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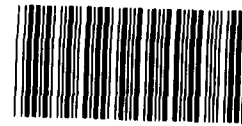
Before the Subcommittee on Western Hemisphere
Affairs, Committee on Foreign Affairs,
House of Representatives

For Release on Delivery
Expected at
3:00 p.m. EST
Tuesday,
March 23, 1993

EL SALVADOR

Status of Reconstruction
Activities One Year After the
Peace Agreement

Statement of Harold J. Johnson, Director, International Affairs
Issues, National Security and International Affairs Division



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Mr. Chairman and Members of the Subcommittee:

We are pleased to be here today to discuss the economic, political, and social reconstruction of El Salvador. My testimony is based on our ongoing evaluation of U.S. assistance to El Salvador--an assignment undertaken at your request--and three recent GAO reports.¹ I will focus on five areas: (1) the National Reconstruction Plan, (2) reconstruction funding, (3) nongovernment organization (NGO) participation in reconstruction, (4) the Municipalities in Action program (MEA by its Spanish acronym), and (5) land redistribution.

SUMMARY

It has been only a little over 1 year since the United Nations-sponsored peace agreement in El Salvador was signed and the reconstruction program is in its early stages, but progress toward peace and economic reconstruction has been made. The Farabundo Marti Liberation Front (FMLN) and the government of El Salvador are successfully negotiating the content and implementation of the National Reconstruction Plan. NGOs are playing an increasing role in implementing social development projects. Through the MEA program, over 1,000 critically needed projects at the community level have been funded, and mayors, local FMLN and other officials, and community residents we spoke with are complimentary of the program. Yet, serious problems continue to face the government and the FMLN.

The overriding problem in El Salvador is that although the international donor community has pledged \$800 million for reconstruction, insufficient money has been forthcoming, particularly for areas such as public safety and land redistribution that many believe are critical to the long-term success of the political settlement. The FMLN and the government were assured by the United Nations that the international donor community would help pay for the cost of reconstruction, and both parties seemed to have unreasonable expectations of what could be done and when. In short, expectations for economic rehabilitation generated by the Peace Agreement have outpaced fiscal realities. The Peace Agreement was intentionally ambiguous with regard to the economic reconstruction plan, and this may have been necessary at the time, but allowing for the details of the plan to be worked out by the parties at a later date has led to some of the problems being seen today.

¹Aid to El Salvador: Slow Progress in Developing a National Civilian Police (GAO/NSIAD-92-338, Sept. 22, 1992); El Salvador: Efforts to Satisfy National Civilian Police Equipment Needs (GAO/NSIAD-93-100BR, Dec. 15, 1992); and El Salvador: Role of Nongovernment Organizations in Postwar Reconstruction (GAO/NSIAD-93-20BR, Nov. 16, 1992).

Solutions to differences between the government and the FMLN on the plan's content are being dealt with through negotiations and concessions. The end result of these negotiations, however, has been to expand programs to the point that the costs exceed the resources available or anticipated. Negotiated solutions were reached without regard to where the money would come from--a natural outgrowth of good-intentioned parties making decisions about other people's money. For example, a United Nations-brokered settlement concerning land redistribution more than tripled the estimated number of beneficiaries to 47,500, creating a shortfall of at least \$61.7 million for land procurement. Also, land is being provided without sufficient agricultural credit, which may cost another \$71 to \$255 million. The costs and sources of funding for some critical programs, like public safety, simply were not thought through when a commitment was made. For example, the new national civilian police force is underfunded by at least \$23 million for operating costs in 1993 alone, and an estimated \$40.3 million is needed for equipment and facilities in 1993 and 1994, but no funding source is in sight.

Mr. Chairman, as you know, the United States committed \$250 million to pay for immediate and longer-term reconstruction needs over a 5-year period. This was to be essentially front loaded to allow other donors time to provide funds they pledged. The problem now is that projects' funding requirements greatly exceed what the United States has to spend. The United States is planning to redirect funds from other planned reconstruction activities to take care of some of these unfunded needs but this has not been enough. While the results of upcoming Consultative Group and European Community meetings may provide some additional resources, at this point in time, the reconstruction plan as currently envisioned may be out of reach.

