United States General Accounting Office

GAO

Report to Congressional Committees

December 1993

FOREIGN ASSISTANCE

Clearer Guidance Needed on When to Use Cash Grants

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

National Security and
International Affairs Division

B-254867

December 22, 1993

The Honorable Claiborne Pell
Chairman, Committee on Foreign Relations
United States Senate

The Honorable Patrick J. Leahy
Chairman, Subcommittee on Foreign Operations
Committee on Appropriations
United States Senate

The Honorable Lee H. Hamilton
Chairman, Committee on Foreign Affairs
House of Representatives

The Honorable David R. Obey
Chairman, Subcommittee on Foreign Operations,
Export Financing, and Related Programs
Committee on Appropriations
House of Representatives

This report responds to section 595(b) of the Foreign Operations, Export Financing, and Related Programs Appropriations Act of 1993 (P.L. 102-391), approved October 6, 1992, requiring us to review and report on cash payment assistance.

We are recommending that the Administrator of the Agency for International Development provide clear guidance to overseas missions on choosing among various forms of assistance, including cash grants, and that the missions fully document the reasons for their choice.

This report was prepared under the direction of Harold J. Johnson, Director, International Affairs Issues, who may be reached on (202) 512-4128 if you or your staff have any questions. Other major contributors are listed in appendix IV.

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Executive Summary

Purpose

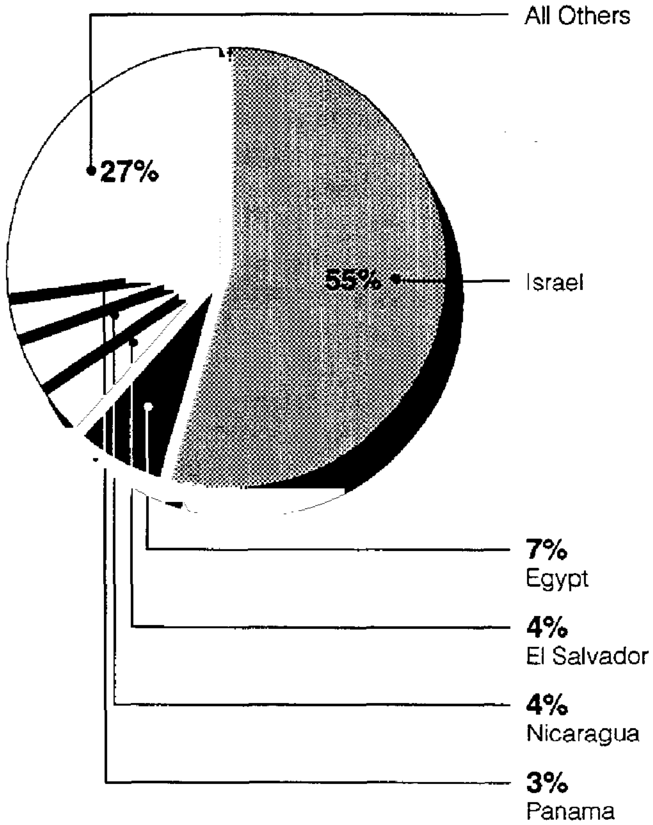
The Agency for International Development (AID) has provided over $9.9 billion in cash grant assistance during fiscal years 1989 through 1992. Section 595(b) of the Foreign Operations, Export Financing, and Related Programs Appropriations Act of 1993 requires GAO to examine and report on cash grant assistance provided under the foreign assistance program. Accordingly, GAO's objectives were to (1) analyze the use of cash grant assistance to purchase U.S. goods and services, (2) assess AID's systems for assuring accountability and monitoring of the use of cash grant assistance, and (3) evaluate AID's basis for deciding when to use cash grants rather than other forms of assistance to achieve U.S. objectives.

Background

AID provides cash grant assistance essentially for two purposes: (1) to support U.S. political or national security objectives and (2) to assist countries to undertake macroeconomic reforms or reforms in specific economic sectors. Cash grants ordinarily come from the Economic Support Fund appropriation account.

Of the $24.4 billion AID provided in economic assistance between fiscal years 1989 and 1992, over $9.9 billion was cash grants; over $1.1 billion was for Commodity Import Programs; and over $13.3 billion was for project assistance. Israel has been the largest recipient of cash grants, as shown in figure 1.

Figure 1: Top Five AID Cash Grant Recipients for Fiscal Years 1989-92



Note: Percentages of AID cash grant assistance between fiscal years 1989 and 1992 of $9.9 billion.

Results in Brief

AID prefers recipients of cash grants to use the money to purchase U.S. goods, but recipients are not required to do so. AID has reported that for fiscal year 1992, an estimated 83 percent of the cash grants (about $1.6 billion) was used by recipient countries to repay debt. AID also reported that about 17 percent was used to purchase goods, of which about one-half (or about $165 million) was used to directly purchase U.S. goods, but these data are of doubtful accuracy.

At the six missions GAO visited (Bolivia, Egypt, Ghana, Nicaragua, the Philippines, and Tanzania), AID generally maintained adequate accountability and monitoring controls as required by legislation and AID guidance for cash grant assistance. AID also has improved its monitoring of policy reform performance by recipient governments. However, the level of financial accountability for cash grants is less than that required for Commodity Import Programs and projects.

AID has not provided clear or consistent guidance to its overseas missions on which form of assistance—cash grants, Commodity Import Programs, or projects—would best meet U.S. objectives or under what circumstances one form of assistance should be preferred to another. Mission officials face competing demands about what mix of assistance modes to use. These competing demands include assuring that the form of assistance is consistent with the objectives, assessing the needed rate of funds disbursement, choosing between debt repayment and commodity purchases, and coordinating programs with other donors. Also, AID officials have different views on staffing levels needed to provide adequate accountability for the different types of assistance. Missions often propose and AID/Washington frequently approves faster disbursing and easier to administer cash grant assistance programs without a full consideration of the alternatives.

Principal Findings

Using Cash Grants to Purchase U.S. Goods

Countries that receive cash grants from AID are not required to use the money to purchase U.S. goods and services, but countries must give preference to such purchases under AID's guidelines. AID has reported that during fiscal year 1992, 9 percent of cash grants were used to directly purchase U.S. goods, but AID's data on this is of doubtful accuracy and reliability. According to AID, the primary use of cash grants in fiscal year

1992 (83 percent) has been to service the U.S. and foreign debts of recipient governments. AID also stated that this debt was incurred to purchase U.S. goods primarily by Israel and Egypt, whose cash grants are mandated by law. Whether these two countries would have purchased the U.S. goods had they not been assured of the mandated grant amounts in advance is unknown.

Meeting Accountability and Monitoring Requirements

The six missions GAO visited generally complied with the requirements for monitoring and accounting for cash grant assistance. However, GAO found that the requirements are more stringent for Commodity Import Programs and capital projects than for cash grants. The separate account requirements for cash grant assistance are less stringent than the competitive bidding, source and origin, and cargo preference requirements for Commodity Import Programs or projects. Therefore, the level of accountability that AID is required to achieve depends to some extent on how the assistance is provided.

GAO also found, in the six countries visited, that AID has improved its monitoring to better assure that recipient governments implement the economic reforms as a condition to receiving cash grant assistance. Missions have established improved monitoring and evaluation systems to assess host governments performance in meeting conditions before each disbursement of AID funds and have been increasingly willing to withhold or delay disbursements when the conditions set in the grant agreements have not been met. For instance, the Bolivia mission de-obligated $6.2 million in 1991 and $19.7 million in 1992 because the government did not meet coca eradication targets.

In meeting the accountability and monitoring requirements for each mode of cash grant assistance, GAO found that there is no agreement within AID about the level and composition of staff needed to meet these accountability requirements. Some AID officials argue that cash grants require less administrative time than Commodity Import Programs and projects, while other AID officials argue that there is little or no difference in the time required for cash grants and Commodity Import Programs when used for similar purposes. As a result, missions often face tradeoffs between (1) the level of accountability and monitoring that is required by a particular mode of assistance and (2) the perceived level and composition of staff needed to meet the requirements for each mode of assistance.

Choosing Alternatives

Missions' decisions to use cash grant assistance are based on considerations of how best to meet U.S. political/security objectives, pursue market-oriented economic policy reform goals, and address program management concerns. AID/Washington has not provided missions with specific criteria for making these decisions, nor has its oversight of those decisions reflected a systematic consideration of using Commodity Import Programs or noncapital and capital projects instead of cash grants. AID is now attempting to develop agencywide guidance for making such decisions.

Although agencywide guidance did not exist, AID's Africa Bureau in October 1992 and February 1993 issued specific guidance to its missions on when to use a particular type of assistance. According to this guidance, when commodity purchases are central to program objectives, a Commodity Import Program or project will be preferred. Cash grants will be used only where a recipient's foreign exchange system is, to some degree, already open and market-determined, where the country belongs to a currency union, or when the dollars could be used most effectively for debt repayment.

AID guidance requires that the reasons for using one form of assistance over another be clearly stated in program documents; however, the reasons were not always documented. In 7 of 34 cases, we could find no reason why one form of assistance was chosen over another. In the other 27 cases, GAO was able to determine the primary reasons for choosing cash grant assistance over other forms. They were (1) the consistency with the economic policy reforms being pursued (22 countries), (2) the method or rate of disbursement reflecting the legislative mandating of funds or the necessity to provide funds quickly (12 countries), (3) the need to use funds for debt service rather than commodities (15 countries), and (4) the relative administrative demands on the missions of cash grants rather than Commodity Import Programs or projects (12 countries).

