

PRESIDENT'S
PRIVATE SECTOR SURVEY
ON COST CONTROL

TASK FORCE REPORT ON
THE DEPARTMENT OF STATE/AID/USIA

SUBMITTED TO THE SUBCOMMITTEE FOR
CONSIDERATION AT ITS MEETING ON MAY 26, 1983

THE PRESIDENT'S PRIVATE SECTOR SURVEY ON COST CONTROL

REPORT OF THE TASK FORCE ON
DEPARTMENT OF STATE/AID/USIA

SUBMITTED TO THE SUBCOMMITTEE FOR CONSIDERATION
AT ITS MEETING ON MAY 26, 1983

CO-CHAIRS:
J. Rawles Fulgham
George L. Shinn



THE PRESIDENT'S PRIVATE SECTOR SURVEY ON COST CONTROL

May 6, 1983

Mr. J. Peter Grace
Chairman, Executive Committee
President's Private Sector Survey
on Cost Control in the Federal Government

Dear Mr. Chairman:

The following Report represents the results of the State/AID/USIA Task Force of the President's Private Sector Survey on Cost Control in the Federal Government. The report culminates the combined efforts of 28 private sector volunteers who contributed 30 person months of their expertise on a pro bono basis to the PPSS initiative. In addition, these team members represented 14 private sector companies who reviewed State/AID/USIA activities during the period from June 22, 1982 through November 12, 1982.

The Report contains proposed major recommendations which, when fully implemented, could result in three-year total cost savings and revenue generation of \$719.3 million. This consists of first year annual cost savings and revenue generation of \$170.1 million. In addition, another \$55.9 million in cash acceleration over three years could be realized. It should be noted, however, that some of the recommendations may require a number of years for the full savings to be realized. While all facets of State/AID/USIA could not be surveyed in the time allotted, areas selected for review were considered to offer significant potential for cost savings and/or other benefits.

Clearly, other opportunities for improvement exist, but due to limited time and personnel resources available, they could not be pursued. Several, however, because they offer significant potential savings opportunities, are suggested for further review. We believe you and the other members of the Executive Committee will find our recommendations to be constructive and fully documented. We urge their adoption by the Executive Committee.

1850 K Street, N.W. • Suite 1150 • Washington, D.C. 20006
(202) 466-5170

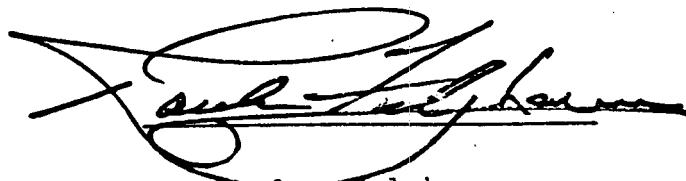
Mr. J. Peter Grace
May 6, 1983
Page 2

The importance of the accompanying recommendations is underscored by their potential to better utilize the finite resources available to the Federal Government, particularly as they relate to State/AID/USIA. It was the intention of this Task Force to suggest approaches and practices that will enable the Executive Branch to carry out its mission of guiding more effectively the State/AID/USIA programs and policies which are important to our country.

Should you, the other members of the Executive Committee, or the Survey Management Office have any questions, please do not hesitate to contact us, the Project Manager, or the individual members of the Task Force.



George L. Shinn
Chairman of the Board (Retired)
The First Boston Corporation



J. Rawies Fulgham
Vice Chairman (Retired)
InterFirst Corp.

THE PRESIDENT'S PRIVATE SECTOR SURVEY ON COST CONTROL

REPORT OF THE TASK FORCE ON
DEPARTMENT OF STATE/AID/USIA

SUBMITTED TO THE SUBCOMMITTEE FOR CONSIDERATION
AT ITS MEETING ON MAY 26, 1983

PREFACE

On June 30, 1982, President Reagan signed Executive Order 12369 formally establishing the President's Private Sector Survey on Cost Control (PPSSCC) in the Executive Branch of the Federal Government. An Executive Committee under the chairmanship of J. Peter Grace was established, consisting of 161 high-level private sector executives--mostly chairmen and chief executive officers--from many of the nation's leading corporations.

Briefly stated, the President directed the PPSSCC to:

- o Identify opportunities for increased efficiency and reduced costs achievable by executive action or legislation.
- o Determine areas where managerial accountability can be enhanced and administrative controls improved.
- o Suggest short- and long-term managerial operating improvements.
- o Specify areas where further study can be justified by potential savings.
- o Provide information and data relating to governmental expenditures, indebtedness, and personnel management.

The Executive Order also provided that "the Committee is to be funded, staffed and equipped . . . by the private sector without cost to the Federal Government." To implement this objective, the Foundation for the President's Private Sector Survey on Cost Control was established. It formed a Management Office which organized thirty-six "task forces," each co-chaired by two or more members of the Executive Committee, to do the "preliminary reports." These are listed below:

Agriculture	Hospital Management/Veterans Admin. (Hospitals)
Air Force	Housing & Urban Development
Army	Interior
Automated Data Processing/Office Automation	Justice
Boards/Commissions-Banking	Labor
Boards/Commissions-Business Related	Land, Facilities, and Personal Property Management
Commerce	Low Income Standards and Benefits
Defense-Office of Secretary	Navy
Education	Personnel Management
Energy (including Federal Energy Regulatory Commission and Nuclear Regulatory Commission)	Privatization
Environmental Protection Agency/Small Business Administration/Federal Emergency Management Agency	Procurement/Contracts/Inventory Management
Federal Construction Management	Real Property Management
Federal Feeding	Research and Development (National Science Foundation/National Aeronautics & Space Admin.)
Federal Management Process	State/USIA
Financial Asset Management	Transportation
Health & Human Services-Department Management/ Human Development Services/ACTION	Treasury
Health & Human Services-Public Health Service/Health Care Financing Admin.	User Charges
Health & Human Services-Social Security Admin.	Veterans Administration

Twenty-two of these task forces were assigned to study specific departments and agencies, and the remaining fourteen studied functions cutting across government such as personnel, data processing and procurement. Apart from the co-chairpersons, none of the task force members were members of the Executive Committee, nor did the task forces have any authority to make recommendations to departments and agencies or to the President.

Each of the 36 task forces prepared a draft report. This is one such task force report. Each, with a few exceptions, also prepared an appendix providing more detailed information supporting the tentative recommendations contained in the task force report. Those appendices are on file at the Department of Commerce's Central Reference and Records Inspection Facility. It should be noted that tentative recommendations relating to any one federal agency may be included not only in the appropriate agency task force report but also in the reports of the functional cross-cutting task forces.

All of the task force draft reports will be considered and acted upon in meetings open to the public by a Subcommittee of the Executive Committee of PPSSCC, along with other statements and recommendations. Accordingly, all tentative recommendations contained in this task force report are subject to possible changes resulting from the Subcommittee's deliberations. In addition, in identifying the implementation authority for each recommendation, the Task Force drew upon all available data at its disposal. Because of the complexities of the appropriations process, as well as historical precedents, further data could result in a change in the PPSS-identified authority.

It is important to note that cost savings, revenue generation, and cash acceleration opportunities in this draft report may duplicate similar dollar opportunities reported in other task force reports. Thus, there may be instances of double counting of dollar opportunities between task force reports. These duplications will be netted-out in the Final Summary Report to the President. Additionally, dollar estimates in this draft report are based on reasonable and defensible assumptions, including standard three-year projections based on first, second, and third year partial or full implementation will occur. Accordingly, estimated savings or revenue opportunities are understandably of a "planning" quality and not of a "budget" quality. Therefore, the reader should guard against drawing conclusions or making dollar projections based on the disclosures contained only in this draft report.

Following action upon all of the task force reports, the Executive Committee will adopt a Final Summary Report to the President, summarizing the scope of its individual task force recommendations and offering general conclusions and advice. This Summary Report is tentatively scheduled for release on or about June 30, 1983.

TABLE OF CONTENTS

	<u>Page Number</u>
EXECUTIVE SUMMARY	i
THE REPORT RECOMMENDATIONS -- A PERSPECTIVE	x
I. INTRODUCTION	1
II. ISSUE AND RECOMMENDATION SUMMARIES	
A. DEPARTMENT OF STATE	5
B. AGENCY FOR INTERNATIONAL DEVELOPMENT	54
C. UNITED STATES INFORMATION AGENCY	90
III. SUMMARY OF RECOMMENDATIONS AND SAVINGS	99
IV. COST CONTROL OPPORTUNITIES FOR FURTHER STUDY	105
V. TASK FORCE MEMBERSHIP	122

TABLE OF EXHIBITS

<u>Table</u>	<u>Title</u>	<u>Page Number</u>
II-1	Foreign Service Personnel Out of Grade	12
II-2	Typical Classifications of Overcomple- ment Personnel	13
II-3	Elimination of Position Grade/ Personnel Grade Overages	18
II-4	Salary Costs of Other Overcomplement Employees	20
II-5	Summary of Overcomplement Savings	21
II-6	Consolidation of 1981 Shipments	82
II-7	AID Shipments Abroad	83
II-8	Savings Resulting from Use of Foreign Shipping	89
IV-1	Administrative Support	108
IV-2	International Organizations' Contributions Assessed	114
<u>Figure</u>	<u>Title</u>	<u>Page Number</u>
1	Interest Rate Comparisons	vii
2	Retirement System Cost as Percent of Payroll	viii

**EXECUTIVE SUMMARY
AND
PERSPECTIVE**

EXECUTIVE SUMMARY

The State/AID/USIA Task Force surveyed the international affairs agencies -- the Department of State (State), Agency for International Development (AID) and U.S. Information Agency (USIA) -- to identify opportunities for increased efficiency and reduced costs, to determine areas to enhance managerial accountability, to suggest managerial operating improvements and to pinpoint specific areas for further study.

The study was conducted by 28 private sector volunteers from investment and commercial banks; consulting and public accounting firms; privately held businesses; a non-profit, private-voluntary organization and several universities. Experts in the areas of personnel, retirement plans, building management and project administration were consulted from other private sector organizations.

While the Task Force findings resulted primarily from analytical studies and interviews conducted in Washington, visits to selected embassies and overseas posts provided substantive and supportive details for the broad, fundamental issues we identified, particularly in the areas of the Foreign Service Personnel System, Foreign Buildings Operation, AID Project Planning and Organization for International Affairs Activities.

We had complete access to all personnel at these agencies and were extended full cooperation and courtesy. We interviewed over one hundred government officers ranging from Department Secretary, Agency Director and ambassador to junior foreign service officer and staff members. A number of former government officers including a Department Secretary, retired ambassadors and ex-agency heads also provided additional information, data and perspectives.

The International Affairs Budget Perspective

The President's FY 1983 budget "to protect and advance the interests of the United States and its people in international affairs"^{1/} amounts to \$18.1 billion, representing

^{1/} Presidential Budget - FY 1983.

2.3 percent of the total \$801.9 billion Federal budget. The department and agencies assigned to this Task Force comprise 46 percent of the international affairs budget, totaling \$8.2 billion or 1 percent of the Federal budget. Employment at these agencies for FY 1983 is estimated at nearly 38,000 personnel both in the United States and abroad. The other international affairs activities (comprising 54 percent of the budget) such as military sales, P.L. 480 and Export-Import Bank have been studied by Task Forces assigned to the Department of Defense, Department of Agriculture and Boards/Commissions-Banking Investment, respectively.

While the combined spending of the departments/agencies reviewed by this Task Force, have increased by 166 percent over the past 20 years, combined personnel headcount has decreased by more than 10,000 or 23 percent, particularly at AID (64 percent) and USIA (32 percent). The most significant budget increase has occurred at the Department of State, where expenditures have multiplied by a factor of seven since 1962, while at AID and USIA the budgeted expenditures have merely increased by 1.8 and 2.4 times their respective 1962 levels.

Task Force Focus

Our Task Force reviewed all budgeted expenditure categories for each of the agencies to identify the most relevant cost saving opportunities. We determined that at least 60 percent of such expenditures was funded to support major international affairs policy initiatives and decisions; for example, Contributions to International Organizations and Economic Support funds amount to \$83.6 million for FY 1983 and are tied to our United Nations position and the "Camp David Accord," respectively. Our focus, therefore, became those areas of operating expenditures in need of a critical objective review and opportunities for cost-saving within the administration of funding for international policy initiatives and decisions.

Opportunities for Cost Savings and Revenue Enhancements

It is our judgment that, if implemented in a vigorous and constructive manner, the Task Force's 38 recommendations, including Issues recommended for further study, could reduce costs and generate increased revenues while improving the effectiveness of the international activities effort by at least \$170.1 million in the first year of implementation, with an overall savings of \$719.3 million over three years. In addition, another \$55.9 million in cash acceleration over three years can be realized. Larger paybacks could result in future years as benefits are gained from the development of more efficient systems, as recommended.

Total dollar savings/revenue enhancement opportunities are as follows by year:

	(\$ millions)			Total
	First Year	Second Year	Third Year	
Cost Savings	\$110.1	\$119.7	\$129.5	\$359.3
Cash accelerations	21.3	18.5	16.1	55.9
Revenue enhancements	60.0	120.0	180.0	360.0
Total	<u>\$191.4</u>	<u>\$258.2</u>	<u>\$325.6</u>	<u>\$775.2</u>

Direct three-year cost savings and cash accelerations of \$258.6 million are achievable at State through the realignment of personnel, elimination of overcomplement personnel, revisions of certain provisions of the retirement system, positioning for foreign currency needs, and collection of interest on refugee loans (see STATE 1 through STATE 5).

Three-year cost savings and revenue enhancements at AID are estimated to be \$516.6 million through elimination of burdensome project paperwork, an increase in the interest rate on AID loans, extension of the overseas assignment period and relief from the Cargo Preference policy (see STATE 6 through STATE 9). Savings by agency are summarized as follows:

	(\$ millions)		
	FY 1983 Budget authority	First year savings	Percentage to budget
State	\$2,673	\$ 84.1	3.1%
AID	4,895	107.3	2.2
USIA	653	*	--
Other	118	--	--
	<u>\$8,339</u>	<u>\$191.4</u>	<u>2.3%</u>

* Specific savings not estimated.

The Task Force has also identified opportunities for further study in the following areas affecting international affairs:

- o the organizational structure;
- o the use of foreign currencies held by the United States;
- o contributions to international organizations; and
- o overseas workmen's compensation insurance.

A recap of recommendations by implementation authority follows:

	<u>Number of recommendations</u>	<u>3-year savings in \$ millions</u>
<u>Implementation by agency authority</u>		
State	19	\$168.0
AID	8	385.8
USIA	2	--
<u>Implementation by presidential authority</u>	8	\$ 6.0
<u>Implementation by congressional authority</u>	<u>11</u>	<u>\$215.4</u>
	48 *	<u>\$775.2</u>

* Includes instances where further study is recommended and implementation is required at more than one agency and/or authority level.

Findings and Conclusions

The 14 issue areas resulting from our Task Force efforts include findings and conclusions that relate specifically to opportunities for improving the management of international affairs, for application of private sector business techniques and for elimination of excess costs in identified programs.

1. The Management of International Affairs

The international affairs activities of the U.S. Government have not only expanded but also changed in direction since our role as an international superpower was established through World War II. The pre-war roles included treaty negotiation, official representation and consular representation. Today, a host of new activities requires a far greater range of skills than provided by formal training in international affairs and host country languages. The new activities include economic analysis; development and financial loan assistance; multilateral negotiation; monitoring of special situations like narcotics traffic, terrorist activities and U.S. capital investment overseas; and international trade negotiations (export of U.S. surplus commodities, military arms and other industrial products and import of needed natural and strategic resources). At the same time, the role of the Secretary of State has become oriented toward that of chief negotiator and shuttle diplomat, leaving less time available for the expanded management requirements.

The Foreign Service Officer Corps initially staffed these activities by assumption of the new duties under the theory that a Foreign Service Officer can/should respond to any overseas job requirement. Beginning in the early 50s, it was realized that these activities had diverted State's Foreign Service Officers from a traditional diplomatic role and also required more specialized skills. Spin-off of some activities like public information, development assistance and (recently) international trade to either new agencies or other departments was initiated. Today, as a result, while Foreign Service Officers from State/AID/USIA comprise the majority (70 percent) of U.S. personnel at overseas posts, representatives from 22 other departments and agencies are found in many posts. However, State has continued to maintain its role as host in each embassy and provides administrative support to other agencies present overseas. In addition, the Secretary of State has maintained a dotted-line responsibility for the information agency and development assistance functions.

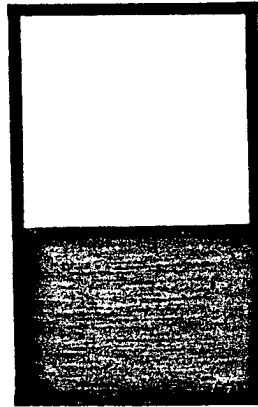
We observed in our visits to embassies and in our Washington interviews, particularly at State, the effects of these shifts in international affairs requirements. Efforts had been expended primarily to respond to those requirements. The presence of business-like managerial skills and controls was not uniformly evident, and their development is just being introduced to Foreign Service Officer training.

Our focus highlighted the broad, fundamental areas which, when corrected, can result in a better managed international affairs function and in cost savings to the government process. Opportunities for better management were seen within the Foreign Service Personnel System, where we found that the distribution of personnel is heavily skewed toward the higher levels in sharp contrast to other professions as shown below.

COMPARISON OF STATE PERSONNEL DISTRIBUTION
TO OTHER ORGANIZATIONS

	State	Accounting	Banking	Military
Senior	<u>20%</u>	<u>12%</u>	<u>8%</u>	<u>6%</u>
Mid-level	<u>66%</u>	<u>16%</u>	<u>40%</u>	<u>65%</u>
Junior	<u>14%</u>	<u>72%</u>	<u>52%</u>	<u>29%</u>

We also found that 56 percent of State's Foreign Service Officers who are not specialists are mismatched in rank to job position due to the rank-in-man staffing approach (see below).



Personnel
Not in Jobs
Equal to
Rank
56%

Personnel
In Jobs Equal
To Rank
44%

As a result, "overcomplement" personnel are maintained within the Department.

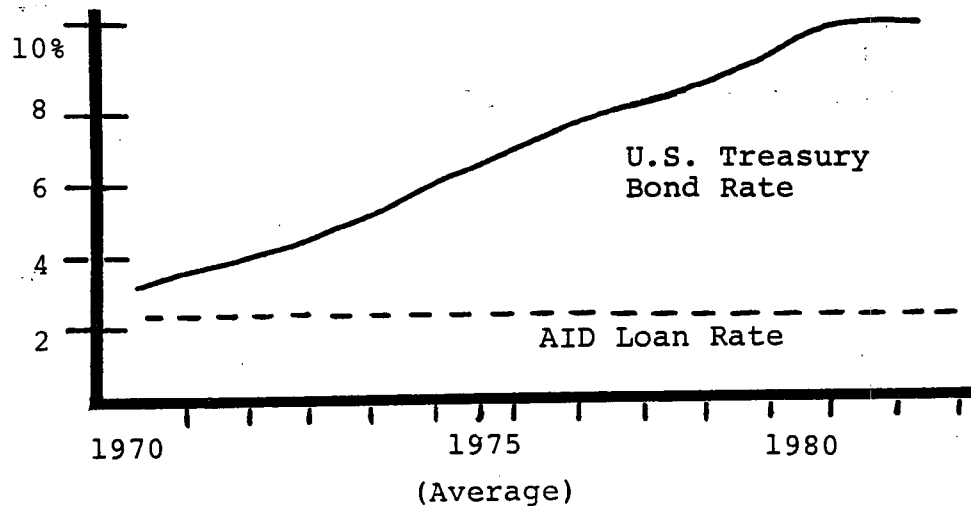
In addition to personnel concerns in the management of international affairs, Foreign Buildings Operations lacks the informational tools to manage the vast (at least \$5 billion) real estate holdings abroad; instead it is oriented toward building design and construction. Also, the three agencies -- State/AID/USIA -- maintain separate regional bureaus and administrative facilities in Washington, while sharing most administrative support overseas; the need for the establishment and continuance of many bureaus, functions and diplomatic posts was not always apparent. The problem is compounded by the fact that most Senior Foreign Service Officers covet the role of negotiator or ambassador and avoid typical management and administrative functions. This is particularly troublesome because the shift of international affairs functions to other departments and agencies, as noted previously, has elevated the need for management and administrative skills at most embassies.

2. Application of Business Techniques

We have found and concluded that the application of specific business techniques could significantly enhance cost-effectiveness. Specifically, adjusting charges to match costs has not taken place, as evidenced by the fact that interest rates on AID loans have not paralleled Federal borrowing costs (see Figure 1).

[Figure 1 on following page]

Figure 1
INTEREST RATE COMPARISONS



Further, foreign exchange fluctuation risks could be minimized by purchasing currencies in advance. Additionally, we found that evaluation processes had not been fully applied to programs at USIA and in State's Bureaus for Refugee Programs and International Organizations.

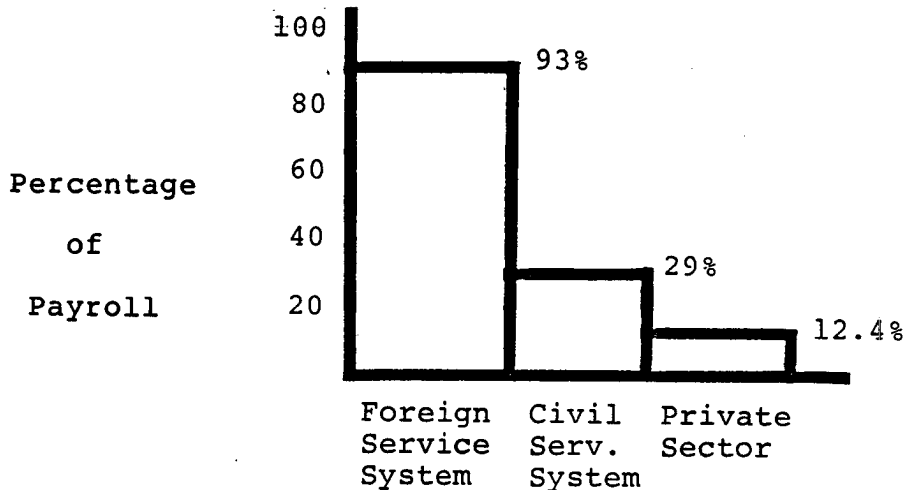
3. Elimination of Excess Costs

We found that U.S. taxpayers are bearing the burden of excessive costs for the Foreign Service Retirement System and AID's Project Planning, Cargo Preference Policy and Rotational Policy. For example, excessive retirement systems costs, primarily from a lower retirement age, result in higher percentage of payroll costs as shown in Figure 2.

[Figure 2 on following page]

Figure 2

RETIREMENT SYSTEM COST AS
PERCENT OF PAYROLL



Recommendations and Implementation

We recommend that corrective action, improvement and further consideration be made in 38 specific ways in our Report. Implementation of these recommendations can result in immediately quantifiable budgetary savings of \$191.4 million in the first year and \$325.6 million in the third year. We believe that larger paybacks in future years will result from the application of management and business techniques, but more importantly enhance the quality of our international affairs functions.

A tabular summary of savings by issue follows:

<u>No.</u>	<u>Issue</u>	<u>Number of recommendations</u>	<u>First year savings (\$ millions)</u>
1	Personnel	6	\$ 25.8
2	Retirement	2	29.7
3	Foreign buildings	5	--
4	Foreign exchange	3	5.7
5	Refugee programs	3	22.9
6	Project planning	5	9.9
7	Interest on loans	3	60.0
8	Rotation policy	1	1.6
9	Cargo Preference	1	35.8
10	Evaluation process	2	--
IV	Further study areas	7	--
		<u>38</u>	<u>\$191.4</u>

More than 70 percent of our recommendations can be implemented by Agency authority, with a cost savings of \$553.8 million over three years. We, therefore, urge the respective agency heads to initiate suggested actions as quickly as possible. Recommendations which require Presidential action do not represent a substantial portion of our cost saving, because those recommendations contain, areas where further study and justification, as well as policy decisions, are required. We believe, however, that the potential savings from those areas could exceed those already quantified and encourage full and expeditious consideration. Lastly, we believe our recommendations requiring congressional action contain realistic and feasible solutions to situations costing the U.S. taxpayer \$215.4 million more than required.

Finally, we recognize that implementation steps may reveal refinements and additional findings that should strengthen these executive agencies in the most efficient way.

THE REPORT RECOMMENDATIONS -- A PERSPECTIVE

As the product of an unprecedented and wide-ranging survey performed in a political atmosphere by private sector executives and specialists, the recommendations in this Task Force Report must be placed in perspective. Our volunteer staff had the formidable task of bringing their expertise to bear on the complex Federal operations in the short span of a few months while holding down other full- or part-time employment.

Despite these challenges -- most of which were anticipated at the outset -- valuable analysis and issue development were achieved. The recommendations contained in this Report will result, if implemented, in real and significant savings and other benefits to American taxpayers whose hard work and personal sacrifices financially support these Federal programs and operations.

