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UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

INTERNATIONAL DIVISION

B-210219

JANUARY 3, 1983

The Honorable M. Peter McPherson
Administrator, Agency for International
Development

Dear Mr. McPherson:

Subject: Potential For Improving AID's Deobligation and
Project Analysis Processes (GAO/ID-83-25)

We have examined aspects of the Agency for International Development's (AID's) deobligation process, including efforts to identify and monitor projects which are potentially subject to deobligation. We identify issues which we believe will be useful for you to consider as the Agency continues to improve the management of its projects.

We make recommendations to you on page 9. As you know, Section 236 of the Legislative Reorganization Act of 1970 requires the head of a Federal agency to submit a written statement on actions taken on our recommendations to the Senate Committee on Governmental Affairs and the House Committee on Government Operations not later than 60 days after the date of the report and to the House and Senate Committees on Appropriations with the Agency's first request for appropriations made more than 60 days after the date of the report. We would appreciate receiving copies of your statements to the committees.

AID has told the Congress that it expects deobligations which are due to good project management actions--rather than those due to write-offs of residual funds--to substantially increase. Although AID management has taken steps to meet this goal, our review of regional bureaus' reports on deobligation actions and our discussions with cognizant bureau officials indicate that the use of the deobligation process as a management tool has not as yet yielded significant results. Many deobligations occur because projects have been completed, leaving residual amounts to be cleared from the books. One difficulty seems to be the inconsistent ways bureaus identify troubled projects. This, in turn, indicates that AID should develop and apply more specific policy guidance and procedures, particularly in the area of deobligations and project extensions.

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OBJECTIVES, SCOPE, and METHODOLOGY

The objectives of this review were to determine what criteria and analysis have been used since August 1981 for identifying troubled projects and for deobligating project funds. Our work did not address the relative merits of reobligation authority (authority to reprogram deobligated funds). In December 1981, ¹ we advised AID that discussions with cognizant AID officials suggested that the pros and cons on management's need for, and usefulness of, reobligation authority had not been fully developed by AID. We believe that AID can best determine and analyze the management and operational implications of having, or not having, reobligation authority.

This review was conducted in accordance with generally accepted "Standards for Audits of Governmental Organizations, Programs, Activities, and Functions." It includes analyses of project and program reports, documentation in support of deobligations, and information obtained in discussions with cognizant officials in the Agency bureaus and offices; we did not assess the accuracy of data AID reported in its project and program reports.

BACKGROUND

On August 4, 1981, the AID Administrator announced that, in keeping with the President's orders to eliminate waste and mismanagement, he was terminating or reducing some AID programs and that other programs would be redesigned. These changes were the result of a targeted effort to analyze ongoing projects with a view toward stopping those which were not working. The Administrator noted that in the past, most savings had occurred only when projects were completed and had not consumed all the money originally budgeted for them. AID identified a total of \$28 million that was to be returned to the U.S. Treasury. The Administrator said that, too often, failing projects have been continued rather than terminated to cut losses. Thus, he decided to return the monies to the U.S. Treasury to demonstrate cuts in programs falling short of expectations.

At hearings on October 6, 1981, ² the AID Administrator noted that AID was proceeding to turn back other projects, in addition to the \$28 million, by going through its inventory of projects on a quarterly basis to terminate or restructure those projects not working. At hearings on March 11, 1982, ³ the AID

¹ Letter dated December 2, 1981, to R. T. Rollis, AID Assistant to the Administrator for Management.

² Legislation and National Security Subcommittee of the House Government Operations Committee.

³ Foreign Operations Subcommittee of the Senate Appropriations Committee.

Administrator pointed out that project portfolio reviews had resulted in total fiscal year 1981 deobligations of \$74 million. He explained that as a result of project reviews, AID's operating bureaus are expected, semiannually, to refer troubled projects to responsible Washington staff or to missions for corrective action. This continuing process is intended to produce either deobligations or other corrective actions sometimes requiring restructuring of individual projects which will not necessarily lead to deobligation of funds.