There are differing perspectives within AID on which form of assistance to use, and Washington oversight of the choices did not reflect a full consideration of using commodity imports or projects instead of cash grants. Justifications were not submitted to Washington in all cases and in others, questions on the use of cash grants were not raised in time to affect the decisions. The result was a less than full consideration of the alternatives.

Recommendations

GAO recommends that the Administrator of AID

- provide clear guidance to missions on when and under what circumstances various assistance mechanisms, such as cash grants, Commodity Import Programs or projects are the most appropriate for accomplishing U.S. program goals and objectives and
- require missions to fully document their rationale for using one type of assistance mechanism rather than another.

Agency Comments

AID agreed with GAO's report and recommendations. AID has recognized the need for clearer, more consistent guidance and has been developing agencywide directives to replace existing handbooks in 1994. These directives will establish requirements for all agency programs, profile the different forms of assistance, and will include guidelines for assessing the most appropriate mode of assistance to use under what circumstances. The directives will also require operating units to document the rationale for their selection of which forms of assistance to use.

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Abbreviations

AID	Agency for International Development
CIP	Commodity Import Program

Introduction

The Agency for International Development (AID) provides cash grant assistance, Commodity Import Programs (CIP), and project assistance to developing countries to further U.S. national security, economic, and developmental objectives. Cash grants are generally used to provide short-term support, including budgetary support, to the host country's economy as a whole or to one of its principal sectors, for example, agriculture, education, and health. CIPs are designed to address the recipient country's balance of payments deficit by importing specific categories of commodities and related services. AID project assistance is used to finance inputs, including capital funds, personnel, training, and equipment, which address discrete long-term development needs such as institutional development and capital infrastructure.

While projects, particularly technical assistance and other noncapital projects represent the largest percentage of the U.S. foreign assistance program, a number of factors have led to an increasing reliance on cash grant assistance and a relative decline in capital projects and CIPs. This greater reliance on cash grants has been primarily related to U.S. political/security objectives and to economic reforms sought by the United States.

For fiscal years 1989 to 1992, U.S. cash grant assistance solely related to political/security objectives has mainly gone to Israel, with smaller amounts to Turkey and Portugal. The United States has not pursued development reform objectives in these countries. The remainder has gone to about 56 countries where the United States is pursuing political/security and/or development objectives, including Egypt.

Forms of Assistance

Cash grant assistance is provided in the form of cash transfers and sector assistance programs, both of which are considered by AID to be "nonproject" assistance. Other forms of nonproject assistance are CIPs and some forms of food aid. Cash grant assistance programs are funded from the Economic Support Fund, Development Assistance Fund, Development Fund for Africa, and the Special Assistance Initiative. Cash grants funded from the Economic Support Fund can be used to finance macroeconomic policy reform programs, whereas the Foreign Assistance Act of 1961, as amended, provides that cash grant assistance programs funded from other resources can be used to support sectoral policy reform programs. Special Assistance Initiative funds are used to support Eastern European countries and the Multilateral Assistance Initiative program in the Philippines.

The primary objectives for cash grant programs include national security, support of macroeconomic policy reforms, general economic and social stability, and development. These objectives are pursued by providing dollars that can be used to (1) repay debt owed to the United States or international financial institutions and (2) finance imports from the United States or other countries. In some cases, cash grants are provided as emergency assistance such as the case in Ethiopia where the new government faced a severe shortage of foreign exchange.

Cash grants provided under sector assistance programs can also repay debts or finance imports but are designed to address policy constraints and promote efficiency in specific economic sectors. Sectoral policy constraints would include such things as subsidies and inappropriate pricing policies for agricultural commodities, electric power, water and sewer services, and the continuation of inefficient government monopolies in these and other sectors.

CIPs are designed to address the recipient country's balance of payments deficits by importing specific categories of commodities and related services. Congress has indicated that CIPs should also support development activities in recipient countries. This requires that AID target the commodities at those activities supporting its development strategy in the recipient country. For example, in some countries, AID provides the necessary resources to promote private sector growth in the industrial or agricultural sectors through enterprise and microenterprise development. A CIP may be used for either public or private sector procurement; however, until recently, AID used CIPs primarily for procuring public sector commodities.

Most cash grant assistance and CIPs generate local currency in one of three ways: (1) when dollars are purchased by the private sector and used to import commodities; (2) when dollars are used by the recipient government to import commodities which, in turn, it sells to the private sector or to a quasi-private entity, such as a self-financing parastatal body; or (3) when AID requires a deposit or set aside of local currency by the recipient government as a condition or term of the assistance agreement. Any local currency generated must be deposited into a separate account for joint programming by AID and the host government and is commonly used to help meet the host country's contribution to AID-funded projects. In cases where the dollars are used to service external public sector debt or when commodities are imported by, and for the use of, the recipient government, local currency may not be generated.

Project assistance includes loans and grants for discrete long-term development needs such as institutional development and capital infrastructure. Most of AID's project assistance is provided in the form of noncapital assistance and, to a lesser extent, capital projects. Examples of project assistance are the training of teachers or health workers, the funding of related facilities and equipment, or the actual construction of more capital intensive capital projects like water and sewage facilities, power plants, telecommunication systems, roads, and bridges. Most larger capital projects are found in only a few countries, including Egypt, the Philippines, and southern Africa.

Trends in AID Assistance

Changing conditions within recipient countries and growing resource constraints within AID impact the trends in cash grant assistance. While all forms of projects have traditionally represented the largest percentage of AID's budget allocation, a number of factors has led to an increasing reliance on cash grant assistance and a relative decline in capital projects and CIPs. The relative decline in capital projects reflects a 1970s congressional mandate that AID focus on directly meeting basic human needs, while leaving larger infrastructure projects to other donors. There is also a clear trend toward sector assistance programs associated with sectoral policy reforms rather than capital projects.

In 1979, Israel, Turkey, Jordan, and Nicaragua were the only countries receiving cash grants. By 1992, AID was providing cash grants to about 38 countries in 5 regions of the world, having greatly expanded the use of this mechanism in Africa and Latin America. By contrast, the use of capital projects and CIPs has declined. According to data obtained from AID's Capital Projects and Engineering Office, in 1984, capital projects represented about 20 percent of the total AID budget. By 1992, they represented only 6 percent. Likewise, in 1983, CIPs represented about 11 percent of the total AID budget. By 1992, they represented only 5 percent.

In the 1990s, there is a renewed interest in capital projects as an element of AID's assistance program. Currently, AID is seeking ways to increase funding for developmentally sound capital projects to be planned and constructed by U.S. firms, potentially resulting in increased U.S. trade worldwide and reflows to the United States.

As shown in table 1.1, from fiscal years 1983 to 1992 the United States provided about $24.3 billion in cash grants, $4 billion in CIPs, and

$29.5 billion in projects. Israel and Egypt have been the largest recipients of U.S. cash assistance during this period. Together, they receive approximately $1.4 billion annually in cash grants funded with Economic Support Funds. Appendixes I and II provide a list of regions and countries receiving cash grant assistance from fiscal years 1989 to 1992.

Table 1.1: Trends in AID Assistance for Fiscal Years 1983 to 1992

Dollars in billions

	Fiscal year										
Assistance Mode	**1983**	**1984**	**1985**	**1986**	**1987**	**1988**	**1989**	**1990**	**1991**	**1992**	**Total**
Cash Grant Assistance											
Actual obligations	$1.6	$1.6	$3.5	$3.5	$2.3	$1.9	$2.2	$2.7	$3.1	$1.9	**$24.3**
Percentage of AID program budget	36	33	52	52	40	39	41	43	45	32	
CIPs											
Actual obligations	$0.5	$0.6	$0.6	$0.4	$0.4	$0.3	$0.4	$0.3	$0.2	$0.3	**$4.0**
Percentage of AID program budget	11	12	9	6	7	6	7	5	3	5	
Project Assistance[a]	$2.4	$2.7	$2.6	$2.8	$3.0	$2.7	$2.8	$3.2	$3.6	$3.7	**$29.5**
Percentage of AID program budget	53	55	39	42	53	55	52	52	52	63	
AID program budget total[b]	**$4.5**	**$4.9**	**$6.7**	**$6.7**	**$5.7**	**$4.9**	**$5.4**	**$6.2**	**$6.9**	**$5.9**	**$57.8**
Percentage Total	**100**	**100**	**100**	**100**	**100**	**100**	**100**	**100**	**100**	**100**	

[a]The total represents capital and sector project obligations combined because AID does not have consistant data to show a breakdown for fiscal years 1983 to 1992.

[b]The data represent Development Assistance, Development Funds for Africa, Economic Support Funds, and Special Assistance Initiative program funds for fiscal years 1983-92. AID's total program budget amount does not include Foreign Service Retirement and Disability, Trade Credit Insurance Program, or Operating Expenses.

Objectives, Scope, and Methodology

Section 595 (b) of the Foreign Operations, Export Financing, and Related Programs Appropriations Act of 1993 (P.L. 102-391), approved October 6, 1992, requires that we examine and report on cash grant assistance provided under the foreign assistance program. Our specific objectives were to (1) analyze the use of cash grant assistance to purchase U.S. goods and services, (2) assess the adequacy of cash grant accountability and monitoring systems, and (3) evaluate AID's basis for deciding to use cash grants versus other forms of assistance to achieve U.S. objectives.