We believe that the majority of our recommendations are fully substantiated. However, it would be misleading to allege that each and every recommendation is rooted in uniformly high level of research, analysis and substantiation. Various time limitations, business resources, and other constraints did not permit achievement of the desired uniformity objective.

We have evaluated, therefore, the "supportability" of the recommendations on their management merits and have grouped them into the following three categories.

- o Category I -- Fully substantiated and defensible. Recommendations in this category are, in the opinion of the Task Force, convincing and deserving of prompt implementation.
- o Category II -- Substantially documented and supportable. Recommendations in this category may not be fully rationalized or documented in the Report, but all indications point to the desirability and defensibility of proceeding with their implementation.
- o Category III -- Potentially justifiable and supportable. Recommendations in this category, while meritorious, are not regarded as fully supported in the

Report, due to time, personnel resources, and other constraints, but are deemed worthy of further analysis to determine the full extent of their merit for implementation.

These category descriptions do not take into account political, social or economic conditions which may alter the supportability of these recommendations for implementation. Accordingly, it is possible, by grouping the recommendations along the above categories, to assess more effectively the cost savings that can be expected. This analysis permits summary estimates of: (1) firm, (2) probable, and (3) potential savings.

The Report Recommendations -- An Assessment

Based on the above perspective and categorization, an assessment of the reported recommendations is contained in the following matrix:

	3-year savings by category with savings/ revenue/cash accelera- tion indicated		
	<u>I</u>	<u>II</u>	<u>III</u>
<u>State 1:</u>			
<u>Foreign Service Personnel System</u>			
o Use models to correct skewed distribution (STATE 1-1)	\$42.4(S)		
o Review ranking of positions, realign personnel (STATE 1-2)	19.9(S)		
o Eliminate overcomplement employees (STATE 1-3)	24.0(S)		
o Redesign the performance evaluation system and train supervisory personnel (STATE 1-4)	--		
o Amend the FSA 1980 to expand definition of management official (STATE 1-5)	--		
o Improve recruiting and training (STATE 1-6)	--		

3-year savings by
category with savings/
revenue/cash accelera-
tion indicated

I II III

STATE 2:Disability System and Foreign
Service Retirement

- | | | |
|---|---|------------|
| o | Increase retirement age
(STATE 2-1) | \$ 56.7(S) |
| o | Change the benefit formula
(STATE 2-2) | 33.9(S) |

STATE 3:Office of Foreign Buildings

- | | | |
|---|--|----|
| o | Develop a real property
management system (STATE 3-1) | -- |
| o | Properly allocate operating
and maintenance expenditures
(STATE 3-2) | -- |
| o | Expand cost accumulation
report (STATE 3-3) | -- |
| o | Consolidate fiscal authority
(STATE 3-4) | -- |
| o | Provide guidelines for
identification of excess
capacity (STATE 3-5) | -- |

STATE 4:Purchase of Foreign Currencies

- | | | |
|---|---|---------|
| o | Develop an accounting system
to gather foreign currency needs
(STATE 4-1) | -- |
| o | Establish foreign currency
futures/forward desk
(STATE 4-2) | 17.1(S) |

3-year savings by
category with savings/
revenue/cash accelera-
tion indicated

I II III

- o Hire staff and define functions of trading desk (STATE 4-3) --

STATE 5:

Refugee Programs

- o Rectify the collection problem; require sponsor guarantee (STATE 5-1) \$ 55.9 (CA)
\$ 11.7 (S)
- o Improve monitoring program (STATE 5-2) 0.0 (S)
- o Develop tracking and integrated data base (STATE 5-3) (3.0) (S)

STATE 6:

Project Planning, Approval, and Monitoring Process

- o Increase the dollar value of block grants (STATE 6-1) 7.1 (S)
- o Request Congress to return deobligation/reobligation authority to AID (STATE 6-2) 6.3 (S)
- o Find additional ways to increase decentralization of authority (STATE 6-3) 7.1 (S)
- o Limit the time spent responding to Congress (STATE 6-4) 6.3 (S)
- o Move to a two-year budget submission cycle (STATE 6-5) 6.0 (S)

	3-year savings by category with savings/ revenue/cash accelera- tion indicated		
	<u>I</u>	<u>II</u>	<u>III</u>
<u>STATE 7:</u>			
<u>Interest Rates on AID Loans</u>			
o Establish a base lending rate (STATE 7-1)	360.0 (R)		
o Establish a uniform set of criteria for the determination of loan terms (STATE 7-2)	--		
<u>STATE 8:</u>			
<u>Foreign Service Rotation Policy</u>			
o Enforce four-year tours (STATE 8-1)	\$ 5.3 (S)		
<u>STATE 9:</u>			
<u>Cargo Preference</u>			
o Seek relief from cargo preference for AID-sponsored shipments (STATE 9-1)	118.5 (S)		
<u>STATE 10:</u>			
<u>Evaluative Procedures</u>			
o Establish analytical resource capability (STATE 10-1)	--		
o Defer expenditure for planned expansions (STATE 10-2)	--		
Total cost savings (S)	\$355.2	\$4.1	--
Total revenue generation (R)	\$360.0	--	--
Total cash acceleration (CA)	\$ 55.9		

I. INTRODUCTION

I. INTRODUCTION

This Task Force has identified cost-saving opportunities within three major agencies responsible for the conduct of international affairs and implementation of foreign policy. These agencies -- the State Department (State), the United States Information Agency (USIA) and the Agency for International Development (AID) -- account for \$8.2 billion¹ of the \$801.9 billion estimated FY 1983 Federal budget, and employ, both overseas and in the United States, 38,000 personnel of the 2,054,000 government-wide civilian headcount. The expenditure of the budgeted resources falls within two categories:

- o Operating expenses - \$2.9 billion or 35 percent of total budget (\$8.2 billion), and
- o Bilateral and multilateral assistance programs -- \$5.3 billion or 65 percent of total budget.

The Task Force had also been assigned to review the Peace Corps but found that its limited funding requirement of \$98.5 million, coupled with evidence of an effective agency-developed cost reduction program, did not justify allocation of our limited study group resources.

Federal government expenditures for other non-military international affairs programs such as arms sales, P.L. 480 (grain sales) and international lending were assigned to other Task Force teams.

The three government units -- State, USIA and AID -- have a common international focus as well as coordinated international roles and similar personnel structures. The Secretary of State was the first cabinet post established by our country's founders and, under the Constitution, the Secretary is third in line of succession to the President; hence, State has been traditionally accorded the senior status amongst all executive departments.

Both USIA and AID were created after World War II. USIA was established in 1953 as a result of the separation of the International Information Administration, the Mutual Security Agency and the Technical Cooperation Agency from the State Department. Under Reorganization Plan No. 2 of 1977, USIA was consolidated with the Bureau of Educational and Cultural Affairs of the State Department to form the International Communications Agency (ICA). The name USIA was reinstated in August 1982.

AID was formed in 1961 by merging two foreign aid organizations -- the International Cooperation Administration and the Development Loan Fund (which were successors to five other post-war agencies). AID has operated as an independent agency under the foreign policy guidance of the Secretary of State although, since 1979, it has reported through the International Development Cooperation Agency (formed by the Carter Administration).

Tradition as well as a Presidential definition of the Secretary of State's role have established State's leading position. "The Secretary of State has responsibility not only for the Department of State and the Foreign Service but also...for the overall policy direction, coordination and supervision of the United States Government activities overseas." ^{1/} The "overall coordination" mandate has caused State to establish an administrative support capability seen in the following ways: In the personnel area, U.S. employees serving overseas^{2/} are members of the Foreign Service Corps, headed by a Director General who is also the Director of Personnel for State. In the facilities area, office and residential space is provided to U.S. personnel through State's Foreign Building Office. Communications facilities and financial services (expenses and payroll) are also established by State and provided to resident agencies.

Organizationally, each bureau uses a similar geographic regional structure to coordinate the activities of its personnel at overseas missions. The distinction amongst

^{1/} Letter of Instruction, 9/22/81; President Reagan to all Ambassadors.

^{2/} Excluded are uniformed military personnel serving at overseas military installations, military attaches and certain other Agency personnel assigned to diplomatic missions.

State, USIA and AID lies in the facet of international affairs for which each agency is responsible, as described below:

	<u>Prime function/activity</u>	<u>Other responsibilities</u>
State	Conduct of official relations with host government Political reporting & analysis Economic reporting & analysis	Consular services Refugee assistance, Administrative support
USIA	Public affairs activities Information distribution programs & reporting Broadcasting services	Cultural & exchange programs
AID	Developmental assistance Economic support	Disaster assistance

Personnel from these agencies performing the above functions comprise 65 percent of the 33,000-person overseas workforce (exclusive of military). ^{1/}

Because the conduct of international affairs inherently requires the expenditure of U.S. taxpayer funds outside the United States, close scrutiny and skepticism have been the standard framework for hearings on funding requirements and individual programs. Besides Congressional subcommittee hearings and General Accounting Office (GAO) review reports, the Office of Management and Budget (OMB) and Inspector General (IG) staff reports document the oversight audit and review of these agencies. These reports, on a collective basis, have been used by our Task Force members as a starting point for the identification of cost-saving issues and opportunities to improve the efficiency of these governmental operations.

During the issue development process, numerous fact-finding interviews were conducted. We found that the current relevance of many issues was confirmed both during the interviews and by the existence of some other previous study on the same issue. In addition to interviews and analytical reviews in Washington during the

^{1/} Personnel performing military and political intelligence functions, and commercial and agricultural trade activities comprise 27 percent of the total, while personnel from 16 other agencies (e.g., Treasury) comprise the remaining 8 percent.

detailed study phase, on-site interviews were conducted at 14 overseas diplomatic posts, where personnel from all agencies were interviewed to the extent possible.

At first glance, a reviewer of the agencies assigned to this Task Force could conclude that measurement of the work product associated with the international affairs functions is difficult. Another initial conclusion is that the major expenditure amounts in each budget are "people costs" -- salaries and other employee benefits. Lastly, it is observed that many decisions could ultimately be related to "policy decisions" which are beyond the boundaries of our mandate.

Each of these preliminary conclusions were found to be correct to some extent with respect to substantive diplomacy conducted over long periods of time. Nevertheless, our Task Force has been able to apply business analysis techniques and private sector examples to the preliminary findings during our work. As a result, ample opportunity for cost-savings was found within the administration of international affairs funding.

Our recommendations present each Agency with opportunities to reduce costs, increase efficiency, obtain managerial accountability and improve control. Several instances where further study should reveal additional savings have also been identified.

Significant Contributors

We found that personnel at each of the agencies were cooperative and provided invaluable direction and support when requested. In particular, we thank Ambassador Robert H. Miller and Mr. Roger B. Feldman at State; Messrs. James T. Hackett and Stanley M. Silverman at AID; and Messrs. Thomas Rollis and Ain Kivimae.

Budgetary Information - Summary Spreadsheet

The size, growth and the significance of an agency is indicated in part by its budget. To allow the reader more data to place these factors into perspective, a summary of budgetary information since 1962 is included as background information. Data shown include numbers of personnel, compensation, operating expenses and capital spending. These data were prepared at the start of the Survey. In some cases, they were updated in the Issue and Recommendation Summaries (Section II). (See spreadsheet on following page.)

12	13	14	15	16	17	18	19	20	21	22	23	24	25	26	27	28	29	30	31	32	33	34	35	36	37	38	39	40	41	42	43	44	45	46	47	48	49	50	51	52	53	54	55	56	57	58	59	60	61	62	63	64	65	66	67	68	69	70	71	72	73	74	75	76	77	78	79	80	81	82	83	84	85	86	87	88	89	90	91	92	93	94	95	96	97	98	99	100											
101	102	103	104	105	106	107	108	109	110	111	112	113	114	115	116	117	118	119	120	121	122	123	124	125	126	127	128	129	130	131	132	133	134	135	136	137	138	139	140	141	142	143	144	145	146	147	148	149	150	151	152	153	154	155	156	157	158	159	160	161	162	163	164	165	166	167	168	169	170	171	172	173	174	175	176	177	178	179	180	181	182	183	184	185	186	187	188	189	190	191	192	193	194	195	196	197	198	199	200

II. ISSUE AND RECOMMENDATION

SUMMARIES

II. ISSUE AND RECOMMENDATION SUMMARIES

A. DEPARTMENT OF STATE

OVERVIEW

The primary role of the Department of State is to advise the President in the formulation and execution of foreign policy. Overall responsibility for U.S. foreign policy rests with the President. The Secretary of State, as principal foreign policy spokesman and advisor to the President, has responsibility for the activities of the Department of State and the Foreign Service and also for U.S. government activities abroad. Individual ambassadors, appointed by the President as personal representatives, share with the President and Secretary of State responsibility for the conduct of U.S. relations in the host country or organization to which they are appointed. As of January 1, 1982, Foreign Service posts were categorized as follows:

Embassies	136	<u>1/</u>
Consulates General	65	
Consulates	34	
Missions (international organizations)	12	
Branch offices, liaison offices, etc.	6	
	<u>253</u>	<u>2/</u>

Broadly, the objective of U.S. foreign relations is to promote the long range security and well-being of the United States. Specifically, State determines and analyzes information relating to U.S. overseas interests, recommends future political action and executes instructions relating to foreign policy decisions. The following data depict

-
- 1/ Includes only countries where actual missions exist; 13 countries have ambassadors accredited to them, but no mission exists.
- 2/ Excludes Consular Agencies numbering 34 at the time this Report was prepared.

State's personnel head-count and funding in selected years over the past 20 years:

	<u>FY 1962</u>	<u>FY 1972</u>	<u>FY 1982</u>	<u>FY 1983</u>	<u>FY 1984</u>
Number of employees	22,919	22,948	22,918	23,230	24,649
Budget authority (\$ millions)	\$352	\$672	\$2,540	\$2,673	\$3,093

The major resource for fulfilling the mission previously described is U.S. citizens who become Foreign Service Officers. The Foreign Service is comprised of individuals who have been selected through an examination process with training in U.S. history and international affairs and a willingness to serve abroad, who have been tenured after a four-year evaluation period and who have an ambassadorial position as a career objective. At overseas posts, Foreign Service nationals provide staffing support in almost all post functions. The Department of State in Washington is staffed with Foreign Service Officers on rotational interludes from overseas assignments and Civil Service employees.

The staffing percentages as of October 1, 1982 were approximately 40 percent Foreign Service Officers, 42 percent Foreign Service nationals and 18 percent Civil Service. Funding for personnel and related expenses comprised 50 percent of the operating expenses of the Department and, hence, became a focal point for our study.

Other major expenditure areas include contributions to International Organizations and Refugee and Narcotics Programs, the costs of which are nearly \$1 billion or 38 percent of the overall State Department budget. Lastly, the appropriation for the construction, maintenance and operation of foreign buildings represents almost 20 percent of the operating budget.

II. ISSUE AND RECOMMENDATION SUMMARIES (CONT'D)

A. DEPARTMENT OF STATE (CONT'D)

STATE 1: FOREIGN SERVICE PERSONNEL SYSTEM

Issue and Savings

Are there opportunities within the State Department's Foreign Service Personnel Management System, which administers payroll costs of \$291 million (FY 1983), to improve the system's effectiveness and reduce operating expenses?

The Foreign Service Personnel System is characterized by the development of a top heavy skewedness, extensive mismatching of personnel and positions and the presence of numerous "overcomplement" employees. The Task Force has developed recommendations to modify these aspects of the personnel management system which can result in first year savings of \$25.8 million. Three years savings are estimated to be \$86.3 million.

Background

The Foreign Service Officer (FSO) corps has maintained its status as an organization separate from the Federal Civil Service by Congressional mandate through Foreign Service Acts of 1924, 1946 and 1980. The Service has historically been set apart due to the character of its mission -- official representation to foreign governments and implementation of foreign policy overseas. The Service has its own Director General, maintains a different pay scale from the General Schedule, a separate benefits package, and separate enabling legislation, to name a few of its unique characteristics. The effect of recent legislation has been to place into law most personnel policies and employee benefits.

FSO corps personnel serve not only in the Department of State (State), United States Information Agency (USIA), Agency for International Development (AID) and Peace Corps, but also serve 22 other governmental departments and agencies directly or through "detail-out" assignments. This study deals only with personnel data for State's FSOs because 70 percent of FSOs are under control of State personnel direction and all FSOs are guided by the Foreign Service Act of 1980.

State's Foreign Service employees comprise 40 percent of the Department's total employment with Foreign Service nationals and Civil Service the remaining 60 percent. Full-time Foreign Service personnel have ranged in number from 8813 to 9700 in the years 1975 to 1981, while average salaries have ranged from \$20,487 to \$31,126.

Salary costs for State's FSO corps for FY 1983 are estimated to be \$290 million. While the number of employees has remained at the same level (within a 5 percent variance) during the past 20 years, the salary costs have risen at an annual increase level of 7.2 percent each year during the period.

Members of the Foreign Service must be available for worldwide service. Further, career members of the Foreign Service are obligated to serve abroad for substantial portions of their careers. Each member of the Service is assigned to a salary class which is not affected by his/her positional assignment. This personnel management practice is known as the "rank-in-man" concept. Conversely, assignment does not influence rank (or salary); on the other hand, the "rank-in-job" system is found in the Civil Service.

The Senior Foreign Service was created by 1980 legislation and modelled after the Senior Executive Service of the Civil Service. Mid-level and junior FSOs are separated into the functional categories of generalists and specialists. The following data depict personnel by level:

<u>Grade</u>	<u>12-31-80*</u>	<u>12-31-81</u>
Senior Foreign Service	11.0	10.7
<u>Mid-level:</u>		
1	12.0	12.6
2	15.3	15.2
3	16.5	16.6
<u>Junior level:</u>		
4	15.8	14.9
5	11.2	12.6
6	6.6	6.6
<u>Clerical</u>		
7	5.0	5.3
8	4.9	4.2
9	1.7	1.3
	<u>100.0</u>	<u>100.0</u>

*Reflects new grade schedule established by Foreign Service Act of 1980.

Generalists perform the "on-line" duties of reporting and analysis of foreign affairs. Specialists are responsible for staff functions such as auditor, medical officer, etc. Our rationale for detailed review of the generalist group includes the limited career growth of specialists and their lower percentage in the Foreign Service.

Most generalists enter the Service through the examination process, as State follows a "promote from within" policy. The Foreign Service exam is administered by the Board of Examiners, reconstituted by the Foreign Service Act of 1980. Each year 200 to 300 are accepted as junior officers from approximately 18,000 university graduate applicants.

Transition to mid-level officer occurs after a trial period of service (currently four to five years), at which time an officer may receive a career appointment. FSOs are subject to performance evaluations at least annually and may be "selected-out" for substandard performance.

Position assignments are handled by the Personnel Bureau using an "open-assignment" process, whereby information on available positions is publicized to employees, and employees bid for those positions. Available positions result from vacancies due to the announced rotation policy and resignations. Assignments to one of State's 253 overseas posts are standardized as between two to four years in length. Besides assignment to overseas posts, FSOs are assignable to State positions as well as other governmental agencies like the National Security Council (NSC) and Department of Defense (DOD), the latter being known as "detailed-out" assignments.

Promotion is also managed by the Personnel Department by developing the range of possible promotions to be granted at each grade level. Promotion selection boards rank order promotion candidates within each competition group, and final promotions result from the matching of this rank order listing and the number of promotions allowed by management.

The 1980 Foreign Service Act defines the rules of labor-management relations in the Department. Foreign Service employees within State and AID are represented by an elected bargaining agent, the American Foreign Service Association (AFSA), in the filing of grievances and negotiation of conditions of employment and other personnel matters.

The substantial changes enacted in the 1980 legislation have placed into law many previous personnel practices. It was also an attempt to modernize the professional career program at the Department of State which had been studied with some intensity over the prior 15 years. Our Task Force received, as briefing documents, reports that gave evidence that personnel problems such as job grade inflation and the use of senior personnel for lower level positions were still in existence and would not be corrected by the implementation of the 1980 legislation. These problems were not quantified or analyzed in detail in such reports. Our Task Force validated their relevance through interviews at State and at embassies and presents them in the findings section on a quantified basis.

Methodology

The Task Force has combined in this review the elements of the Foreign Service Personnel Management System that have been identified in previous studies and developed their interrelationships. The Task Force also interviewed key State personnel in Washington and at several overseas posts and reviewed many aspects of the Foreign Service Act of 1980 and subsequent implementation activities. Several quantitative analyses were performed, including a review of positions by grade level, a comparison between position levels and ranks of incumbents and an evaluation of attrition rates resulting from selection-out. Also, algebraic models of personnel distributed by level were developed for the Foreign Service and similar organizations.

Findings

As a result of the analysis and review, the Task Force found that the distribution of State's Foreign Service Officers (generalists) among senior, mid and junior level ranks shows a top heavy profile; this pattern is dissimilar to other government and private sector organizations as shown below:

	<u>State</u>	<u>Military</u>	<u>Accounting</u>	<u>Banking</u>
Senior	19.7%	6.1%	12.0%	8%
Mid-level	65.9	64.9	16.0	40
Junior	14.4	29.0	72.0	52

The Task Force found these three levels have an interactive, dynamic relationship in that personnel from level 3 (junior level) provide the resource pool for level 2 (mid-level) and personnel in level 2 in turn provide the pool for level 1 (senior). In the three-part process flow among the level, personnel pool overages or shortfalls will affect the availability (both number and quality) of personnel input to the next level. Such relationships can be expressed as shown below:

<u>Key</u>	<u>Level 3</u>	<u>Level 2</u>	<u>Level 1</u>
Resource pool	449	2,062	616
Average years in level	5	20	12
Annual turnover rate	89.8	103.1	51.3

The Task Force found that the relationships between resource pool size, average years in a level, and turnover rate are important factors in managing the composition of the Service and are important to the management of promotional opportunity.

The Task Force found that, when using data for September 30, 1981, level 3 turnover, 89.8 personnel per year, is slightly less than the demand of 103.1 personnel created by level 2. Conversely, level 2 generates roughly twice as many personnel outputs as can be absorbed by level 1.

Due to the application of the "rank-in-man" concept, more than 42 percent of the Service is assigned to positions one grade above or below their personnel rank, while 14 percent of Foreign Service personnel are assigned to jobs two or more grades above or below their personnel rank. In short, 56 percent are not matched job to rank/salary.

Table II-1 depicts those Foreign Service personnel assigned to positions two or more levels below their personnel grade (pay scale).

[Table II-1 on following page]

Table II-1FOREIGN SERVICE PERSONNEL OUT OF GRADE

<u>Grade</u>	Incumbents in positions below their personnel grade (pay scale)				<u>Total</u>
	<u>2</u>	<u>3</u>	<u>4</u>	<u>5</u>	
Counselor	2				2
FS-1	10				10
FS-2	14				14
FS-3	10	65			75
FS-4	19	47			66
FS-5	0	29			29
FS-6	12	43			55
FS-7	2	6	3	16	27
FS-8	8	32	40		80
FS-9	6	5	9		20
Total	<u>83</u>	<u>227</u>	<u>52</u>	<u>16</u>	<u>378</u>
Percent	22%	60%	14%	4%	100%

An overcomplement committee has been formed to review quarterly the status of approximately 150 personnel classified as overcomplement.

Typical classifications used by the committee to describe the status of overcomplement personnel and the numbers in such classification at two recent dates are shown in Table II-2.

[Table II-2 on following page]

Table II-2TYPICAL CLASSIFICATIONS OF OVERCOMPLEMENT PERSONNELS

<u>Status description</u>	<u>Number of personnel</u>	
	<u>1/29/82</u>	<u>4/29/82</u>
Pending establishment of position	17	15
Pending Department Assistant Secretary approval	8	2
Pending Presidential/Senate action confirmation	3	3
Pending movement to onward assignment (working)	5	22
No funded position	9	6
Otherwise fully employed	75	69
Training	1	2
FS conversion to GS	3	1
Sick/annual leave	5	11
Board of Examiners	8	11
Time in class/retiring	7	7
AWOL	2	1
Nothing firm	14	2
Campbell cases	-	2
	<u>157</u>	<u>154</u>

Further, 40 senior officers were identified by State Senior Department management to the Secretary of State as surplus in July 1982 and were included in a group of 576 officers occupying positions outside the Department's direct responsibilities.

The results of the present performance evaluation process show most FSOs to be rated above average, e.g., 96 percent of Senior Foreign Service were rated as above average in 1981. Hence, use of the evaluation system to identify selection-out possibilities is limited.

Other findings identified by the Task Force include the following:

- o Supervising management and AFSA members represented by the bargaining unit can be the same people under present definitions.
- o Personnel assigned to senior levels of management at embassies were found, in several instances, to operate in a reactive mode rather than with modern management techniques like objective setting and integrated functional planning.

