal years 1995 to 2002 are actual obligations adjusted to constant fiscal year 2003 dollars. Fiscal year 2003 data are estimated amounts. Fiscal year 2003 operating expenses include \$21 million provided by supplemental legislation. Program data for fiscal years 2000 to 2003 include disaster recovery, emergency response, and supplemental funds. Program funding obligations sources include development assistance; child survival and health; development fund for Africa; international disaster assistance; transition initiatives; economic support funds; support for Eastern European democracy; Freedom Support Act; Public Law 480; Iraq relief and reconstruction fund; and credit program funds.

Figure 2: Operating Expense Obligations, Fiscal Years 1995 to 2003

Constant 2003 dollars in thousands



Source: GAO analysis of USAID data.

Note: See figure 1 notes.

As shown in figure 3, from fiscal years 1995 to 2002, USAID's operating expense obligations fluctuated as a percentage of program obligations but averaged about 8.5 percent. In fiscal year 2003, estimated operating expense obligations dropped to about 5 percent of estimated program obligations, including the supplemental funding.

Figure 3: USAID's Operating Expense Obligations as a Percentage of Program Obligations, Fiscal Years 1995 to 2003



Source: GAO analysis of USAID data.

Note: See figure 1 notes.

USAID's Operating Expense Account Does Not Include All Administrative Costs

USAID's operating expense account does not fully reflect the agency's cost of doing business primarily because the agency pays for some administrative activities done by contractors and other nondirect-hire staff with program funds. As we reported in August 2003, as the number of U.S. direct hire foreign service officers has declined over the years, USAID missions have often hired personal services contractors—usually foreign nationals—to manage development activities and provide technical project support.¹⁴ Approximately 60 percent of USAID's staff are foreign national personal service contractors. Many of these nondirect-hire personnel are engaged in activities that directly support USAID programs and are paid with program funds.

¹⁴[GAO-03-946](#).

Many nondirect-hires perform administrative duties that directly benefit the United States, and it is often difficult to distinguish between the administrative duties they perform and those done by U.S. direct-hire personnel. These staff can be paid with program or operating expense account funds. In four missions we visited—the Dominican Republic, Mali, Peru, and Senegal—some foreign national personal services contractors were financial and procurement analysts, secretaries, and drivers. Although these analysts and support staff performed primarily administrative tasks for USAID’s benefit, some were assigned to specific technical teams and their salaries and support costs were paid from program funds because USAID considered their services directly allocable to these activities and did not report them as operating expenses. According to USAID officials, based on data recently collected from its missions, USAID estimates that about \$350 million in program funds will be used to pay for personal services contractors performing administrative functions overseas in fiscal year 2003.¹⁵

Institutional contract staff also provide administrative and technical services in support of USAID programs. In 2002, for example, USAID estimated that 758 institutional contractor staff were involved in the administration of foreign assistance at an estimated cost of \$95 million. Of this total staff, 450 positions were funded from operating expense appropriations (\$56 million), and 308 positions were funded from program funds (\$39 million).¹⁶ USAID is continuing its review of institutional contractors to decide how to characterize their work.

A 2002 USAID team examining USAID’s operating expense account found that most of the agency’s evaluations and analyses have been paid with program funds, based on the rationale that these activities are intended to enable the agency to better serve its “ultimate beneficiaries.” But this may not be what Congress intended.

¹⁵One senior level USAID program planning officer told us that about 10 to 15 percent of program funds may be a more realistic estimate of USAID’s cost of doing business (compared with the 8.5 percent average since 1995).

¹⁶According to USAID, these figures were developed as part of a staff study of institutional contractors and were as of September 30, 2002.

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- The team’s report stated that “although strategy development, project design, evaluation and other activities relate to the agency’s cost of doing business, in the longer run they are essential building blocks of agency operations and are necessary for program oversight. Ultimately, the impact of improved strategies, design, and projects has an impact on the agency’s beneficiaries. In that sense, there clearly is a rationale for providing program funding for these activities.¹⁷”
 - In contrast, a USAID attorney assisting the team noted that a 1980 Senate Appropriations Committee report stated that only such planning and evaluation activities that are project specific should be paid with program funds, but that activities with a primary objective of serving the agency, including analyses for development assistance policy planning, were part of the cost of doing business.