We reviewed legislative history, AID cash grant assistance guidance, and special studies and evaluations in Washington, D.C. We also obtained data on AID obligations for cash grants, CIPs, nonproject sector assistance, and regular projects from AID/Washington for fiscal years 1988 to 1992. Based on the data obtained in Washington, D.C., we selected countries to visit to review the management of cash grant assistance programs in a variety of conditions, including both small and large programs in various regions of the world used to finance imports or to repay international debts.

In the six countries we chose—Egypt, Bolivia, Ghana, Nicaragua, the Philippines, and Tanzania—we reviewed the program design and approval documents, bilateral agreements, management reports, financial records, audit reports, and other documents for cash grant assistance programs. We interviewed AID, U.S. Embassy, and host government officials. In some of the countries we visited, we met with International Monetary Fund and World Bank representatives. The issues we discussed during our meetings included

- the overall U.S. objectives for agreeing to provide assistance to the country,
- the reasons for the choice of cash assistance over CIPs or projects,
- advantages or disadvantages of cash grant assistance compared to CIPs or projects,
- AID's accountability and monitoring of cash grant assistance, and
- the actual use and purpose of the form of assistance provided.

In addition to the six countries visited, we obtained information on the amounts and uses of cash grant assistance to 31 additional countries. We conducted our review from November 1992 to June 1993 in accordance with generally accepted government auditing standards.

The Uses of Cash Grants

AID's cash grants are legally exempt from most U.S. procurement and shipping requirements governing other forms of assistance. However, according to AID's policy guidance, such funds should be used, to the extent possible, (1) to finance imports from the United States or other eligible countries and/or (2) to service debt owed to the United States or other eligible financial institutions. It is difficult to determine the actual extent to which such funds are used to finance imports from the United States. According to AID, about 83 percent of the fiscal year 1992 funds were used to repay debts and 17 percent of the funds were used to purchase commodities. About 9 percent were used to purchase goods from the United States alone. However, as we recently reported, AID's Buy America Reporting System is of doubtful accuracy and reliability because of significant data and methodology limitations.[1]

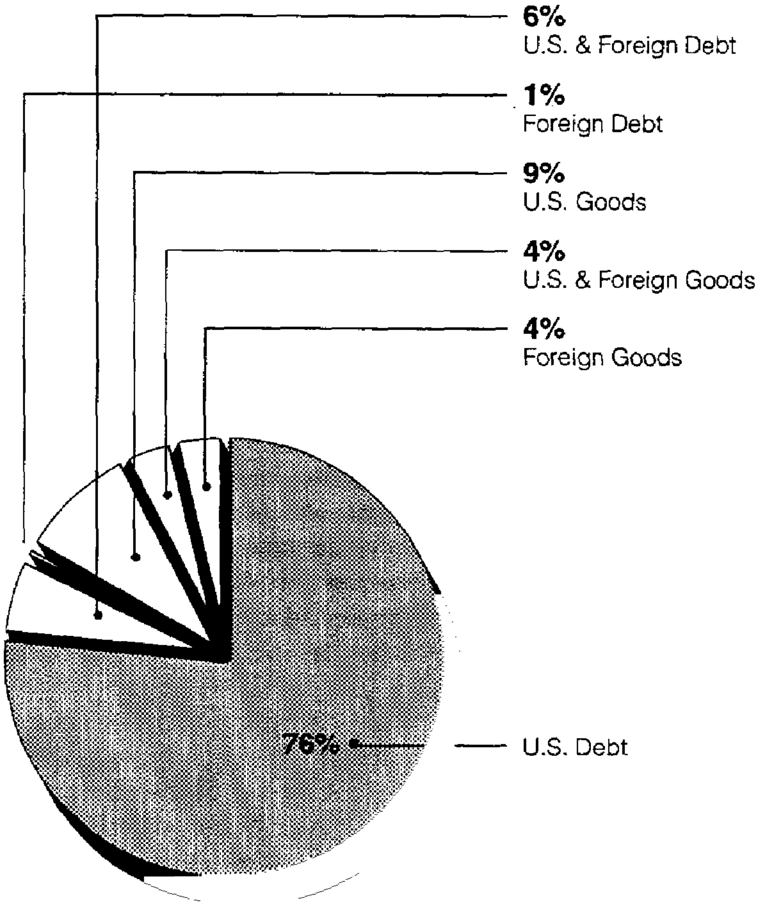
As noted in AID cash grant guidance, statutory provisions[2] that apply to project assistance and CIPs (e.g. cargo preference, strict source/origin rules, and competitive bidding) do not apply to cash grants and nonproject sector assistance programs. Nevertheless, AID guidance states that its first preference is to finance the purchase of U.S. goods with cash grant or nonproject sector assistance dollars. Debt service is an alternative in some instances, as is a combination of import financing and debt service.

In fiscal year 1992, AID implemented the Buy America Reporting System to provide data to Congress on how much economic assistance dollars flow back to the United States through the procurement of U.S. goods and services. This directly reflects congressional interest in the extent to which alternative forms of assistance promote development and U.S. exports. According to AID's "Buy America" data for fiscal year 1992, about \$1.9 billion was disbursed in the form of cash grants, 83 percent was used to repay debt and 17 percent to purchase goods. Funds to repay debts solely to the United States were 76 percent of the total, and those used to purchase goods solely from the United States were 9 percent of the total. (See fig. 2.1.)

[1]Foreign Assistance: Accuracy of AID Statistics on Dollars Flowing Back to the U.S. Economy Is Doubtful (GAO/NSIAD-93-196, Aug. 3, 1993).

[2]Section 571 (b)(2) of the Foreign Operations, Export Financing, and Related Programs Appropriations Act of 1993, P.L. 102-391 [H.R. 5368], 106 Stat. 1633, approved October 6, 1992.

Figure 2.1: Uses of Cash Grants: AID's Buy American Reporting System for Fiscal Year 1992



In our August 3, 1993, report on AID's Buy America Reporting System, we concluded that the accuracy and reliability of that system is doubtful because of significant data limitations and the methodology used. Our current review confirmed that conclusion. For example, the Buy America report on the Philippines showed about $104.6 million for debt repayment and $11.3 million in goods purchased by cash grant funds while separate account data showed all cash grant funds were used to repay debts to international financial institutions. In Pakistan, the Buy America report showed $12.3 million of cash grant funds used for the purchase of commodities while separate account reports indicate that all cash grant funds were used for debt repayments.

Not only is the Buy America data of questionable accuracy and reliability, but it also may be misleading by understating the amount of cash grants used to purchase goods. We found that for Israel and Egypt most of the funds used to service debts were for the repayment of U.S. loans and guaranteed loans that financed the purchase of U.S. military and commercial goods in the case of Israel and U.S. agricultural products in Egypt. Cash grants for both countries are mandated by law. Therefore, both countries know in advance the amount of cash grant funds they will be receiving. As such, they can incur debts they might not otherwise have incurred to import goods with the full knowledge that they will have the funds to repay those debts. Israel and Egypt received about $5.3 billion in cash grants to repay such loans between fiscal years 1989 and 1992.

Program and Financial Accountability and Monitoring

AID performs two types of accountability and monitoring functions. First, program accountability and monitoring involves ensuring that U.S. objectives and reform conditions are met. Second, financial accountability and monitoring is related to proper accounting and reporting on the use of the dollars provided and any local currency generated. Israel, Turkey, and Portugal receive cash grants without having to meet the economic reform conditions required of most other recipients.

At the six AID missions we visited, we found that they appeared to be following both forms of accountability and monitoring controls as prescribed by legislation and AID guidance for each mode of cash grant assistance. However, the controls are more stringent for CIPs and projects than for cash grants. Therefore, the level of accountability that AID is required to achieve depends, to some extent, on the form of assistance chosen.

We also found that the level and composition of overseas staff available to administer the programs affects the mode of assistance chosen. AID officials noted that in choosing the mode of assistance, the missions often face tradeoffs between (1) the level of accountability and monitoring that is required by a particular mode of assistance and (2) the perceived level and composition of staff needed to meet the controls for each mode of assistance. However, we found that there is no agreement within AID on the level and composition of staffing needed to implement its assistance programs. This is because AID has not assessed its staffing needs for each mode of assistance. Thus, missions are making these tradeoffs individually and not necessarily using valid or consistent criteria.

Program Accountability and Monitoring

According to AID guidance for cash grant assistance, program accountability and monitoring involves ensuring that U.S. objectives and reform conditions are met before funds are disbursed. This guidance also contains the program accountability and monitoring controls for each mode of assistance and whether the funds will be used to repay debts or purchase commodities. Cash grants used to import commodities are exempt from the procurement and special procedures for CIPs.

Our review of the six country program strategies, program agreements, memorandums of understanding, and program implementation letters showed that AID is increasingly using conditions precedent to the disbursement of funds in leveraging host government macroeconomic and sectoral policy reforms.[1] AID has also used improved monitoring and evaluation systems to monitor host governments' progress in achieving reforms and meeting conditions precedent. For example, in all of the countries we visited, the missions have established procedures to monitor and review the host governments' progress in achieving economic reforms. AID officials in Egypt and Ghana told us that AID mission representatives frequently meet with host government officials, implementing agencies, and other donor representatives to ensure that satisfactory progress is being made. A program review team reviews the information provided by the host government as evidence of the fulfillment of conditions precedent. The teams then forward the results to the mission director who makes the final decision on whether or not the host governments' progress warrants release of the program funds.