- o Recruiting processes do not result in the selection of enough individuals with administrative and managerial skills to fill the number of administrative positions because recruiting is not performed at business schools and the entrance examination is oriented toward history and international affairs. Several ambassadors identified management training as a specific need amongst mid-level FSOs. Further, training programs for entry and mid-level officers have not included substantive management training.

Conclusions

The Task Force concludes that the present personnel system has allowed FSOs to continue their careers to the point that major imbalances in the personnel work force have been created. Correlation of position rank and job classification occurs in a minority of instances. Performance evaluations do not appear to be useful in their current form for identification of the most qualified officers, and "selection-out" has not been an effective element in employee attrition. The current personnel system does not cope with the inherent characteristics of managing a carefully selected, elite group of professionals from recruitment to the ultimate career goal -- an ambassadorial assignment. Further, pressures to manage personnel resources are countered by devices that encourage imbalances, such as the "rank-in-man" concept and "detail-out" assignments. In short, the system does not balance individual career development needs and position requirements.

Specific conclusions are:

- o it is desirable and necessary to shift distribution of personnel;
- o elimination of mismatching employees should provide cost savings and increase job opportunities for mid-level employees, and
- o the number of overcomplement employees is too large.

Although State's personnel management believes that, in time, the overcomplement ranks will be reduced, we have concluded that the "rank-in-man" concept and other factors will contribute to the process of creating more such personnel and that a more stringent approach is necessary.

There are opportunities for improvement in personnel administrative practices in:

- o performance evaluations,
- o selection-out,

- o union participation,
- o management of embassies, and
- o recruiting and training.

Recommendations

The Task Force recommends that the Secretary of State initiate a reassessment of the Foreign Service personnel system with the aim of conversion to a manager-oriented personnel system with equally fixed position and manpower levels and more stringent performance evaluations.

STATE 1-1: The State Department should use models to correct skewed distribution. The Task Force recommends the Secretary of State initiate a review of position rankings to better match incumbents with position and to achieve lower graded jobs where appropriate. The Task Force recommends the use of more pyramid-shaped models to balance the overall resource pools, promotion opportunity, and economic costs.

STATE 1-2: The State Department should review ranking of positions and realign personnel. The Secretary of State should direct the reduction in the number of employees in positions two grades below their personnel ranks by realignment of mismatched personnel and by conducting a position analysis to reexamine each position in relation to its grade classification.

STATE 1-3: The State Department should eliminate the overcomplement concept. The Secretary of State should eliminate the concept of overcomplement employees and enforce the policy of "selection-out" of any employee whose contribution to the organization is minimal, or whose skills are not needed by the Department.

STATE 1-4: The Secretary of State should direct the redesigning of the performance evaluation system so that meaningful standards are used for performance measurement and appraisal. The results of this system should yield a bell-shaped distribution curve of rankings. Additionally, supervisors should be trained in preparing more critical evaluations and counseling subordinates.

STATE 1-5: The Secretary of State should seek the elimination of the conflict of interest situations in labor-management practices by requesting legislative amendment to expand the definition of management official to include all senior officers and other personnel serving in supervisory positions.

STATE 1-6: The Secretary of State should direct the initiation of new recruiting procedures to attract officers with skills in management and encourage the development of supervisory skills in middle level and senior officers.

Savings and Impact Analysis*

1. Correction of Skewed Distribution (see State 1-1)

In order to calculate savings for correction of the skewed distribution of personnel, we assumed that the Department of State would adopt the following structure:

	<u>Junior</u>	<u>Mid-level</u>	<u>Senior</u>
Proposed inventory level	885	1,732	510
Average years in classification	5	20	12
Average turnover rate	177	87	43
Promotion opportunity	49%	49%	

This structure was assumed because we believe it is the most likely model to follow and represents a conservative and realistic range of savings.

Using this model the first-year savings would be calculated as follows:

	<u>Junior</u>	<u>Mid-level</u>	<u>Senior</u>
Proposed inventory	885	1,732	510
Current State inventory	449	2,062	616
Inventory difference	(436)	330	106
Average salary	\$23,800	\$41,900	\$57,600
Salary savings	(\$10,376,800)	\$13,827,000	\$6,105,600
Savings			\$9,555,800
Employees normal cost of retirement (34%)			\$3,248,972
Total savings			\$12,804,772

* All savings and impact analyses based on salary levels as of December 31, 1982.

2. Realignment to Match Position and Personnel Rank (see STATE 1-2)

In order to estimate savings attributable to position realignments, an analysis was made of the difference between salaries of incumbents in the position and salaries commensurate with the position grades. This analysis assumes:

- o averages within senior ranks have displaced some junior and mid-level employees, creating averages at lower levels. Elimination of averages at senior levels will remedy averages at lower levels, and
- o personal grade/position grade data supplied by personnel are accurate.

Table II-3 shows this analysis. Estimated first-year savings are \$6 million.

[Table II-3 on following page]

Table II-3

ELIMINATION OF POSITION
GRADE/PERSONNEL GRADE OVERAGES^{1/}

Position grade	a Overages ^{2/} (number employees)	b Average salary employee	c Average salary position grade	d Potential savings for position (b-c)	Total potential savings (a x d)
OC-2	2	\$58,500	\$58,500	\$ 0	\$ 0
FS-1	10	57,632	51,310	6,322	63,220
FS-2	14	57,632	41,441	16,191	226,674
FS-3	10 65	57,632 51,310	33,063	24,569 18,247	245,690 1,186,055
FS-4	19 47	51,310 41,441	27,214	24,096 14,227	457,824 668,669
FS-5	0 29	41,441 33,063	23,474	17,967 9,589	278,081
FS-6	12 43	33,063 27,214	20,627	12,436 6,587	149,232 283,241
FS-7	2 6 3 16	41,441 33,063 27,214 23,474	18,126	23,315 14,937 9,088 5,348	46,630 89,622 27,264 85,568
FS-8	8 32 40	33,063 23,474 20,627	16,024	17,039 7,450 4,603	136,312 238,400 184,120
FS-9	9 5 6	23,474 20,627 18,126	14,500	8,974 6,127 3,626	80,766 30,635 21,756
					\$4,472,759
	Plus:		Savings on salary costs Savings on employer's normal retirement contribution		<u>\$1,520,738</u>
	Total				<u>\$5,993,497</u>

^{1/} All data as of January 11, 1982, for Generalist and Specialist categories of Foreign Service Corps.

^{2/} Number of employees in positions two or more grades below their personnel grades. Taken from Personnel Bureau computer run SPSS RAT SYSTEM Full-time permanent (more than one year) Foreign Service employees: creation date 8/5/82.

3. Overcomplement Employees

Management estimates the number of "overcomplement" Senior Foreign Service employees to be 70. Our cost analysis is as follows:

THREE YEAR COST SAVINGS FROM ELIMINATION OF
CONCEPT OF OVERCOMPLEMENT SENIOR FOREIGN SERVICE EMPLOYEES

(\$ millions)

	<u>Year 1</u>	<u>70 employees Year 2</u>	<u>Year 3</u>
Salary ^{1/} costs	\$4.03	\$4.43	\$4.87
Plus employer's retirement contribution ^{2/}	<u>1.37</u>	<u>1.51</u>	<u>1.66</u>
Total potential savings	5.40	5.94	6.53
Buy-out costs ^{3/}	<u>1.34</u>	<u>1.34</u>	<u>1.34</u>
Net savings	<u>\$4.06</u>	<u>\$4.60</u>	<u>\$5.19</u>

^{1/} Assumes average salary of \$57,632 and 10% inflation adjustment in years 2 and 3.

^{2/} Approximately 34% of salary.

^{3/} One year's salary distributed over three years.

Source: Memorandum to the Secretary of State by R. T. Kennedy, 7/21/82

As discussed above, the Task Force concluded that other positions should be considered overcomplement. The cost estimate for these positions is shown below:

Table II-4

SALARY COSTS OF OTHER OVERCOMPLEMENT EMPLOYEES

<u>Grade</u>	<u># of overcomplement^{1/}</u>		<u>Average</u>	<u>Average salary</u>	<u>Savings</u>
	<u>4/29/82</u>	<u>1/29/82</u>			
FS 1	22	26	24	\$51,310	\$1,231,440
FS 2	23	24	23	41,441	953,143
FS 3	14	7	10	33,063	330,630
FS 4	12	15	13	27,214	353,782
FS 5	<u>4</u>	<u>4</u>	<u>4</u>	<u>23,474</u>	<u>93,896</u>
	75	76	74		<u>\$2,962,891</u>

^{1/} Per overcomplement quarterly reports.

THREE YEAR COSTS SAVINGS FROM ELIMINATION OF "OVERCOMPLEMENT" MID-LEVEL AND JUNIOR OFFICERS

(\$ millions)

	<u>Year 1</u>	<u>Year 2</u>	<u>Year 3</u>
Salary costs ^{1/}	\$2.96	\$3.26	\$3.58
Plus employer's retirement contribution ^{2/}	<u>1.01</u>	<u>1.12</u>	<u>1.22</u>
Total potential savings	\$3.97	\$4.38	\$4.80
Buy-out costs ^{3/}	.99	.99	.99
Net savings	<u>\$2.98</u>	<u>\$3.39</u>	<u>\$3.81</u>

^{1/} See Table II-4 above for derivation of salary costs. Includes 10% inflation adjustment in years 2 and 3.

^{2/} Approximately 34% of salary.

^{3/} One year's salary distributed over three years.

Table II-5 summarizes overcomplement savings.

[Table II-5 on following page]

TABLE II-5

SUMMARY OF OVERCOMPLEMENT SAVINGS

	(\$ millions)		
	<u>Year 1</u>	<u>Year 2</u>	<u>Year 3</u>
I Senior (70)	\$4.06	\$4.60	\$5.19
II Other (75)	<u>2.98</u>	<u>3.39</u>	<u>3.81</u>
Total	<u>7.04</u>	<u>\$7.99</u>	<u>\$9.00</u>

3. Summary of Cost Savings

	Savings ^{1/}		
	<u>Year 1</u>	<u>Year 2</u>	<u>Year 3</u>
	(\$ millions)		
Correction of Skewed Distribution (STATE 1-1)	\$12.8	\$14.1	\$15.5
Realignment to Match Position and Personnel Rank (STATE 1-2)	6.0	6.6	7.3
Elimination of Overcomplement (STATE 1-3)	<u>7.0</u>	<u>8.0</u>	<u>9.0</u>
	<u>\$25.8</u>	<u>\$28.7</u>	<u>\$31.8</u>

^{1/} The Task Force recognizes that certain positions could be duplicated in the savings analysis; however, due to the inability to identify specifically where duplication would occur, it has presented the total potential savings.

Implementation

1. Agency Authority

STATE 1-1: Use models to correct skewed distribution of personnel.

STATE 1-2: Review ranking of positions and realign personnel.

STATE 1-3: Reduce overcomplement employees and apply more rigorous selection-out procedures in conjunction with revised performance evaluations.

STATE 1-4: Redesign the performance evaluation system and train supervisory personnel in evaluation and management methods.

STATE 1-6: Initiate a program to enhance managerial skills.

2. Congressional Authority

STATE 1-5: Amend the Foreign Service Act of 1980 to expand the definition of management official in Chapter 10.

II. ISSUE AND RECOMMENDATION SUMMARIES (CONT'D)

A. DEPARTMENT OF STATE (CONT'D)

STATE 2: FOREIGN SERVICE RETIREMENT AND DISABILITY SYSTEM

Issue and Savings

Does the Foreign Service Retirement and Disability System with an estimated FY 1983 cost of \$372 million present an opportunity to realize cost-savings from comparisons to Civil Service and private sector retirement programs?

Our recommendations result in a first-year savings of \$0.2 million if changes to the System are phased in beginning with all new employees and \$29.7 million if immediate, full implementation is chosen. Savings for the three years would total \$3.9 million if phase-in implementation is elected and \$90.6 million if full implementation is chosen.

Background

1. Description

The Foreign Service Retirement and Disability System covers all 13,000 Foreign Service employees. Most of the participants are employed in the State Department (State), but the system also includes those in the United States Information Agency (USIA), Agency for International Development (AID), Department of Agriculture and elsewhere. In several important respects, the benefits are substantially more generous than those under the Civil Service Retirement System which covers most other civilian employees of the Federal Government.

2. Budget Figures and Trends

The employees contribute 7 percent of their salary and the Federal Government pays the balance of the funding cost for the Retirement and Disability System.

The total Government funding cost for the system for FY 1983 has been estimated by State to be \$371.8 million, or 93 percent of the annual payroll cost. Of this amount, approximately \$331 million is included in the State's budget (including USIA) and most of the balance is for AID. This \$331 million represents approximately 13 percent of State's total budget.

The Department has estimated the Government's budgeted cost of the System as follows:

<u>Fiscal year</u>	<u>Dollars (\$ millions)</u>	<u>Percent of annual payroll costs</u>
1983	\$372	93
1984	387	95
1985	400	97
1986	412	98
1987	422	100

The above costs do not include the pension costs for 25,000 other international affairs employees, who are covered by either the Civil Service Retirement System or the programs for foreign service national employees.

Methodology

Estimated cost savings were developed by a Task Force member who is an actuarial consultant using data provided by State combined with the actuarial valuation report prepared by the Department of the Treasury.

Personnel interviewed included those in the personnel and accounting departments responsible for employee benefits, and those personnel at Treasury charged with responsibility for actuarial computations.

Findings

The cost of the Foreign Service Retirement program is increasing both in dollars and as a percent of pay. The Government's estimated budgeted cost of the System equals 93 percent of pay in FY 1983, and is expected to rise to 100 percent within four years primarily due to "normal cost" increases.

In contrast, the Government's cost for 1981 for the U.S. Civil Service Retirement System, which covers most Federal civilian employees, was 32.7 percent of actual pay. Further, on a funded basis the cost of the Foreign Service Retirement System was 112 percent of payroll compared to 85 percent for Civil Service in FY 1981. The Civil Service System budgeted cost is substantially lower than the Foreign Service System, in part because the Foreign Service System provides more generous benefits and in part because the budgeted amount for the Civil Service System does not reflect the true accruing costs of that System. The Civil Service Retirement System has a lower normal cost percent than the Foreign Service System but requires higher past service contributions as the result of past underfunding.

Most private sector employers have pension costs under both Social Security and under a private pension plan with combined cost less than 15 percent of total payroll (Social Security costs 6.7 percent of payroll).

Under the Foreign Service System, the normal retirement age (the age at which an employee may first retire on an unreduced pension) is 50 with 20 years of service, or 60 with 5 years of service.

This retirement plan aspect is far more liberal than the Civil Service Retirement System.

A comparison of retirement ages for the two systems for employees hired at various ages is as follows:

<u>Age at hire</u>	<u>Retirement age</u>	
	<u>Foreign Service</u>	<u>Civil Service</u>
25	50	55
30	50	60
35	55	60
40	60	60
45	60	62
50	60	62
55	60	62

The Task Force is not aware of any requirement of the Foreign Service that renders employees unable to perform their duties at age 50.

The Foreign Service System provides larger benefits than are provided under the Civil Service Retirement System for employees with equal records of service and salary, for all except a very small number of very long service employees. The benefit payable upon retirement under the Foreign Service System equals 2 percent of the employee's average pay during the highest three consecutive years multiplied by the years of credited service (maximum 35 years). Under the Civil Service Retirement System, the benefit equals 1.5 percent of the three-year-average-pay for each of the first five years of credited service, 1.75 percent for each of the next five years, and 2.0 percent per year thereafter (maximum approximately 43 years).

For an employee retiring after 20 years of service, the Foreign Service System provides a benefit which is 10.3 percent greater than the Civil Service Retirement System would provide. There is no indication that the needs for retirement income of the two groups differ and no ascertainable reason for a difference in the benefit formulas.

Conclusions

Because the Foreign Service Retirement and Disability System and the Civil Service Retirement System are in most aspects the same, there are broad cost reduction opportunities that apply equally to both systems. Where the two systems are identical, we assume that any change made in the Civil Service Retirement System would be made in the Foreign Service System, and that any such changes would be made primarily in response to a review of the much larger Civil Service Retirement System. Therefore, this Report addresses only the cost reduction opportunities related to differences in the two systems.

Two cost reduction opportunities are considered in this Report:

- o an increase in retirement age to conform with the Civil Service Retirement age, and
- o a change in the benefit formula.

Both the retirement age and benefit formula provisions of the Foreign Service plan are substantially more generous than those of the Civil Service Retirement System or private sector plans, are not needed or justified, and create substantial excessive costs.

Recommendations

STATE 2-1: Increase retirement age under the Foreign Service Retirement and Disability System. It is recommended that Congress amend the Foreign Service Act of 1980 to increase the retirement age under the Foreign Service System to be the same as that under the Civil Service Retirement System, including any future increases in retirement age adopted under the Civil Service Retirement System.

STATE 2-2: Change the benefit formula under the Foreign Service Retirement and Disability System. It is recommended that Congress amend the Foreign Service Act of 1980 to change the benefit formula for the Foreign Service System to equal that of the Civil Service Retirement System.

Savings and Impact Analysis1. Increase Retirement Age Under the Foreign Service Retirement and Disability System (See STATE 2-1).

The estimated total government expenditure for the Foreign Service Retirement and Disability System if no change is made, the estimated amount of savings which would occur if the change were fully phased in, and the estimated actual savings phased in for employees hired after April 1, 1983, are shown below for fiscal years 1982 through 1985.

(\$ millions)

<u>Fiscal year</u>	<u>Present program estimated expense</u>	<u>Estimated annual savings</u>	
		<u>If fully phased-in</u>	<u>Partial phase-in</u>
1982	\$343		
1983 (year-1)	372	\$18.6	\$0.1
1984 (year-2)	387	18.9	0.8
1985 (year-3)	400	19.2	1.5

Estimated cost savings depend upon numerous actuarial assumptions, including the following:

- o number of new employees hired in future years and their distribution by age, sex and salary;
- o rates of mortality;
- o rates of disability;
- o rates of actual retirement among employees who have become eligible;
- o rates of termination of employment;
- o rates of salary increase;
- o rates of cost of living increase; and
- o rate of interest.

The Task Force relied upon the actuarial methods, assumptions and computations of the Government Actuary of the Department of the Treasury, as contained in the report for the Plan Year ending September 30, 1980.

The Retirement Division Chief provided information that the average retiring employee does so at age 57 with 28 years of service. Under the proposal such an employee,

hired at age 29, would first be eligible to retire at age 60. To obtain the approximate relative cost, the level annual cost was determined to fund a pension of 2 percent of pay times years of service for an individual hired at age 29 and retiring at either age 57 or age 60. Because only the relative cost, and not the absolute cost, was sought, and because of the constraints, simplified assumptions were used, consisting solely of the 1971 group annuity mortality table for males after retirement and 6 percent interest. The level annual cost thus calculated for retirement at age 60 was 11.23 percent less than for retirement at age 57. The normal cost rate most recently determined by the Government Actuary of the Department of the Treasury^{1/} is 41.546 percent of covered payroll. Therefore the cost savings was estimated to be 4.66 percent of covered payroll (11.23 percent of 41.546 percent). This 4.66 percent was multiplied by projections of covered salary prepared by State to determine the estimated cost savings if the change were fully phased in.

Projections were made of the proportion of covered salary attributable to employees hired after April 1, 1983, based upon data included in the "Report to the Speaker of the House of Representatives and The Committee on Foreign Relations of the Senate Concerning Implementation of the Foreign Service Act of 1980." The proportions determined were applied to calculate the portion of the cost phased-in for each fiscal year. Because the retirement ages are set forth in statute, legislative action is required to change them. This could be accomplished by amendments to the retirement age provisions of the Foreign Service Retirement and Disability System.

2. Change the Benefit Formula Under the Foreign Service Retirement and Disability System (see STATE 2-2).

The estimated total government expenditure for the Foreign Service Retirement and Disability System if no change is made, the estimated amount of savings which would occur if the change were fully phased-in, and the estimated

^{1/} Report for Plan Year Ending September 30, 1980, Table Y.

actual savings phased-in for employees hired after April 1, 1983, are shown below for fiscal years 1982 through 1985.

(\$ millions)

<u>Fiscal year</u>	<u>Present program estimated expense</u>	<u>Estimated annual savings</u>	
		<u>If fully phased-in</u>	<u>Partial phase-in</u>
1982	\$343		
1983	372	\$11.1	\$0.1
1984	387	11.3	0.5
1985	400	11.5	0.9

As stated above, the average retiree was assumed to have 28 years of service. An employee retiring under the Foreign Service System would receive a pension of 56 percent of average compensation, while an employee retiring under the Civil Service Retirement System would receive a pension of 52.25 percent of average compensation. 52.25 percent is 93.3 percent of 56 percent. Hence this change would reduce benefits and normal costs by an estimated 6.7 percent. We have estimated that the average retirement benefit under the revised formula would be 6.7 percent smaller than under the present formula, and that the System's normal cost would be reduced by approximately that percentage.

As stated above, the normal cost rate most recently determined by the Government Actuary of the Department of the Treasury is 41.526 percent of covered payroll. Therefore the cost savings was estimated to be 2.78 percent of covered payroll (6.7 percent of 41.526 percent). This 2.78 percent was multiplied by projections of covered salary prepared by State to determine the estimated cost savings if the change were fully phased-in. Projections were made of the proportion of covered salary attributable to employees hired after April 1, 1983, based upon data included in the "Report to the Speaker of the House of Representatives and the Committee on Foreign Relations of the Senate Concerning Implementation of the Foreign Service Act of 1980." The proportions determined were applied to calculate the portion of the cost phased-in for each fiscal year.

No change should be made in any benefits already accrued. It would be possible to make the change effective for all future accruals; this approach would have no effect upon employees with ten or more years of service (for whom the benefit formula would not change), a small effect upon those with five to nine years service (reducing the accruals from 2.00 percent to 1.75 percent, and a larger effect

upon those with less than five years service (from 2.00 percent to 1.50 percent. Any reduction at all for existing employees could be expected to meet strong opposition. Therefore it is recommended that the change affect only employees hired after the effective date of the change.

The effect would be to provide Foreign Service employees hired in the future with benefits equal to those of most other government civilian employees, rather than the higher benefits they now receive. This would not have any impact at all upon the Department or its operations.

Because the benefit formulas are set forth in statute, legislative changes are required to change them. This could be accomplished by amendments to the benefit amount provision of the Foreign Service Retirement and Disability System.

The following recaps savings by year if implementation is phased-in (P) starting with new employees and if elected for all current members of State's Foreign Service (A):

(\$ millions)

	<u>Year 1</u>		<u>Year 2</u>		<u>Year 3</u>		<u>Total</u>	
	<u>P</u>	<u>A</u>	<u>P</u>	<u>A</u>	<u>P</u>	<u>A</u>	<u>P</u>	<u>A</u>
Increase retire- ment age: STATE 2-1	\$0.1	\$18.6	\$0.8	\$18.9	\$1.5	\$19.2	\$2.4	\$56.7
Change benefit formula: STATE 2-2	<u>0.1</u>	<u>11.1</u>	<u>0.5</u>	<u>11.3</u>	<u>0.9</u>	<u>11.5</u>	<u>\$1.5</u>	<u>\$33.9</u>
	<u>\$0.2</u>	<u>\$29.7</u>	<u>\$1.3</u>	<u>\$30.2</u>	<u>\$2.4</u>	<u>\$30.7</u>	<u>\$3.9</u>	<u>\$90.6</u>

Implementation

Recommendations STATE 2-1 and STATE 2-2 require amendment of the Foreign Service Act of 1980 by Congress.

II. ISSUE AND RECOMMENDATION SUMMARIES (CONT'D)

A. DEPARTMENT OF STATE (CONT'D)

STATE 3: OFFICE OF FOREIGN BUILDINGS

Issue and Savings

What cost-saving opportunities exist in the areas of responsibility of the Office of Foreign Buildings (FBO) which has a budget authority of \$190 million for FY 1983?

Specific savings opportunities have not been quantified in this area, but should be significant with the implementation of a real property management system. While the Department of State's management has taken action by proposing within its FY 1983 budget funds for design of such a system, we believe that presentation of this Issue in this Report may accelerate the approval process and encourage quicker implementation and sharper attention to the problems identified.

Background

FBO within the Bureau of Administration, is responsible for the acquisition, maintenance, and disposal of real property holdings, and leases in excess of 10 years, for U.S. diplomatic and consular posts throughout the world.

The authority for the management of overseas building programs stems from the Foreign Buildings Act of 1926, as amended, and is vested in the Deputy Assistant Secretary for Foreign Buildings through delegation from the Secretary of State.

The U.S. Government property holdings under the responsibility of FBO are estimated to be more than 2,700 buildings and long-term leaseholdings at 287 foreign locations. Currently FBO is supervising \$34 million in architectural and engineering contracts and \$250 million in construction contracts, and maintaining in excess of \$5 billion in real property holdings.