At the request of the Senate Appropriations Committee, AID reported in May 1982 on steps it had taken to improve its program monitoring and implementation, including terminating projects early which are not performing satisfactorily. The report notes that AID has followed the normal practice of deobligating remaining funds at the end of a project, but AID has rarely taken action on an ongoing project which was not reaching its agreed-upon objectives. Another reported step is that the Administrator instructed all bureaus to review their projects at least twice a year to determine if projects are progressing properly. If projects do not appear to be progressing properly, they should be redesigned or closed down.

DEOBLIGATED AMOUNTS REPORTED TO DATE

Since the Administrator's August 4, 1981, announcement on project deobligations, he has periodically requested the regional bureaus to report on their efforts to deobligate projects which are not working and cannot be redesigned effectively. Based on bureau reports, actual deobligations totaled \$74.13 million for fiscal year 1981; estimated deobligations were \$48.59 million for fiscal year 1982. (See table below.)

AID DEOBLIGATIONS

<u>Bureau</u>	<u>FY 81 actual deobligations</u>	<u>FY 82 estimated deobligations</u>
	----- (millions) -----	
Asia	\$ 20.264	\$ 11.08
Africa	7.714	14.79
Latin America	26.460	15.00
Near East	14.974	7.72
All other offices	<u>4.718</u>	<u>-</u>
Total	<u>\$ 74.130</u>	<u>\$ 48.59</u>

In the following sections, we explore how troubled projects and the reported deobligations were identified. We also describe the extent to which reported deobligations were attributed to corrective management actions or normal operating actions. Sections which follow also outline the need for more definitive policy guidance and procedures in identifying poten-

tial problem projects and in reviewing whether project funds should be deobligated.

HOW AND WHY DEOBLIGATIONS
HAVE OCCURRED

AID's portfolio supervision report, prepared annually, is intended to provide top-level AID management with conditions and trends needing management attention concerning AID-financed activities. In this report, the AID regional bureaus attempt to identify projects with possible implementation problems and suggest remedial actions which might include deobligations. We found, however, that the regional bureaus and missions could use more consistent quantitative and qualitative criteria for identifying and reporting on possible problem projects and programs.

Inconsistent reporting raises questions as to the comparability of data from year to year and the nature and extent of remedial actions which are most appropriate. Thus, we see a need for more consistent project analysis and reporting. We recognize that such analysis and reporting requires flexibility due to wide variations of development environments among AID bureaus. We believe, however, better indications of whether AID's portfolio performance is improving, or not, each year can be achieved by (1) consolidating and standardizing the various criteria which the regional bureaus currently use and (2) using this criteria to consistently report on the project portfolio status. The criteria for identifying problem projects includes

- projects more than 7 years old and less than 95 percent expended,
- projects more than 6 years old and less than 90 percent expended,
- projects more than 5 years old and less than 75 percent expended, and
- projects more than 3 years old with over one-third of total obligated funds unspent.

Other criteria of a more general or subjective nature includes

- lagging disbursements,
- borrower/grantee difficulties in complying with conditions and covenants,
- likely need for terminal date extension, and
- unsatisfactory progress toward achieving project purposes.

The inconsistent categorization of problem projects and the use of criteria which varies so widely to identify and report potential and/or actual deobligations indicates a need to rationalize and standardize the portfolio reporting and deobligation process. To illustrate further regarding deobligations, different project divisions, geographic offices, and field missions were asked to review projects and provide comments as to why projects should not be deobligated--based on such varying categories as

- project completion date not expired, some problems are suspected;
- project completion date not expired, achievement of project objectives is suspect;
- projects where terminal dates for disbursing authorizations have been reached; and
- projects where terminal dates for completion and disbursements have been reached.

The May 1982 AID report to the Senate Appropriations Committee states that AID expected that deobligations due to good project management actions would be substantially increased for fiscal year 1982. We do not believe this expectation has materialized. Based on bureau reports of actual deobligations, we observed that cited reasons for actual deobligations were primarily due to project completions rather than terminating projects early. Sources and criteria used by the bureaus for identifying actual deobligations vary considerably and included

- problem projects identified from semiannual portfolio reviews; and/or
- contacts with country-support officers, finance division chiefs, and other AID officials; and/or
- simple reference to deobligations recorded in the Agency Project Accounting Information System and loan activity reports.