We also found, in all the countries we visited, that AID is increasingly willing to withhold funds when host governments do not fulfill all of the required conditions. For example, in the Philippines, the mission withheld the first tranche of funds under its cash grant program funds because the host government met only 13 of the 16 required conditions related to liberalization of shipping routes and increasing the number of businesses paying value added tax. In Bolivia, the mission de-obligated $6.2 million in 1991 and $19.7 million in 1992 because the government did not meet coca eradication targets. In some cases, AID extends the deadline for meeting the conditions if it feels that the government is making satisfactory progress toward achieving policy reforms. Such was the case in Ghana when the government lacked sufficient evidence that it had expanded its essential drug list to include all types of oral contraceptives.

Financial Accountability and Monitoring

According to legislation and AID's guidance, AID is responsible for proper accounting and reporting on the use of the dollars provided and any local currency generated. These guidelines also provide the financial accountability and monitoring controls for each mode of AID assistance. The controls for cash grants state that, for all cash grant programs, regardless of the amount or funding source, a separate account or accounts must be established for dollar deposits and the use of funds tracked. Under CIPs, the host government is responsible for procuring the commodities and establishing accounting and monitoring systems to track the use of AID funds. In the case of project assistance, the standard provisions of project agreements between AID and the host country require

[1]Conditions precedent are a set of actions agreed upon by AID and the host country government, which when completed, triggers the disbursement of funds. Examples of conditions precedent include eliminating tariffs or liberalizing import and export trade regimes.

the host country to maintain, in accordance with generally accepted accounting principles, books and records relating to the project to show the receipt and use of goods and services financed by AID. In all cases, host governments are required to furnish AID missions financial reports on the status of AID funds and perform audits of the project or program accounts.

For cash grants that are used for external debt financing, AID is responsible for ensuring that host governments use the funds for eligible debts such as official debt to the U.S. government and international financial institutions. When using cash grants to import commodities, AID is responsible for ensuring that the funds are used for commodities, but is legally exempt from procurement and standard financing procedures such as the authorized source and origin, competitive bidding, or U.S. cargo preference. For CIPS, AID must certify that each transaction meets controls for commodity eligibility, competitive bidding, authorized source and origin, and the use of U.S. shipping.

Exemptions to separate account controls are allowed for specific programs where separate accounts and dollar tracking might not be appropriate. These exemptions can be made for countries where

- the foreign exchange allocation system is open, nondirected and functioning on market principles;
- there are well-run foreign exchange auctions and other free-market mechanisms;
- as members of monetary unions such as the West African Monetary Union, foreign exchange is shared by all members of the unions; and
- there are open import licensing systems that are sufficiently broad so as not to restrict imports of goods required to achieve the goals of the assistance program that AID is supporting.

For each country, we reviewed program agreements, management reports, financial records, and audit reports to determine if AID and host governments complied with the financial accountability and monitoring controls prescribed by congressional legislation and AID guidance. We also obtained financial reports for 15 additional countries. We found that AID generally requires that host governments establish separate accounts as a condition precedent for the initial disbursement of AID funds. However, when providing cash grants, AID is often unable to track the funds after they are disbursed into the separate accounts, thereby relying on host government systems for information on the end use of funds.

AID/Washington and mission officials also point out that the implementation procedures required for each mode of assistance provide greater accountability and monitoring for projects and CIPs than for cash grants. For example, projects and CIPs provide greater assurances that (1) the funds are used as intended and (2) there is a positive identification between AID financing and imports from the United States. CIPs and projects generally require competitive bidding by suppliers, are more stringent in requiring that the United States be the source and origin of the goods and services, and give preference to U.S. merchant ships in carrying any related cargo.

We found that AID is increasingly using independent audit firms to assess and audit the integrity of host government accounting and financial systems. While mission and independent assessments of cash grant programs indicated that host governments appeared to be complying with AID's reporting controls, they were often slow in providing the required information.

Although AID appears to meet the accountability and monitoring controls prescribed by legislation and AID guidance for cash payment assistance, our July 1993 report on Food Aid noted a potential weakness in AID's resource accountability because of unclear guidance. Specifically, we found that AID guidance for monitoring local currency did not specify whether missions are responsible for monitoring only the initial use or repeated uses of local currencies when these funds are used for revolving loan projects.[2] AID responded that it believed its current guidance on this matter was adequate, although subsequent uses of the local currency were not addressed in this guidance.

AID's Mixed Perceptions About the Administrative Controls of Cash Payment Assistance Modes

Of the 27 country proposals that cited reasons for choosing cash grants, 12 cited greater and more stringent administrative controls of CIPs and projects as one of the reasons for choosing cash grants over the other modes of assistance. See chapter 4 for more details. However, in interviewing AID/Washington and mission officials, we found that, while most AID officials agree that projects are by far the most staff intensive of assistance modes, there are different perceptions about the relative level and composition of staff needed to administer cash grants and CIPs.

[2]Food Aid: Management Improvements Needed to Achieve Program Objectives (GAO/NSIAD-93-168, July 23, 1993).

Several AID officials indicated that the overall administrative controls (i.e., accountability and monitoring) for cash grants involve less administrative time than CIPs. Cash grants are legally exempt from the stringent procurement and financing procedures required for CIPs and projects such as competitive bidding, authorized source and origin, and U.S. cargo preference. Such grants thereby require less AID and host government administrative time than CIPs when used to import commodities. Also, where host government systems are reliable and transparent, cash grants require a minimal amount of AID administrative involvement.

Some AID officials have argued, however, that once a CIP is established in a developing country, the staffing controls are not any greater than for cash grants and less than for projects. Moreover, some simple CIPs have been implemented in countries with minimal U.S. direct hire AID presence. For example, AID officials noted that a CIP in Morocco that disbursed $10 million a year from 1968 to 1973 was monitored by only two aid employees, one an American and the other a foreign national. AID officials noted that CIPs similar to that in Morocco or smaller do not necessarily require a full-time commodity management officer to administer the program. They also point out that support is available from AID/Washington and from regional offices for missions lacking full-time commodity management specialists. Also, in some cases, where U.S. banks issue letters of credit to host government suppliers for commodities, the U.S. banks almost totally run the program with AID/Washington certifying the transactions, thereby requiring very little or no involvement by AID missions.

We also found that differing perceptions about the level and composition of staff needed to meet the controls for each mode of assistance generally come from a lack of experience and knowledge by mission staff about the advantages of AID assistance modes, particularly with using CIPs in the private sector. AID officials acknowledge that missions have little experience or knowledge about the advantages of private sector CIPs because, for more than two decades, CIPs were primarily used for public sector commodities. AID mission officials that we interviewed often perceived private sector CIPs as (1) more cumbersome to administer because of the procurement and standard pricing procedures and (2) counterproductive to AID's objective of promoting free markets. According to one AID official, in practice, a private sector CIP, when used to purchase simple commodities such as wheat, is no more cumbersome than importing the same commodity under a cash grant. However, when using a private sector CIP to import commodities such as complicated medical equipment, the required administrative time significantly increases.

AID officials told us that, in meeting the accountability and monitoring controls for each mode of cash grant assistance, the missions often face tradeoffs between (1) the level of accountability and monitoring that is required by a particular mode of assistance and (2) the perceived level and composition of staff needed to meet the controls for each mode of assistance. Mission officials in Egypt believe they have too few U.S. staff available to oversee too many programs and projects. According to the 1992 country strategy document, the mission has reduced its U.S. direct hire personnel since 1985 from 124 to 98 or 21 percent without commensurate reductions in the program funding level of over $800 million. Because of these staff reductions, the mission has eliminated programs in some sectors such as basic education to increase accountability and monitoring of other programs such as its $200-million sector reform program. Mission officials in the Philippines also noted that, while funding levels increased immediately after 1988 to support foreign policy objectives, staffing levels did not grow commensurately, thus making its work load per staff ratio among the highest of all missions.

In June 1993, we reported that while direct-hire staff reductions challenge AID's ability to manage its activities, AID had not effectively used or managed its work force to provide accountability and oversight over its programs and projects. Specifically, the report showed that (1) work force planners were constrained by the absence of basic information on the work force; (2) AID did not have a good picture of the work force in terms of its size, components, and skills; (3) mission reports on staff composition were not standardized so data among missions could not be compared in a meaningful way; and (4) AID had not performed work load analysis to determine what work needs to be done, what skills will be required to accomplish the work, and how the demand for staff and skills matches the current staff and skill profile. In addition, AID also lacks standards for making staff allocations among missions.

AID officials generally agreed with our report and pointed to several recent efforts to improve work force planning, including baseline data collection and the development of new systems to more proactively manage human resources. The integration of work force planning and management into the larger restructuring of the agency could help AID address such questions as the level of staffing needed to adequately account for such cash grant assistance compared to CIPs or projects.

Choosing Alternative Forms of Assistance

AID overseas missions have wide latitude in choosing which forms of assistance to include in program and project plans. However, AID has not provided clear or consistent guidance on how the missions should make that choice. AID also has not maintained a systematic record of how alternative forms of assistance have been considered in developing country assistance programs even though its regulations require it to do so.