The FY 1983 budget request for acquisition, operation, and maintenance of buildings abroad was \$190 million, an increase of \$4 million (2.2 percent) over the FY 1982

budget of \$186 million. The appropriation request is to construct, acquire by purchase or long-term lease, and operate and maintain office space and housing abroad. The request detail shows that one major construction project (RIYADH) accounts for 27.3 percent of the FY 1983 budget.

The FBO staff consists of 103 individuals; the office is organized by area of technical expertise. These include architectural, engineering, construction and maintenance, interior design, contracts, budget and automated data management staff in addition to executive and administration offices.

Within State, the Office of the Comptroller is responsible for the Foreign Affairs Administration Support (FAAS) System, which is designed to allocate certain administrative costs based upon the support services provided to other agencies present overseas.

The Comptroller had engaged outside consultants to review the Department's financial accounting needs. The study has recommended, and the Department has authorized the design of a Financial Management System (FMS). The FMS design concept includes a real property management module because of the extensive existing problems revealed in the study.

Several government investigative agencies have addressed the problems associated with effectively performing their responsibility for over a decade. According to these reports, State's FBO has traditionally been viewed as poorly organized, inefficient, and insufficiently concerned with sound budget practices (especially in the area of developing realistic cost estimates and construction schedules for new construction projects). Buildings management and maintenance have also been weak, according to these studies.

Methodology

Two Task Force members were assigned to determine changes required to develop a comprehensive real property management system and necessary to make informed, timely, and effective decisions, as well as to determine the appropriateness of cost allocations. We conducted interviews with the Deputy Assistant Secretary, Deputy Director and other professional staff of FBO. Additional interviews included the Department's Inspector General, and other agency users.

We reviewed the Inspector General's report entitled "Management Audit of Management Information Systems, Office of Foreign Buildings, Bureau of Administration" (September 1982). The inspectors reviewed FBO policies and practices, legislation, budget documents and reports. This extensive review resulted in 93 report recommendations, and recognized that a number of the recommendations cannot be implemented until a real property management system is installed and functional.

In addition, we consulted with private sector executives with overseas real estate management expertise and visited 14 overseas posts where the physical condition of both office and residential property was examined.

Findings

FBO does not have a comprehensive real property management information system:

- o an inventory of property holdings is not complete, in that all properties are not appraised nor is their present condition recorded, and
- o accurate inventories of furniture and furnishings are not maintained at the consular posts or communicated to FBO central office.

FBO action is based on reaction to specific problems rather than on regularly scheduled reports that monitor progress, measure performance, and identify developing problems.

The present financial management system does not provide the necessary financial information to identify all costs associated with the operation of an individual building.

FBO lacks an effective centrally-managed system for identification and disposal of excess property.

FBO's role as the single overseas property manager is undermined by Congressional funding for only 67 percent of the funds authorized to acquire, operate, and maintain overseas property are under the control of FBO. Additional property costs not reflected in FBO budgets are managed by the geographic regional bureaus within State, and funded from "Salaries and Expenses Appropriations."

Policy guidelines to assist managers in examining options and alternatives do not exist. Special examples of excessive spending were obtained during visits to embassies such as:

- o failure to exercise an option to buy property with lease renewal terms that would justify the purchase (London), and
- o failure to buy available property in depressed markets when present and forecasted space needs have justified the purchase and new construction was subsequently authorized (Madrid).

As a related issue no longer under the control of FBO but the Office of the Comptroller, the Task Force found that the FAAS System does not allocate any operating and maintenance costs (approximately \$87.7 million) in its allocation of costs among recipient agencies.

Conclusions

The absence of a complete information data base limits management's capacity to make informed, critical decisions relating to the following:

- o lease versus purchase alternatives;
- o preparation of an efficient maintenance program;
- o timely identification of cost overruns;
- o costing savings due to construction redesign;
- o monitoring achievement of construction milestones;
- o "red-flagging" potential construction delay; and
- o justification of budget appropriations.

Significant maintenance needs and long-term capital renewal needs cannot be recognized on a timely basis because of lack of availability of critical information required to plan and implement improvements. The lack of such recognition can result in extensive cost overruns.

The lack of identification of reusable furniture and furnishings leads to the inability of accurately appropriating funds for this purpose.

The lack of a cost accounting system denies identity of building operating costs and results in FBO officials basing their decisions upon incomplete facts.

Reluctance to identify excess property precludes use of alternative means to finance new construction and improvements.

Allocations of costs from State to other U.S. Government agencies who utilize foreign offices and residential facilities do not now represent full allocation of costs.

Recommendations

STATE 3-1: Develop a real property management system. FBO should proceed with its plan to develop a real property management system to compile a reliable accurate inventory of worldwide property holdings. The management system should be inclusive of a real property cost accounting system.

FBO should ensure that the proposed real property management system provides:

- o construction cost reporting:
 - original budget amounts,
 - change orders to date,
 - payment status,
 - budget overrun amounts, and
 - construction phase milestones;
- o real property inventory capability:
 - cost and appraised value,
 - useful life, and
 - anticipated repair and renovation dates; and
- o building operation costs.

STATE 3-2: Expansion of the cost accumulation report. We recommend that FBO design and implement an expanded cost accumulation report (to be included in the FMS when implemented) for individual capital projects which should provide the original budget amounts based upon a realistic financial construction plan. The plan should be detailed enough to record and compare actual expenditures by budget classifications (land acquisition, design and engineering fees, demolition, excavation, foundation, etc.). In addition, the cost report should include revised budget estimates, contractual commitments, additions to contractual amounts resulting from approved change orders, pending change orders (if significant) and payments to date for each respective detail budget classification.

STATE 3-3: Consolidation of fiscal authority. We recommend that the Office of Management direct the consolidation of fiscal authority inclusive of regional bureau expenditures for property costs in Salaries and Expenses to be appropriated and administered by FBO, commensurate with their level of responsibility. Note that consolidation of such funds should promote a more effective means of accumulating cost information.

STATE 3-4: Provide guidelines for identification of excess capacity. The Office of Management should direct FBO to develop procedures to aid in the identification of unused and potentially saleable property at the post level. We recommend that FBO study the possibility of developing a questionnaire to be answered at the post level in an attempt to identify excess capacity.

In addition, FBO should provide performance incentives to the geographic posts identifying excess capacity. We recommend FBO study the possibility of offering posts incentives in terms of percentage of proceeds realized for the identification of excess capacity. This will result in the timely identification of excess capacity.

STATE 3-5: Allocation of operating and maintenance expenditures. The FAAS coordinator should allocate the \$87.7 million of operating expenses presently not being allocated by the FAAS System on the basis of square footage utilized; if this is too complex, the allocation should be based on the number of U.S. personnel abroad. The allocation of operating and maintenance expenditures should promote clear definition and responsibility for user agency requirements.

Savings and Impact Analysis

Cost savings can be anticipated from more effective decision making based upon realistic, accurate information prepared by a real property management system. The implementation of the real estate management information system will require approximately \$6.1 million. Such funding has already been requested for FY 1983 through FY 1985 and therefore, is not a cost attributable to this study.

We believe management's ability to operate more economically and efficiently overseas is inherently correlated to comprehensive and reliable information, and future management decisions could generate millions of dollars in cost avoidance that are not measurable at this time but could include cost justification of purchase versus lease decisions, market value realizable from under utilized real estate, more effective maintenance programs or monitoring contractor compliance with preestablished timetables.

FBO appropriations for operations of buildings, and maintenance and repairs of buildings, of approximately \$61 million in the first year, \$67 million in the second year, and \$74 million in the third year should be shifted to the agencies utilizing the buildings abroad. Although the FBO appropriations reduction is not a cost savings to the Government, it is expected that allocating costs to the appropriate user areas will result in proper accountability and greater responsibility by the user agency for escalating expenditures.

The reduction is based upon overseas personnel statistics derived by the Office of the Comptroller. Statistics reveal that State personnel comprise approximately 30 percent or 4,334 of the total 14,218 U.S. personnel abroad. The remaining 70 percent of U.S. personnel abroad will utilize approximately \$61 million of the \$87 million proposed additional costs to be allocated. Other methods for allocation are possible as hard data are developed. For example, space utilized could be used when accurate measurements are available.

Implementation

1. Agency Authority

STATE 3-1: The State FBO should engage appropriate consultants to perform the concept design phase of the development of a real estate management system.

STATE 3-2: The Assistant Director for Construction and Maintenance of FBO should develop a monthly cost accumulation report to provide additional information, in a more useful format, for decision making.

STATE 3-3: The Deputy Assistant Secretary for Foreign Buildings should request an appropriation of the magnitude commensurate with the level of funding included in Salaries and Expenses Appropriations for operational costs associated with real property overseas. In addition, the Deputy Assistant Secretary for Foreign Buildings should provide the necessary guidance and reporting requirements to post level officials regarding the accumulation of a complete accurate information data base.

STATE 3-4: The Deputy Assistant Secretary should perform a study to develop a checklist and/or questionnaire to aid in the identification of excess capacity. In addition, the study should address the opportunity to provide incentives for recognition of excess capacity at the post level.

STATE 3-5: The Office of the Comptroller should provide for the allocation through FAAS of approximately \$87 million in operations and maintenance and repairs of buildings in FY 1983. The Interagency Council on Administrative Support should ensure during the FAAS hearing process the allocation of operations and maintenance expenditures.

2. Congressional Action

STATE 3-1: Congress should be requested to favorably accept such an appropriation request to engage appropriate consultants to perform the concept design phase of the development of a real estate management system.

STATE 3-4: Congress should be requested to approve the additional FBO appropriation to cover salaries and expenses appropriations associated with operations of real property overseas. Congressional approval will centralize funds appropriated for overseas real property and therefore centralize responsibility.

II. ISSUE AND RECOMMENDATION SUMMARIES (CONT'D)

A. DEPARTMENT OF STATE (CONT'D)

STATE 4: PURCHASE OF FOREIGN CURRENCIES

Issue and Savings

Does the purchase of foreign currencies (\$1.6 billion in FY 1981) by the Department of State for payment of overseas operating expenses in other countries provide an opportunity for cost savings?

Our Task Force recommendations should reduce the exposure to foreign currency fluctuations which are estimated to have caused budget overruns of approximately \$52 million during the period FY 1972 to FY 1980 against the major industrial countries' currencies. If similar conditions prevail in the next three fiscal years, cost savings of over \$17.1 million could be achieved.

We believe this recommendation is justified because the State Department is always a purchaser in the foreign currency market and because the size of the purchases are insignificant (less than .03 percent) to the total foreign currency market.

During the same period -- FY 1972 to FY 1980 -- foreign currency fluctuations for the military are estimated to have caused budget overruns of approximately \$1,265 million. If similar conditions prevail in the next three fiscal years, cost savings of over \$421 million could be achieved.

Background

The United States buys foreign currencies for payment of operating expenses in other countries, including salaries of foreign nationals, contractual services, rents, supplies and equipment, and travel. These expenses are financed from appropriated funds and account for more than 50 percent of approximately \$10 billion worth of foreign currency purchased from outside sources (excluding the Treasury) in FY 1982. The remainder of the foreign currency purchased is used for such nonappropriated fund activities as the post exchange system and for sales to U.S. military, civilian, and contractor personnel in exchange for dollars.

The foreign exchange market is the largest market in the world. On a busy day, the volume of transactions may reach \$100 billion, forty times the dollar volume on the New York Stock Exchange. Further, in March 1980, gross currency transactions by 90 banking institutions in the U.S. foreign exchange market amounted to \$491 billion. Of this monthly amount, approximately 6 percent represented outright forward contracts.

Although State's exposure to foreign currency fluctuations was smaller than that of the Department of Defense (DOD), purchases of foreign exchange by U.S. disbursing officers (USDOS) have increased 233 percent from \$482 million in FY 1972 to \$1.605 billion in FY 1981. It has been estimated by Department of State personnel that FY 1982 purchases of foreign currencies by USDOS exceeded \$2 billion. Of this amount, approximately \$488 million of foreign currency disbursements (gross funds) were made under State's budget. The difference between the USDOS and State budget is accounted for in various other government agencies' budgets who purchase through the USDOS.

In order to maintain approved levels of activity under rapidly changing economic conditions, the Buying Power Maintenance Account (BPMA) was established by Congress (P.L. 97-241, Section 112) in 1982 at the request of State's Comptroller. This account provides budget authority to offset losses in budgeted buying power due to adverse exchange rate fluctuations and to unanticipated but related wage and price changes. Gains due to favorable exchange, wage and/or price movements would be transferred into the BPMA to offset future losses.

Methodology

The Task Force conducted interviews with responsible State, Treasury, and General Accounting Office (GAO) personnel in order to define the issue, gather data on foreign currency transactions, study the current procedures for foreign currency purchases, and review departmental correspondence on the issue.

The Task Force obtained historical information on foreign currency purchases made by disbursing officers (DOs) since FY 1972. We then constructed a model which estimated foreign currency losses over the specified period. In the model, it was assumed that losses could have been substantially avoided on currencies with active trading markets through the use of forward or futures contracts. The transaction costs and the discount or premium to the spot rate associated with the use of these contracts have not been estimated due to the difficulty of making the appropriate assumptions. However, it is assumed

that these costs would be substantially less than the losses realized on foreign currency fluctuations during the study period.

Findings

No system exists for forecasting and reporting foreign currency expenditures. There is no system of gathering data on foreign currency expenditures and matching them with the budgeted information to determine the effects of foreign currency fluctuations. The current Treasury reports on foreign currency purchases are not agency specific (denoting the budget source), and do not specify the amount of foreign currency units purchased. In addition to the lack of historical information, there is no system requirement for budget forecast reporting in both U.S. dollar and foreign currency obligations.

Purchases of foreign currencies are always on a "spot basis." Current Treasury regulations prohibit the use of hedging techniques to minimize foreign currency exchange losses. The Treasury Fiscal Requirements Manual (I TFRM 6-8065.30) specifically states, "All exchange of dollars for foreign currencies is to be conducted for spot delivery. No use may be made of forward contracts, or of purchase at negotiated rates directly from foreign governments or private contractors." The Office of the Assistant Secretary for International Affairs of the Department of the Treasury informed us in a letter dated October 14, 1982 that they would be willing to consider again the "pros and cons" of buying currencies in the forward market.

The United States never sells currencies -- it only buys. The USDOS in each embassy or consulate assesses his/her daily foreign currency needs, maintains a financial plan which tracks obligations and receivables, and informs the Regional Administrative Management Center (RAMC) of his/her foreign currency needs by forwarding vouchers for payment of local goods and services. The RAMC purchases the appropriate foreign currencies after aggregating the daily requirements for each post. The RAMC then deposits the necessary foreign currency in the posts' bank accounts and checks are drawn and sent to the payees.

No studies on foreign currency hedging exist. The GAO studies that have been published to date are directed at government procedures for buying foreign currencies and have not addressed the subject of hedging. Treasury personnel were not able to provide any studies on the subject either. However, Treasury personnel provided correspondence outlining their reasons for avoiding the use of forward contracts.

State has requested and received supplemental appropriations due to foreign currency losses. State made supplemental appropriation requests in 1975 and 1979, citing weakness of the U.S. dollar as a reason. An Office of Management and Budget (OMB) submission for FY 1975 cited a request for \$10.5 million of which \$2,500,500 was directly associated with an "adverse dollar exchange rate." This supplemental appropriation was granted. State also requested a \$6 million increase in FY 1979 in a Congressional submission citing "exchange losses...in six Organization for Economic Cooperation and Development (OECD) countries." When the U.S. dollar strengthened, the resulting appreciations (gains) were removed from budgeted funds by OMB or Congress to the extent not already spent.

Task Force estimates effects of current practice to exceed \$52 million. While the U.S. dollar lost approximately \$52 million of its budgeted value against the industrial countries' currencies for the period 1972 to 1980, it gained approximately \$196 million against the non-oil developing countries (primarily in the Western Hemisphere) and \$9 million against the oil-exporting countries for a net gain of \$153 million. Such gains have been experienced in countries where inflation is so accelerated that gains were not realized or realizable.

Active forward and futures contract markets exist in the major foreign currencies. As noted earlier in the Background section, the forward market is a significant portion of the total foreign exchange market. In addition to the forward market, trading in foreign exchange futures (forward contracts for standardized currency amounts and maturities not tailored to the exact requirements of individual parties or selected value dates) has been conducted in the International Monetary Market (IMM) in Chicago since 1972, and in the Commodity Exchange (Comex) in New York City since 1980. In addition, a foreign currency options market has recently been established by the Philadelphia Exchange to trade in put and call options for fixed amounts of several major currencies.

Treasury and GAO have concerns regarding foreign currency hedging. In an interview with Treasury personnel, the following areas of concern were discussed regarding implementation of a foreign currency hedging program: (1) the staffing and procedures used to purchase the contracts, (2) who would administer the program, (3) whether the program gives the appearance of currency speculation (which is undesirable), and (4) the impact that the program would have on the foreign exchange markets. Specifically, Treasury personnel were concerned that transactions would imply a policy statement was being made on the U.S. dollar's strength or weakness.

Conversations with GAO personnel revealed other concerns. GAO personnel felt that U.S. Government hedging was undesirable since the U.S. Government is "self-insuring" against all claims and losses, and gains and losses would balance out over time.

Conclusions

State will continue to experience huge budget fluctuations. State will continue to suffer foreign currency losses in periods when the dollar is declining in value against the major industrial countries' foreign currencies unless some mechanism to remove that risk is implemented.

State needs a foreign currency forecasting system. State needs a system to forecast foreign currency obligations and purchases since current foreign currency reports by Treasury are not agency specific. The new Financial Management System (FMS) at the Department could be used to gather this information.

BPMA does not prevent foreign currency losses. Although BPMA will provide for a more orderly budgeting process for foreign currency fluctuations, it does not alleviate the risk of an unhedged foreign currency obligation.

Recommendations

STATE 4-1: Develop an accounting system to gather foreign currency needs. We recommend that the State Department Comptroller develop a uniform system of budgeting and reporting the forecasted statistics on foreign currency obligations. This information system will be necessary in order to estimate the size and maturity of the contracts. The system will also require coordination with all other agencies for which State acts as foreign currency purchasing agent. Cost is estimated to be minimal in that such systems are already developed by the banking community and information is provided to clients free of charge. Minimal cost may be experienced for clerical staffing of the function.

STATE 4-2: Establish foreign currency futures/forward desk. We recommend that the Secretary of State request exemption from Treasury regulations and establish a foreign currency futures/forward/options positioning desk in Washington. This forward positioning desk will buy or direct the purchase of contracts in major industrial countries' currencies and in amounts for which the U.S.

Government has fixed and budgeted obligations for the fiscal year ahead. No additional cost is expected since several personnel perform the "buy function" at this time (although only for three day periods).

STATE 4-3: Hire staff and define functions of trading desk. A Washington staff consisting of a manager, an analyst and a clerk/secretary will be necessary to collect and process the forecasted disbursement data. This staff will report to the Comptroller and be given an operating budget of approximately \$100,000 in their first year of operation. The staff will determine: (1) the foreign currency to be hedged, (2) the duration and the amount of the contract, (3) the market or intermediary to be used for the purchase of the contract, and (4) direct the purchase or sale of a specified contract.

Savings and Impact Analysis

1. Savings could amount to \$17.1 million over the next three years.

Savings of \$17.1 million (or \$5.7 million per year) represents approximately one-third of the loss that was estimated for the nine-year period from FY 1972 to FY 1980 in the major industrial countries' foreign currencies. The estimated over budget expenditure by the military (DOD) due to foreign currency fluctuations during the period was \$1.265 million. Savings over the next three fiscal years could be as much as \$421 million (one-third of the estimated loss). This savings analysis assumes that the historical pattern from FY 1972 to FY 1980 will be typical of the future variation in foreign exchange rates.

2. Hedgings should be limited to major industrial countries' currencies only.

State cannot be perfectly hedged against all budgeted foreign currency obligations due to the limited number of currencies for which futures and forward markets are available, and the relatively small requirement in some currencies. However, most of the major European currencies and the Japanese yen have active forward/futures markets with enough depth to permit large forward contract purchases.

3. Cost of forward contracts.

The cost of forward exchange contracts can be put into annual percentage terms for analytical purposes. The premium or discount is calculated by the following simplified formula:

$$\begin{array}{l} \text{Discount} \\ \text{(or premium)} \\ \text{in percent} \end{array} = \frac{\text{Foreign currency} \\ \text{spot minus forward rate}}{\text{Spot rate}} \times \frac{12}{\text{Months} \\ \text{to} \\ \text{maturity}} \times 100$$

The timing of forward coverage is important, since any delay while the U.S. dollar is deteriorating may involve a higher cost as opposed to the initial spot rate used for booking.

4. Cost of futures contracts.

The cost of futures contracts could involve a negotiated commission but no advanced funds.

5. Cost of options contracts.

The cost of options contracts includes the option cost and a margin deposit.

6. Addressing concerns over recommendations.o Treasury concerns:

- The burden of staffing and the development of procedures that are used to purchase the contracts would fall within State, not Treasury. State would be responsible for developing procedures which would give adequate notification of transactions to the proper Treasury [and Federal Reserve Bank (FRB)] personnel.
- State would administer the program for DO purchases. There would appear to be no current advantage to the U.S. Government for the Treasury (or FRB) to administer one or both of these programs since they have no system in place which is forecasting foreign currency needs and they do not have any staff with administrative experience in forward or futures trading other than the swap desk at the Federal Reserve Bank of New York (FRB NY).

- The program should not give the appearance of currency speculation. Hedging is defined as a temporary substitute for a transaction in the spot market to protect against adverse price movement. In this case, the purchase of a forward or futures or options contract is used as a substitute for a future cash transaction.
 - The program should not have a significant impact on the market in terms of dollar volume. As discussed in the Background section above, approximately 6 percent of the foreign exchange market activity was outright forward contracts. If the annual activity in forward contracts is approximately \$353 billion ($\$491 \times 12 \times .06$), then the \$2 billion in foreign currency purchases represents less than 1 percent (2 divided by 353). Furthermore, the industrialized countries' currencies being hedged represented less than \$1 billion of FY 1982 purchases.
- o GAO concerns:
- The "self-insuring" policy works on the premise of large numbers and unknown future obligations. The argument for absorbing foreign currency losses because the U.S. Government can afford it is a weak one since the obligations are known and have been budgeted.
 - The assertion (or belief) that the foreign currency fluctuations among industrial countries' currencies (and therefore the gains/losses experienced) will somehow balance out over time has no empirical proof.

Implementation

1. Agency Authority -- State Department

STATE 4-1: The Secretary of State must direct the Comptroller to develop this system. It is the Task Force's understanding that this information can be gathered as part of the new FMS currently being developed by State.

STATE 4-2: The Secretary of State must request exemption from Treasury regulations prohibiting the use of future/forward/option contracts (I TFRM 6-8065.30).

STATE 4-3: The Secretary of State must direct the Comptroller to hire staff and develop an operating procedure (as described in the Recommendations section above).

2. Agency Authority -- Treasury Department

STATE 4-2: The Secretary of the Treasury must rescind or revise the rule prohibiting the use of future/forward/option contracts (I TFRM 6-8065.30). The rule should state that USDOS with authorization from Treasury will be permitted to enter into contracts for future/forward/option delivery of foreign currencies in amounts to satisfy their projected foreign currency obligations.

Additional Information

The recommendations made in this Issue are consistent with sound business practices where there is a requirement to purchase foreign currencies on a regular basis. International political considerations may extend beyond the savings that have been estimated. Before implementation, State should consider the international political implications of the recommendations. We were not in a position to make such an assessment.

II. ISSUE AND RECOMMENDATION SUMMARIES (CONT'D)

A. DEPARTMENT OF STATE (CONT'D)

STATE 5: BUREAU FOR REFUGEE PROGRAMS

Issue and Savings

What changes pertaining to the Refugee Transportation Loan Program can be made in the prevailing procedures in order to maximize the collection rate?

Our recommendations result in savings and accelerated collections of approximately \$22.9 million in the first year and \$21.5 million in the second year and \$20.2 million in the third year.

What managerial improvements can be made to help monitor the performance of voluntary agencies and international organizations involved with Refugee Programs.

Although future savings are not presently determinable, enhanced monitoring can reveal various organizations dispensing funds that are not in the best interest of U.S. foreign policy.

Background

The Bureau for Refugee Programs is surrounded by the complexities and policy considerations consciously weighted into foreign policy development to promote national interest. The FY 1983 budget for refugee programs is approximately \$419 million. The FY 1983 budget contains an allocation of \$67 million to replenish a transportation loan fund administered by the International Committee for Migration (ICM). Recent transportation loans range from \$200 to \$800 per refugee on an unsecured basis with no fixed term.

The relief assistance for refugees (including establishment and collection of transportation loans) is provided through voluntary agencies and international organizations and totalled approximately \$384 million of the \$419 million in FY 1983. The United States contributions approximate 30 percent of the funding level of each international refugee relief program.

In addition to the Department of State, other Federal agencies incur major costs after refugee admission and resettlement in the United States which is estimated to be \$1.1 billion for FY 1983.