THE NATIONAL RECONSTRUCTION PLAN WORKING, BUT IS STILL BEING NEGOTIATED

Developing and maintaining the National Reconstruction Plan has proven to be difficult. The government of El Salvador and the FMLN have differed from the start on the content of the plan and how funds to implement it would be allocated, but both have been flexible and willing to settle their differences through negotiation on a case-by-case basis. While negotiations have taken time and some target dates have been missed and programs delayed, we do not believe that this has been a significant barrier to the overall reconstruction efforts.

FMLN and Government Beginning to Cooperate

The Peace Agreement facilitated by the United Nations assigned responsibility to the government to develop a reconstruction plan to implement the social and economic reforms in the areas most affected by the war. The government was also responsible for

coordinating the execution of the plan, managing reconstruction resources from donors, and controlling and accounting for funds. The agreement required, however, that the government consider recommendations from the FMLN and others so that the plan would reflect the collective will of the nation. While the government has considered FMLN input to the plan, the FMLN has continued to criticize the plan for emphasizing infrastructure reconstruction over social development and failing to sufficiently incorporate a role for grass-roots organizations and NGOs. Also, the FMLN has accused the government of denying it full participation in the plan's design and execution.

We cannot comment on the merits of each party's position on the plan because each side's position is rooted in a different political agenda, but it is apparent that both sides have made significant concessions to make the plan work. For example:

- Although the FMLN was not satisfied with the reconstruction plan, it joined the government in presenting the plan to the international donor community at the Consultative Group meeting in March 1992, thus enhancing its chances for international funding.
- After the FMLN linked force demobilization to the provision of certain benefits, the government increased benefits specifically for FMLN ex-combatants to include household goods packages and a rehabilitation program for the wounded.
- Although not necessarily to its political advantage, the government has accepted and has been abiding by a United Nations-brokered land agreement that increased the number of beneficiaries and gave FMLN ex-combatants first priority to receive land.

Distribution of Funds

The National Reconstruction Plan stipulates that the government use three entities to implement reconstruction projects: (1) the MEA program, which performs small infrastructure projects critical to local community development; (2) NGOs, which focus on social issues such as training, credit, and maternal health and child care; and (3) government ministries and organizations that implement national health and education programs and major infrastructure reconstruction projects. Some NGOs that were once affiliated with the FMLN, and their supporters, are concerned that government funding decisions will disproportionately favor the MEA and organizations that the government used during the war.

Based on our assessment of how reconstruction funds have so far been distributed, we did not find these concerns to be well founded. As of January 1993, about 28 percent of funds approved

went for NGO projects, 26 percent for MEA projects, and 47 percent for central government organizations' projects. Our work to date indicates that the government has allocated funding based on the type of activity to be provided and the merit of individual projects, and has not favored one type of implementing entity over another in its funding decision.

FUNDING IMMEDIATE RECONSTRUCTION NEEDS IS A PROBLEM

The FMLN and the government were encouraged to sign the Peace Agreement with assurances from the United Nations that the international donor community would help fund the cost of rebuilding the social, political, and economic structure of the country. Although donors pledged \$800 million in March 1992, contributions have been insufficient for critical activities.

Some programs, most notably public safety and land redistribution, are among the most contentious issues confronting the government and the FMLN, and are closely tied to demobilization and continued peace. Costs for some critical programs have increased substantially, mainly because of new agreements that were made to avoid breakdowns in the peace process. For example, additional benefits were provided to FMLN ex-combatants under the threat that the FMLN would not otherwise demobilize. The government agreed to provide \$1.3 million for agricultural credit, \$5.3 million for household goods starter packages, and \$1.3 million to begin a rehabilitation program for FMLN wounded. The FMLN has recently asked for funding to provide housing to 11,000 of its ex-combatants, estimated to cost between \$16 and \$35 million, but money to fund this request is not available.

The \$250 million pledged by the United States was intended to take care of immediate and longer-term reconstruction needs over a 5-year period, but due to increasing costs of immediate reconstruction needs, AID is planning to redirect about \$48 million of this pledge from other planned reconstruction activities in El Salvador. Still, severe funding shortfalls exist in key programs, such as public safety and land redistribution.