We found a general preference among AID missions for cash grant assistance over CIPs and projects reflecting mission decisions on how best to meet U.S. political/security objectives, development policy reform goals, and program management concerns. Specific reasons included perceived advantages in pursuing economic reforms, easier and more rapid disbursement of funds, using dollars to service country debts, and the relative demands on mission staff. We also found that the choice of which form of assistance to use and the AID/Washington review of these choices did not always reflect a systematic consideration by AID decisionmakers of the advantages and disadvantages of alternative modes of assistance.

Unclear and Inconsistent Guidance on Cash Grant Assistance

AID has not provided clear or consistent guidance to its overseas missions on how to determine which mix of assistance (i.e., cash grants, CIPs, or projects) would best meet U.S. objectives, including policy reform objectives. AID policies and procedures are described in a series of handbooks first issued 18 years ago. Over the years, these handbooks have been updated and revised with widely varying degrees of thoroughness but with less frequency in the last several years. Updates and revisions to these handbooks have focused more on implementing accounting requirements for Development Assistance and Economic Support Fund programs than for determining when to use cash grant assistance or other forms of assistance. AID is now engaged in revising and updating its policy guidance manuals, including those for cash grant assistance, but differing perspectives within AID on the use of such assistance remain.

The original AID policy guidance, dating back to 1975, specifically stipulated that cash grants are generally to be used to provide budget support usually under emergency conditions and then only when the particular AID purpose cannot be accomplished in any other manner. In addition, cash grants were not to be used as a method to finance commodities. This guidance still remains in the current AID handbook.

In 1987, AID amplified its policy guidance on Economic Support Fund funded cash grant assistance incorporating the legal requirement to establish separate accounts to track the use of the funds and stipulated what the eligible and ineligible uses of the funds would be. Unlike the earlier guidance, the amplified guidance states that AID's preference is to use the dollars for U.S. imports, directly contrary to the earlier guidance that stipulated that cash grants were not to be used to finance commodities. Debt service is cited as an alternative. In 1990, this guidance, which included the legal exemption of cash grants from the procurement and shipping regulations usually associated with project assistance and CIPs, was extended to cover Development Assistance and Development Fund for Africa funded cash grant assistance, and is the current guidance.

This guidance set forth conditions for determining the priority uses of the dollars. It stated that imports, with a priority for U.S. imports, would be the preferred use of the funds where a recipient government controlled foreign exchange allocations and exchange rates and no substantial movement to market-oriented systems was underway. Where such movement was underway, AID would allow use of the funds under foreign exchange auction arrangements as part of a multidonor effort to foster the trend toward market-oriented allocations and rates of exchange. In certain instances, funds could be used to pay external debts where those debts were a significant barrier to development and particularly where such payments would leverage additional flows of development finance from other donors.

While the above guidance stipulated what the cash grant funds could be used for, it did not provide a basis for choosing between cash grants and other forms of assistance. The absence of clear agencywide guidance and inconsistencies in what guidance was available has also been noted at the mission level. The U.S. mission in Egypt, in January 1993, issued its own "Mission Order" on nonproject assistance noting that while some guidance on the use and procedures for cash grants and CIPs is provided in AID's handbooks, only limited and outdated guidance exists for sector cash grant assistance. Mission officials in Tanzania noted that the guidance issued by the Africa Bureau, incorporating a preference for but no requirement that cash grant funds be used to finance imports from the United States, "appears somewhat inconsistent" with guidance from AID's Directorate for Operations stressing Buy America objectives. As such, mission officials told us they were unsure of what Washington wanted in the way of relative emphasis on directly promoting U.S. commercial interests through procurement requirements. These same officials also noted that, in general, AID and the Africa Bureau guidance has offered projects, CIPs, and cash grant programs as alternatives, but has not clearly indicated which is preferable. This leaves each mission to resolve on its own what form of assistance to choose.

Africa Bureau Guidance

The Bureau for Africa first circulated guidance on nonproject assistance under the Development Fund for Africa for use by the Africa Bureau in AID/Washington and overseas in July 1988. After extensive discussions and refinement, the Bureau formally issued the guidelines in October 1992. In February 1993, the Africa Bureau modified its procurement guidelines regarding cash grant assistance. The Latin America and Caribbean Bureau developed similar preliminary guidance in February 1991, which currently remains in draft form.

The Africa Bureau's attempt to formulate its own guidance followed the 1987 World Bank announcement of a Special Program of Assistance for the 24 debt-distressed, low-income countries in Sub-Saharan Africa, and the creation of the AID Development Fund for Africa in December 1987. A key objective of the Special Program was to encourage recipient countries to establish unified, market-related systems for foreign exchange allocation. Under program guidelines, cash grants were not to be tied to the purchase of donor country goods and services when and where donors were satisfied that the grants would be used effectively and fairly.

The Africa Bureau nonproject assistance guidance stated that the decision as to the best mode of delivery and whether sector nonproject assistance is appropriate at all, would largely depend on a combination of factors that are country, sector, mission, and time specific. The guidance further states that while there is no definitive guidance as to when it is more appropriate to use a CIP versus a cash disbursement mechanism, many factors must be weighed. The factors include the use of the dollar or dollar-financed resource, the host country's foreign exchange system, and the host country's ability to manage funds. For example, if the most appropriate use of the assistance were to finance debt payments, it would not make sense to provide the resource as a CIP. If the host country's foreign exchange system is market-determined and is fully accountable and transparent, then using a cash grant would support that system by allowing AID resources to flow through it.

The Africa Bureau issued further guidelines on procurement in February 1993, which noted that prior guidance, among other things, had resulted in occasional failures to adequately pursue U.S.-source procurement involving cash financing of commodity imports. This guidance was designed to maximize U.S. procurement and made more explicit the conditions for choosing between forms of assistance.

Where specific commodities are critical to sector reform objectives then a project or CIP, not a cash grant, is to be used. Specific commodities would not require disbursing cash to recipients and U.S.-source procurement would be maximized by using project or CIP procedures.

Cash programs would be used selectively, preferably only where the host country's foreign exchange system was, to some degree, already transparent and market-determined, the country belonged to a currency union, or when the dollars could be most effectively used for debt repayments. When the host country's foreign exchange system was government managed, cash grants would not be used. The only exceptions would be where cash grants were essential to meeting sector reform objectives. Under these exceptions only general categories rather than specific imports could be called for and measures would have to be taken by the mission to restrict any financing of imports from other donors that were tying their cash assistance. The choices on what form of assistance to use in Africa noted in this report were made before the October 1992 and February 1993 guidelines.

While this guidance provides a much clearer indication of when to choose among alternative forms of assistance, no guidance can be expected to resolve all the issues in specific cases. For example, mission officials in Tanzania stated that the Africa Bureau's new guidance requiring that the recipient's foreign exchange system already be transparent and market-determined and that only general, rather than specific, imports could be financed, would likely have precluded the adoption of its present cash grant program. As a result, the United States would not have been able to be a leading participant in promoting the reform of Tanzania's government controlled foreign exchange and import licensing systems, but would have been forced into the role of a follower.

The Latin American and Caribbean Bureau circulated draft guidance on nonproject assistance in February 1991, which noted that previous AID guidance was incomplete and out of date. However, the Bureau offered little guidance on the choice of assistance mode. It noted only that the CIP mechanism is generally, but not always, deemed appropriate where government foreign exchange allocation procedures are judged to lack transparency or where a more directed form of import intervention is necessary. The Bureau noted that CIPs were not used in Latin American or Caribbean countries.

Choice of Alternatives

Among those countries where U.S. political/security objectives are strong, but where there are no major economic reform objectives, cash grant assistance is provided as the simplest method to quickly transfer resources. For example, Israel, Portugal, and Turkey receive cash grants with little or no conditionality. AID does not require justification of the choice of cash grant assistance programs to these countries.

The picture is more complex where the United States has strong political/security objectives as well as economic reform goals. For example, a mixture of cash grants and major capital projects are included in the Egypt and Philippines assistance portfolios. Egypt also has the largest CIP of any AID recipient. In Nicaragua, the economic situation in 1990 led mission officials to choose cash grants as the fastest way to achieve a rapid infusion of foreign exchange into the economy.[1] In Bolivia, mission officials thought the combination of antinarcotics and economic reform goals were best obtainable through the use of cash grants.

We reviewed records for 34 countries that received cash grant assistance from fiscal year 1989 through fiscal year 1992. Among these, we found 27 cases that stated reasons for the selection of cash grant assistance over CIPs or capital projects. In seven cases, we could find no record of why one form of assistance was chosen over another. AID does not maintain a complete central record of its cash grant program documents nor has it assured that the reasons for the choice of assistance mode be clearly documented, despite AID's guidance that these reasons be set out in program planning documents.

Among the 27 cases where the reasons for choosing cash grants were stated in documents or obtained by interview, we found that the primary reasons were (1) the consistency with the economic policy reforms being pursued, (2) the method or rate of disbursement reflecting the earmarking of funds or the necessity to provide funds quickly, (3) the need to use the funds for debt service rather than directly procuring commodities, and (4) the relative administrative demands on the missions of cash grants versus other forms of assistance. The cases are summarized in table 4.1.

[1] Aid to Nicaragua: U.S. Assistance Supports Economic and Social Development (GAO/NSIAD-92-203, Aug. 14, 1992).