Cognizant USAID officials contend that congressional intent has shifted and that from 1980 to the present, Congress has increasingly encouraged the agency to use program funds to support certain administrative costs. However, these officials also stated that the increased reliance on program funded staff for some administrative activities further demonstrates the need to restructure how operating expenses are accounted for to better reflect USAID’s cost of doing business.

Conclusion

Since 1976, Congress has provided a separate appropriation for USAID’s operating expenses and, over the years, has approved additional funding sources for operating expenses to separate administrative costs from USAID’s humanitarian and development assistance programs. However, as U.S. direct-hire staff levels have declined, overseas missions have hired personal services and institutional contractors and other nondirect-hire staff to manage development activities and perform various administrative duties, but pay for some of these services with program funds. But USAID has not fully identified or reported the extent of these costs. Therefore, separating USAID’s cost of doing business from its humanitarian and development programs is not always done. As a result, the operating expense account and other funds USAID has available for operating expenses do not fully reflect the cost of delivering foreign assistance.

¹⁷U.S. Agency for International Development/Bureau for Policy and Program Coordination, *USAID’s Operating Expense Account: Current Practices and Planned Reforms* (Washington, D.C.: Oct. 7, 2002).

Recommendation for Executive Action

To help provide increased visibility over USAID's operating expenses, better reflect what USAID spends on program administration, and provide a more realistic accounting of the agency's cost of doing business, we recommend that the USAID Administrator identify all administrative costs that primarily benefit the United States—whether paid for with operating expense funds or program funds—and report this information to the Congress in its annual budget requests for operating expense account appropriations. Such an accounting should form the basis of USAID's annual budget request for operating expense funds.

Agency Comments

USAID provided written comments on a draft of this report (see enc. II). It fully agreed with the recommendation. USAID acknowledged that the current structure of the operating expense account does not serve workforce planning needs or foreign policy objectives because (1) staffing decisions are often made according to funding source rather than workforce requirements and (2) as a result, the heavy reliance on short-term contractors has limited USAID's capacity to respond to foreign assistance needs.

USAID also stated that it is well aware of the issues raised in the report and is taking corrective action. USAID noted that, within the past 18 months, it has completed assessments of operating expenses and overseas staffing, a survey of program-funded personnel, and an approach for full costing of assistance at a unit level. It has also initiated a long-term assessment of human resources. As a result of these efforts, USAID is reviewing ways to fundamentally restructure financing for the administration of foreign assistance to reflect the full cost of assistance delivery and match resources with changing circumstances.

In addition, USAID officials provided clarification of certain technical matters that we have incorporated into this report, as appropriate.

Scope and Methodology

To examine trends in USAID's spending for operating expenses and program activities since 1995, we analyzed obligations data reported by USAID in its annual budget justification documents. We converted obligations for operating expenses and program activities into constant fiscal year 2003 dollars to adjust for inflation and better reflect the agency's purchasing power during this period. We also met with cognizant budget officials at USAID to better understand the reported operating expense and

program funding data. We did not verify the accuracy of USAID's reported data.

To determine whether USAID's operating expenses reflect its cost of doing business, we reviewed USAID reports and annual budget justifications and met with knowledgeable officials in USAID's Bureau for Policy and Program Coordination, the U.S. Department of State, and the U.S. Office of Management and Budget. In conjunction with other work,¹⁸ we conducted fieldwork at seven overseas missions—the Dominican Republic, Ecuador, Egypt, Mali, Peru, Senegal, and the West Africa Regional Program in Mali.¹⁹ We reviewed mission staffing reports to determine whether staff were funded from the operating expense account or program funds and discussed the duties of personnel with cognizant mission officials.

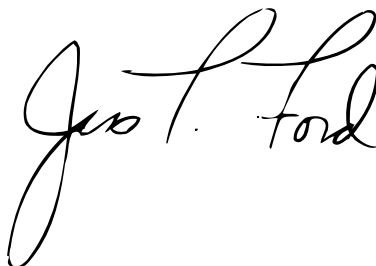
Our review was conducted from May through September 2003 in accordance with generally accepted government auditing standards.