NEED FOR MORE DEFINITIVE POLICY
GUIDANCE AND PROCEDURES

Existing AID deobligation guidance and criteria, based largely on adherence to established target dates for project completion, give AID the option to terminate projects and deobligate project funds if target dates are not met. Our analysis suggests that AID normally extends projects rather than exercising the deobligation option. In addition, as of September 30, 1982, there were over 100 projects in the AID portfolio with expired project dates and undisbursed balances. Under these

circumstances, AID generally has the option of deobligating most, if not all, unused project funds--an option not often exercised. Thus, if AID expects to increase the use of the deobligation option, we believe more definitive policy guidance and procedures are needed.

Loan project extensions

An official in the Office of Financial Management explained that their reports show loan terminal dates, as well as past extensions, so that bureau personnel can consider these facts in their decisions on further extensions. The staff may also send memos to bureaus alerting them that expired terminal dates require action, either to extend or deobligate.

Our analysis of AID's May 31, 1982, Status of Loan Implementation report shows the following.

--About 32 percent of the 406 loans listed, or 132 loan projects, had their Project Assistance Completion Date extended. This date, which is set in the project agreement, is the date that all AID-financed services under the project are to have been performed, and all AID-financed goods for the project are to have been furnished. Over 80 percent of the 132 loans (111) with an extended completion date were extended, some several times, ranging from 1 year to over 5 years.

--Almost 40 percent of the 406 loans listed, or 157 active loans, have had their terminal date for disbursements extended. The project completion date in the project agreement also sets in effect a terminal date for disbursements, usually set at 9 months following the project completion date. Beyond the terminal date for disbursement, AID may decline to accept requests for disbursement, and may initiate deobligation. Over 80 percent of the 157 loans (140) with an extended terminal date for disbursement were extended, some several times, ranging from 1 year to over 5 years.

Grant projects with expired and extended completion dates

AID's Project Accounting Information System produces a number of quarterly status reports for loans and grants. Our analysis of completion dates and undisbursed balances reported for grant projects as of March 31, 1982, showed 321, or 21 percent of all grant projects, had expired completion dates and undisbursed balances.

The Project Accounting Information System reports do not show grant projects' final disbursement dates or project completion-date extensions. Our analysis of the September 30, 1982, reports showed that of the 321 grant projects, 157 projects--about half--with expired completion dates had been extended. These extensions range from less than 1 year to over 3 years. Moreover, of the 157 projects with expired and extended project-completion dates, 31 of them had again expired as of September 30, 1982. An additional 83 grant projects with expired completion dates as of March 31, 1982, continued to have expired completion dates as of September 30, 1982 (and undisbursed balances).

Potential steps in the right direction

During the course of our work, we noted recent Agency guidelines and several suggestions which the AID staff had made. We believe that, if implemented by all missions and bureaus, these suggestions would result in better identifying and reporting on troubled projects and making judgements on remedial actions, including deobligations.

In November 1980, Near East Bureau Office Directors stated that if each bureau had a set of common criteria for a simple categorization of projects, a basis for a regular report to the Administrator, by exception, could be readily available. They stated that Bureau pipeline reviews should focus on identifying troubled projects, using a single set of criteria. In addition, a report could be prepared to the Administrator in a standard format for each troubled project; and, each bureau could report on projects which, by design, do not follow generally accepted disbursement patterns, such as projects with major procurements and large payments not due until the projects are nearly completed. With such reporting, the Bureau officials observed that the Bureau for Program and Policy Coordination would be able to meaningfully analyze the Agency pipeline. The division chiefs cited the following guidelines which bureaus might use to identify problem projects.

1. Projects which have not met one or more conditions precedent after one extension of the time allowed by the project agreement.
2. Projects in which one or more inputs (e.g., technical advisors) have not been provided 6 months after the planned date, and the delay will affect project completion.
3. Projects with Project Assistance Completion Dates (PACDs) which will not be completed within 6 months of that date.

4. Projects which require detailed revision because of changes in the project setting, faulty design, incorrect assumptions, or other unforeseen circumstances.

For the 1982 portfolio report, the Near East Bureau listed their projects into the following categories.