Statistical information on the worldwide refugee situation is based largely on information from the international community, foreign governments (if willing), and U.S. diplomatic posts throughout the world and, accordingly, is subject to considerable variation.

Methodology

During the initial phase of this study, discussions held by Task Force personnel with the management personnel of the Bureau for Refugee Programs identified various issues. We also reviewed and analyzed various Bureau for Refugee Programs' budget information, U.S. Coordinator for Refugee Affairs' reports to the Congress, and audit reports supplied by the Department of State Inspector General.

Evaluation of the effectiveness of the loan program was not possible because there are no terms and conditions on these loans. In addition, removal of the collection responsibility to the Voluntary Agencies' (VOLAGs) further complicates the analysis process. Nevertheless, we used collections compared to loan balance as a measurement tool.

Findings

The actual transportation loan collection rate is 8.81 percent based on the total outstanding balance, as of June 30, 1982. There existed an outstanding receivable balance of \$165 million at that date. The loan collection rate of 8.81 percent is extremely low relative to private sector experience. For example, the collection rate for personal unsecured loans experienced by collection agencies is 21.7 percent. ^{1/}

Since loan collection is administered by various VOLAGs involved with resettling refugees, it is difficult to estimate collectibility.

No formal procedures to monitor and evaluate the effectiveness of VOLAGs and international organizations are in use by State's Refugee Bureau. (Recently, a U.S. payment to a United Nations Agency, to which the United States has contributed for many years, was withheld because the Agency had supported terrorist activities.)

^{1/} Per American Collection Association, a composite of 2,800 agencies.

Procedures to track secondary migration of refugees do not exist. Hence, loan collection becomes difficult due to inability to locate the refugees.

Accurate cost data on total refugee costs to the U.S. Government were not available.

Conclusions

In general, the nature of the loan instrument is inconsistent with standard, conventional loans and resembles more a grant with provisional payback. More specifically, the Task Force has concluded that:

- o the inability to enhance the collection rate of outstanding promissory notes results in annual additional appropriations;
- o the Bureau for Refugee Programs has not assessed the VOLAG's ability to collect loans;
- o without monitoring capabilities, management is limited in its ability to maximize resources utilization to the most effective VOLAGs and international organizations, and
- o the loan collection process is hampered by the absence of refugee tracking systems.

Recommendations

STATE 5-1: To rectify the loan collection problem.
The Secretary of State should direct:

- o establishment of the loan program on a more conventional basis, to wit, with fixed terms and security/guaranties;
- o an assessment of the VOLAGs' ability to increase loan collections;
- o establishment of a centrally managed collection activity within the Department;
- o regulations be changed to obtain sponsor guarantee for refugee promissory notes; and
- o application of funds for future transportation costs from loan receivable collections.

STATE 5-2: The Secretary of State should require the monitoring process be documented as to the effectiveness of voluntary agencies and international organizations. Specifically:

- o the Deputy Assistant Secretary for International Refugee Assistance and Relief should develop performance criteria for international organizations upon which efficiency evaluation could be compared, and
- o the Deputy Assistant Secretary for Refugee Resettlement should develop performance criteria upon which to evaluate the private voluntary agencies.

STATE 5-3: To develop tracking and integrated data base, the Secretary of State should request funding for the:

- o development of a computerized tracking system which will provide refugee address information (to respective VOLAGs), and for the
- o integration of Refugee Bureau information with that of other computer systems amongst varying agencies supporting refugees in order to provide complete cost data on refugees.

Savings and Impact Analysis

1. Rectify the Loan Collection Problem (see STATE 5-1).

The Task Force believes that increased loan collections will produce results similar to the private sectors. We have chosen to apply the 21.7 percent rate because it represents collection experience on loans which were in default before being given to the collection agency. The following data summarize the expected loan collections.

(\$ millions)

<u>Year</u>	<u>Beginning receivable balance</u>	<u>Increased collections rate</u>	<u>Collections</u>	<u>Ending balance</u>
1	\$165.00	12.89%	\$21.27	\$143.73
2	143.73	12.89	18.53	125.20
3	125.20	12.89	<u>16.14</u>	109.06
	Total collections:		<u>\$55.94</u>	

These collections represent cash accelerations. The interest savings can be calculated based on this cash acceleration.

<u>Year</u>	(\$ millions) cumulative cash <u>accelerations</u>	<u>Interest savings</u>
1	\$21.27	\$2.13
2	39.80	3.98
3	55.94	5.59
	Total savings	<u>\$11.70</u>

2. Improve the Monitoring Program (see STATE 5-2).

It is anticipated that the monitoring of the VOLAGs' will identify cases of inefficiencies which will be used as the basis for reducing contributions. However, since a reasonable level of reductions cannot be determined, no savings will be estimated.

3. Develop Tracking System and Integrated Data Base (see STATE 5-3).

An essential element of the Task Force recommendation is the development of a computerized tracking system and integrated data base for refugee affairs. Until the requirements for the system can be specified, it is not possible to accurately estimate the design development and operating costs. For analysis purposes we will use budgetary figures of \$0.5 million, \$1 million and \$1.5 millions as approximate cost figures.

In summary the estimated savings for this Issue are as follows:

<u>Recommendation</u>	<u>First year</u>	<u>Second year</u>	<u>Third year</u>	<u>Total</u>
Improved collections				
- cash acceleration	\$21.27	\$18.53	\$16.14	\$55.94
- interest savings	2.13	3.98	5.59	11.70
Monitoring VOLAGs	-	-	-	-
Development of integrated system	<u>(0.5)</u>	<u>(1.0)</u>	<u>(1.5)</u>	<u>(3.0)</u>
Total savings	<u>\$22.9</u>	<u>\$21.51</u>	<u>\$20.23</u>	<u>\$64.64</u>

Implementation

1. Agency Action

STATE 5-1: Assess the VOLAGs' ability to increase loan collections, or establish a centrally managed collection activity within State. Future transportation cost should be applied from loan receivable collections.

STATE 5-2: Require that the monitoring of VOLAGs and international organizations be documented.

STATE 5-3: Request sufficient funding for the development of a computerized tracking system and integrated information data bases. Approve funding for fully integrated computerized system.

2. Congressional Action

STATE 5-1: Require sponsor guarantee for refugee promissory notes.

II. ISSUE AND RECOMMENDATION SUMMARIES (CONT'D)

B. AGENCY FOR INTERNATIONAL DEVELOPMENT

OVERVIEW

The Agency for International Development (AID) was created by the Foreign Assistance Act of 1961. Its predecessor agencies operated under the Marshall Plan (1948 to 1952) and the Mutual Security Act (1953 to 1961). AID presently manages most of the foreign economic and development assistance programs of the U.S. Government. AID does not administer foreign military aid.

The avowed aim of AID is "to help people in the Third World acquire the knowledge and resources to build the economic, political and social institutions necessary for a better life." Another AID objective is to further the interests of U.S. foreign policy. This dual character is reflected in the types of assistance AID dispenses:

- o Development Assistance -- includes loans and grants in agriculture, rural development, nutrition, family planning, health, education and human resources, energy, and science and technology (FY 1983 -- \$1.3 billion); and
- o Economic Support Fund -- provides loans and grants to selected countries of special political and security interest to the U.S. (FY 1983 -- \$2.9 billion)

In addition, AID administers the Food for Peace Program (P.L. 480) with funds from the Department of Agriculture, provides disaster relief to foreign countries, and disburses multilateral assistance to international organizations.

AID currently has 5,386 employees, including 2,224 in Washington headquarters and 3,162 in field missions overseas. AID missions are in 71 countries in Africa, Asia, Latin America and the Caribbean, and the Near East.

The current AID personnel complement reflects a 70 percent decrease from the peak of 17,600 personnel that was attained in 1968. The AID staff has diminished in number primarily as a result of the ending of the conflict in Vietnam where AID was heavily involved in development and

relief assistance. Other factors that have worked to reduce the number of employees include a policy change that has restricted AID to a planning role and prohibited direct implementation of projects, and pressure from the Office of Management and Budget (OMB) to reduce staff as part of general budget cutting that has resulted in an understanding to reduce staff by an additional 150 per year over the next four years.

The following data depict AID's personnel headcount and funding in selected years over the past 20 years:

	<u>FY 1962</u>	<u>FY 1972</u>	<u>FY 1982</u>	<u>FY 1983</u>
Number of employees	14,800	12,800	5,386	5,137
Budget authority (\$ millions)	\$2,508	\$2,072	\$4,607	\$4,895

AID's total request of \$4.9 billion represents 0.61 percent of the Federal budget for FY 1983, and is \$288 million or 6.3 percent greater than the FY 1982 allocation. Fifty-three million dollars of the increase is earmarked for Latin America as part of the Caribbean Basin Initiative.

The Economic Support Fund is dispensed in two ways -- as a direct payment to the recipient or as an allocation to fund a specific development project that has been planned, approved, and contracted for by AID personnel.

In 1983, about \$1.8 billion or 62 percent of the total Economic Support Fund will be disbursed through direct payments. This amount includes the entire \$785 million to be sent to Israel and approximately \$350 million of the funds budgeted for Egypt. With the exception of the grant to Israel, most of the outright grants are disbursed through Commodity Import Programs, Economic Stabilization Grants and Balance of Payment Support.

The balance of AID assistance -- about \$2.5 billion in 1983 -- is allocated to specific development projects. This total includes all funds budgeted through the Development Assistance program. AID projects are meticulously planned by Agency personnel and carefully scrutinized by Congress. AID's operating expenses are primarily dedicated to planning these projects, overseeing their implementation, and reporting on them to Congress. In 1983, operating expenses were \$376 million, up \$45 million or 14 percent over 1982. Over the last five years, operating expenses have grown at a compound annual rate of 10 percent.

AID's disbursements are classified as either grants or (low interest rate) loans. Of the \$4.3 billion budgeted for FY 1983, approximately 67 percent is allocated to grants and 33 percent to loans. The loans typically carry an interest rate of 2 percent for the first ten years and 3 percent thereafter, usually with a term of 30 years and no principal repayments for ten years.

The challenges facing AID in the near term center on the difficulty of managing its extensive program with a shrinking staff. The pressure on AID is intensified by the need to respond quickly to unexpected new foreign policy initiatives, such as the Caribbean Basin Initiative or a proposed increase in aid to Pakistan. AID's difficulty is compounded by the onerous reporting requirements imposed by Congress.

II. ISSUE AND RECOMMENDATION SUMMARIES (CONT'D)

B. AGENCY FOR INTERNATIONAL DEVELOPMENT (CONT'D)

STATE 6: IMPROVEMENTS IN THE PROJECT
PLANNING, APPROVAL AND MONITORING

Issue and Savings

How can the management process at the Agency for International Development (AID) be improved so as to eliminate waste and overcontrol in the planning, approval, and monitoring of development projects?

The economies recommend in this Issue will reduce personnel time spent planning, approving, and monitoring AID projects. General changes in the management process we are recommending will eliminate at least 10 percent of personnel time currently dedicated to these functions, resulting in a savings of \$4.3 million in the first year. Specific changes we are recommending will eliminate another \$5.6 million in personnel costs in the first year. Total savings will amount to \$9.9 million in the first year, \$10.9 million in the second year and \$12.0 million in the third year.

Background

In FY 1983, AID will distribute \$4.3 billion in funds to the developing world through grants and low interest rate loans. \$2.5 billion of these funds will be disbursed to finance specific development projects, which are planned, approved, and controlled within a framework known as the Project Assistance Cycle. In 1978, independent consultants estimated that the following numbers of work-years were spent on three important planning, approval, and monitoring functions of the cycle:

Project development cycle	410 work-years
Annual budget submission	198 work-years
Congressional presentation	<u>205 work-years</u>
Total	813 work-years

AID officials in the Bureau for Management and in the Office for Financial Management estimated that total time spent on the three identified phases of the cycle has been reduced by 15 percent since 1978. Assuming the 15 percent reduction, we calculate that 691 work-years are today dedicated to planning, approval and monitoring.

AID's total operating budget of \$376 million for 1983 will be spent almost entirely to support AID's 5,300 (1983 average) employees, according to the Office of Financial Management. We have calculated the all-inclusive current cost of a work-year of service to be \$71,000. Multiplying the \$71,000 amount by the 691 work-year figure derived above, we have determined the current all-inclusive cost of planning and control to be \$49.06 million.

The Project Assistance Cycle includes only those AID activities directed toward planning a project and receiving Congressional approval for the disbursement of funds. It should be emphasized that the majority of AID's effort is invested in other, primarily implementation, activities. Since AID implements its programs in the less developed countries throughout the world, it was impractical for the Task Force to evaluate implementation procedures and recommend cost savings with respect to them. The Task Force therefore concentrated on finding cost savings in the Project Assistance Cycle, which could be effectively monitored in Washington. Furthermore, it was believed that the Project Assistance Cycle, as the focus of planning, oversight, and other activities, would prove to be the most promising area for cost cutting.

Despite improvements made in recent years, the Project Assistance Cycle remains a sluggish mechanism. Some of the reasons for its persistent cumbersomeness include:

- o the pressures of Congressional mandates and oversight;
- o the impingement of foreign policy and strategic considerations;
- o the bureaucratic inadequacies and socio-economic weaknesses of beneficiary countries; and
- o the bureaucratic inertia within AID itself.

Methodology

Interviews were carried out with senior AID executives in Washington and in the field. An extensive round of meetings were held with AID personnel in Egypt to explore the problems of one of AID's largest and most complicated field missions.

A review of available, appropriate AID documents was made. Various AID internal memoranda, reports, and letters were inspected. Historical personnel and cost data were analyzed.

Financial and personnel information was gathered from other development agencies with project functions comparable to AID's. Senior executives of outside agencies, including CARE, the YMCA, United Nations Fund for Population Activities (UNFPA) and a selection of smaller agencies were interviewed regarding their procedures and costs. Foreign assistance programs of other donor countries, such as Canada and Sweden, were also explored.

Findings

AID's procedures for planning, approving, and controlling development projects are not as efficient as those of other major development agencies.

AID's relative inefficiency can be demonstrated by comparing AID to other major development agencies along two broad measures:

- o Operating expenses as a percentage of total disbursements:
- o Average elapsed time to develop and approve a project.

<u>Agency</u>	<u>Size of total program (\$ millions)</u>	<u>Operating expenses as a % of total disbursements</u>	<u>Average elapsed time to plan and approve</u>
CARE	\$ 273.0	7.0%	9 months
Meals for Millions	3.6	4.8	9 months
Partnership for Productivity	2.5	10.0	9 months
Technoserve	2.6	13.5	4 months
AID	2,500.0	13.5	16.7 months

We have compared AID to several international organizations involved principally in development and human welfare work, primarily Private Volunteer Organizations (PVOs). Our results show that AID compares unfavorably with most of these organizations, with respect to the measures specified above.

There are two possible explanations for AID's relative inefficiency:

- o AID requires an excessive amount of scrutiny and documentation of its projects, and
- o many other development agencies are more vertically integrated than AID.

Outside agencies provide other advantages. In addition to their economic advantages, outside agencies are often preferable channels of disbursement because of their ability to reach geographical areas where AID has no presence. PVOs have also shown themselves willing to handle politically sensitive projects that AID would rather avoid. In addition, host governments would like to see PVOs strengthened and expanded.

AID is less efficient than other national donor agencies. Our research also shows AID to be less efficient than other national donor agencies. The Swedish International Development Authority (SIDA), for example, is able to disburse \$1,025,000 per employee as compared to AID's \$416,667 per employee. If we assume that the two programs are roughly equivalent in per dollar effectiveness, AID is apparently achieving far less labor productivity than SIDA. (Labor productivity used here rather than operating expense measures due to lack of expense data from SIDA.)

Operating expenses are growing as a percent of allocations. Not only are AID operating expenses high in relation to other development agencies, they are growing over time as a percentage of allocations. Operating expenses have grown from 6.4 percent of allocations in 1977 to 8.0 percent in 1983 or a 25 percent increase.

Centralization causes delays and excess costs. The centralization of budgetary and decision-making authority of AID in Washington (AID/W) is reported by officials in the Bureau for Program and Policy Coordination and the Bureau for Management to be a cause of program delay and excess cost. These officials report that an excessive amount of documentation and unconstructive review of field operations occurs in Washington as a result of a reporting and decision-making structure that concentrates too much authority in the central office. These views are supported by the outside consultants' study, which found that the greater the degree of Bureau centralization, the more time required to develop and approve project plans. The more centralized Bureaus have not shown superior results, despite their greater efforts.

The deobligation/reobligation procedure is inefficient. A major source of inefficiency within AID is the present procedure for deobligation and reobligation of funds which requires that funds unspent on a completed or terminated project be deobligated (not used on other projects without approval by Congress). Until 1977, AID missions in the field enjoyed the management flexibility to deobligate funds for projects which failed to meet objectives and to reobligate those funds to successful or fast-moving projects which could readily absorb the additional support.

In 1977, Congress decided that the reobligation authority gave too much latitude to AID and disallowed the procedure. Consequently, deobligated funds must now be returned to the U.S. Treasury.

The present deobligation/reobligation procedure is costly. Approximately \$60 million in AID program funds were deobligated in FY 1982. Before that \$60 million can be redirected to other AID projects, it must be requested through the Project Assistance Cycle. That \$60 million will be approximately 7.8 percent of FY 1983 project-oriented new program fund requests of \$763 million. If AID were allowed to escape the Cycle for the \$60 million and reobligate the funds on its own authority to other projects which have already been approved, a theoretical 7.8 percent of staff time dedicated to planning could be eliminated. With staff planning time put at 348 work-years (derived by taking the independent consultants estimate of Project Development Cycle work years of 410 and reducing by 15 percent to account for recent improvements), the savings would equal 27 work-years. (Savings in the budget submission and Congressional cycle are not claimed since it is assumed that reobligated funds would still be reported under these phases.)

Specific evidence of this inefficiency was seen during the field visit to Egypt. Recently, AID officials have publicly requested permission to reprogram \$300 million in obligated funds for "turkey" projects in Egypt (Washington Post, January 27, 1983).

Returning deobligation/reobligation authority to AID would provide the Agency with an excellent management tool that it now lacks. AID administrators would have incentive to terminate projects that are not succeeding and to redirect funds to those that are, and State will receive fewer complaints from host countries and save operating costs in the process.

Congressional oversight cost AID \$12.78 million in 1982. The high level of Congressional oversight of AID is costly to the Agency in three ways:

- o time spent reporting to Congressional Committees: Senate Foreign Relations Committee, House Foreign Affairs Committee, and Foreign Operations Subcommittees of the House and Senate;
- o time spent answering written queries from congressmen and senators; and
- o time spent preparing the annual Congressional Presentation.

AID sends approximately 94 reports per year to Congress, not including the massive six volume annual Congressional Presentation. In addition, AID personnel spend approximately six work-years on correspondence. The cost is estimated to total \$12.78 million per year.

AID officials at all levels called this burden excessive and claimed that much of it was self-imposed. The form and length of the Congressional Presentation, for example, is determined by AID itself, and not specified by Congress.

The annual budget submission is redundant and wasteful. AID is required to submit all projects for annual budget review by the Office of Management and Budget (OMB) even though most projects receive multi-year authorization. In the years after the initial appropriation, this submission is often a perfunctory exercise. AID will submit an updated version of the previous year's submission and OMB will generally give its approval. This mechanical process consumes a significant amount of staff time without adding to the effectiveness of Agency control.

The redundancy and waste in the current procedure for annual budget submission could be largely eliminated if AID were allowed to move from annual budget authorization to two-year authorization.

The process is inhibiting and counterproductive. Management inefficiency and Congressional and bureaucratic overcontrol are costly not only in terms of dollars, but also in terms of effectiveness.

Conclusions

Outside agencies are preferred channels for AID funds. AID is relatively less efficient at administering development projects than are other major development agencies.

If AID were to channel more of its funds through outside agencies -- using the mechanism of block grants -- it would be able to provide development assistance more efficiently than it does through its current practice of dispensing individual project grants. A block grant in this context would be a lump sum allocation to the outside agency in return for an accounting of how the funds will be spent.

Increased decentralization is needed. Funds that do go through the AID network can be more efficiently administered if the system is more decentralized.

This conclusion is backed up by three of the Task Force's findings:

- o consultants have determined that the less centralized regional bureaus in AID spent significantly less personnel time planning and monitoring projects without suffering a loss in effectiveness;
- o there is a widespread belief among AID/W personnel that they spend too much time on paperwork and "red tape" and that much of this time could be eliminated if more authority were given to field mission directors; and
- o control procedures have been simplified in the last four years but AID/W personnel -- who carry out most of the control functions -- have remained at nearly the same high percentage of total AID personnel.

Returning deobligation/reobligation authority to AID will cut costs. Planning costs can be cut 7.8 percent and effectiveness improved if deobligation/reobligation authority is substantially returned to AID and AID allows its field mission directors wide latitude to deobligate and reobligate funds.

The Task Force believes that the appropriate Congressional oversight is at the level of country/regional development and not at the level of specific project.

A return of deobligation/reobligation authority to AID will be an effective measure only if AID does not lose any budgetary authority in the process.

The work-years spent responding to Congressional demands are excessive. Officials in AID's Bureau of Legislative Affairs believe that a reasonable amount of oversight can be achieved with a cut of 15 percent in work-years spent responding to Congress.

Changes effected over the last three years have cut 15 percent from total time spent on the Congressional Presentation and most AID officials believe that the quality of AID reporting has improved. With this success behind them, AID personnel have reason to believe that further cuts are possible in what is still a 180 work-year reporting procedure.

Moving to a two-year annual budget submission cycle would eliminate needless paperwork. The Annual Budget Submission consumed 198 work-years of staff time in 1978, according to the consultants' report. If we assume that this process, like other aspects of the Project Assistance Cycle, has been cut by 15 percent, we can calculate that 168 work-years are still dedicated to it. Moving to a two-year Annual Budget Submission cycle for multi-year projects would cut personnel time spent on the function still further. Half of the repetitive and time-consuming paperwork for multi-year projects would be eliminated.

Recommendations

STATE 6-1: AID should increase the dollar value of block grants. The Agency Director should channel more AID funds through outside development agencies through the mechanism of block grants.

At present, the Agency is disbursing \$182 million, or 13 percent of total Development Assistance allocations through PVOs. Congress has ordered that at least 12 percent of disbursements continue to go through these agencies. The Agency Director should set a higher target level -- for example, 15 percent by 1984. Raised targets should be set in future years as PVOs demonstrate the ability to make good use of the funds.

As AID increases its allocations to PVOs, it should explore the possibility of making multilateral/bilateral (Multi/Bi) grants. A Multi/Bi grant is a grant with a specific designation as to how and/or where a portion of the funding is to be spent.

STATE 6-2: The Agency Director should request Congressional action to return deobligation/reobligation authority to AID. AID should provide field mission directors with latitude to cancel failing projects and reallocate funds committed to them to other projects within their mission.

The legislative action that returns this authority to AID must provide that exercising deobligation/reobligation authority will not lower overall budgetary authority.

STATE 6-3: The Agency Director should empower a panel of AID officers to study ways of further decentralizing authority. The stated goal of the study should be to reduce AID/Washington staff as a percentage of total AID personnel.

STATE 6-4: The Agency Director should instruct members of his/her staff to consult with Congressional staffers about ways to reduce AID reporting time by 15 percent. Areas to target for cuts would include: length of the Congressional Presentation, number of reports AID sends to Congress, volume of correspondence between AID and Congress, and number of Congressional committee meetings AID staffers are required to attend.

STATE 6-5: The Agency should move to a two-year budget submission cycle. The Agency Director should work with OMB and Congressional leaders to change Congress's policy of reviewing all budget requests annually. The Director should lobby for a two-year appropriation cycle for AID budget requests. Under the two-year cycle, all AID appropriations would be made and reviewed by OMB and Congress every other year rather than annually.

Savings and Impact Analysis

The recommendations outlined above will result in a projected \$9.9 million in savings in the first year of implementation. \$5.6 million of this total are savings the Task Force estimates will result from the specific changes recommended. The remaining \$4.3 million are potential savings we believe will flow from the general changes recommended.

Specific savings would result from the following measures:

- o Return deobligation/reobligation authority to mission directors (see STATE 6-2). We estimate that this change will result in a savings of 7.8 percent, or 27 work-years, of planning time. At \$71,000 per work-year, this savings amounts to \$1.9 million in the first year.
- o Cut the level of Congressional reporting (see STATE 6-4). AID officials believe Congressional reporting could be cut by 15 percent and still be adequate to meet Congressional oversight needs. The Task Force agrees with this estimate. The savings in annual costs would be 27 work-years, or \$1.9 million per year.

- o Move to a two-year budget submission cycle (see STATE 6-5). A two-year Budget Submission cycle will entail a full justification of each AID project in its initial year, followed by bi-annual rejustifications of the project over the course of the project life. The current procedure requires annual rejustification of already-approved projects. Although these annual rejustifications account for a minority of the time currently spent on the annual budget submission, the personnel time they require is still significant. If the annual rejustifications were replaced by a bi-annual procedure as suggested, the Task Force estimates, based on the judgments of officials in the office of Legislative Affairs and the Office of Financial Managements, that 15 percent of the current work-years expended on the ABS would be eliminated. The savings in annual costs would amount to \$1.8 million per year.

