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Report to the Chairman, Committee on Armed Services, House of Representatives

May 1992

OPERATION DESERT SHIELD/STORM

Update on Costs and Funding Requirements

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The Honorable Les Aspin
Chairman, Committee on Armed Services
House of Representatives

Dear Mr. Chairman:

As agreed with your office, we are providing further information on the costs and financing of Operation Desert Shield/Desert Storm.[1] In a prior report to you, we stated that the total costs incurred by the United States in support of the operation by the end of fiscal year 1992 would exceed allied contributions, but that some of those costs did not actually require new funding.[2]

We also reported that the Department of Defense's funding requirement estimate appeared to be overestimated. We noted that DOD's estimate reflected (1) higher-than-actual costs incurred by the revolving fund accounts, (2) overestimated maintenance needs, (3) replacement of recoverable munitions, and (4) procurements that were canceled because of the operation's short duration.

This report provides updated information on the operation's costs, funding requirements, and financing. Specifically, our objectives were to determine (1) the status of the Defense Cooperation Account (DCA) through fiscal year 1992, (2) the extent of future funding requirements, (3) the impact of operation related and financed revolving fund surpluses on DOD's budget, and (4) the status of the Persian Gulf Regional Defense Fund.

Background

The cost of the U.S. commitment to the operation can be viewed in terms of total costs, incremental costs, and funding requirements. We estimate that the total cost of the operation could be over $120 billion. This total includes about $50 billion for the direct and indirect costs to raise, equip, operate, maintain, and support a force of 540,000 personnel. It also includes an estimated $10 billion in other costs, such as the forgiveness of Egypt's $7 billion debt to the United States.

[1]This report refers to Operation Desert Shield/Desert Storm as the operation.

[2]Operation Desert Shield/Storm: Costs and Funding Requirements (GAO/NSIAD-91-304, Sept. 24, 1991).

The total cost also includes incremental costs for the operation. The Omnibus Budget Reconciliation Act of 1990 (P.L. 101-508) defines incremental costs to be only those costs that would not have been incurred except for the operation. For example, the regular pay of active duty personnel deployed for the operation would not be an incremental cost because these personnel would have been paid whether or not the operation took place. However, personnel costs for imminent danger pay and the pay of reservists called to active duty for the operation, less their normal drill pay, would be considered incremental. The Office of Management and Budget (OMB) is required by law (P.L. 102-25) to report on the costs of the operation and currently estimates incremental costs at $61.1 billion.

Funding requirements represent outlays that the United States has made or will ultimately be required to make, either from funds contributed by the allies or from the budget authority provided by Congress. Not all costs translate into funding requirements, thus making funding requirements lower than costs. For example, the loss or destruction of weapon systems and inventory drawdowns are clearly costs of the operation. However, if the weapons and inventories are not replaced, there is no need for additional funding. Of OMB's estimated $61.1 billion in incremental costs, we believe $7 billion will not require funding. This amount includes $5.8 billion provided as assistance-in-kind from allies and $1.2 billion for equipment that was lost but not replaced. The remaining $54.1 billion would be the estimated funding requirements for the operation. This amount includes $2.1 billion for fiscal year 1990 requirements, $1 billion in DOD budget realignments for fiscal years 1990 and 1991, $47.1 billion for current needs, and an estimated $3.9 billion for the present value of future personnel benefits costs. This amount does not include additional equipment maintenance funding that DOD believes may be required for fiscal year 1993 and beyond.

In fiscal year 1991, Congress established DCA to receive contributions from foreign countries and others for national defense purposes (P.L. 101-403). This account was intended in part to defray the costs of Operation Desert Shield and later Desert Storm. Funds are transferred from this account to agency appropriation accounts pursuant to congressional authorization and appropriations. A total of $48.1 billion in cash has been received from our allies and deposited in this account.

Congress has appropriated money to cover the operation's funding requirements. In October 1990, Congress appropriated $2.1 billion from the U.S. Treasury for fiscal year 1990 funding needs (P.L. 101-403). For fiscal year 1991, Congress appropriated $44.5 billion[3] from DCA—$1 billion in November 1990 (P.L. 101-511); two different amounts in April 1991: $42.6 billion (P.L. 102-28) and $655 million (P.L. 102-27); and $252 million in June 1991 (P.L. 102-55). However, DOD did not transfer all its funds within the fiscal year and, according to DOD officials, about $8.4 billion in appropriation authority expired. In December 1991, Congress appropriated $10.4 billion for fiscal year 1992—$6.3 billion of the expired fiscal year 1991 appropriations and an additional $4.1 billion from DCA in new appropriations (P.L. 102-229). In total, DOD and other agencies have had access to $48.6 billion in funds for fiscal years 1990-92—$46.5 billion from DCA and $2.1 billion from the U.S. Treasury to pay the incremental costs of the operation.