The Public Safety Program

A new police force and police academy were explicitly called for by the Peace Agreement, and assurances that a new public safety system would be implemented helped convince the FMLN to sign the agreement. We reported in September 1992 that (1) the government had made limited progress establishing and funding the National Civilian Police and (2) the police academy, though operating, was in serious financial trouble. In February 1993, the police academy graduated 600 police recruits but money was not available for adequate salaries, equipment, facilities, or supplies. As of

March 1993, only three donors have provided money for police and academy activities--the United States provided \$20 million, Spain \$1 million, and Norway \$350,000.

For fiscal year 1993, the national civilian police force will need an additional \$23 million for operating costs. This figure does not include the estimated \$40.3 million needed for equipment, supplies, and facilities in 1993 and 1994. The police academy is also short of operating funds and the government is using money originally designated for construction to pay for operating expenses such as utilities, food, and health care for police academy students.

The El Salvadoran government hopes international donor assistance will make up the shortfall, but officials from the United States, the United Nations, and other organizations have expressed doubt that such funding will be provided. Two appeals for funds have gone out to the international donor community, but no response was received. U.S. officials told us that other donor countries, by law or preference, are not interested in funding public safety projects.

Land Redistribution Program

One of the most important aspects of the Peace Agreement and reconstruction plan is the redistribution of land. AID originally planned to provide \$15 million to this program, which would cover the cost of land for 10,000 beneficiaries. In October 1992, a United Nations-brokered agreement increased the number of beneficiaries to 47,500,² significantly increasing program costs. By redirecting funds from other planned activities, the United States plans to increase its contribution to about \$50.2 million. The Land Bank, the government's agency for land redistribution, will also receive \$12 million from the European Community, and the government is providing land it owns valued at \$18.6 million, bringing total resources for land redistribution to \$80.8 million. Based on the average land price specified in the United Nations-brokered land agreement, this is still at least \$61.7 million short of what is needed. AID has said that the shortfall could be as much as \$89 million, based on a more realistic land price. This shortfall estimate could grow even further if higher quality land requested by the FMLN is provided to its beneficiaries.

AID officials are reluctant to consider redirecting further funding to these projects. Except for the European Community,

²These beneficiaries include ex-combatants and the families who have occupied land (without legal title of ownership) that had been abandoned by its owner during the war.

other donors have not provided or pledged funds for land redistribution.

Issues Related to Other Donor³ Funding

World Bank and U.S. officials told us that some donors were hesitant to fund projects until the El Salvadoran government and the FMLN had demonstrated their commitment to peace by reducing or demobilizing their military forces. A World Bank official said that the World Bank, the sponsor of the Consultative Group, was also hesitant to encourage donors to fulfill pledges for this same reason. Additionally, according to U.S. officials, some donors expect the United States to fund highly visible and politically risky projects, such as public safety and land redistribution.

Some funding may be available later this year. The Inter-American Development Bank plans to provide an unrestricted \$90 million loan for disbursement starting later this year, but the bank will disburse the loan in three installments over 18 months. A \$75 million loan from the World Bank, tentatively scheduled to be disbursed in 1992, will not be available until September 1993. The European Community and Germany pledged to finance some reintegration assistance for ex-combatants, but this money is not expected until mid-1994. Finally, the Inter-American Development Bank and Japan have developed a \$250 million water and energy project, but the majority of the project will not be funded until 1994 or 1995.

Another donor conference is scheduled for April 1993, and World Bank officials have indicated that at that time they plan to aggressively encourage donors to provide funding. The El Salvadoran government has been preparing presentations for this meeting as well as a meeting with the European Community later in April, specifically asking for quick-disbursing cash for critical needs. However, since most donors prefer more traditional development activities, and previous attempts to secure funding have been largely unsuccessful, it is unclear how successful the government will be during these meetings.

NGOs AS MAJOR PARTICIPANTS IN RECONSTRUCTION

Forty-five NGOs have been involved in a wide range of reconstruction projects. Over the past 6 months, politically motivated attitudes have softened, the working relationship between the government and NGO community has improved, and more information is being disseminated on reconstruction procedures,

³Other donors include the World Bank, the Inter-American Development Bank, several international organizations, and 18 individual countries pledging bilateral assistance.

increasing their participation. Although few of the NGOs formerly affiliated with the FMLN⁴ have received funding directly from the government, many have received indirect government funding as sub-grantees under umbrella organizations. Many NGOs have weak financial and management controls and do not meet the technical and management requirements of the reconstruction program, and progress in improving these capabilities has been slow.