We are sending copies of this report to appropriate congressional committees, the Administrator of USAID, the Secretary of State, and the Director of the Office of Management and Budget. We will also make copies available to others upon request. In addition, this report will be available at no charge on our Web site at <http://www.gao.gov>.

¹⁸GAO-03-946.

¹⁹We also examined documents and interviewed officials at USAID's mission to Indonesia at its temporary location in Arlington, Virginia, following its evacuation in October 2002.

If you or your staff have any questions concerning this report, please contact me at (202) 512-4268 or Al Huntington, Assistant Director, at (202) 512-4140. Other key contributors to this report were Kimberley Ebner, Emily Gupta, and Audrey Solis.

A handwritten signature in black ink that reads "Jess T. Ford". The signature is written in a cursive style with a large, looping initial "J" and a distinct "T" and "F".

Jess T. Ford, Director
International Affairs and Trade

Enclosure I: Description of Sources of Funding for USAID's Operating Expenses Fiscal Year 2003

Since 1976, Congress has approved funding sources other than the U.S. Agency for International Development's (USAID) operating expense account appropriation to pay for operating expenses. Although USAID reports these other funds as operating expenses, they are not part of its single budget item appropriation. As shown in table 2, for example, in fiscal year 2003, other sources comprised 14.2 percent (\$95.8 million) of what USAID is estimating as operating expense obligations.

Table 2: USAID's Estimated Obligations for Operating Expenses in Fiscal Year 2003 by Sources of Funding (Dollars in millions)

Funding source	Amount	Percent
Annual appropriation	\$572,200	85.6
Unobligated balance	34,231	5.1
Local currency trust funds	27,557	4.1
Supplemental funding	21,000	3.1
Authorized program funds	7,417	1.1
Reimbursements	5,600	0.8
Total	\$668,005	99.8^a

Source: USAID fiscal year 2004 congressional budget justification documents and the Emergency Wartime Supplemental Appropriations Act of 2003 (P.L. 108-11), which provided supplemental operating expense funding.

^aDoes not add to 100 percent due to rounding.

Annual appropriation: These are funds for which USAID receives new budget authority every fiscal year and do not include supplemental appropriations for operating expenses obtained during the course of the fiscal year.

Unobligated balance: The unobligated balance is of any unobligated funds that USAID has the authority to transfer to the following fiscal year's operating expense account.

Local currency trust funds:²⁰ U.S. commodity import programs normally generate this type of funding. In fiscal year 2003, 18 USAID missions have local currency trust funds. The Egypt mission's trust fund is the largest

²⁰USAID cites a recurring provision in its appropriations bills as legal authority to use local currency trust funds. For fiscal year 2003, see Public Law 107-115, section 529.

(almost \$73 million in January 2003), and the mission uses it to pay for training, housing, and dependents' education.

Supplemental funding: Supplemental legislation for an emergency response or large-scale reconstruction generally specifies an amount that USAID may use as operating expenses in administering such activities.

Authorized program funds: Some specific program funding can be transferred to the operating expense account. The amount varies according to different rules governing the transfer of program funding from each account. For example, USAID can transfer a limited amount of program funds to the operating expense account to finance travel to countries with USAID activities but no USAID field presence. Additionally, USAID has the authority to transfer larger program funding amounts from other accounts to the operating expense account, not to exceed 10 percent of the originating program account.²¹ But this action requires presidential approval and is rarely undertaken.

Reimbursements: These funds are primarily generated internally by USAID. Examples include reimbursements to USAID from the its Office of the Inspector General or the Development Credit Program—units that receive separate operating expense appropriations—for services by USAID, such as computer services and rent. Proceeds from the sale of equipment overseas are also included in this category.

²¹Foreign Assistance Act of 1961, as amended, title 22, section 610a.

