

Tools to Implement Foreign Aid – Why Contracts Make Sense

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With an impending change in administration and recent, rapid changes in how the U.S. engages with developing countries, the time is ripe for a lively debate on the future directions of America's foreign aid programs. The appropriate roles of for-profit and not-for-profit implementing partners are a key part of that discussion. But defining those roles without considering the broader context risks misallocating resources.

The U.S. provides foreign aid in one form or another to over 140 countries, in a wide range of sectors that vary by country. We use the term “development” to lump together many complex processes affecting billions of people across the globe in countries as diverse as Ukraine and Uruguay, India and Ethiopia. For a job so diverse and so complex, we need, quite simply, to leverage the best that America has to offer, irrespective of whether it resides in nonprofits, large businesses, development contractors, universities, think tanks, small businesses, the public sector or elsewhere. And the best resides in all of these places, oftentimes working in tandem. For example, IRG is working abroad today with nonprofit partners that range from Winrock International to the World Wildlife Fund.

Foreign assistance objectives are multiple and varied—supporting the foreign policy of the United States, providing disaster relief in hard-hit areas, and offering world-class development assistance to peoples and nations. The one chosen at any given time can affect, in relative terms, the selection of partners and implementation mechanisms. USAID's Glossary of Automated Directives System defines the legal instruments used by the U.S. government to fund the work done by its non-government partners. The three types of legal instruments used by USAID to fund foreign aid programs are:



Contractors are working around the world to improve the lives of others. Photo courtesy of IRG

Contract

A mutually binding legal instrument in which the principal purpose is the acquisition of property or services for the direct benefit or use of the federal government.

Cooperative Agreement

A legal instrument in which the principal purpose is the transfer of money, property, or services to the recipient in order to accomplish a public purpose of support authorized by federal statute and where substantial involvement by USAID is anticipated.

Grant

A legal instrument in which the principal purpose is the transfer of money, property, or services to the recipient in order to accomplish a public purpose of support authorized by federal statute and where substantial involvement by USAID is not anticipated.

The closer one ties development assistance to U.S. foreign policy, the more desirable control over how the money is spent becomes. This then dictates which legal instrument should be used, because the three implementation mechanisms permit very different levels of government authority and control over how taxpayer resources are spent.

The debate over who should implement more of our foreign aid programs—nonprofits or contractors—is the wrong debate. The more useful question is what type of implementation instrument is most effective for a given program. In many cases, a contract is the most effective because it provides for greater government control over results; greater accountability and transparency; more opportunities for competition; and an equally cost-effective result.

Greater Government Control over Results

Under cooperative agreements and grants, taxpayer dollars are transferred to the implementing organizations. Grants are specifically designed for situations where “substantial [government] involvement is not anticipated.” This makes good sense when a public purpose strongly coincides with a grantee’s existing program or objectives.

However, there will be many instances when the U.S. government wants specific activities implemented in a specific manner, whether for institutional, technical or foreign policy reasons. United Nations Ambassador Zalmay Khalilzad recently flagged that particular minefield, noting, “We have some mechanisms for distributing assistance—for example, cooperative agreements and grants—with no prescribed deliverables and timelines. In a word, money obligated or disbursed is not the same thing as outcomes achieved.”

Contractors, on the other hand, when implementing U.S. government programs, are subject to the government’s direct instruction and control. In addition, their private sector practices permit rapid mobilization, change in direction or a swift wrap-up when a government so requests. The 2007 HELP Commission, a bipartisan collaboration of the best foreign assistance minds appointed by the president and Congress, found that “using a grant when a contract would be more appropriate weakens program effectiveness and responsibility [and that] USAID officers reported they had few avenues to use when faced with poor performance by a grantee.” A contract is the easiest to modify or to end when it is in the government’s best interest to do so.

Greater Accountability, Transparency

Contracts also provide the greatest accountability and transparency because contractors implement scopes of work clearly specified by USAID. Contractors are, by law, subject to close public scrutiny for every taxpayer dollar spent, through annual independent and gov-

ernment audits, and potential review and audit by the inspector general. While the majority of contracts are implemented by for-profit firms, nonprofits regularly compete for and win contracts. When they do, they are subject to the same standards of accountability. Conversely, for-profit firms seldom compete for cooperative agreements and almost never for grants. Not that this accountability guarantees that funds will never be misused, as several high-profile cases demonstrate; but it is rare, and grants and cooperative agreements are also sometimes abused.