Category A: Projects newly authorized and projects operating within planned time and funding limits and not experiencing implementation

Category B: Projects with past problems but currently back on track and progressing satisfactorily based on revised time schedules, funding levels, modified goals and purposes, etc.

Category C: Projects presently experiencing implementation problems and/or time delays and requiring significant management attention in the coming months.

Category C projects were identified, using the following criteria:

- extended delays in accomplishing initial implementation actions, such as meeting conditions precedent;
- problems in delivery of critical inputs, especially contract services;
- substantial and repeated extensions of terminal dates and/or cost overruns;
- the failure of host-government agencies to meet major commitments;
- the failure of project inputs to produce planned outputs, such as poor contractor performance; and
- the failure of outputs to reach beneficiaries and/or produce the effects necessary to achieve project goals and purposes.

We observed that the other bureaus are not implementing similar portfolio categorization and reporting.

Most recently, AID's revised Handbook 3 has provided suggested guidelines for project reporting, including rating

project progress. However, we noted that the bureaus have also not implemented this suggested reporting and rating of projects, and future implementation by individual missions and bureaus is uncertain. The new guidance tasks the project officer with primary responsibility for effectively operating a project-monitoring system and for seeing that "Project Implementation Status Reports" are prepared. The Handbook also provides a suggested reporting format and notes that the project report may also include a "rating of project as to conditions and progress," including a point scale, which can be used by the bureaus to consistently compare implementation progress.

CONCLUSIONS

Criteria, guidance, and procedures for actually identifying, monitoring, and reporting on potential problem projects and deobligations varies at each bureau and may change each year. Inconsistent procedures and reporting raises questions as to the comparability of data from year to year and the nature and extent of appropriate remedial actions. We believe that better indications of whether AID's portfolio performance is improving, each year, or not, can be achieved by consolidating and standardizing the various criteria currently used by the regional bureaus and by using this criteria to report on project portfolio status.

The reasons usually cited for reported project deobligations continue to be based primarily on project completions and residual funds to be written off, rather than on terminating projects early because they are not functioning properly. The application of existing criteria, controls, and limits by bureaus and missions usually results in project extensions, rather than project deobligations. Increased use of deobligations as a management tool will require definitive deobligation policy guidelines and procedures.

In particular, when AID has the option of terminating potential problem projects or extending them, guidance is needed, for example, to help the AID staff identify

- candidates for potential deobligation by providing a consistent range of qualitative and quantitative factors which should be considered and
- projects and amounts to be actually deobligated by providing, for example, regional factors and country-specific factors which should be considered, including relevant political, security, and economic considerations.

We believe that the views expressed by the Near East Bureau and the recently revised Handbook 3 can potentially improve consistency in identifying, monitoring, and reporting on potential problem projects and deobligations.

RECOMMENDATIONS

We recommend that the AID Administrator establish more definitive policy guidelines and procedures for all bureaus and missions to use in identifying and reporting potential problem projects and in reviewing whether project funds should be deobligated. The policy and guidelines should include

- the development of a common set of agencywide criteria for categorizing the Agency's project portfolio and identifying potential pipeline problem projects by consolidating and/or improving the various criteria which the regional bureaus use; and
- the use of common set agencywide procedures for applying the criteria established, including (1) how and when the results are to be reported, (2) what reports and data the Washington staff should produce, and (3) how and when the AID staff should follow up on problem projects identified.

We have discussed the matters herein with cognizant AID officials and have taken their views into account, as appropriate. AID officials generally agree with our conclusions and recommendations. They do point out that project redesign is the preferred remedial action for potential problem projects and that deobligations, if considered, requires delicate and/or complex discussions between U.S. and host-country officials. We look forward to hearing what actions you plan to take in resolving the issues outlined in this letter. We appreciate the consideration and cooperation given our staff during the review and will be happy to discuss any of the matters contained in this letter with you. We are sending copies of this report to the Director, Office of Management and Budget, and to cognizant House and Senate authorization committees.

Sincerely yours,



Frank C. Conahan
Director

ERRATA SHEET

For the letter report GAO/ID-83-25, issued January 3, 1982, the recommendations to the Administrator, Agency for International Development, are on page 10, rather than page 9, as stated.