Savings would be realized through the reduction of personnel, in both Washington and the field missions. The Task Force is not prepared to recommend specific Bureaus where these cuts should fall, but believes that a goal of cutting personnel dedicated to planning, approving, and monitoring by 10 percent in conjunction with these general charges is a realizable one. With the cost of these activities projected to be \$43.4 million, after the specific cost savings of \$5.6 million indicated above have been realized, first year savings of \$4.3 million are indicated.

General areas of savings will include:

- o More funds disbursed through block grants (see STATE 6-1). These lump-sum allocations should be made to outside development agencies which operate more efficiently than AID.
- o Greater decentralization of authority (see STATE 6-3). Implementation of this measure will permit a reduction in AID/W staff without necessitating an equivalent increase in foreign-based personnel. In addition, it will result in a reduction in expenses for travel and meetings.

Savings listed above are summarized below:

	(\$ millions)		
	<u>Year 1</u>	<u>Year 2</u>	<u>Year 3</u>
STATE 6-2	1.9	2.1	2.3
STATE 6-4	1.9	2.1	2.3
STATE 6-5	1.8	2.0	2.2
STATE 6-1, 3	<u>4.3</u>	<u>4.7</u>	<u>5.2</u>
Total	<u>\$9.9</u>	<u>\$10.9</u>	<u>\$12.0</u>

Implementation

1. Agency Authority

STATE 6-1: The Agency Director must establish a higher target for PVO block grants as a percentage of total AID allocations. As a first cut, a target of 15 percent of Development Assistance funds by 1985 should be mandated. The Office of Private and Voluntary Cooperation should be made into a separate bureau and strengthened so that it may become the focal point for the increased PVO effort.

STATE 6-2: The Agency Director must select a panel to study ways AID can further decentralize authority. The panel should be composed equally of experienced personnel from AID/W and the field. The panel should be given six months to write its report and required to present concrete recommendations at the end of its work.

STATE 6-4: The Agency Director should order that a series of meetings be set up between officials of AID's Bureau of Legislative Affairs and staff members of the House and Senate Appropriations and Foreign Affairs Committees. At these meetings AID officials will explain the need to reduce Congressional reporting as a cost-cutting measure. Congressional suggestions should be solicited and concerns addressed. Once an appropriate amount of consultation has taken place, the Agency Director should order cuts in the Congressional Presentation and in other Congressional reporting functions with the aim of reducing time spent on these functions by 15 percent.

2. Presidential Authority

STATE 6-5: The President must issue a directive to OMB instructing that Agency to work with AID to persuade Congress to accept the reobligation authority and a two-year Budget Submission cycle. Once the two-year cycle is accepted by Congress, OMB will be required to change its own procedures with respect to AID budget requests to reflect the new system.

3. Congressional Action

STATE 6-2: Congress should be requested to enact legislation to provide AID with authority to deobligate and reobligate funds. AID should be allowed to reobligate to already-approved projects, so long as the reobligation does not exceed the original obligation amount and is in the same geographic or functional area as the deobligated project.

STATE 6-5: Congress should pass legislation that would allow AID to present projects for its approval biannually instead of annually, as is now the practice.

II. ISSUE AND RECOMMENDATION SUMMARIES (CONT'D)

B. AGENCY FOR INTERNATIONAL DEVELOPMENT (CONT'D)

STATE 7: INTEREST RATES ON AID LOANS

Issue and Savings

Do the interest rates on new Agency for International Development (AID) loans provide an opportunity for additional revenues?

Implementation of our Task Force recommendations reduces government costs due to hidden foreign aid by as much as \$60.0 million for each year of new AID loans and, if started in FY 1983, the cumulative effect in three years alone would be \$360.0 million in additional revenues.

Background

1. AID Made Over \$1.4 Billion in Loans in FY 1982

From the outset, U.S. foreign economic assistance has been provided through grants and loans. The level of loan authorizations has risen over time and is currently channeled through three separate funds administered by AID:

	<u>FY 1982</u>
Development Assistance (DA)	\$ 398,162,000 AID
Economic Support Fund (ESF)	365,690,000 AID
P.L. 480 (Food for Peace)	719,900,000 AGR
	<u>\$1,483,752,000</u>

(These amounts are presented in AID reports and are included in several Budget Appendix categories.)

2. Maturity of Development Assistance Loans Governed By Per Capita Gross National Product (GNP) of Recipient Country

Under the Foreign Assistance and Related Programs Appropriations Act (FAA) of 1982, loans to less developed countries (LDCs) with a per capita GNP greater than \$730 but less than \$1,180 are repayable within 25 years; loans to countries with per capita GNP equal to or greater than \$1,180 are repayable within 20 years.

Methodology

The Task Force sought to determine historical trends of AID loan terms and compare these with the borrowing cost of the U.S. Government. In doing so, the Task Force re-researched the legislative history of AID loans, determined the current terms of interest of international development banks, and conducted interviews with AID personnel.

Findings

U.S. loan terms show little change. It is U.S. policy for loan terms to be determined by an LDC's income level and not by the type of project being supported. A social infrastructure project will be funded on the same terms as a project that generates revenue.

In 1979, Congress established loan maturities based on the GNP of LDCs, using cutoffs patterned after those used by the World Bank's International Development Agency (IDA).

It is AID policy to assess annually the individual country situation to identify those countries that can service loans on intermediate terms -- terms harder than the authorized minimum. This policy applies to both development assistance and economic support fund loans. AID officials state that only a few countries have been offered loans on harder than standard development terms.

As for interest rates, the United States has not changed the minimum loan rate shown below since 1968:

MIMINUM INTEREST RATE (%)

<u>FAA of</u>	<u>Principal grace period (usually 10 years)</u>	<u>Period thereafter (usually 30 years)</u>
1963	0.75%	2.0%
1964	1.00	2.5
1967	2.00	2.5
1968	2.00	3.0

Multilateral development banks have two loan windows -- AID has only one. The multilateral development banks (MDBs) have both a hard (capital) window, which provides loans on near-market terms to higher income developing countries, and a soft window, which provides loans on concessional terms to lower income LDCs or, in some cases, for projects with a strong social benefit in higher income LDCs. The MDBs base the interest rate for their hard window loans

on the cost of funds basis. The current interest rates charged on loans for each of these MDBs is shown below:

	<u>% INTEREST (GRACE PERIOD/THEREAFTER)</u>	
	<u>Hard window</u>	<u>Soft window</u>
IDB - Inter-American Development Bank	10.5%/10.5%	1%/2% to 4%
IBRD - World Bank	11.43/11.43	0/0
ADB - Asian Development Bank	11.0/11.0	0/0
AFDB - African Development Bank	9.5/9.5	0/0

AID, on the other hand, does not use a cost of funds approach when determining its loan terms.

Interest on AID loans has not reflected the cost of borrowing by the U.S. Government. The interest rate on U.S. Official Development Assistance (ODA) loans has borne no relationship to the Treasury's cost of borrowing. Our analysis reveals that as the annual interest rate on Treasury bonds (marketable issue) has risen from 3.762 percent in 1970 to 9.321 percent in 1981 (a 148 percent increase), the average interest rate on ODA loans has decreased from 2.6 percent to 2.5 percent for the same period.

Conclusions

Interest on ODA loans has not kept pace with the cost of funds and represents hidden foreign aid. Whereas the interest rate on the ODA loan represented 69 percent of the Treasury bond rate in 1970, it represented only 27 percent of the rate in 1981. The differential between cost of U.S. borrowings and interest rate to LDC represents hidden foreign aid.

There are no uniform loan terms for development assistance, economic support and P.L. 480 funds. AID personnel in the working group of the Food Aid Subcommittee of the Development Coordination Committee are currently drafting a document which would standardize criteria by using the same AID eligibility criteria currently used for DA loans for P.L. 480 Title I Loan Terms for use in the interagency negotiations. However, there is no assurance that this proposal will be adopted due to the conflict of interagency foreign policy objectives.

The State Department sets the terms for ESF loans with advice from AID personnel. Although the current practice is to use maturity criteria identical to DA loans when possible, State has not established a set of guidelines so that its flexibility is maintained.

Recommendations

STATE 7-1: Establish a "base" lending rate for all ODA loans based upon cost of funds to the U.S. Government. This base rate may be calculated on a periodic basis (annually perhaps): (1) as a percentage of the interest on Treasury bonds, or (2) as a percentage of the interest on all outstanding Treasury debt, or (3) as a percentage of the interest rate yield on the most recent Treasury bond auction. The objective in choosing the most appropriate Treasury rate is to match the borrowing cost to the interest rate on the loan. The determination of an appropriate percentage of the borrowing rate should be fixed after careful consideration of Agency objectives and historical percentages. Our analysis reveals that ODA interest rates ranged from 77 percent of Treasury bond interest rates in 1971 to 27 percent in 1981.

STATE 7-2: After establishing a minimum base rate, quantitative (objective) criteria can be applied to borrowing countries in order to determine the appropriate interest rate and maturity. Objective criteria based on per capita GNP are already available from the MDBs. The International Bank for Reconstruction and Development (IBRD) publishes per capita GNP data annually to determine IDA eligibility. This or other data available to AID could be used to determine the appropriate "cutoff" levels in per capita GNP. Once these cutoff levels are determined, the appropriate interest rate and maturity for loans can be applied.

STATE 7-3: Additional principal takedowns on loans should not be granted to offset increased interest rates on loans. AID policy personnel should be cognizant that borrowers may request additional loan principal to pay the higher interest rates. Careful analysis should reveal this attempt to circumvent the U.S. objective. We recommend that additional borrowings to pay the higher interest rates be denied.

Savings and Impact Analysis

Savings could be \$60.0 million in the first year and \$360.0 million after three years. The Task Force has determined that, if the relationship between the average interest rates on LDC loans of 2.5 percent and on U.S.

borrowing costs of 3.6 percent were maintained at the 1968 level (when Congress last changed the minimum rate) for new loans created in 1981, the interest rate on the 1981 loans would be 6.5 percent as the Treasury rate was 9.3 percent in 1981. Therefore, an additional \$60 million in interest income would be received in each year of the loan period for those loans.

Since most loans are of, at least, a 40-year length, the cost impact on the U.S. taxpayer is substantial in each budget year. For example, the cumulative effect of this change would be \$360 million for a three-year period.

Further, to the extent that the average interest rate on ODA loans were raised one percent, the incremental interest earned on new ODA loans would be \$15 million in the first year and \$90 million for the three years. This analysis assumes that ODA loans remain at the 1982 level of \$1.5 billion for each of the next three years ($\$1,500,000,000 \times .01 = \$15,000,000$ each year).

The following data illustrate how these savings are achievable for each 1 percent increase in interest rate. If the full 4 percent increase to 6.5 percent was in effect, the savings would be four times each category.:

(\$ millions)

Loan Year	<u>INTEREST EARNED DURING THE YEAR</u>			
	<u>Year 1</u>	<u>Year 2</u>	<u>Year 3</u>	<u>Total</u>
First year	\$15	\$ 15	\$ 15	\$ 45
Second year	-	15	15	30
Third year	-	-	15	15
Subtotal @ 1%	<u>15</u>	<u>30</u>	<u>45</u>	<u>90</u>
Total @ 4% increase	<u>x 4</u> <u>\$60</u>	<u>x 4</u> <u>\$120</u>	<u>x 4</u> <u>\$180</u>	<u>x 4</u> <u>\$360</u>

Implementation

1. Agency Authority -- AID

STATE 7-1: The Administrator of AID must direct AID officers to establish a base lending rate (pursuant to F.1) for (DA) loans. Economic Support Fund and P.L. 480 loans will require the formation of an interagency task force to determine appropriate base rates. It is to be hoped that the same base rate will apply to all three funds.

STATE 7-2: The Administrator of AID must direct his/her staff to formulate a uniform set of criteria (presumably per capita GNP) to determine a borrowing country's ability to pay, to establish cutoff categories, and to formulate a range of interest rates and maturities for each category.

2. Congressional Authority

Congressional action could be invoked and loan terms legislated each year, but necessary changes can be accomplished through Agency authority.

0

II. ISSUE AND RECOMMENDATION SUMMARIES (CONT'D)

B. AGENCY FOR INTERNATIONAL DEVELOPMENT (CONT'D)

STATE 8: FOREIGN SERVICE ROTATION POLICY

Issue and Savings

Can the Foreign Service rotation policy be changed to reduce personnel transfer costs and make the performance of the officers more effective?

By enforcing the policy of four-year minimum assignments, annual transfer cost savings of \$1.6 million could be achieved, based on FY 1982 outlays, and project oversight and implementation would be improved. Three-year savings are estimated at \$5.3 million.

While AID is gradually closing the gap between announced and actual tour lengths, we believe that presentation of this Issue in this Report may accelerate the process and produce savings within a shorter time frame.

Background

1. Nature of Foreign Service

The Foreign Service of AID and the Department of State comprises a unique cadre of career professionals who are prepared to accept the challenge of sequential assignments in countries around the world. In each foreign post, they make their home, acquaint themselves with the country and its officials, and carry out their assigned responsibilities.

2. AID Service Is in Hardship Posts

As compared to that of State, AID Foreign Service is chiefly in missions classified as hardship posts. U.S. employees at such posts receive modest extra compensation in the way of a salary differential and are eligible for travel at Government expense to designated rest and relaxation (R&R) locations.

3. AID Rotation Policy

AID's rotation policy has been for Foreign Service officers to serve four years at a post, with an interval for home leave (20 consecutive working days) at the end of the first two years.

After four years at a post, the officer is eligible for transfer, presumably to a different region. Travel there will frequently be via the United States for briefing and orientation. After eight years overseas, there is a strong presumption of a Washington assignment.

4. Rules Governing Travel and Allowances

In general, AID follows State rules regarding Foreign Service travel, allowances, salary differentials for hardship posts, and eligibility for R&R travel at government expense. Whereas State makes a general policy of shipping the household furniture of officers transferred overseas, AID ships certain personal effects, but generally places overseas personnel in furnished quarters.

AID and State Foreign Service personnel availing themselves of R&R opportunities must use annual leave and pay the first \$100 of travel costs themselves. The remainder is borne by the U.S. Government. Per diem is not included. Those serving in maximum hardship posts (carrying a 20 to 25 percent salary differential) are eligible for R&R travel to the nearest point of entry into the United States.

Methodology

The Task Force conducted interviews with officials in AID's Offices of Personnel Management and Financial Management and with Personnel Officers of the Department of State. It reviewed AID analyses and projections, cited in the text, of the pattern of Foreign Service rotation and an AID operating expense budget summary of September 1982.

Findings

Four-year tour of duty not enforced. In practice, the four-year assignment rule has not been observed. AID analyses and projections done in July 1981, and again in October 1982, show the average tour of duty at a foreign post to be 32 to 33 months in 1980, rising to 35 months in 1981 and averaging 36 to 38 months in 1982.

Personnel and transfer data. As of September 30, 1982, AID had 3,405 full-time U.S. employees, of which 1,462 were assigned overseas. In FY 1981, AID spent \$1,539,000 on travel associated with post assignments and \$4,874,700 on freight charges associated with post assignments, for a total of \$6,413,700. As of September 1982, the combined total for travel and freight had risen to \$6,505,700.

AID intends to tighten rotation rules. According to AID officials, it is the intention of the Agency to make stricter application in the future of the four-year rule for Foreign Service assignments, enforcing it for all posts where the hardship differential is less than 25 percent.

Statistical analyses project longer assignments in the future. Based on samplings drawn from the Foreign Service assignment system, AID has recently performed analyses which project a rising trendline in the average number of months spent by Foreign Service officers at each post of assignment. The projected data assume an average of 40 to 41 months in 1983. AID personnel officials hope to be able to fulfill this projected goal. These same analyses project the possibility of an average tour of duty of 46 to 47 months in 1984, conceivably reaching 48 months in 1986.

Were AID to pursue a policy of five-year tours of duty beginning in 1983, the analyses project a sharp uptrend in average number of months per assignment, increasing at the rate of four months per year to reach an average of 60-month assignments toward the end of 1987.

Conclusions

Longer tours of duty at a post present opportunities for modest cost savings to AID. An increase in average time on post from 36 months (the average length of tour in 1982) to 48 months (projected for 1986) would save approximately \$1.6 million in personnel travel and freight charges, based on the FY 1982 level of expenditures of \$6.5 million.

The figure of \$1.6 million is arrived at by assuming that if the annual transfer costs of \$6.5 million which would obtain each year during a three-year (36-month) period were stretched out over a four-year (48-month) period, there would be a saving over the four years of \$6.5 million (25 percent), or \$1.6 million on an annual basis.

Assuming that 40 months were to become the average length of tour during 1983, as projected in AID's analyses, the costs associated with 40 months would be distributed

over 48 months, with a saving of 16 percent, or \$1,075,000 on an annual basis (using FY 1982 expenditures).

Should AID adopt a policy of five-year average length of tour, it is estimated that travel and transfer costs would be reduced by approximately 40 percent, as compared with a 36-month average length of tour. The resulting savings to AID would be \$2.6 million on an annual basis. (The costs associated with three years at \$6.5 million per year would be \$19.5 million. If these same costs were spread over five years, the total spent per year would be \$3.9 million, a saving of \$2.6 million per year.)

Hardship posts pose a morale problem. Most AID missions are classified as hardship posts. Longer tours of duty pose health and morale problems and increase the prospect of growing "stale" on the job. Thus, the more highly qualified and experienced Foreign Service officers may well become restive with longer assignments and be lured away from AID by higher salaries in the private sector or in international organizations.

Rapid rotation reduces project oversight. On the other hand, under the present rotation system there is a tendency for Foreign Service officers participating in the design and approval of new projects to be transferred before these projects are implemented. Not only may the projects suffer from inadequate oversight, but the officers, once transferred, are no longer held responsible for the success or failure of projects which they initiated.

Recommendations

STATE 8-1: The Administrator should take immediate steps to enforce the four-year length of tour (two years plus home leave and return), making exceptions only on compassionate grounds or for reasons relating to program support.

The Administrator should instruct the Office of Personnel to undertake an analysis of the extent to which greater emphasis can be given to the rotation of Foreign Service officers to posts within the same region. Regional postings would make for some saving in travel and freight costs and enhance the officers' qualifications as language and area specialists and as experts in the development problems characteristic of particular regions.

The Administrator should also instruct the Office of Personnel to undertake an analysis of the feasibility of extending the four-year average tour of duty to a five-year average tour, broken by home leave.

The Administrator should further instruct the Office of Personnel that in making its analyses it should weigh the gains, in terms of direct financial savings and improved project oversight, against the possible losses in terms of deteriorating Foreign Service morale and resignations.

Savings and Impact Analysis

It is estimated that adherence to a four-year length of tour, as compared with the recent 36-month average for 1982, should reduce by approximately 25 percent, or \$1.6 million (based on FY 1982 outlays of \$6.5 million) the cost to the Government resulting from overseas travel, the travel status of personnel, and the shipment of effects associated with transfers. Using a 10 percent inflation factor the savings would be:

<u>Year 1</u>	<u>Year 2</u>	<u>Year 3</u>	<u>Total</u>
\$1.6	\$1.8	\$1.9	\$5.3

Implementation

The Administrator has authority to implement the recommendations cited above.

Additional Information

This Issue has been referred to State and United States Information Agency (USIA) for their review and potential applicability within their areas of responsibility.

II. ISSUE AND RECOMMENDATION SUMMARIES (CONT'D)

B. AGENCY FOR INTERNATIONAL DEVELOPMENT (CONT'D)

STATE 9: CARGO PREFERENCE

Issue and Savings

What is the additional cost associated with the requirement that U.S. flag ships be used to transport at least 50 percent of commodities made available to needy countries through the AID-financed commodity import programs, the Food for Peace program (P.L. 480, Title II), and U.S.-monitored shipments to Israel?

If the cargo preference requirement were removed from AID-sponsored shipments, first-year savings of over \$35.8 million could be achieved. The total saving over three years would be \$118.5 million. The savings would not only allow for purchasing and shipping more food to recipient countries, without increasing program costs, they would also eliminate dissatisfaction in the recipient country and among U.S. farmers with the shortfall in the volume of food and grain exported.

Background

1. Legislative Requirements

The Merchant Marine Act of 1936, as amended, requires that U.S. flag ships carry at least 50 percent of the commodities shipped under the U.S. development assistance and Food for Peace programs. Since U.S. freight rates on bulk cargo vessels (tramps), in particular, exceed those charged by foreign flag tramps, the incremental cost to the U.S. Government is considerable. The implementation of the Congressional mandate affects the following categories of U.S. aid shipments:

- o AID-financed commodities -- project and non-project,
- o commodities ("Food for Peace") shipped under P.L. 480, Title II, and
- o shipments to Israel on a global cash grant basis.

2. Tonnage Affected

Total quantities shipped in 1981 amounted to 4,090,000 metric tons at a cost of \$373.6 million (see Table II-6). Approximately 59 percent of tonnage is shipped by tramps as opposed to approximately 41 percent by liners. (AID can monitor only the part of the grant to Israel that involves the use of tramps for bulk shipments, 65 percent of which is grain and subject to preferential rates provided for in a side agreement.)

(See Table II-7 for AID shipments by tonnage, use of U.S. and foreign flag ships, and resulting costs for calendar years 1980 and 1981.)

[Tables II-6 and II-7 on following pages]

Table II-6CONSOLIDATION OF 1981 SHIPMENTS

	<u>Tramps</u>		<u>Liners</u>	
	<u>Tonnage</u>	<u>Cost (\$ millions)</u>	<u>Tonnage</u>	<u>Cost (\$ millions)</u>
AID- Financed	882,000	\$ 48.7	355,000	\$ 64.2
P.L. 480, Title II	221,000	19.7	1,233,000	193.0
To Israel (Cash transfer)	<u>1,399,000</u>	<u>48.0</u>	<u>-</u>	<u>-</u>
	<u>2,502,000</u>	<u>\$116.4</u>	<u>1,588,000</u>	<u>\$257.2</u>
Total tons shipped		4,090,000		
Total cost shipments		\$373,600,000		

Source: Data presented in Appendix.

Table II-7AID SHIPMENTS ABROAD1. AID-Financed Commodities; Project and Non-Project

(Calendar year)	<u>Tramps</u> (bulk cargoes)		<u>Liners</u>	
	<u>Tonnage</u>	<u>Cost</u> (\$ millions)	<u>Tonnage</u>	<u>Cost</u> \$ mil.
<u>1980</u>				
U.S. ships	401,000	\$33.3	273,000	\$ 43.8
Foreign ships	484,000	18.7	156,000	20.4
<u>1981</u>				
U.S. ships	240,000	\$20.5	235,000	\$ 44.9
Foreign ships	642,000	28.2	120,000	19.3

2. P.L. 480, Title II1980

U.S. ships	24,000	\$ 3.67	826,000	\$122.5
Foreign ships	347,000	22.63	446,000	64.0

1981

U.S. ships	38,000	\$ 5.60	798,000	\$125.0
Foreign ships	183,000	14.19	435,000	68.0

3. To Israel (cash transfer)1980

U.S. ships	396,000	\$25.0	None	
Foreign ships	1,380,000	31.7	None	

1981

U.S. ships	290,000	\$22.4	None	
Foreign ships	1,109,000	25.6	None	

Source: AID Office of Commodity Management.

Methodology

Meetings were held with officials of the Office of Commodity Management and its subordinate Transportation Support Division. A relevant General Accounting Office (GAO) report^{1/} was reviewed. Finally, an attempt was made, with the assistance of AID's Office of Commodity Management, to determine the total savings possible if the cargo preference subsidy were eliminated from freight shipment costs.

Findings

Legislation results in extra shipping costs of over \$35 million. Section 901(b) of the Merchant Marine Act of 1936, as amended, which requires that U.S. flag ships carry at least 50 percent of commodities shipped under AID-financed programs, results in extra shipping costs of more than \$35 million (see Table II-8 at the end of this Issue).

Extra shipping costs reduce AID commodities shipped. Because foreign aid appropriations are inclusive of shipping costs, the impact of the cargo preference subsidy is to reduce the amount of AID funds available for the purchase of food and other commodities for needy countries. This shortfall represents a direct loss to the recipient government and deprives the U.S. farmer of his/her full export opportunities.

Liners vs. bulk cargo carriers (tramps). AID shipments are made in two types of carriers: scheduled/regular liners and bulk cargo/tramps. Shipments on the former are governed primarily by international agreement, known as "conference rates," while rates on the latter are determined by competitive bid.

Seventy-five percent of liner shipments conform to conference rates. However, a sizeable tonnage is not subject to conference rates and is affected by other factors such as the use of independent carriers, the shipment of open-rated commodities not covered by conference rates, differences in average time/distance between trips made by U.S. and foreign ships and differences in rates applied to commodities carried by them.