Enclosure II: Comments from the Agency for International Development



U.S. AGENCY FOR
INTERNATIONAL
DEVELOPMENT

SEP 29 2003

Mr. Jess T. Ford
Director
International Affairs and Trade
U.S. General Accounting Office
441 G Street, N.W.
Washington, DC 20548

Dear Mr. Ford:

I am pleased to provide the formal response of the U.S. Agency for International Development (USAID) to the draft GAO report entitled "FOREIGN ASSISTANCE: USAID's Operating Expense Account Does Not Fully Reflect the Cost of Delivering Foreign Assistance" (September 2003).

The GAO report indicates accurately a critical and timely issue for USAID. It is clear that USAID must have a better approach to both recognizing the full cost of assistance delivery and better linking and matching available resources for administration with the programs. While direct hire staff have declined over time, program requirements and, internal budgetary requirements for mandatory operating cost increases--i.e., emerging technology needs, security, and ICASS costs--have grown, placing great pressure on the Agency.

USAID is well aware of the issues within the Report and is taking action. Within the past 18 months, USAID has completed an assessment of operating expenses, completed a survey and costing of program funded personnel, prepared an assessment of field presence and overseas staffing, from which USAID staff will be redeployed, completed an approach for full costing of assistance at a unit level and initiated a long term assessment of Human Resources. Most importantly, in light of the results of these efforts, USAID has initiated a review of a fundamental restructuring of the financing of the administration of foreign assistance to reflect the full cost of assistance delivery and to match resources with changing circumstances. USAID sees this GAO Report as a confirmation of the validity of the issues which

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have been identified and as encouragement to reach consensus on a new approach for the financing of the administration of foreign assistance.

With regard to the history of the OE account, we believe it is important to emphasize that Congressional intent evolved over time with changing circumstance. From 1980 on Congress has increasingly encouraged the agency to use program funds (in lieu of increased OE) to support salaries of certain types of personnel, payment of administrative expenses like travel for certain programs, and costs of managing unanticipated program increases (e.g. HIV/AIDS and supplementals). The increasing reliance on program funded staff underscores the need to restructure the cost of administration to transparently reflect the total cost of doing business.

It is important to note too that USAID is monitoring the use of program-funded staff. The Agency's HR staffing pattern report has included such non direct staff since 1995 as does our Congressional Budget Justification (CBJ). USAID completed a costing of program funded staff last year. We have efforts in process to expand monitoring and control of non-direct hire staff including a USAID notice which sets out procedures and the Agency's Annual Report now includes efforts on costing. We are increasing our efforts through methodology which brings all cost together against the pertinent program cost, including allocation of support functions.

We want to emphasize that non-direct hire staff is funded both through OE and program accounts, depending on the functions of the position, in accordance with USAID guidance. OE-funded PSC's have been used to fill critical staffing gaps. USAID uses such short-term measures because it does not have adequate numbers of staff (a "float" capacity) to cover training time and gaps between assignments. In contrast, program funded people are, by definition, related directly to programs and strategic objectives rather than support function in accordance with USAID guidance. All costs not specifically and directly related to identified strategic objectives are funded from Operating Expenses. USAID staffing pattern reporting distinguishes between OE and program funded non-direct hire staff.

In summary, the GAO report highlights a key issue for USAID—the structure and sufficiency of resources for the administration of foreign assistance. USAID agrees fully with the proposed recommendation to modify our approach to administrative cost to provide a realistic accounting of the

**Enclosure II: Comments from the Agency for
International Development**

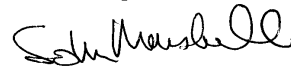
3

Agency's cost of doing business. The report is particularly timely as USAID is engaged in the development of a new approach to administrative cost financing, which responds to this requirement. We do not believe the current structure of the Operating Expense account serves foreign policy objectives or workforce planning needs. Because Operating Expenses have been supplemented by program resources, by both Congress and USAID, workforce decisions are made according to funding source rather than workforce need. As a result, a wide variety of personnel systems has evolved with heavy reliance on short-term contract assignments limiting the institutional capacity of the Agency to respond to foreign assistance needs.

If you have any questions concerning this response please contact James Painter, USAID Bureau for Policy and Program and Coordination at (202) 712-0280.

Thank your for the opportunity to respond to the draft report and for the courtesies extended by your staff in the conduct of this review.

Sincerely,



John Marshall
Assistant Administrator
Bureau for Management

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