In April 1991, Congress established the Persian Gulf Regional Defense Fund and appropriated $15 billion from the U.S. Treasury for its operation (P.L. 102-28). This fund was to be used to supplement DCA to the extent foreign contributions were insufficient to cover the operation's funding needs. No such supplemental funding has been required. However, Congress has appropriated $320.5 million from this fund to finance humanitarian efforts in the Persian Gulf region (P.L. 102-55).

Results in Brief

Contributions to DCA will not fully cover the operation's estimated incremental costs or funding requirements. However, not all of the operation's costs have been funded from DCA, and, as a result, almost $2.3 billion in contributions and interest, plus any interest accruing after April 1992, should remain in DCA by the end of fiscal year 1992, given the current level of appropriations. Incremental costs incurred but not funded by DCA total at least $4.3 billion.

DOD has requested additional spending authority from DCA to finance operation related maintenance requirements for fiscal year 1993. However, the amount of the funding required has not been fully determined. For example, the Army has increased its maintenance estimate from $1.7 billion to almost $3.5 billion. The Air Force and Marine Corps are also expected to increase their estimates. Also, the extent it is operation related

[3] Of this fiscal year 1991 total, $536 million was appropriated to the Departments of State, Education, Veterans Affairs, the Coast Guard, the Executive Office of the President, and the Defense Relief Societies. The remainder was appropriated to DOD.

is difficult to determine. In addition to future maintenance funding, DOD, using Department of Veterans Affairs (VA) data, has identified an estimated $3.9 billion in future benefits costs for veterans and their spouses. Neither of these items have been funded through DCA.

Operation related and financed surpluses in DOD's revolving funds total at least $2.6 billion. Revolving fund surpluses were used to offset a $600 million operation and maintenance (O&M) account budget reduction in fiscal year 1992. DOD has reduced its fiscal year 1993 O&M budget request to offset an estimated $2 billion surplus in operation financed supplies and equipment.

DOD states that it has no plans at this time to request any additional funding from the Regional Defense Fund.

Funds Remaining in DCA

DCA should have almost $2.3 billion in remaining contributions and interest, plus any interest accruing after April 1992, at the end of fiscal year 1992, provided there are no changes in the current level of appropriations. The United States expected and has received a total of almost $48.1 billion in cash from foreign governments to help pay for the operation. As of April 15, 1992, interest earned on the contributions totaled almost $685 million.

DOD and other agencies have access to $46.5 billion from DCA to cover the operation related funding requirements for fiscal years 1991 and 1992. At the end of fiscal year 1992, assuming DOD spends the full amount provided, DCA would have almost $2.3 billion plus any additional interest earned remaining.

Table 1 provides details on the amounts currently available from DCA to pay for the operation's funding requirements.

Table 1: Status of Defense Cooperation Account as of April 15, 1992

Dollars in billions

DCA contributions and interest		
Contributions received	$48.065	
Interest through 4/15/92	.685	
Total		**$48.750**
DCA withdrawals		
1991 Transfers	$36.067	
1991 Authority available	.035	
1992 Appropriations	10.366	
Total		**$46.468**
DCA funds remaining for use		**$2.282**[a]

[a]This total does not reflect any interest earned after 4/15/92.

DCA Not Used to Fund All Operation Costs

DCA has not been used to reimburse the Treasury for (1) $2.2 billion in incremental costs incurred that did not require new funding and (2) $2.1 billion in fiscal year 1990 funding provided by the U.S. Treasury before contributions were received in DCA.

The $2.2 billion includes $1.2 billion in equipment lost and munitions consumed that will not be replaced as part of the planned reduction in forces over the next several years and $1 billion in budget realignments from non-operation related programs in fiscal years 1990 and 1991. Although these costs did not require new funding, they do represent a past expenditure of funds from the U.S. Treasury.

Future Costs Will Be Incurred but Amounts Are Uncertain

In addition to costs incurred that have not been paid from DCA, there are outstanding current and future funding requirements that have not been covered through the DCA appropriations to date. These funding requirements include the costs for additional maintenance needs that are now being identified and costs for personnel benefits. The funding requirements for both these items are still uncertain.