^{1/} op. cit.

Shortage of U.S. tramps results in use of costlier liners. U.S. flag tramps -- of which only 15 are in operation -- are reluctant to make costly port calls for small tonnage shipments. GAO reports that in only four instances were U.S. flag tramps used to transport P.L. 480, Title II, commodities in 1981. Costwise, P.L. 480, Title II, shipments represented 60 percent of all AID shipments abroad in 1981.

Due to the limited availability of U.S. flag tramps, U.S. flag liners must carry more than 50 percent of all Title II commodities to ensure that the overall 50 percent cargo preference requirement is met. In FY 1981, U.S. flag liners carried 65.7 percent of Title II commodities.

Shipments to Israel represent a special case, inasmuch as AID assistance is on a cash transfer basis. A side agreement provides for the usual 50 percent minimum cargo preference. AID can monitor only that part which involves the use of tramps for bulk shipments, of which 65 percent are grain.

Comparative cost of U.S. vs. foreign vessels. According to the aforementioned GAO report, the U.S. Maritime Administration estimates that despite the equivalence of liner rates the operational costs of foreign built and operated liners are 50 percent less than those of U.S. liners.

Based on actual charges, the GAO report calculated that the differential between the average cost per ton of U.S. vs. foreign flag liners and tramps in 1981 was as follows:

- o liners -- \$154.45 (U.S.) vs. \$147.96 (foreign) or \$6.49 per ton, and
- o tramps -- \$152.44 (U.S.) vs. \$74.53 (foreign) or \$77.91 per ton.

These comparative figures show that whereas charges made by U.S. liners are only moderately higher than those made by foreign liners, charges made by U.S. tramps are 104 percent higher than those by foreign flag tramps.

GAO estimates potential savings of \$15.6 million for Title II shipments alone. The GAO report is confined to an examination of the impact of cargo preference on P.L. 480, Title II, Food for Peace commodities. It estimates that in FY 1981, the Government could have saved a maximum \$2.6 million by substituting foreign flag tramps for U.S. flag tramps, \$5.5 million by substituting foreign flag liners for U.S. flag liners, \$8.2 million by consolidating liner

shipments onto foreign flag tramps, and \$15.6 million by consolidating all Title II shipments onto foreign flag tramps.

AID data indicate potential total savings of more than \$35 million. The AID Office of Commodity Management has estimated that the use of foreign flag vessels for all commodities shipped by AID would have resulted in savings of \$47.3 million in 1980 and \$35.8 million in 1981, an unusual year affected by shipping strikes and other problems.

Loss of cargo preference would diminish profitability of U.S. companies operating tramps. According to the GAO estimate, the elimination of cargo preference in the case of U.S. flag tramps would result in earnings losses of 17.9 percent, 12.7 percent and 1.6 percent respectively for the three U.S. companies involved.

Conclusions

The Task Force concludes that changing the current policy of requiring the use of U.S. ship bottoms would provide a cost-saving opportunity for AID, inasmuch as the present policy results in incremental shipping charges which could otherwise be avoided.

Further, as AID funds are now appropriated, with the cost of cargo preference charged against AID's program budget, the volume of commodities provided to recipient countries is reduced by the amount of the incremental shipping charges, as is the income to the U.S. farmer-exporter.

Finally, the Task Force concludes that affirmative action to realize this considerable cost-saving will reap political benefits abroad and among the farming community at home.

Recommendations

STATE 9-1: AID should request relief from cargo preference for AID-sponsored shipments. AID should identify the true cost and assess the overall impact of cargo preference in the administration of its programs. The Administrator should request total relief from the application of the cost of cargo preference to AID-sponsored shipments.

Alternatively, the cargo preference subsidy should be transferred from the AID budget to that of the U.S. Maritime Administration.

If politically infeasible to obtain such relief, the cargo preference subsidy should be identified as such and be the subject of a separate allocation of funds. A precedent exists, in that the U.S. Department of Agriculture carries the cost of cargo preference in the shipment of P.L. 480, Title I, commodities as an explicit budgetary item.

Savings and Impact Analysis

The AID Office of Commodity Management has estimated (see Table II-8 at the end of the Issue) that the elimination of cargo preference in the shipment of AID commodities would have meant a saving to the U.S. Government of \$47.3 million in 1980 and \$35.8 million in 1981, a year marked by shipping strikes and other problems. Using the \$35.8 million as the first-year savings figure and applying a 10 percent inflation factor, the three-year savings would be:

<u>Year 1</u>	<u>Year 2</u>	<u>Year 3</u>	<u>Total</u>
\$35.8	\$39.4	\$43.3	\$118.5

The removal of cargo preference costs of \$35 million per year from AID's program budget will have certain political benefits both at home and abroad. It will satisfy the U.S. farmer as well as the recipient countries that they are receiving the full value of the program funding allocated to the purchase and distribution of commodities by AID.

Implementation

1. Congressional Action

Congress should abolish cargo preference as applied to AID-administered commodity shipments on the grounds that it does not provide adequate benefits to the U.S. taxpayer and it adversely affects the interests of the U.S. farmer-exporter. Cargo preference is not a necessity for U.S. liners whose rates are governed by conference and are thus internationally competitive. As for bulk cargo carriers, only three U.S. companies operate such vessels and only two of them would be significantly affected.

2. Agency Action

Pending Congressional action to abolish cargo preference, the Administrator should seek the approval of the Office of Management and Budget (OMB) for relief from the cost of cargo preference now applied to AID-sponsored shipments of commodities.

The Administrator should seek first to assign the cost of cargo preference to the budget of the U.S. Maritime Administration.

Failing that, he/she should seek to remove the cost of cargo preference from AID's program and project budget and have it cited as a line item in AID's overall operating budget.

3. State Department Action

Because the incremental cost of cargo preference is charged against the funds appropriated for purchase and shipment of AID-sponsored commodities, there is a diminution of funds available for the purchase of these commodities. The resulting shortfall in shipments creates dissatisfaction in the recipient country and can have adverse political consequences for its relations with the United States. Therefore, the Secretary of State should support the Administrator of AID in seeking relief from the cost of cargo preference.

4. Presidential Action

The President should issue a directive to OMB instructing the Agency to remove the cost of cargo preference from AID's program and project budget. This cost should either be identified as a line item in AID's operating budget or be transferred to the budget of the U.S. Maritime Administration.

Table II-8SAVINGS RESULTING FROM USE OF FOREIGN SHIPPING
(BASED ON COMPARATIVE FREIGHT RATES GIVEN BELOW)

	1980 (\$ millions)		1981 (\$ millions)	
	<u>Tramp</u>	<u>Liner</u>	<u>Tramp</u>	<u>Liner</u>
AID-Financed	\$17.8	\$ 8.1	\$10.9	\$7.2
P.L. 480, Title II	2.1	3.4	2.7	.079
Israel (cash)	<u>15.9</u>	<u>-</u>	<u>14.9</u>	<u>-</u>
Totals	\$35.8	\$11.5	\$28.5	\$7.279
Grand Total	\$47.3		\$35.8	

COMPARATIVE FREIGHT RATES FOR U.S.
AND FOREIGN FLAG VESSELS
(dollars)

<u>Year</u>	<u>Flag</u>	<u>AID-Financed</u>		<u>Title II</u>		<u>Israel</u>	
		<u>Tramps</u>	<u>Liners</u>	<u>Tramps</u>	<u>Liners</u>	<u>Tramps</u>	<u>Liners</u>
1980	U.S.	83.16	160.57	152.17	147.96	62.94	--
	Foreign	<u>38.73</u>	<u>130.96</u>	<u>65.21</u>	<u>143.87</u>	<u>22.92</u>	--
	Differential	44.43	29.61	86.96	4.09	40.02	
1981	U.S.	85.24	191.14	148.03	156.84	74.94	--
	Foreign	<u>43.99</u>	<u>160.43</u>	<u>77.06</u>	<u>156.74</u>	<u>23.55</u>	--
	Differential	41.25	30.71	70.97	.10	51.39	

N.B: Any apparent discrepancy in the amounts representing potential savings (as for Title II) is attributed to the use of calendar figures by AID and FY figures in GAO's report.

Source: AID Office of Commodity Management.

II. ISSUE AND RECOMMENDATION SUMMARIES (CONT'D)

C. UNITED STATES INFORMATION AGENCY

OVERVIEW

The United States Information Agency (USIA) plays a central role in the implementation of U.S. foreign policy. As a complement to the private diplomacy conducted by the Department of State (State), USIA serves the national interest through the performance of public diplomacy, especially relating to the broadcasting of U.S. information to foreign countries. Specific tasks identified by the Agency are strengthening foreign understanding of U.S. policies; advising on the implications of foreign opinion; promoting exchange programs; cooperating with private sector institutions and assisting the free flow of international communication.

USIA's headcount and funding are shown below for selected years over the past 20 years and with current estimates:

	<u>FY 1962</u>	<u>FY 1972</u>	<u>FY 1982</u>	<u>Estimated</u>	
				<u>FY 1983</u>	<u>FY 1984</u>
Number of employees	11,454	9,987	7,793	8,114	8,636
Budget authority (\$ millions)	\$203	\$255	\$496	\$653	\$828

For FY 1983, USIA staffing consisted of 4,416 U.S. citizens and 3,698 foreign nationals. Of the U.S. complement, 992 (22 percent) are assigned to overseas missions, with the remaining 3,424 based in the United States.

USIA is headed by a Director who reports to the President with functional reporting to the Secretary of State.

The personnel assigned to 203 overseas posts in 124 countries receive instructions and report through five regional bureaus, which are located in Washington and organized geographically, as follows: Asian Affairs; European Affairs; East Asian and Pacific Affairs; American Republics Affairs; and North African, Near Eastern and South Asian Affairs. For the ten year period ending in FY 1982, the overseas missions' portion of the USIA budget was at least 30 percent in each year. Four areas support the posts and regional bureaus; Broadcasting Service; Programs; Educational and Cultural Affairs, and Management.

II. ISSUE AND RECOMMENDATION SUMMARIES (CONT'D)

C. U.S. INFORMATION AGENCY (CONT'D)

STATE 10: EVALUATION PROCEDURES

Issue and Savings

What opportunities for cost savings exist at the United States Information Agency (USIA) where FY 1983 appropriations exceed \$588 million and are estimated to exceed \$828 million for FY 1984?

Our Task Force found that, while the Agency has proposed major activity expansions costing \$144 million for FY 1984, it has not developed techniques that quantitatively evaluate the existing programs. If USIA establishes an analytical resource capacity by employment of a highly experienced financial analyst and appropriate staff, and defers the planned activity expansion until the effectiveness for the current activities are measured, then such actions will result in an expansion of the program that can be better justified. Specific savings will depend on the results of the evaluation process and, therefore, cannot be estimated at this time. The deferral of the expansion by one or more years will result in cost reduction in each budget year until the expenditures are made.

Background

USIA has experienced significant growth in appropriated funding in the ten year period ending FY 1982, with a 150 percent increase to \$496 million. While the major expenditure leaps occurred prior to 1978 with modest growth since. The funding for FY 1983 and FY 1984 show another dramatic increase with FY 1983 expected to increase by 19 percent over FY 1982. The budget request for FY 1984 projects another 41 percent increase:

	<u>Appropriations</u> <u>(\$ millions)</u>
1972	\$198
1978	349
1982	496
1983 (estimate)	588
1984 (requested)	828

This upsurge results from a combination of legislated requirements, correction of identified deficiencies and expansion of broadcasting and public affairs activities, as well as inflationary effects on operating costs.

More specifically, P.L. 97-241 (August 24, 1982) stipulates that USIA "grants for exchange of person activities shall be increased, through regular annual increases, so that by FY 1986, the amount obligated for such grants is at least double the amount (of)...FY 1982." Such expenditures for FY 1982 were \$96.7 million. This legislative action -- the so-called Pell Amendment -- was enacted in spite of objections by the Agency and the President.

Secondly, the National Security Council (NSC) performed a study of international broadcasting during FY 1982, which identified deficiencies at the Voice of America (VOA) (operating arm of the Broadcasting Service section of USIA). The NSC report identified six categories for improvement which required additional funding of \$35.4 million be sought as augmentation to the FY 1983 budget and a total of 442 positions be added to VOA for initial improvement implementation. More broadly, the two major technical requirements were established by NSC, to wit:

- o to provide broadcasting service in additional languages, and
- o to meet minimum performance standards.

Implementation mandates the construction of new facilities, an expansion of selected existing sites, and a rehabilitation/modernization program of all existing facilities with an estimated project cost of \$625 million through FY 1989.

Lastly, an expansion of programs and staff at the overseas missions in all regional bureaus is planned for FY 1984; such expansion includes opening ten new posts, a 5 percent increase and expansion of programs in 40 countries at a total increased cost of \$8 million and headcount increase of 127 personnel.

Methodology

This study focused on the justification for, and evaluation of, the current activities in all three areas (i.e., exchange of person activities, improvement of VOA programs and expansion of programs and staff at overseas missions) designated for expansion in the FY 1984 budget estimate. Such budget estimate data were prepared by the Agency on a preliminary basis and summarized for presentation in the Budget Submission. In addition, the adequacy

of management controls and information systems as a basis for decision making was assessed.

Three Task Force members were assigned to perform the study. Our methodology included:

- o interviews with current USIA management personnel, staff assigned to Educational and Cultural Affairs (ECA), VOA and the Inspector's staff;
- o review of various financial information relating to program spending;
- o review of various General Accounting Office (GAO) reports;
- o review of internal reports on:
 - foreign scholarships,
 - NSC study requirements, and
- o review of budget request data.

Findings

Educational and cultural affairs program evaluation is decentralized, subjective and incomplete. Our Task Force found that the relative importance of ECA programs can only be evaluated quantitatively at the individual post or mission. ECA records showing program participants, their employment position and follow-up data, are not forwarded (nor copied for transmittal) to Washington.

We were informed that individuals at overseas posts such as the Ambassador, Deputy Chief of Mission and USIA officials are aware of the ECA program impact and, generally, maintain files documenting program results and participants.

We also found that, as a starting point for an analysis that we performed, it is assumed by USIA personnel that measurement of public diplomacy results is either impossible or extremely difficult. Therefore, evaluations are limited in scope or at a superficial level. In our discussions with Agency personnel, we learned that, although a survey of ECA overseas activities is conducted annually, it is limited to roughly 25 posts, the responses are difficult to obtain and the usefulness of the information is "variable." Further, the Task Force found that a budget analysis which

establishes priorities for requested items is based on hypothetical situations and data from a small number of posts.

Our Task Force found that monitoring of exchange program alumni was incomplete. Such monitoring is important from the standpoint of determining the ongoing political, social and cultural influence of the program participants in their respective countries. Such information is also of importance in assessing the effectiveness of the exchange programs.

Although alumni of the International Visitors program are tracked, those from the much larger Fulbright program are not. The Fulbright program included approximately 3,800 participants at a cost of \$35.5 million in FY 1980, while the International Visitors program included nearly 1,800 individuals at a cost of \$16.2 million.

Planning and goal setting at overseas missions is too broad; available monitoring tools are unused. The Task Force found that GAO had reviewed overseas missions earlier in FY 1982 and reported thereon on February 11, 1982 (GAO ID-82-1). Findings include:

- o "In the past two decades....the programs and staffing patterns used by USIA to operate overseas....have remained the same in 125 countries."
- o "...Overseas missions do not set forth measurable objectives to be achieved in their plans and in carrying out their major objectives - personal contact."

More specifically, the annual country plans prepared at each mission were described as follows:

- o Issues in country plans are enumerated without stating specific measurable goals or objectives to be accomplished...
- o Examples included were: "Promote a full knowledge of U.S. Government; education and social models; articulate U.S. foreign policy."

Further, a system for recording personal contacts has been designed and installed at all overseas missions -- entitled "Distribution and Record System" (DRS). However, our Task Force received commentary at foreign posts that the number of Information/Public Affairs Officers who use it or find it useful is small. The GAO study reports similarly:

"The DRS System...is severely hampered in achieving goals because it has failed to convince a significant number of post officers of its utility and has been plagued by delays in delivery, installation and operational (equipment) readiness.

International broadcasting deficiencies include lack of identification and examination of performance requirements. The Task Force found that the NSC Study of International Broadcasting identified as one of two primary deficiencies the lack of an essential initial engineering step -- identification and examination of the overall performance requirements. The Agency has identified this step as a "logical precursory effort for all specific implementation projects."

Regular and methodical evaluation has been recommended. The Task Force found that the 1982 Report of the United States Advisory Commission on Public Diplomacy (submitted to the Congress and the President by Mr. Leonard L. Silverman, Chairman of the Commission) has recommended that the Office of Research (within USIA) "....should have the resources to carry out regular and methodical evaluation of Agency programs and products." 1/

The report cites that this recommendation had been made in its prior report and noted, "Regrettably, the shortage of staff and funds limits the Agency's research activities."

Conclusions

The basis for expanded activities has not been established within the Agency. The Task Force has concluded from the findings recited that the expanded activities in each of the areas:

- o ECA,
- o overseas missions, and
- o broadcasting,

have been projected without an objective evaluation of the existing staff and facilities by the USIA staff. This conclusion has been reached from the reports reviewed and clear evidence that the Agency does not have such evaluative skills at this time. The Task Force concedes that a study

1/ Page 34, Report of the United States Advisory Commission on Public Diplomacy, 1982

of international broadcasting was performed; however, it was done from outside the Agency, by NSC (and its results focus on this same conclusion). Our Task Force further concludes that projected expansion of headcount and program activities has ignored the abilities and skills within the existing staff in these areas.

Recommendations

STATE 10-1: Establish analytical resource capability within the Agency. We recommend that the Agency Director establish an analytical resource capability within USIA directed by a highly experienced financial analyst and staffed by adequate supporting personnel.

We further recommend that a program review system be established for the entire Agency which enables effective measurement on an annual basis and also provides long-term planning abilities.

STATE 10-2: Defer expenditure in planned expansions. We recommend that program expansions planned for FY 1984 be deferred until an initial evaluation of existing staff and facilities can be completed. At that time a better (and presumably smaller) amount for expansion could be programmed.

Savings and Impact Analysis

No specific savings are claimed for this Issue. The deferral of the planned expansion until the completion of an adequate and detailed analysis will result in a better program. Since no analysis of current activities is available, it is difficult to speculate on the extent to which the planned expansion might be curtailed.

Implementation

1. Agency Authority

Recommendations 10-1 and 10-2 require the Agency Director to supplement his/her staff through the budgetary process and also to initiate an amendment to P.L. 97-241.

2. Presidential Authority

Recommendation 10-2 requires Presidential endorsement of the deferral of implementation steps for correction of the NSC study deficiencies.

3. Congressional Action

Recommendation 10-2 requires Amendment to P.L. 97-241 to relieve USIA from mandatory expenditures for ECA activities.

**III. SUMMARY LIST OF
RECOMMENDATIONS AND SAVINGS**

III. SUMMARY LIST OF RECOMMENDATIONS AND SAVINGS

Savings, Revenue Enhancements or Cash Accelerations
(\$ millions)

	<u>Year 1</u>	<u>Year 2</u>	<u>Year 3</u>	<u>Total</u>
<u>STATE-1: Foreign Service Personnel Service</u>				
<u>1. Implementation by Agency Authority</u>				
o Use Models to Correct Skewed Distribution (STATE 1-1)	\$12.8	\$14.1	\$15.5	\$42.4(S)
o Review Ranking of Positions Realign Personnel (STATE 1-2)	6.0	6.6	7.3	19.9(S)
o Eliminate Overcomplement Employees (STATE 1-3)	7.0	8.0	9.0	24.0(S)
o Redesign the Performance Evaluation System and Train Supervisory Personnel (STATE 1-4)				
o Recruiting and Training (STATE 1-6)				
<u>2. Implementation by Congressional Authority</u>				
o Amend the FSA 1980 to Expand the Definition of Management Official (STATE 1-5)	\$25.8	\$28.7	\$31.8	\$86.3(S)
o Projected Savings for STATE 1				
<u>STATE 2: Foreign Service Retirement and Disability System</u>				
<u>1. Implementation by Congressional Authority</u>				
o Increase Retirement Age (STATE 2-1)	\$18.6	\$18.9	\$19.2	\$56.7(S)
o Change the Benefit Formula (STATE 2-2)	11.1	11.3	11.5	33.9(S)
o Projected Savings for STATE 2	\$29.7	\$30.2	\$30.7	\$90.6(S)

III. SUMMARY LIST OF RECOMMENDATIONS AND SAVINGS (CONT'D)

Savings, Revenue Enhancements or Cash Accelerations
 (\$ millions)

	<u>Year 1</u>	<u>Year 2</u>	<u>Year 3</u>	<u>Total</u>
<u>STATE 3: Office of Foreign Buildings</u>				
<u>1. Implementation by Agency Authority</u>				
o Develop a Real Property Management System (STATE 3-1)	--	--	--	--
o Expansion of Cost Accumulation Report (STATE 3-2)	--	--	--	--
o Consolidation of Fiscal Authority (STATE 3-3)	--	--	--	--
o Provide Guidelines for Identification of Excess Capacity (STATE 3-4)	--	--	--	--
o Allocation of Operating and Maintenance Expenditures (STATE 3-5)	--	--	--	--
<u>2. Implementation by Congressional Authority</u>				
o Provide Funding for Development of Real Property Management System (STATE 3-1)	--	--	--	--
o Approve Consolidation of Fiscal Authority (STATE 3-3)	--	--	--	--
Projected Savings for STATE 3	--	--	--	--

III. SUMMARY LIST OF RECOMMENDATIONS AND SAVINGS (CONT'D)

Savings, Revenue Enhancements or Cash Accelerations
(\$ millions)

	<u>Year 1</u>	<u>Year 2</u>	<u>Year 3</u>	<u>Total</u>
<u>STATE 4: Purchase of Foreign Currencies</u>				
<u>1. Implementation by Agency Authority</u>				
o Develop an Accounting System to Gather Foreign Currency Needs (STATE 4-1)	--	--	--	--
o Establish Foreign Currency Futures/Forward Desk (STATE 4-2)	\$5.7	\$5.7	\$5.7	\$17.1(S)
o Hire Staff and Define Functions of Trading Desk (STATE 4-3)				
Projected Savings for STATE 4	<u>\$5.7</u>	<u>\$5.7</u>	<u>\$5.7</u>	<u>\$17.1(S)</u>
<u>STATE 5: Refugee Programs</u>				
<u>1. Implementation by Agency Authority</u>				
o Rectify the Collection Problem (STATE 5-1)	\$21.3 2.1	\$18.5 4.0	\$16.1 5.6	\$55.9(CA) 11.7(S)
o Improve Monitoring Program (STATE 5-2)	--	--	--	--
o Develop Tracking and Integrated Data Base (STATE 5-3)	(0.5)	(1.0)	(1.5)	(3.0)(S)
<u>2. Implementation by Congressional Authority</u>				
o Require Sponsor Guarantee (STATE 5-1)				
o Provide Funding for Integrated Computer System (STATE 5-3)				
Projected Cash Accelerations for STATE 5	<u>\$21.3(CA)</u> 1.6(S)	<u>\$18.5(CA)</u> 3.0(S)	<u>\$16.1(CA)</u> 4.1(S)	<u>\$55.9(CA)</u> 8.7(S)

III. SUMMARY LIST OF RECOMMENDATIONS AND SAVINGS (CONT'D)

Savings, Revenue Enhancements or Cash Acceleration
 (\$ millions)

	<u>Year 1</u>	<u>Year 2</u>	<u>Year 3</u>	<u>Total</u>
<u>STATE 6: Improvements in the Project Planning, Approval, and Monitoring Process</u>				
<u>1. Implementation by Agency Authority</u>				
o Increase the Dollar Value of Block Grants (STATE 6-1)	\$4.3	\$4.7	\$5.2	\$14.2(S)
o Find Additional Ways to Increase Decentralization of Authority (STATE 6-3)				
o Limit the Time Spent Responding to Congress (STATE 6-4)	1.9	2.1	2.3	6.3(S)
<u>2. Implementation by Congressional Authority</u>				
o Congress Return Deobligation/Reobligation Authority to AID (STATE 6-2)	1.9	2.1	2.3	6.3(S)
o Move to a Two-Year Budget Submission Cycle (STATE 6-5)	1.8	2.0	2.2	6.0(S)
<u>3. Implementation by Presidential Authority</u>				
o Move to a Two-Year Budget Submission Cycle (STATE 6-5)				
Projected Savings for STATE 6	\$9.9	\$10.9	\$12.0	\$32.8(S)
<u>STATE 7: Interest Rates on AID Loans</u>				
<u>1. Implementation by Agency Authority</u>				
o Establish a Base Lending Rate (STATE 7-1)	\$60.0	\$120.0	\$180.0	\$360.0(R)
o Establish a Uniform Set of Criteria for the Determination of Loan Terms (STATE 7-2)	--	--	--	--

III. SUMMARY LIST OF RECOMMENDATIONS AND SAVINGS (CONT'D)

Savings, Revenue Enhancements or Cash Accelerations
(\$ millions)

	<u>Year 1</u>	<u>Year 2</u>	<u>Year 3</u>	<u>Total</u>
<u>2. Implementation by Congressional Authority</u>				
o Work Within the Guidelines and Public Law Set by Congress in Establishing a Base Lending Rate on Loan Terms (STATE 7-2)	\$60.0	\$120.0	\$180.0	\$360.0(R)
Projected Revenue Enhancements for STATE 7				
<u>STATE 8: Foreign Service Rotation Policy</u>				
<u>1. Implementation by Agency Authority</u>				
o Enforce Four-Year Tours (STATE 8-1)	\$1.6	\$1.8	\$1.9	\$5.3(S)
PROJECTED SAVINGS FOR STATE 8	\$1.6	\$1.8	\$1.9	5.3(S)
<u>STATE 9: Cargo Preference</u>				
<u>1. Implementation by Congressional Authority</u>				
o Relief From Cargo Preference for AID-Sponsored Shipments (STATE 9-1)	\$35.8	\$39.4	\$43.3	\$118.5(S)
Projected Savings for STATE 9	\$35.8	\$39.4	\$43.3	\$118.5(S)
<u>STATE 10: Evaluative Procedures</u>				
<u>1. Implementation by Agency Authority</u>				
o Establish Analytical Resource Capability (STATE 10-1)				1/
o Deferral of Mission Expansion (STATE 10-2)				1/

III. SUMMARY LIST OF RECOMMENDATIONS AND SAVINGS (CONT'D)
Savings, Revenue Enhancements or Cash Accelerations
 (\$ millions)

	<u>Year 1</u>	<u>Year 2</u>	<u>Year 3</u>	<u>Total</u>
<u>2. Implementation by Congressional Authority</u>				
o Relieve USIA From Mandatory Expenditures for ECA Activities (STATE 10-2)				<u>1/</u>
<u>3. Implementation by Presidential Authority</u>				
o Deferral of Implementation Steps for Correction of the NSC Study Deficiencies (STATE 10-2)				<u>1/</u>
Projected Savings for STATE 10				<u>1/</u>
Total Projected Savings:	\$110.1(S)	\$119.7(S)	\$129.5(S)	\$359.3(S)
Total Projected Cash Acceleration:	21.3(CA)	18.5(CA)	16.1(CA)	55.9(CA)
Total Projected Revenue:	<u>60.0(R)</u>	<u>120.0(R)</u>	<u>180.0(R)</u>	<u>360.0(R)</u>
Total	\$191.4	\$258.2	\$325.6	\$775.2

1/ Management Improvement Recommendation, savings not quantified.