NGO Participation Has Increased

In June 1992, 29 NGOs were approved to implement reconstruction projects funded either directly or indirectly by the government. By February 1993, 45 organizations had been approved to receive \$11.5 million. It appears that the factors that hindered earlier NGO participation have been resolved. For example, the FMLN told us that FMLN-affiliated NGOs decided in June 1992 not to participate in reconstruction activities until the government and FMLN agreed on the reconstruction strategy. In addition, at that time, NGOs were confused about the process for receiving funding and the general eligibility criteria. But now the government, alone or in concert with FMLN NGOs, has increased efforts to explain the program. Over the past 6 months, NGOs have become more willing to accept funding from the government. One NGO formerly affiliated with the FMLN told us in June 1992 that it would not accept funding from the United States under any circumstances, whereas, in December 1992 it indicated it was willing to work with the government, accept technical assistance, and apply for reconstruction funds. Another NGO formerly affiliated with the FMLN met with AID and the government to discuss four potential projects and has received funding for one project.

Few FMLN Affiliated NGOs Receive Direct Funding

Few NGOs formerly affiliated with the FMLN are receiving funds directly from the government. As of February 1993, the government had approved about \$9 million in direct funding for 5 U.S.-based NGOs and 18 Salvadoran-based NGOs. Only 2 of the 18 were NGOs formerly affiliated with the FMLN and they received about \$176,000, less than 2 percent of the total approved for all NGOs. However, 25 Salvadoran-based NGOs have received funding through subgrants from other NGOs and organizations that are

⁴We define the NGOs formerly affiliated with the FMLN as those organizations that operated primarily in the former conflictive areas and were historically affiliated with the FMLN. In discussions with some of these NGOs, we were told that they no longer wish to be affiliated with any political faction.

funded directly;⁵ 17 of these are NGOs formerly FMLN-affiliated and they received about \$2 million, or 17 percent of the total approved.

The FMLN and its NGO, the Fundación 16 de Enero, claimed that the government has been discriminatory in deciding which NGOs to approve. They said they would like to see greater participation of NGOs, such as those that are members of the Coordinating Council of Private Humanitarian Institutions in El Salvador (CIPHES).⁶ At the time they told us this, however, 13 of the 37 NGOs in the group were already involved in reconstruction activities or other U.S. funded projects. We noted that many of the NGOs receiving direct funding could be considered pro-government, but they also had prior experience delivering development assistance funded by the United States or El Salvadoran government. While one can never be totally certain, we did not find evidence that the government's selections were made for political reasons.

Slow Progress in Improving NGO Capabilities

While we found that few formerly FMLN-affiliated NGOs have received funds for reconstruction activities, this is because of their limited management and technical capability to design projects and meet accountability requirements established by the El Salvadoran government and AID. As we reported in November 1992, we believe that the standards for project proposal submission and administration, control, and accountability are reasonable and do not represent a political barrier to participation. With adequate technical assistance, these administrative and financial management standards can generally be met. Such technical assistance is available through U.S.-funded projects, multinational assistance, and umbrella NGO organizations. However, it has been slow to begin.

Many NGOs, particularly those without prior experience working with the El Salvadoran government or AID, are generally unfamiliar with U.S. requirements for management control. Also, because many NGOs that worked in the conflictive zones during the war provided largely emergency-type assistance, they have little or no experience preparing proposals with project strategies, objectives, approach, methodology, and realistic cost estimates.

Some efforts have been made to improve NGO administrative and technical capabilities; however, they have yet to produce

⁵Three of the 25 NGOs receiving indirect funding also receive direct funding.