Future Maintenance Funding Requirements Are Uncertain

The $47.1 billion estimated funding requirement includes $3.6 billion in depot level maintenance funding that may be required as a result of the operation as well as an undetermined amount for operational and intermediate maintenance. The DCA maintenance funding is in addition to normal maintenance funding. DOD's total depot level maintenance costs, including operation costs, were $10.8 billion for fiscal year 1991 and were estimated to be $10 billion for fiscal year 1992 and $7.2 billion for fiscal year 1993. Funds for organizational and intermediate level maintenance funds are included in other parts of the budget, such as land forces and reserve forces, and cannot be identified specifically.

In earlier discussions with service officials, we were told that equipment used in the operation was returning in better condition than anyone had expected and maintenance costs would not be as high as estimated. However, Army officials have revised their original total maintenance estimate of $1.7 billion ($1.4 billion for depot level and $0.3 billion for organizational and intermediate level maintenance). Officials now estimate that it may take almost $3.5 billion (almost $2 billion for depot and $1.5 billion for organizational and intermediate maintenance) to cover increased equipment maintenance and refurbishment costs because of problems that were undetected in early equipment inspections. This increase is in addition to the Army's original maintenance budget estimates for depot and other levels of maintenance. DOD Comptroller officials stated that the Air Force and Marine Corps may also be increasing their estimates.

In response to expected increased maintenance cost estimates, the President's fiscal year 1993 budget submission contains a proposal allowing DOD to transfer from DCA, after appropriate notice, any amounts not previously transferred under previous Desert Shield legislation. These funds would be used for the cost of organizational, intermediate, and depot level maintenance requirements of the operation in fiscal year 1993.

The DCA funded maintenance may reduce normal maintenance costs. Some equipment used in the operation is scheduled for depot repair using DCA funding. According to an Army official, some of this maintenance and repair could have been scheduled using the Army's normal O&M appropriation. To the extent that the DCA funded maintenance reduces normal scheduled maintenance requirements, additional funding is available to reduce maintenance backlogs, fund other non-maintenance related requirements, or reduce the O&M funding. Army officials stated that it is often difficult to distinguish operation related maintenance from normal maintenance and it becomes more difficult the further away in time from the operation the maintenance is performed. DOD policy is that the services must consider the value of normally budgeted maintenance in its determination of incremental maintenance costs for the operation.

DOD officials have indicated that the Department cannot accomplish all its operation related maintenance requirements this year, which means that some appropriated funds may not be spent. If this occurs, DCA would have a larger amount remaining at the end of fiscal year 1992 than previously indicated. Army officials explained that although equipment may require more maintenance, it is necessary to control the flow of equipment into the depots because (1) depot capacity is limited and (2) putting too much equipment in the depots for maintenance could adversely impact unit training and readiness. Also, increased maintenance requirements may not show up for several years. For example, instead of a tank transmission being replaced at its scheduled time, it may now have to be replaced sooner because of the adverse desert conditions. Some equipment to be transferred to National Guard and Reserve units may not have to be repaired as quickly and some may not have to be repaired at all due to the drawdown in forces. Similar situations exist for the Marine Corps and the Air Force. We are continuing to monitor the maintenance funding requirements.

Future Personnel Benefits Will Cost Treasury Dollars

The Persian Gulf Conflict Supplemental Authorization and Personnel Benefits Act of 1991 (P.L. 102-25) established that veterans of the operation would be eligible for certain benefits and that these benefits would be paid from DCA funds. DOD, using VA data, has estimated average present values for these benefits, which total over $3.9 billion. This total includes an estimated $2.5 billion for pensions to be paid out to veterans or their survivors over a 100-year period, $800 million for other veterans benefits, and $400 million for additional retirement credits for members of the reserves to be paid out over a 50-year period. It also includes almost $300 million for benefits that have already been funded.

The $3.9 billion average present value estimate is uncertain. The estimate is based on a number of critical long-term assumptions regarding interest rates, inflation rates, and eligibility rates. Relatively minor changes in the assumptions can have a significant impact on the cost estimates.

The act also states that only those costs incurred for fiscal years 1991 through 1995 are "incremental costs associated with Operation Desert Storm." Therefore, only a small portion of this $3.9 billion should be considered incremental costs. The DCA funds have not yet been appropriated for the long-term costs of these benefits. If this occurs, procedures would have to be established to supplement VA's normal pay-as-you-go benefits appropriation with funds from DCA.