Table 4.1: Primary Justifications for Using Cash Grants

Region/ country	Policy reforms	Method/rate of disbursement	Debt service priority	Administrative requirements
Africa				
1. Benin	X	X		
2. Burundi	X			
3. Chad	X	X		X
4. Djibouti			X	X
5. Ethiopia	X	X	X	X
6. Gambia	X	X	X	X
7. Ghana	X	X		X
8. Madagascar	X	X	X	
9. Mali	X			
10. Namibia	X			
11. Senegal	X		X	
12. Tanzania	X			X
13. Togo		X	X	X
14. Uganda	X		X	
15. Zambia	X		X	
16. Zimbabwe	X			
Asia				
17. Pakistan	X			X
18. Philippines	X		X	X
Latin America and Caribbean				
19. Bolivia	X		X	
20. Chile	X	X		
21. Colombia			X	X
22. Costa Rica	X	X		X
23. El Salvador	X			
24. Jamaica			X	
25. Nicaragua	X	X	X	
26. Panama		X	X	
Near East				
27. Egypt	X	X	X	X
Total	**22**	**12**	**15**	**12**

Because of the variation in the completeness of the documentation, table 4.1 does not indicate the relative importance attached to the different reasons. Table 4.1 simply reflects those reasons that were made clear either in documents or interviews with AID officials in Washington and overseas.

Consistency With Economic Policy Reforms

Mission officials generally cited cash grant assistance as their preferred mode of assistance when seeking free-market reforms. In particular, movements away from public sector allocation of foreign exchange were pursued as central features of many cash grant assistance programs. Other free-market reforms included increased support for private sector growth, promotion and liberalization of international trade, and banking sector reform. Projects were sometimes viewed as too narrowly focused to promote reforms outside of the immediate sector in which they operated. CIPs requiring U.S. source and origin of commodities were often viewed by some AID officials as running counter to free-market reforms because CIPs represented a government-determined rather than market-determined allocation of foreign exchange.

Mission officials in the Philippines cited the consistency with reform objectives as one of the reasons why they preferred cash grants over CIPs. The mission wanted to focus its resources on bolstering the Philippines' economy. Economic support was necessary to provide the basic stability for planned policy reforms, and the mission viewed reform conditioned cash grants as the most effective way to encourage policymakers to consider and initiate needed policy changes.

The mission selected cash grant assistance when this mode was consistent with the overall mission objective of bringing about policy reform. For example, reform conditioned cash grants were used to get the Philippine Department of Health to fully plan and implement an integrated nationwide child survival program because such grants could more readily induce the needed policy changes. Also, the new local leadership was willing and prepared to make the required changes under such conditions.

The Philippine mission has not used CIPs as a form of assistance in recent years. Mission officials told us that CIPs would not have been as desirable as cash grants because (1) they would not lead to the high level dialogue and policy discussions needed to accomplish policy reforms desired by the United States and (2) the United States and the Philippines already have a long-standing trading relationship. Therefore, the funds could be better used to achieve reforms and the dollars expended to repay official debts.

Mission officials in Ghana told us that cash assistance is the most effective means to promote the overall U.S. objective, which is to promote economic stability and development. The World Bank and the International Monetary Fund strongly urged bilateral donors to follow their lead in using Ghana's inter-bank foreign exchange auction and to move increasingly toward quick disbursing forms of program assistance. Only cash grants could effectively be used in this context. Neither CIPs nor capital projects would readily lend themselves to foreign exchange auction arrangements. Additionally, World Bank estimates of Ghana's balance of payments deficit in the near future will require continued support by the donor community. According to several mission personnel, CIPs were not considered because they viewed the program as being (1) very bureaucratic with many administrative controls and (2) counterproductive to the positive results already achieved such as the liberalization of the foreign exchange rate regime.

In Tanzania, the mission converted a CIP originally intended to finance an agricultural transport assistance program to a cash grant program to finance the same sector reforms. Mission officials noted that the program was originally designed as a CIP in fiscal year 1988 to better assure accountability over the use of the dollars. In fiscal year 1991, the mission requested that the CIP be changed to a cash grant because (1) new AID regulations would assure cash grant dollar tracking, (2) a CIP would require additional staffing to oversee commodity import management, and (3) a CIP would not disburse effectively and efficiently in a liberalized foreign exchange system. The reform of that system was being urged upon the Government of Tanzania by several donors, including the United States and the World Bank.

Linked to this program is a more recent cash grant assistance effort to reform Tanzania's government-controlled foreign exchange allocation system to one which is market determined. This movement was taking place in the context of a World Bank led multidonor effort that included a shift away from import programs tied to procurement from the donor countries.

Mission officials also noted that a CIP would not work to forge stronger U.S./Tanzanian business contacts because it is an artificial means of providing commodities rather than one based on market demand. To help forge these business links, the mission has included a proposed business services center to increase U.S./Tanzanian private sector contacts under a new cash grant program. This program is designed to help reform and lead to greater investment in that country's financial and commercial sectors. The ongoing agricultural transport assistance program has been revised to stress imports from the United States by revising the list of eligible commodities to favor U.S.-made transport and telecommunications equipment. Mission officials viewed a return to a CIP as a return to an administratively determined allocation of foreign exchange that would run counter to the multidonor effort to reform that process. It would send a highly negative signal to the Government of Tanzania and to other donor governments at a crucial point in the reform process, they noted.

The AID cash grant program in Bolivia is designed primarily to support the counternarcotics program and to foster economic reforms. Missions officials told us that cash grants are the most effective means of encouraging the country to make difficult reform efforts. CIPs were not considered to be a viable mode of assistance in Bolivia because they would be counterproductive to market liberalization efforts. In addition, a CIP would not increase U.S. imports to Bolivia, but rather, in the view of mission officials, introduce a cumbersome mechanism to provide foreign exchange to pay for U.S. imports that otherwise would be paid for under the existing open market system. Mission officials stated that the United States is already Bolivia's largest trading partner.

Method or Rate of Disbursement

How and how fast funds can be provided under cash grant programs compared to CIPs or projects is one of the reasons cited by mission officials as to their choice of assistance modes. In Egypt, congressional earmarks have played a role in determining the method of disbursement. In Ethiopia and Nicaragua, the need for rapid disbursement reflected the emergency nature of economic conditions in those countries. In other countries, the rate of disbursement was cited as important to quickly meet external debt payments, finance imports, or provide budget support.

For most of the 1980s, Congress annually earmarked $815 million in Economic Support Funds for Egypt, of which no more than $115 million was to be used for cash grants and no less than $200 million was for commodity imports. The balance was used to finance projects, including capital projects. In fiscal year 1992, following congressional deletion of the $115-million cap on cash grants, AID increased that mode of assistance to $200 million to place greater emphasis on economic policy reform. In prior years, reform conditionality for cash grants to Egypt was less specific than that spelled out under a new sector policy reform cash grant program initiated in fiscal year 1992. This program was designed to promote policy reforms in four areas—financial, fiscal, trade, and privatization and enterprise. There has been no reform conditionality attached to the CIP. However, that program has been converted from the financing of public sector imports to where, by fiscal year 1993, it was solely financing imports for the Egyptian private sector. Specific projects have included efforts at reforms, particularly pricing reforms, in agriculture and power generation.

Given the annual earmark of $815 million, AID mission officials believe that a mix of cash grants, commodity imports and project assistance is necessary to provide incentives for the Egyptian government to carry out policy reforms. So long as Egypt can expect a given level of assistance, the Egyptian mission has less leverage with which to push for specific economic reforms. The mission's new strategy allows for a reduction of funds if reform conditions are not met. These funds subsequently can be carried over to the next fiscal year or made available for project assistance. This allows the mission to meet the $815-million earmark while maintaining some leverage with the Egyptian government to promote the adoption of specific policy reforms in the financial, fiscal, trade, and privatization and enterprise areas of the economy.

In Nicaragua, as in Ethiopia, the mission selected a cash grant program as the mode of assistance because it offered the quickest form of relief to a country that required immediate action to stabilize a volatile economy and support a new democracy. These programs were designed to provide emergency funds to stabilize the economy, procure imports critical to economic recovery, and overcome enormous debt problems. In the case of Nicaragua, with an economic stabilization program underway, the program has been redesigned in an attempt to create favorable conditions for increased investment and diversified exports in support of sustainable, broad-based growth. Projects were considered inconsistent with Nicaragua's immediate needs because projects have longer term goals and a slower rate of disbursement.

In other countries, particularly those in Africa, missions cited the need for cash grant assistance to more rapidly assure the availability of foreign exchange to pay pressing external debt obligations, finance imports, and to generate local currency for budget support. While the use to which these funds were put affected the choice, the rate of disbursement was also considered important because of the pressing nature of the recipient's needs.

As noted in our previous report on cash grants,[2] AID believes that it is important that cash grant funds be counted as part of the foreign exchange calculations of the International Monetary Fund. This better enables recipient governments to meet conditions under International Monetary Fund assistance arrangements. AID officials have also noted that this helps to stabilize the market for the recipient's currency and adds to the recipient's credit standing in international credit markets. Under a CIP or project, the United States generally retains ownership of the funds until actually disbursed directly to contractors or suppliers. This method of disbursement would prevent their being counted as part of the recipient government's foreign exchange holdings.