⁶This organization performs a coordinating role for 37 Salvadoran-based NGOs.

significant tangible results. The government began developing a manual for NGOs in August 1992, describing the requirements and procedures for reconstruction funding, but as of January 1993, the manual had not been distributed to NGOs. Further, according to a U.S.-based NGO, the manual is too technical for NGOs seeking government funds for the first time. Another project implemented by the U.S.-based NGO Private Agencies Collaborating Together (PACT) has not made much progress until recently. In June 1992, PACT planned to assist 40 NGOs and NGO coordinating councils during their first year. However, because it took from July to November 1992 for the government to approve the PACT project, few NGOs have received this training until recently. PACT did initiate contact with NGOs and assessed their capabilities during the 4-1/2 month approval period, but did not begin formal assistance until November. By February 1993, however, PACT had begun providing varying levels of assistance to about 39 NGOs, 21 of which are formerly affiliated with the FMLN.

Other entities have provided some help to NGOs. The U.S.-based Catholic Relief Services is implementing a credit project through subgrants with 19 Salvadoran-based NGOs. Even though Catholic Relief Services is financially responsible for funds administered by the 19 NGOs, it provides these NGOs with on-the-job training in project administration and implementation. A similar umbrella arrangement through the United Nations Development Program is helping five NGOs--two formerly affiliated with the FMLN--develop project planning and management capabilities. The NGO council CIPHES, in conjunction with a local university and United Nations Development Program, has instructed NGOs on how to prepare, evaluate, and manage projects. Between September and December 1992, 37 representatives from NGOs attended the course.

MUNICIPALITIES IN ACTION PROGRAM

The MEA program is the main program used to provide assistance and promote democratic processes at the local level. However, because of its counter-insurgency role during the war, its use to deliver post-war assistance has been viewed by some with suspicion and distrust. Further, critics have said that it fails to encourage democratic processes and is ineffective as a delivery system. However, officials and residents in communities served by MEA told us it is meeting its objectives.

MEA Is a Primary Means to Deliver Assistance to Communities

MEA was chosen by the government as a primary means to deliver post-war assistance in the former conflictive areas because it (1) was already in place, (2) had demonstrated an ability to get things done, and (3) allowed for a participatory, decentralized approach to delivering assistance. Open town meetings are held to provide a forum for residents to discuss community needs. The

mayor and the municipal council then rank those needs and request appropriate funding. Between February and December 1992, 1,066 projects, valued at \$11.3 million, were implemented through MEA in the 115 municipalities targeted by the National Reconstruction Plan.

In December 1992, we attended three town meetings and held extensive discussions in another 15 municipalities with mayors of various political parties, municipal council members, and citizens and representatives of the church, local grass-roots organizations, NGOs, and the FMLN. We found that they viewed MEA favorably as a means of delivering assistance and promoting democratic processes. No one we spoke with said or implied that MEA carried a negative image from its past counter-insurgency role.

MEA Considered Democratic and Efficient Program

Some critics have said the MEA program denies residents full participation in the process and is inefficient. Criticisms include the following: (1) people do not have full opportunity to be heard at open town meetings, (2) residents should be allowed an opportunity to prioritize projects and choose which ones to seek funding for, (3) project oversight is limited, and (4) the MEA process is inefficient and results in delays in project completion or incomplete projects.

As mentioned earlier, we met with mayors, FMLN officials, and others at 18 municipalities and attended three open town meetings. We learned that the process of allowing for full citizen participation is maturing, and most people we talked with praised the program and told us that it was working. Further, we believe the program has mechanisms in place to provide for full citizen participation. We asked officials and residents about each of the above mentioned criticisms. Very few complained about lack of opportunities to voice opinions, make decisions, or oversee the projects. Local FMLN officials, the most severe critics of the MEA process in the early period, told us that their organizations have largely accepted the participatory mechanisms of MEA, and, in some areas, are undertaking activities to further develop and strengthen the mechanisms.

With regard to complaints that the MEA process has led to incomplete projects and inordinate delays in project implementation, community officials and residents we spoke with were proud of the project completion rate under MEA. In the 18 municipalities we visited in mid-December 1992, 143 projects had been completed over the past 10 months or were underway at the time of our visit. Community officials and citizens reported that only six of the projects had experienced problems or delays, but attributed these to unavoidable circumstances outside the control of the community. For example, one road project in

Chalatenango, which was cited by critics as a prime example of an incomplete project typical of MEA problems, was delayed due to a strike at a cement factory. The road could not be completed within its budget when the price of cement doubled after the strike. Although the road was 15 meters short of its intended length, the community and municipal government used municipal funds to finish the project. Community officials explained that some projects, such as electrification and water projects, take longer because they require greater coordination and longer planning.