Options for Using Funds Remaining in DCA

Although operation related funding requirements are to be paid from DCA, there will not be enough money in the account to cover all past, present, and future costs of the operation. However, as previously mentioned, there should be at least a $2.3 billion balance in DCA at the end of fiscal year 1992. We believe that there are two main options for which these funds could be used.

- Option 1: Deposit the funds remaining in DCA after fiscal year 1992 in the U.S. Treasury's general fund as partial reimbursement for (1) $1.2 billion in incremental costs incurred for lost items that will not be replaced, (2) $2.1 billion in funding appropriated before DCA received contributions, (3) $1 billion in internal realignments from fiscal years 1990 and 1991, and (4) future benefits and maintenance costs that may require funding.
- Option 2: Retain the funds in DCA to apply toward estimated future operation expenses for maintenance and personnel benefits.

Under the first option—depositing the remaining DCA funds in the U.S. Treasury's general fund—any future operation costs to DOD and VA would either have to be absorbed or funded through annual or supplemental appropriations. If future costs are absorbed within existing funding levels, or are not incurred at all, this option would reduce total federal spending by the $2.3 billion currently in DCA and thus lower the deficit by that amount. However, absorbing any such costs may require DOD to make budget offsets through either operating efficiencies or program reductions. The impact of absorbing any future costs may be minimal since such costs can be spread over a number of years. VA would require appropriations to pay the benefits of operation veterans and their survivors. As noted earlier, the extent of such future costs are uncertain.

DOD officials do not support the first option because they believe the costs incurred or realigned in prior fiscal years and the cost of items not to be replaced are "sunk costs." They also intend that the remaining funds should be used to finance the balance of incremental costs. However, we believe that the past costs are legitimate incremental costs and should be reimbursed by the DCA funds.

Under the second option, which DOD prefers and has proposed through the President's budget, Congress would allow DOD, with appropriate notice, to use funds remaining in DCA to pay for additional operation related maintenance costs that are estimated to be incurred. Under this plan no additional DCA funds would be available to finance DOD and VA future personnel benefits, as authorized by Public Law 102-25. This option, however, could help mitigate the effects of any additional cuts in defense spending being considered for fiscal year 1993.

In making a decision to either reimburse the general fund or retain the funds in DCA for future operation related maintenance costs, a number of unknowns or questions need to be considered. They include (1) the nature and extent of additional maintenance requirements; (2) the impact that additional DCA funding would have on existing maintenance schedules and depot capacity; (3) the impact the defense drawdown will have on future requirements; (4) the impact of stretching out maintenance schedules for equipment going to active duty components, reserve components, war reserve stocks, and Foreign Military Sales; (5) the ability to absorb additional maintenance costs under current funding levels, that is, through offsets to other programs or operating efficiencies; (6) the extent that DCA funding offsets or reduces non-operation related maintenance costs; and (7) the validity of the assumptions used to calculate the present value of personnel benefits.

Impact of Operation Related and Financed Revolving Fund Surpluses

DCA funding has been indirectly used to offset DOD budget reductions. In our prior report on the operation's costs, we questioned whether DOD would require as much funding as estimated for equipment maintenance, munitions, and supplies. We also reported that free fuel and transportation, fuel prices, and high transportation costs could produce a surplus in the revolving funds. We reported that if any items proved to cost less than estimated, there could be more money left in DCA. Some of these observations have since proven to be accurate.

The conference report for the fiscal year 1992 DOD Appropriations Act (P.L. 102-172) recognized that there were surpluses in the stock funds due to supplies and transportation purchased for the operation with DCA funds. The conferees reduced the services' O&M appropriations by a total of $600 million and directed the transfer of that amount from the revolving funds into the O&M appropriations accounts. Accordingly, operation related surpluses were used to finance normal DOD O&M funding requirements. This, in turn, reduced DOD's fiscal year 1992 O&M appropriation requirement by $600 million.

According to DOD officials, the services are still holding large, unknown inventories of supplies purchased for the operation primarily with DCA funding that have not been accounted for or returned to the wholesale supply system. To encourage this return, the DOD Comptroller's Office reduced the services' fiscal year 1993 O&M new budget authority request by over $2 billion. To make up for this reduction and enable execution of the planned program, the fiscal year 1993 budget submission states that over $2 billion will be transferred to the services from the Defense Business Operations Fund[4] once the identification of residual inventories from the operation is complete and transfer of the residual to the wholesale supply system has begun.