Debt Service Priority

The use of funds to service external debts was viewed by many missions as a distinct advantage of cash grants over other forms of assistance. Cash grants unlike CIPs or projects could assist in clearing or avoiding arrears on the part of recipient governments to the United States and international financial institutions. Doing so would either avoid cutoffs in assistance or make it possible to reinstate recipients as once again eligible to receive assistance from these sources. In addition, the use of the funds to repay external debts was viewed by some missions as the simplest way to track them.

In Egypt, Zambia, Jamaica, Nicaragua, and Panama, U.S. cash grant funds were used to assist the government to either avoid or to clear arrears with the United States or international financial institutions. In February 1991, a $57-million cash grant to Egypt was used to repay prior AID loans thereby preventing a cutoff of other U.S. assistance. In the other countries, cash grants were used at various times to avoid or clear arrears with international financial institutions. According to AID program documents, cash grants to Jamaica assisted in keeping that country in compliance with International Monetary Fund requirements. In Panama and Nicaragua, cash grant funds helped make it possible for those countries to clear arrears with the International Monetary Fund, the World Bank, and the Inter-American Development Bank. By clearing these arrears, Panama and Nicaragua became eligible to once again receive assistance from those institutions.

In Colombia, the decision to use cash grant funds to repay official debts to the United States and international financial institutions was taken in part

[2]Foreign Assistance: Cost Reductions Possible From Improved Cash Transfer Management (GAO/NSIAD-93-58, Nov. 18, 1992).

because of the simplicity of accounting for such uses. Cash grants were provided to support Colombia's counterdrug and economic revitalization programs and, given concerns over personnel safety, were to be provided without a buildup of AID's in-country presence. The simplicity of accounting for debt repayments would lessen the staff required to administer the program.

Administrative Requirements

The administrative requirements of CIPs and projects were also cited by missions as a reason for choosing cash grant assistance. CIPs require extensive documentation on competitive bidding, source and origin of goods, and shipping of commodities. Projects, like CIPs, also entail extensive competitive contracting, sourcing and shipping requirements. The perceived need for increased staff to meet these requirements was cited in 12 of the countries included in our review as a reason to choose cash grant assistance.

In Egypt and Tanzania, mission officials noted that demands on staff to meet these administrative requirements either implied a higher cost to bring such staff on board or took away from the mission's flexibility in staffing other priority program areas. In Egypt, mission officials stated that the staff demands on capital projects and CIPs had to be balanced against the need to monitor and oversee Egyptian economic reforms, maintain or expand mission efforts in other sectors, and to do so while holding the line or even reducing the mission's overall staffing levels. In Tanzania, mission officials noted that CIPs would likely require the services of a full-time commodity management officer that would take away from their ability to staff other priority areas, including specific health sector projects.

Some AID officials believe that the perceived need for additional staff—particularly for commodity management specialists—may not be accurate. They told us that commodity specialists could provide the smaller missions with part-time assistance from AID/Washington or AID regional offices.

AID/Washington Review of Choices

AID's Associate Administrator for Operations in October 1991 requested that all proposals for cash disbursements as nonproject assistance (except for clear legislative and policy earmarks like Israel, Turkey, and Portugal) be submitted to that office for clearance. The regional bureaus were requested to submit a 1-page explanation that identified the individual responsible for the decision to use cash, the amount, how the amount was determined, how the dollars would be spent, what controls would operate to account for the funds, how success would be measured, and an explanation of why alternate means (i.e., CIPs, capital projects, and technical advice), were not used.

We found that 18 of the 24 subsequent country proposals did include information on whether alternate means were considered. In the six other cases, the decision to use cash or an explanation of why alternate means were not used were unclear and at times not stated. AID records show that some AID/Washington officials reviewing the proposals found the rationale in six of the proposals to be questionable but generally had not been able to raise the issue before the deadline for a decision had already passed.

Some AID officials argue that often the missions do not seriously consider CIPs as alternatives to cash grant assistance. They note that AID has used CIPs mostly for financing public sector imports and that as a result, many AID officials are unfamiliar with private sector CIPs that might be more in line with mission efforts to achieve market-oriented reforms in developing countries. These officials believe that the capacity of CIPs to influence market-oriented reforms has not been sufficiently acknowledged or exploited.

CIPs, they note, can be used to encourage macroeconomic or sectoral reforms, including privatization, banking reform, trade regulations, and distribution systems. Not all CIPs have to require U.S. source and origin of all commodities. They can include less developed countries as sources as a means of fostering intra-regional trade. Private sector CIPs can be used to assist in promoting the growth of the recipient country's private sector importers and shifting U.S. support away from the public sector.

Some AID officials have also noted that while not as fast disbursing as cash grants, CIPs are faster disbursing than projects. Also, since cash grant disbursements are almost always a function of the recipient country meeting reform conditions, such disbursements may be only marginally faster than a CIP. This would depend on the relative pace of reform and the speed with which import transactions take place. Therefore, they believe (1) that a decision to use cash grants to achieve a more rapid infusion of funds needs to be more carefully considered than in the past and (2) that previous decisions to use cash grants may not always have been valid.

These officials also argue that the more extensive requirements for transaction control and accounting under CIPs may not be as onerous as generally perceived. While program design and implementation may require some commodity management expertise much of that can be provided from AID/Washington or regional offices on a part-time basis. Private sector CIPs are run much like standard international commercial transactions through international banking, thereby minimizing the demands on mission staff.

Conclusions

There has been (1) a lack of clarity and consistency in AID guidance on choosing one form of assistance over another and (2) an incomplete consideration of which form of assistance can best be used under what circumstances. Mission officials are faced with a complex matrix of competing demands in deciding what forms of assistance to propose to meet the needs of the host country. These demands include seeking consistency between the choice of assistance mode and reform objectives, determining what relative rates of disbursements are needed, deciding on whether to use the funds to pay debts or to purchase commodities, and coordinating programs with other donors. Overlaying all the other considerations is the demand on staff to meet administrative requirements for the form of assistance chosen in the face of staffing constraints.

Ensuring full consideration of the alternatives will require not only clearer and more consistent guidance, but a more complete understanding among decisionmakers of the relative advantages of the different forms of assistance and the consistency of each with U.S. objectives. The Africa Bureau's most recent guidance sets out conditions for guiding missions on which forms of assistance to use. However, such guidelines cannot always assure the right or most appropriate choice in every country.

More effective assistance to missions where competing interests make choices difficult should be a priority concern of AID/Washington. There will likely continue to be differing perspectives within AID on when and under what circumstances to provide capital and noncapital projects, commodity imports, or cash grant assistance and/or in what mix. There are differences among countries in the level of market-oriented reforms already achieved versus those still to be accomplished, as well as important choices as to whether AID should lead or follow other donors in pursuit of those reforms, such as in Ghana and Tanzania. The need for rapid disbursement of funds, such as in Nicaragua or Ethiopia, may change over time calling for more measured approaches dealing with infrastructure rather than emergency foreign exchange needs. In like manner changes in the external debt and foreign exchange position of countries like Bolivia, Egypt, or the

Philippines may call for less use of cash grants to repay debts and more emphasis on other forms of assistance.

The cases and circumstances previously mentioned serve to illustrate that mission officials face a dynamic set of conditions as they strive to support U.S. economic development objectives. Devising a country assistance strategy rarely involves providing one form of assistance to the total exclusion of all others, especially in a multidonor context. Realizing the appropriate mix of assistance requires an open process that takes various perspectives within AID into account.

By providing a means for systematically airing these perspectives during the country program review and approval process, AID could help assure a more complete consideration of the alternatives and the implications of those alternatives over time. Brief summary papers, as currently required, reviewed on a less than systematic basis do not provide an adequate basis for airing these differences or provide missions with the assistance needed for a full consideration of the alternatives.

Recommendations

To achieve (1) clearer and more consistent guidance for mission officials and (2) a more systematic record of program decisions we recommend that the Administrator of AID

- provide clear guidance to missions on when and under what circumstances various assistance mechanisms, such as cash grants, CIPs, or projects, are the most appropriate for accomplishing U.S. program goals and objectives and
- require missions to fully document the rationale for using one type of assistance mechanism rather than another.

Agency Comments

AID agreed with our recommendations in commenting on a draft of this report. Concerning our recommendation on providing clear guidelines, AID noted that it has recognized the need to establish clearer, more consistent guidance to U.S. AID missions as well as AID/Washington in choosing among alternative forms of assistance. For the past year, AID has been developing guidance to this end as part of a larger effort to replace existing AID program handbooks. New agencywide directives will be issued in 1994 dealing with choosing among forms of assistance. These directives will include profiles of the distinctive characteristics of these forms of assistance and provide guidelines for assessing the appropriateness of each type and the circumstances under which each can best be used.

Concerning our recommendation on documenting the assistance mechanism chosen, AID acknowledged past lapses in assuring the documentation of the reasons for selecting one form of assistance over another. Documentation requirements will be an explicit requirement of the new directives.

AID's comments are included in their entirety as appendix III of this report.