IV. COST CONTROL OPPORTUNITIES

FOR FURTHER STUDY

IV. COST CONTROL OPPORTUNITIES FOR FURTHER STUDY

The Task Force has identified four issue areas for further study that have been given varying amounts of attention but require fuller consideration and/or major policy decisions.

First, the Organization of International Affairs Agencies should be reviewed; the three major agencies in our review represent 70 percent of the U.S. personnel abroad, but individually they represent a minority of U.S. personnel from all agencies. Additionally, certain similar functions are performed independently by each of the agencies. A current review and consolidation process could enhance our international affairs activities and produce cost-saving opportunities.

Secondly, foreign currencies held abroad have been identified as being slowly used but costing considerable funding requirements. Other agencies are the major contributors to the presence of such balances and should join in a committee to speed their use.

Next, the U.S. contributions to international organizations have grown by 76 percent in the past five years, and our control over the budgetary process has been lost. Major policy considerations must be addressed by the Administration to gain control of this major expenditure area.

Lastly, substantial reductions have been made in workman's compensation insurance costs for contractors and personnel; application of a similar program at other overseas agencies, like the military, could substantially reduce U.S. outlays.

IV. COST CONTROL OPPORTUNITIES FOR FURTHER STUDY (CONT'D)

A. ORGANIZATION FOR INTERNATIONAL AFFAIRS ACTIVITIES

Issue and Savings

Are there significant financial or administrative control advantages to reorganizing the structure of the foreign affairs agencies, bureaus and/or diplomatic posts?

Many alternatives are available, each of which could result in significant benefits. It is not possible to estimate the actual dollar savings at this time.

Background

The U.S. Government maintains 253 diplomatic posts outside the United States at which 33,000 U.S. citizens and foreign nationals are employed. Presently, 28 U.S. government agencies are represented at these posts by over 14,000 U.S. personnel.

Although the Secretary of State was the first cabinet post established by the United States, the foreign policy functions currently performed by the Department of State have evolved since World War II, based on a combination of factors most predominant among which was the viewpoint of each incumbent Secretary.

The U.S. Information Officer/Public Affairs Officer positions at State and the Voice of America were transferred to a separate agency, United States Information Agency (USIA) in 1953. Other functions (Exchange and Cultural Affairs) performed by State Department were transferred to USIA in 1977.

The Agency for International Development (AID) was created in 1961 under the Foreign Assistance Act from existing commissions as an adjunct to the State Department. In 1979, AID's direct reporting line was moved to the International Development and Cooperation Agency which reports directly to the State Department. Today, the directors of USIA and IDCA (AID) have "dotted-line" responsibility to the Secretary of State.

As a means of providing support to foreign posts and staffing areas of special concern, individual bureaus have been established under State's Deputy Secretary, each of

of which is headed by an Assistant Secretary. Presently, there are 19 bureau chiefs at State.

Methodology

During the course of our study, interviews were conducted with numerous personnel based in Washington and at overseas posts from the three agencies -- State, USIA and AID.

Manning chart data and organizational outlines were reviewed. Functions of bureaus were outlined.

Findings

The separation of International Affairs Agencies has emanated from two sources:

- o The ongoing debate over the functions of Foreign Service Officers amongst themselves; and
- o The actions of individual Secretaries of State, particularly John Foster Dulles.

A Presidential letter dated September 22, 1981 has underscored that the Secretary of State, as the principal foreign policy spokesman, has responsibility for not only Department of State and Foreign Service but also overall policy directives, coordination and supervision of U.S. government activities overseas.

Each of the three agencies has established a regional bureau in Washington to coordinate the European, African, East Asian/Pacific, Inter-American and Near Eastern/South Asian area activities. Headcount for the domestic personnel at the regional bureaus by agencies is as follows:

	<u>Headcount</u>
State	662
USIA	114
AID	519
	<u>1,295</u>

Administrative support for the agencies exceeds \$330 million or 20 percent of the operating budgets as shown in Table IV-1.

[Table IV-1 on following page]

Table IV-1

	<u>Headcount</u>	<u>Management & admin.</u>	<u>Operating expenses</u>	<u>Percentage management & admin.</u>
State	2,842	\$ 248.	\$1,021.	24%
USIA	907	40.	277.	14
AID	641	44.	376.	12
	<u>4,390</u>	<u>\$332.</u>	<u>\$1,674.</u>	<u>20</u>

Although the Agencies use State's administrative support system overseas, each Agency maintains separate support functions in Washington.

As a combined percentage, State/USIA/AID comprise over 70 percent of the workforce at our overseas missions.

In addition to the 600 personnel in regional bureaus supporting directly the overseas posts, there are 14 bureaus with a total of 1,700 personnel in Washington who provide other staffing support in areas such as human rights, environment, intelligence and policy planning. The head of each such bureau also reports to the Secretary/ Deputy Secretary level.

There are 30 diplomatic embassies with 20 (or less) State Department personnel and an additional 55 embassies with 20 to 50 State personnel. More than 50 percent of these embassies are located on the African continent. African Bureau personnel have indicated that staffing for these posts is difficult and that duty tours are as short as possible due to the remoteness of the posts. Several Western allies have consolidated diplomatic functions for remote countries into regional posts serving several countries.

Task Force personnel questioned the ongoing need at State for International Narcotics matters and Combatting Terrorism, and at AID for the Bureau of External Relations, Bureau for Private Enterprise and the Bureau for Science and Technology.

Conclusions

Current mandates legitimize a thorough examination of the similarities of functions amongst the three agencies and of the opportunities to cut costs by merging support functions. cursory examination reveals more similarities than differences.

Proliferation of bureaus to handle problems of the moment has taken place without review of their ongoing need. If each is justified, span of control concepts should be applied for better management control.

Consideration of alternates to separate embassies for each remote sovereignty is warranted.

Recommendations

The Task Force recommends consideration of the following alternative courses of action:

STATE IV-1: Merge foreign affairs agencies. The consolidation of State/USIA/AID will make explicit the Presidential directive and provide the opportunity to merge those basic functions, not already shared (e.g., personnel, payroll, financial reporting) as well as to integrate the common regional bureau functions.

STATE IV-2: Examine the bureaus; group where possible. Examination of all bureaus not associated with management and regional operations for current validity should provide the opportunity to shift responsibilities to line (embassy and bureau) organizations and provide cost savings and, where not eliminated, control opportunities by grouping into manageable control spans.

STATE IV-3: Examine the need for individual posts; establish regional posts where feasible. By establishing regional posts, consolidation of marginally functional remote locations can be achieved on an embassy as well as consular level.

The Administration should study the opportunity further to identify the specific details and potential extent of consolidation of similar activities among the three agencies.

IV. COST CONTROL OPPORTUNITIES FOR FURTHER STUDY (CONT'D)

B. FOREIGN CURRENCIES HELD BY THE U.S. GOVERNMENT

Issue and Savings

Can the foreign currencies held by the U.S. Government (which totalled \$1.0 billion at the end of FY 1981) be utilized more quickly to reduce interest costs on U.S. borrowings, or reduce the foreign currency rate exposure or reduce the deficit?

Alternative courses of action for use of the avenues have been proposed which are worth exploring; quantification of the savings is not determinable at this time.

Background

The U.S. Government acquires and spends large amounts of foreign currencies in the course of its overseas operations. Some foreign currencies are received without direct purchase using dollars (so called non-purchased foreign currencies), primarily through:

- o exchange for agricultural commodities financed by the Department of Agriculture;
- o repayment of loans financed by dollar assistance under the Foreign Assistance Act of 1961;
- o payment of interest on deposits of foreign currency in foreign banks; and
- o various other programs.

The Department of Treasury, Fiscal Service, Bureau of Government Fiscal Operations, produces an annual report on foreign currencies held by the U.S. Government. This report categorizes the currencies as to the U.S. Government's freedom to convert or spend such currencies. Where the supply of a non-restricted currency meets more than a two-year U.S. requirement, such currencies are designated as excess.

Methodology

The U.S. Treasury report for FY 1981 was reviewed, and discussions held with personnel at Treasury and State.

Findings

Of the \$7,075 million of foreign currencies held by the United States at September 30, 1981, \$916 million were available for U.S. use on a nonrestricted basis and \$805 million of that amount was in excess of two years' requirements.

Further, currencies of three countries -- India, Pakistan and Poland -- totalled over \$836 million of the nonrestricted category.

A Wall Street Journal article dated July 21, 1982 cited the accumulated amount of these foreign currencies and slow progress being made in their utilization by U.S. agencies. Specifically, the article noted that \$22,000 worth of Indian rupees had been spent by USDA to translate its soil dictionary into French over an eight-year period. This latter point was an example of the extremes to which government agencies have sought to utilize such funds.

A total of \$111 million in foreign currency losses were experienced in FY 1981 for all currencies reported by the Treasury.

Conclusions

Cost savings opportunities exist in substantial dollar amounts in the areas of:

- o foreign currency risks;
- o interest on U.S. government borrowings;
- o the projected budget deficit; to the extent that these currencies can be utilized.

Recommendations

STATE IV-4: A joint study council should be formed, consisting of the major U.S. agencies creating these non-purchased currency balances, under State leadership to determine methods to utilize them more quickly.

Specific considerations should be:

- o Use of local currencies to purchase strategic stockpile reserves like MICA from India, and

- o Sale of soft currencies to multinational private sector companies operating in host countries (either to cover their local costs or to purchase goods for export).

IV. COST CONTROL OPPORTUNITIES FOR FURTHER STUDY (CONT'D)

C. CONTRIBUTIONS TO INTERNATIONAL ORGANIZATIONS

Issue and Savings

Are there opportunities for cost savings or avoidance in the area of contributions to international organizations which are estimated at \$723 million for FY 1983?

Implementation of recommendations requires major policy decisions and perhaps treaty negotiations, but could also result in substantial dollar savings.

Background

The United States has been a major contributor to the multilateral international organizations since their inception. The majority of these contributions have been made according to assessments resulting from negotiated treaties, while the remainder have been voluntary (see Table IV-2).

[Table IV-2 on following page]

Table IV-2

INTERNATIONAL ORGANIZATIONS' CONTRIBUTIONS
ASSESSED

1983	Total budget	United States			Total United States
		Percentage	Amount	Voluntary	
United Nations	\$ 719.1	25.0	\$179.8	\$ -	\$179.7
UNDB	-	-	0	106.8	106.8
UNICEF	-	-	-	26.0	26.0
UNESCO	199.2	25.0	49.8	-	49.8
WHO	247.0	25.0	61.7	-	61.7
FAO	198.4	25.0	49.6	1.0	50.6
ILO	111.0	25.0	27.7	-	27.0
Total UN & affil	\$1,681.5	24.21/	41.4	15.5	56.0
PAHO	50.4	61.3	30.9	-	30.9
OAS	62.8	66.0	41.4	15.5	56.9
Total inter-American	132.6	63.6	84.3	15.5	99.8
NATO	76.5	24.2	18.5	-	18.5
OECD	110.5	25.0	29.8	-	29.8
Total regional	192.9	29.0	49.4	-	49.4
Other (24)	71.7	13.5	9.8	-	9.8
Total 1983	\$2,078.8	26.48	\$550.52/	\$173.2	\$737.7
Total 1982	\$1,883.4	26.32	\$495.92/	\$210.1	\$706.0
Growth percentage	10%	-	11%	-18%	3%

1/ Soviet Bloc 17.12
OPEC Countries 2.89
Saudi, Arabia .58

2/ Funds Available - 1983 - \$439.7
1982 - \$375.9

The assessments are made on a percentage basis from a formula which involves dividing the countries' net national product by the total net national product of all participating countries multiplied by 100. The percentages are reviewed and adjusted biannually.

The growth in the budget of the international organizations over the past five years has been substantial -- as has the U.S. assessment -- at 76.6 percent for representative agencies like the United Nations (UN); Food and Agricultural Organization (FAO); United Nations Education, Science and Cultural Organization (UNESCO); World Health Organization (WHO); International Atomic Energy Agency (IAEA) and International Labor Organization (ILO).

A recently issued House Investigations and Survey Report on Selected Programs and Organizations of the United States was critical of the UN contributions system and cited the loss of U.S. control over the budgetary process -- because of inflation and Third World pressures/majority vote.

Methodology

Two Task Force members conducted interviews with State personnel of the Bureau of International Organizations, developed statistical trend data and read the applicable reports issued by the House, General Accounting Office (GAO) and the Heritage Foundation.

Findings

Certain UN agencies have ignored the zero growth policy statement issued by the United States and Western allies by passing substantial (10 percent) budget increases for FY 1983.

The Office of Management and Budget (OMB) has recommended several alternative actions:

- o the United States place a cap on appropriations and vote against increases over their targets;
- o the United States not pay more than 25 percent above the change from each year;
- o the United States withhold payments when it disagrees with a budget; and

- o the United States give notice of withdrawal from an organization which ignores our budget recommendations.

Recently, West Germany temporarily withdrew its financial support from FAO because its Director refused to answer to questions regarding its expenditures. Also, the United States temporarily withdrew from ILO over a policy matter and rejoined after ILO reconsidered its decision.

The House Survey Report cited in State's Bureau of International Organizations (IOs):

- o fragmentary documentation on policy and long-range planning;
- o lack of bureau structure and high leadership turnover;
- o contradictory information on lead agency responsibility; and
- o no control over information provided by IOs.

The UN contributions system allows equal vote to each member no matter what its percentage contributions. Since the UN's creation, the number of the Third World countries has increased and now outnumbers the other countries in the UN system -- 127 out of 157 countries; a typical contribution from one Third World country is .01 percent of the total budget. By contrast, see the following UN contribution percentages for 1982:

20 Western Bloc Nations	69.92%
10 Eastern Bloc Nations	17.12%
13 OPEC Members	2.89%

Conclusions

The ability to control increases in U.S taxpayer dollars contributed to IOs has been lost by the Federal Government.

Alternative actions have been proposed and have been taken by others and the United States.

The Bureau of International Organizations at State does not appear equipped to monitor and control the contribution process.

The voting process is a major hurdle that needs corrective action, but will require hard political decisions.

Recommendations

STATE IV-5: State should consider the UN agency policy proposal to allow "cumulative voting" on budgetary matters in proportion to percentage contribution and sovereignty voting on all other matters.

STATE IV-6: State should consider the OMB courses of action as alternatives to the first recommendation.

Savings and Impact Analysis

The Task Force believes that these recommendations require the level of policy decisions that exceeds our charter and has, therefore, not quantified any projected cost savings.

IV. COST CONTROL OPPORTUNITIES FOR FURTHER STUDY (CONT'D)

D. REDUCTION OF COSTS FOR
WORKMAN'S COMPENSATION INSURANCE OVERSEAS

Issue and Savings

Can the cost of workman's compensation insurance be reduced overseas?

The costs of workman's compensation insurance contracts required by the Defense Base Act (DBA) have been reduced 50 percent by a plan developed at the Agency for International Development (AID). This plan could be applied to other departments with overseas personnel, especially military. AID estimates its contractors will save \$45 million in insurance premiums over the five-year life of its two blanket contracts covering AID direct contracts and AID-financed contracts between host governments and third parties. The later contract accounts for a savings of \$40 million of the total savings over the five-year life based on contract awards of \$175 million per year. Given the size of contract awards in other departments of the Administration, the total savings could be substantial.

Since other task forces are assigned to other departments, we submit this Issue and potential savings as a recommendation without attempting to present more than the AID picture of it.

Background

DBA insurance is a form of workers' compensation insurance required by P.L. 208 for U.S. citizens, residents and persons hired in the United States for work overseas on contracts approved and financed by the Federal Government. DBA insurance is an extension of the Longshoreman and Harbor Worker's Compensation Act and is intended to provide equitable coverage for persons working outside the U.S. State's workers' compensation varies widely, and is generally not applicable outside territorial limits of a state.

Benefits under DBA are subject to administrative and judicial interpretation. Generally, however, the Act provides 24-hour coverage for contract employees, and most

sicknesses, accidents, injuries, and deaths are interpreted as job related since the employee would not have been exposed to the hazard except for his/her job overseas.

DBA insurance rates were relatively stable and reasonable until late 1974 (averaging less than 1 percent of payroll according to the Management Bureau of AID). At that time, legislative amendments which increased benefits, and more particularly, the Rasmussen Decision in November 1974, caused insurance premiums to suddenly skyrocket. In the Rasmussen Case, an administrative law judge made the interpretation that recent legislative amendments removed the previous cap on benefits to survivors, thus exposing insurance companies to unpredictable liability. As a result, premium rates climbed at least 20-fold.

In February 1976, AID worked out an informal agreement with the insurance industry which reduced rates from an average of 20 percent of payroll to 14 percent of payroll and eliminated minimum premiums. In October 1977, a formal agreement was concluded which reduced rates 8.75 percent and provided for an escalation/de-escalation formula which subsequently reduced rates to 7.14 percent commencing in November 1979, 4.84 percent in 1980 and 3.05 percent in November 1981.

Since then, AID has concluded another agreement with the insurance industry reducing rates on AID-financed host country contracts written by other governments from previous rates of 15 percent for construction and 10 percent for services to new rates of 3.4 percent for construction and 2.3 percent for services.

The total savings to AID from the programs are estimated by AID at \$9.1 million annually. Based upon a study and recommendations of the General Accounting Office (GAO), other government agencies including the Department of Defense (DOD) have been encouraged to adopt similar programs. Our Task Force strongly endorses this recommendation as a substantial cost savings formula readily available for immediate application.

Methodology

Interviews were carried out with senior AID executives including the Administrator and Assistant Administrator for Management to verify the accuracy of claims made for the program. Correspondence from GAO to Departments of the Army, Navy, Air Force, Labor, NASA, Army Corps of Engineers and Defense Logistics Agency were studied. Summary reports within AID were analyzed. An AID administrative bulletin exists on the subject.

Findings

Many AID contractors experienced difficulty obtaining DBA coverage due to high premiums charged by carriers. Often the minimum premium approached or even exceeded the contractor's salary cost. To remedy the situation, AID entered into a blanket contract at a guaranteed premium rate at least 50 percent less than rates charged on individual contracts. Subsequent experience with this policy by AID has resulted in even lower rates and the insurance has been readily available to all contractors.

The Office of Longshoreman and Harbor Worker's Compensation has called the matter to the attention of DOD in a letter dated October 27, 1981. On May 27, 1982 similar letters were sent to all the military branches by the GAO International Division. GAO also met with representatives of the military departments May 1982. However, to our knowledge, no department has as yet effected this blanket policy approach.

Conclusions

The potential savings, if this approach were applied to other departments, would be substantial.

This Task Force has neither the time nor jurisdiction to document such savings.

Based upon our verification of AID's experience with this improved program, we conclude that the GAO recommendations to other departments are well taken.

Recommendations

STATE IV-7: The Administration should give instructions to study the applicability of the blanket policy approach in workman's compensation for overseas personnel and contractors used by other applicable departments.

Savings and Impact Analysis

Our Task Force cannot determine the cost impact for other agencies but believes that departments with similar overseas personnel and programs, especially the military should, if they convert to the blanket policies referred to in this Issue, be able to save a proportionally comparable amount to AID's \$45 million over five years. Since their overseas operations are substantially larger than AID's,

the savings across-the-board to the Government should count in the hundreds of millions of dollars over the five-year life of such insurance policies.

Implementation

STATE IV-7: An administrative order to investigate the applicability of this plan to other departments should be issued immediately. A one-month reporting date should be set for such reports. The order should instruct all departments where potential savings are found to implement a similar plan as soon as possible and to report when the plan is in effect.

V. TASK FORCE MEMBERSHIP

V. TASK FORCE MEMBERSHIP

A. John Allen
President and CEO
Allen & Associates, Inc.
Washington, D.C.

Nancy Holland
Associate
Deloitte, Haskins & Sells
Washington, D.C.

Louise S. Armstrong
Research Analyst
Office of Daniel Parker
Washington, D.C.

Peter F. Heuzey
Partner
Deloitte, Haskins & Sells
New York, N.Y.

Dr. C. Cary Barton
President
C. Cary Barton Associates, Inc.
Los Angeles, California

James A. Hynes
Chairman
Oak Partners, Inc.
Chicago, Illinois

Robert B. Calhoun, Jr.
Managing Director
First Boston Corporation
New York, N.Y.

Charles Katsainos, Ph.D.
Retired, U.S. Army,
U.S. Foreign Service
Washington, D.C.

James E. Connor
Managing Director
First Boston Corporation
New York, N.Y.

Alice W. Lorillard
Owner/Manager
Bindon Farm
Far Hills, N.J.

J. Rawles Fulgham*
Vice Chairman (Retired)
InterFirst Corp.
Dallas, Texas

Michael L. McAllister
Associate
First Boston Corporation
New York, N.Y.

K. Craig Gallenhugh
Credit Analyst
Mercantile Bank
Dallas, Texas

Stacie E. McGinn
Credit Analyst
Republic Bank of Dallas
Dallas, Texas

David Glazer
Student
Harvard University Law School
Cambridge, Mass.

Cheryl M. Neimuth
Auditor
Arthur Anderson & Co.
Dallas, Texas

Donald S. Grubbs, Jr. (o)
Consulting Actuary
George B. Buck Actuarial
Consultants
Washington, D.C.

Robert A. Pikul
PPSS Desk Officer
MITRE Corporation
Washington, D.C.

Dr. Fred O. Pinkham (o)
President
Population Crisis Committee
Washington, D.C.

George L. Shinn*
Chairman of the Board
and CEO (Retired)
First Boston Corporation
New York, N.Y.

Robert J. Reynolds
Student
Stanford University
Graduate School of
Business
Stanford, California

Lawrence A. Silverstein (o)
Senior Auditor
First Boston Corporation
New York, N.Y.

William Rita
Consultant
Deloitte, Haskins & Sells
Washington, D.C.

Chris D. Simpson
Partner
Price Waterhouse
Dallas, Texas

Mack F. Rossoff
Associate
First Boston Corporation
New York, N.Y.

Robert J. Starry
Partner
Deloitte, Haskins & Sells
Washington, D.C.

Arthur M. Scutro, Jr. (+)
Vice President
First Boston Corporation
New York, N.Y.

G. William Vining (o)
Partner
Deloitte, Haskins & Sells
Washington, D.C.

*Co-chairman
(+)Project Manager
(o)Issue Coordinator