Municipal Development Needs Further Strengthening

According to AID, the MEA program can be strengthened by educating and training mayors and community officials on democratic processes. In addition, gains can be obtained through greater education of residents of the MEA process. However, AID is most concerned about the program's fiscal sustainability. According to AID, the tax base varies considerably between municipalities, but generally revenues generated from local sources have been low. User fees and tariffs have remained unchanged for decades, despite significant increases in the cost of services, and municipalities do not have a property tax, which could be a principal source of revenue.

Although municipalities are beginning to adjust their fees and service charges to recover a greater portion of the cost of the service, the revenues will be inadequate to finance expanded local government services. As of December 1992, AID was finalizing the details of a new municipal development project that will address these issues.

LAND REDISTRIBUTION PROBLEMS

Let me turn now to the problems associated with land redistribution. As mentioned earlier, the land redistribution program is severely underfunded. In addition, the government has been slow in transferring land to recipients, the recapitalization of the Land Bank from loan repayments is doubtful, and insufficient agricultural credit is available to farmers receiving land.

Expectations and Results

Redistributing land to 47,500 ex-combatants and others is a critical aspect of reconstruction. Yet, land transfers are behind schedule, and few have received land. About 15,000 beneficiaries were to have received land by January 1993, but as of mid-February 1993, only about 3,800 beneficiaries had actually received land. About 179,000 acres are available to be transferred, which would provide land for at least another 20,000 beneficiaries.

Several factors have contributed to delays in land redistribution. The government and the FMLN did not agree on the basic details of land transfer until the United Nations brokered an acceptable land agreement in October 1992, 9 months after the Peace Agreement was signed. Even after the agreement was signed, negotiations over the quality of land to be provided to FMLN beneficiaries continued. Also, the FMLN is required to identify potential properties and provide the government with lists of beneficiaries but this has not been completed. The FMLN told us it lacks the technical capability and resources to complete its identification of land and beneficiaries, and as far as we know, there are no plans to help the FMLN in this area.

Loan Repayments Doubtful

The Land Bank, established in 1991, is intended not only to help in the reconstruction, but also to become a permanent government institution. This means that the Land Bank must be recapitalized from loan repayments from land beneficiaries. However, most officials agree that land recipients probably will not be able to repay their loans. Both the loan terms and technical factors contribute to this problem.

The terms of the Peace Agreement call for loans to be provided at 6 percent over 30 years, with a 4-year floating grace period. Agricultural experts we spoke with indicated that most farmers will probably use the first 4 years of their loan as the grace period, which means the Land Bank will not be able to recapitalize. They added that the ability of the farmers to repay their loans is further hindered because of inadequate agricultural credit, limited technical assistance, the less than ideal quality of the land provided, and the farmers' unwillingness to grow nontraditional crops, such as garlic and melons, that produce income.

Agricultural Credit Inadequate

Agricultural credit provided by the government might help farmers sustain themselves and give them the ability to repay the Land Bank. Experts predict that the current informal system of agricultural credit, which includes personal loans from friends and family, will not sustain agriculture in the 1990s.