AID Assistance for Fiscal Years 1989 to 1992

Dollars in millions

	Fiscal year				
Region	**1989**	**1990**	**1991**	**1992**	**Total**
Cash grants					
Africa	$123.7	$114.8	$227.3	$140.0	**$605.8**
Asia	310.1	96.5	87.0	10.0	**503.6**
Europe	110.0	63.7	327.0	80.8	**581.5**
Latin America and Caribbean	344.2	906.9	523.5	301.9	**2,076.5**
Middle East	1,315.0	1,473.0	1,965.0	1,407.0	**6,160.0**
Total cash grants	**2,203.0**	**2,654.9**	**3,129.8**	**1,939.7**	**9,927.4**
Commodity Import Programs					
Africa	46.5	57.5	29.1	67.0	**200.1**
Middle East	304.5	204.2	224.2	200.0	**932.9**
Total Commodity Import Programs	351.0	261.7	253.3	267.0	**1,133.0**
Project assistance[a]	2,776.7	3,243.9	3,603.5	3,711.1	**13,335.2**
Total AID assistance	$5,330.7	$6,160.5	$6,986.6	$5,917.8	**$24,395.6**

[a]The total represents capital and sector project obligations combined for all regions because AID does not have consistent data to show a breakdown for fiscal years 1989 to 1992.

Source: AID Office of Budget, Office of Financial Management, and Policy Directorate.

AID Cash Grant Recipients for Fiscal Years 1989 to 1992

Dollars in millions

	Fiscal year				
Africa	**1989**	**1990**	**1991**	**1992**	**Total**
Cash grants					
Senegal	$24.2	$26.5	$5.5	$2.0	**$58.2**
Ghana	8.6	12.4	15.4	13.0	**49.4**
Tanzania			29.0	18.6	**47.6**
Uganda		20.0	3.0	22.5	**45.5**
Malawi	5.0		34.0		**39.0**
Burundi		13.0	8.0	10.0	**31.0**
Zambia			19.4	10.0	**29.4**
Madagascar	12.6			15.0	**27.6**
Cameroon	6.0	12.3	5.3	3.5	**27.1**
Niger	5.8	5.0	6.8	8.6	**26.2**
Nigeria	25.0				**25.0**
Rwanda			25.0		**25.0**
Kenya	15.0	8.1			**23.1**
Guinea		5.3	8.8	8.2	**22.3**
Benin			16.4	5.0	**21.4**
Mali	4.0		5.0	7.0	**16.0**
Namibia			16.0		**16.0**
Cote d'Ivoire		7.0	6.0	2.5	**15.5**
Chad	8.0	2.0		2.0	**12.0**
Djibouti	3.0	1.7	4.0	2.0	**10.7**
Zimbabwe	5.0		5.0		**10.0**
Gambia			6.0	3.0	**9.0**
Lesotho			6.1	0.4	**6.5**
Guinea Bissau	1.5	1.5	1.5		**4.5**
Seychelles				3.3	**3.3**
Togo				3.0	**3.0**
Cape Verde			1.1		**1.1**
Sao Tome and Principe				0.4	**0.4**
Total cash grants	**$123.7**	**$114.8**	**$227.3**	**$140.0**	**$605.8**

Dollars in millions

	Fiscal year				
Africa	**1989**	**1990**	**1991**	**1992**	**Total**
Commodity Import Programs					
Mozambique	$13.5	$22.5	$17.4	$8.0	**$61.4**
Ethiopia				35.0	**35.0**
Kenya	10.0	12.0	8.4		**30.4**
Uganda		20.0			**20.0**
Zambia				14.0	**14.0**
Zaire	14.0				**14.0**
Zimbabwe				10.0	**10.0**
Seychelles	3.0	3.0	3.3		**9.3**
Cameroon	6.0				**6.0**
Total Commodity Import Programs	46.5	57.5	29.1	67.0	**200.1**
Total Africa Region	**$170.2**	**$172.3**	**$256.4**	**$256.4**	**$805.9**

Dollars in millions

	Fiscal year				
Asia	**1989**	**1990**	**1991**	**1992**	**Total**
Cash grants					
Philippines	$219.0	$49.0	$60.0		**$328.0**
Pakistan	76.1	35.0			**111.1**
South Pacific Regional	10.0	10.0	10.0	10.0	**40.0**
Mongolia			10.0		**10.0**
Thailand	5.0	2.5			**7.5**
Indonesia			7.0		**7.0**
Total Asia Region	**$310.1**	**$96.5**	**$87.0**	**$10.0**	**$503.6**

Dollars in millions

Europe	Fiscal year 1989	1990	1991	1992	Total
Cash grants					
Turkey	$60.0	$14.3	$250.0	$1.0	**$325.3**
Portugal	50.0	39.4	42.0	40.0	**171.4**
Ireland		10.0		39.8	**49.8**
Czechoslovakia			15.0		**15.0**
Bulgaria			10.0		**10.0**
Hungary			10.0		**10.0**
Total Europe Region	**$110.0**	**$63.7**	**$327.0**	**$80.8**	**$581.5**

Dollars in millions

Latin America and Caribbean	Fiscal year 1989	1990	1991	1992	Total
Cash grants					
El Salvador	$157.0	$98.0	$90.0	$82.0	**$427.0**
Nicaragua		178.0	162.5	25.0	**365.5**
Panama		351.7			**351.7**
Honduras		120.0	58.0	25.0	**203.0**
Costa Rica	85.0	60.0	24.0	10.0	**179.0**
Bolivia	11.7	23.9	66.0	66.0	**167.6**
Guatemala	69.5	50.0	20.0		**139.5**
Colombia			20.0	59.3	**79.3**
Jamaica	10.0	13.7	10.0	22.0	**55.7**
Peru			50.0		**50.0**
Haiti		10.0	12.0		**22.0**
Ecuador	9.0			6.2	**15.2**
Chile			9.7	0.4	**10.1**
Dominican Republic				5.0	**5.0**
Caribbean Regional	2.0	0.6	1.0	1.0	**4.6**
Guyana		1.0	0.3		**1.3**
Total Latin America and Caribbean Region	**$344.2**	**$906.9**	**$523.5**	**$301.9**	**$2,076.5**

Dollars in millions

	Fiscal year				
Middle East	**1989**	**1990**	**1991**	**1992**	**Total**
Cash grants					
Israel	$1,200.0	$1,195.0	$1,850.0	$1,200.0	**$5,445.0**
Egypt	115.0	278.0	115.0	200.0	**708.0**
Morocco				7.0	**7.0**
Total cash grants	**1,315.0**	**1,473.0**	**1,965.0**	**1,407.0**	**6,160.0**
Commodity Import Programs					
Egypt	300.0	200.0	202.5	200.0	**902.5**
Jordan			21.7		**21.7**
Tunisia	4.5	4.2			**8.7**
Total Commodity Import Programs	304.5	204.2	224.2	200.0	**932.9**
Total Middle East Region	**$1,619.5**	**$1,677.2**	**$2,189.2**	**$1,607.0**	**$7,092.9**

Source: AID Office of Budget, Office of Financial Management, and Policy Directorate.

Comments From the Agency for International Development

USAID

U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT

NOV 24 1993

Mr. Frank C. Conahan
Assistant Comptroller General
United States General
Accounting Office
441 G Street, N.W. - Room 5055
Washington, D.C. 20548

Dear Mr. Conahan:

I am pleased to provide the U.S. Agency for International Development's (USAID) formal response to the draft GAO report entitled "FOREIGN ASSISTANCE: Clearer Guidance Needed on When to Use Cash Grants" (October 1993). The GAO recommendations and our responses follow.

GAO recommends that the Administrator of USAID:

-- provide clear guidance to missions on when and under what circumstances various assistance mechanisms, such as cash grants, Commodity Import Programs or projects are the most appropriate for accomplishing U.S. program goals and objectives

The issuance of this GAO draft report is very timely as we ourselves have recognized the need to establish clearer, more consistent guidance to USAID missions overseas, as well as here in USAID/Washington, and the importance of such guidance for the achievement of our development objectives.

Over the last year, we have been developing a new set of Agency program guidelines, "Core Directives for the Programming and Delivery of USAID Assistance," which are currently in draft and will shortly proceed through the Agency's internal clearance process. The "Core Directives" are intended to replace USAID's Handbooks 1-4. In addition to establishing the core programming requirements applicable to all Agency programs, they provide profiles of different types of assistance. Each profile describes the distinctive characteristics and unique requirements of these different assistance types, including guidelines for assessing the appropriateness of each type of assistance and the circumstances under which that mode of assistance can best be

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used. The profiles also identify the resource transfer mechanisms pertinent to a particular assistance mode and discuss the variables which must be considered when choosing among mechanisms.

-- **require missions to fully document their rationale for using one type of assistance mechanism rather than another.**

Although current USAID guidance does require program documentation to discuss the reasons for which one type of assistance has been selected over another, there have been lapses during the review process in ascertaining that this documentation is included and in ensuring that all types of assistance have been adequately considered and the most appropriate type selected.

Documentation requirements will be established in the new "Core Directives" which will explicitly require that operating units include their rationale for selecting a particular assistance type and/or resource transfer mechanism. The format of the new guidance should expedite the decision making process and ensure that important elements within that process are not neglected. Once issued, we will be pleased to forward a copy of the "Core Directives" to you.

As you are aware, USAID is currently being reorganized as well as undergoing a process of "rightsizing," both in the field and in Washington. Once we have completed both of these exercises, we will be putting into place the "Core Directives" during the beginning of next calendar year and initiating the new streamlined project documentation system. It is our intent that the simultaneous development of new Agency strategies as well as the streamlining of USAID's management and operating procedures will result in a new invigorated agency with systems in place to accomplish its development objectives.

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

Sincerely,

Larry E. Byrne
Assistant Administrator
Bureau for Management

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