In both cases, operation related and financed surpluses are being used to finance normal O&M funding requirements. Accordingly, the services' O&M budget request was reduced by $600 million in fiscal year 1992 and over $2 billion in fiscal year 1993.

Persian Gulf Regional Defense Fund No Longer Needed

When Congress created the Persian Gulf Regional Defense Fund, its purpose was to supplement DCA. It was anticipated that any withdrawal from the fund would be reimbursed back to the fund when and if money became available from DCA. However, Congress has appropriated $320.5 million from this fund to be used for humanitarian relief efforts in the Persian Gulf and reduced the $15 billion in the fund by that amount (P.L. 102-55). This appropriation would indicate that Congress did not intend that the fund be reimbursed for this withdrawal.

As stated previously, DOD has requested, through the President's budget submission, additional spending authority for fiscal year 1993 from DCA, but at this time officials do not foresee a further need for funds from the Persian Gulf Regional Defense Fund. However, DOD officials have also stated that, depending on the availability of DCA funds to cover the future personnel benefits, a decision could be made to finance these benefits from the fund.

According to Public Law 102-28, the fund will terminate upon payment of all incremental costs associated with the operation. DOD officials state that it is precipitous to change the status of the fund at this time. However, we believe that, given the uncertainty of the estimate assumptions and the length of time the benefits are expected to cover, it may not be practical to maintain the fund and its entire amount at DOD's or VA's disposal for

[4]The Defense Business Operations Fund is a newly created entity incorporating selected revolving funds previously called the stock and industrial funds. This new fund finances the business operations of industrial, commercial, and support type activities.

100 years. We also believe that DOD and VA, through normal appropriations, could pay for the additional benefit coverage for operation veterans and survivors with little or no increase in the total amounts already being appropriated for those benefits.

Matters for Consideration by the Congress

Although operation related funding requirements are to be paid from DCA, there will not be enough money in the account to cover all past, present, and future costs of the operation. However, as indicated previously, there should be at least a $2.3 billion balance in DCA at the end of fiscal year 1992.

The Congress, through its actions, intended that the incremental costs of the operation be paid for from DCA. The fiscal year 1990 and some fiscal year 1991 costs of $3.1 billion were either paid for from a supplemental appropriation or absorbed by DOD through internal realignments. These costs were paid for in this manner because, at that time, funds were not yet available from DCA. Because these are actual incurred incremental costs subject to payment had the DCA funds been available, we believe that they should be covered first by any remaining DCA funds after fiscal year 1992. This would have the beneficial effect of immediately reducing the deficit while requiring DOD to absorb any additional costs and would be better than retaining these funds to cover unknown or questionable future maintenance and personnel costs.

We, therefore, believe the Congress should consider using the remaining funds in DCA after fiscal year 1992 to reimburse the general fund of the Treasury for operation related costs already incurred.

After Congress has made a decision regarding the remaining DCA funds, Congress should also consider terminating the Persian Gulf Regional Defense Fund as soon as practicable.

Scope and Methodology

To determine the effects of transfers and appropriations on DCA, we reviewed legislation and account activity data. We also interviewed officials from the Office of the Comptroller for the Office of the Secretary of Defense, the Army, VA, and OMB.

We conducted our review from December 1991 through March 1992 in accordance with generally accepted government auditing standards. We did not obtain agency comments on this report. However, we discussed our report with the DOD Comptroller and Army budget officials and have incorporated their comments where appropriate.

As agreed with your office, unless you publicly announce its contents earlier, we plan no further distribution of this report until 30 days from its issue date. At that time, we will send copies to the Chairman, Senate Committee on Armed Services; the Secretary of Defense; the Director, OMB; the Secretary of Veterans Affairs; and appropriate congressional committees. We will also send copies to other interested parties on request.

This report was prepared under the direction of Paul F. Math, Director, Research, Development, Acquisition, and Procurement Issues, who may be reached on (202) 275-4587 if you or your staff have any questions. Other major contributors to this report were: Michael Motley, Associate Director; James Wiggins, Assistant Director; Steven Sternlieb, Assistant Director; and Ann Borseth, Evaluator-in-Charge.

Sincerely yours,

Frank C Conahan

Frank C. Conahan
Assistant Comptroller General

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