More Opportunities for Competition

Competition lowers cost, provides best value and assures greater responsiveness. It has always been an engine of innovation, broadening the pool of players and providing greater scope for small businesses. The use of contracts, the vast majority of which are competed openly, increases competition by allowing both private sector firms, including small businesses, and nonprofits to participate.

Legitimate concerns exist about the level of competition under all three implementation instruments, particularly as personnel-strapped agencies bundle programs into larger and larger packages to limit the number of transactions. The HELP Commission identified several ways in which USAID could increase competition under all three implementation instruments.

But the commission was particularly critical of the ability to give millions of dollars to nonprofits without further competition or justification under the “Leader with Associates” (LWA) program. Speaking of one LWA consortium with 17 members, it noted, “Having won an LWA award in 2005, these 17 organizations quickly obtained \$70 million in additional non-competitive grants in the first year and expect to receive \$350 million over the initial five-year term of the award.” Moreover, the LWA grants can be extended another five years without further competition.

While there is room for improvement in the competitiveness of all implementation instruments, there is no doubt that contracts allow for the highest degree of

competition. Yet grants and cooperative agreements accounted for 63 percent of USAID obligations in 2006, the most recent year for which data are available.

Equally Cost-Effective

Much has been written in the media about “high-priced private contractors.” But the issue is more complex than attention-grabbing headlines imply. Unlike other U.S. government agencies, USAID has, for decades and with rare exception, not permitted development contractors to receive higher salaries than U.S. government employees. Most USAID contractor employees receive the same salary as their USAID or nonprofit counterparts of similar qualifications and experience.

It is true that some nonprofits, particularly private voluntary organizations (PVOs), may have lower overhead rates, but this can be deceptive. Nonprofits are allowed to direct-charge many costs that private contractors must include in their overheads—for example, full-time home office management staff—so comparing overhead rates is like comparing apples to oranges.

Whether paid for directly or indirectly, the U.S. government’s total cost is most often the same for all three implementation mechanisms—contracts, grants or cooperative agreements. Indeed, in FY 2005 USAID conducted such an analysis, comparing costs of several programs carried out by private contractors versus by nonprofits. In testimony before Congress, the Agency reported that it found no appreciable cost difference.

While cost-effectiveness is not always a meaningful differentiator between for-profits and nonprofits implementing most types of USAID programs, it is important to note that there are some PVOs working in the field who place staff willing to work at well-below market rates and live under difficult circumstances. Their sacrifice and dedication should be recognized, and there are circumstances when they provide the most cost-effective solution. In those cases, a grant is the appropriate vehicle to use. But there is no “one size fits all” solution.

In Summary: Choose the Legal Instrument that Suits the Job

It has been said that certain sectors inherently require a certain type of instrument—that a grant or cooperative agreement is best used for governance programs, for example, or a contract for an infrastructure project. The better answer is “it depends” —on context, purpose and ultimate outcome. Most importantly, there is a role for all mechanisms.

Many developing countries have failed to recognize the value of competitive free markets or a robust civil society. And so many USAID, Millennium Challenge Corporation or other U.S. government programs are specifically aimed at strengthening the role of markets and bringing small and medium enterprises into market value chains. U.S. governance programs emphasize the need to build a robust, multi-stakeholder civil society. Public-private partnership programs are designed both to leverage private sector resources for development and to demonstrate to recipient countries the importance of the private sector in development. What signal do we send to the governments and populations of the countries we assist if our own aid programs do not include the diverse actors that make America’s civil society so robust?

As the U.S. launches its foreign assistance programs, it needs first to establish the best criteria for implementing a

given program; then select the mechanism that scores best on accountability, control and cost-effectiveness. Finally, it needs to open it up to the broadest range of competition. Nonprofits, universities, think-tanks, the private sector, development contractors—large and small—all have important roles to play as implementation partners in foreign aid. None should be artificially limited in offering best value to the government, and none should be artificially favored.

About the Authors



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