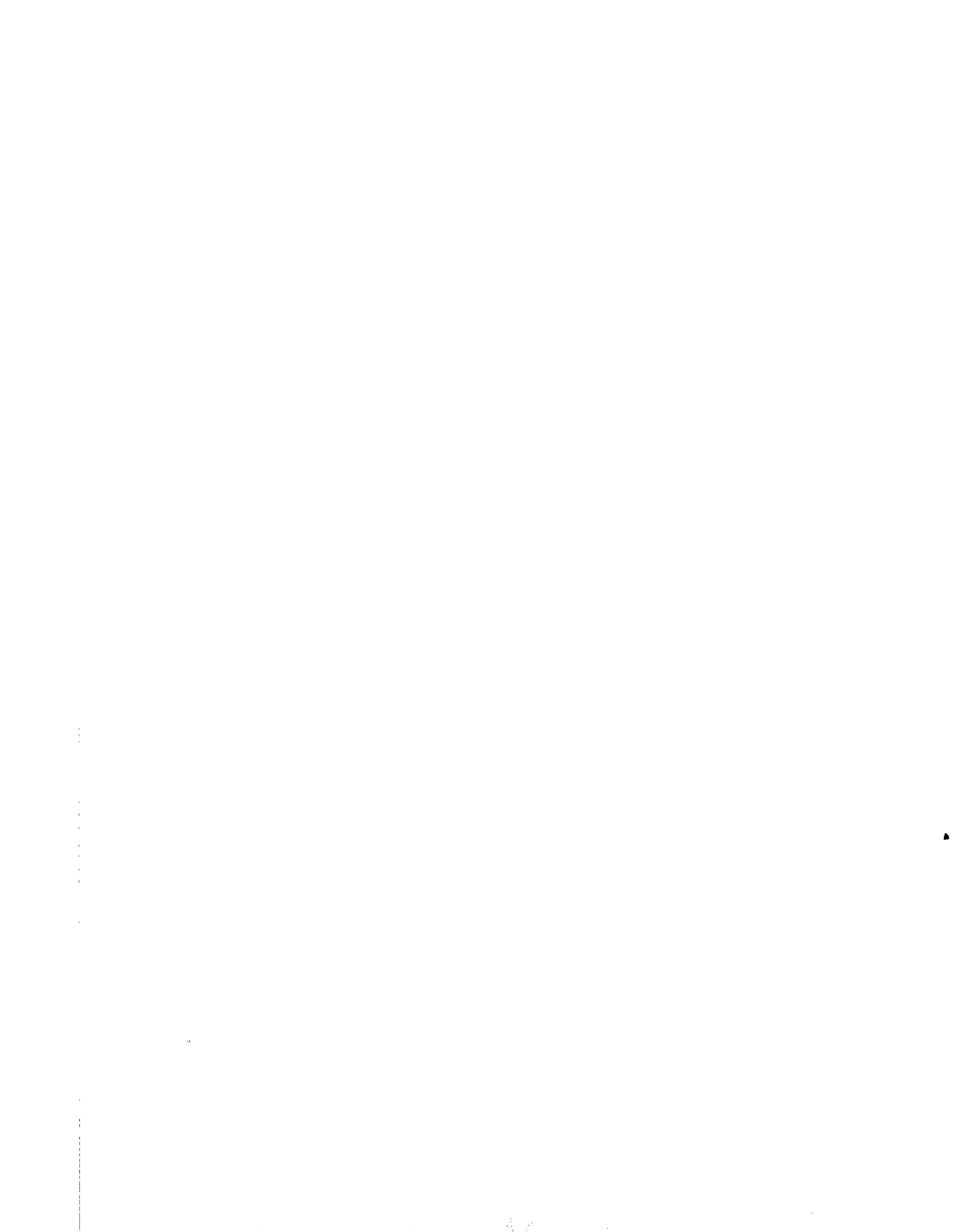
The United States provided agricultural credit of about \$111 per acre to about 8,000 families through the Catholic Relief Services. Although considered a successful program by U.S. officials, it satisfies only a small part of agricultural credit needs, since that is a minimal level of credit, according to agricultural experts. AID estimates that between \$170 and \$615 in credit is needed for each acre, depending on the type of crop grown. Using AID data, we estimate that between \$71 and \$255 million is needed to provide agricultural credit to the 47,500

land beneficiaries.⁷ This estimate does not include credit needed by other farmers in the former conflictive areas who did not receive land through the land redistribution program. To date, however, only about \$34 million from all sources, including \$32 million from the United States, has been committed specifically for farmers in the areas targeted by the National Reconstruction Plan.

We do not know if additional international donors are prepared to make commitments to assist the government in funding this requirement. We were told that private banks are unlikely to respond to the needs of the farmers, and government banks do not have the resources. The government hopes the European Community, the United Nations, and others will contribute funds for agriculture credit, but U.S. officials are not optimistic that these sources will provide sufficient funds.

Mr. Chairman, this completes my prepared statement. I will be happy to answer questions from the subcommittee.

⁷This estimate is a mathematical calculation based on 47,500 beneficiaries each receiving 8.75 acres of land. The amount and quality of land provided and the beneficiary's financial condition would affect the amount of credit needed.



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