Conceptual Framework for Manage-to-Budget

A Mandatory Reference for ADS Chapter 200-203

Reference Issuance Date: 08/04/2011
Policy Issuance Date: 08/31/2006
Responsible Office: ES
File Name: 200mbk_080411

Conceptual Framework for Manage-to-Budget

The attached document provides further information on the Manage-to-Budget (MTB) exercise being implemented Agency-wide beginning October 1, 2006. Eleven working groups were established to assist in developing comprehensive Agency MTB implementation procedures. These working groups have conducted initial analyses and made recommendations on how to expand the scope of MTB from the pilot stage. These recommendations, as well as lessons learned from the four pilot operating units who have been managing to budget since April, are the basis for the conceptual framework contained in the attached document.

The goal of MTB is to strategically align OE and program resources as well as ensuring that managers are able to use the Agency's resources in the most efficient and effective way. To this end, the MTB process will help control costs, lower overhead, and reduce the use of program funds for administrative expenses.

<u>Conceptual Framework for Manage to Budget (MTB)</u>

Background

In April 2005, OMB and Congress asked the Agency to study the administrative budget process with particular emphasis on better understanding USAID's full costs of operations and providing management incentives for controlling these costs. This exercise was known as the "shadow budget." A year later, in April 2006 the Administrator stated in testimony to the House International Relations Committee (HIRC) that USAID would broaden the shadow budget exercise and implement "Manage-to-Budget" (MTB) worldwide in FY 2007.

Consequently, the Agency will establish an FY 2007 Operating Expense (OE) budget by October 31, 2006 for all operating units (OUs) that decentralizes more of the Agency's operating expense budget and captures allocations for space and IT support costs. MTB will also provide transparency in the amount of program funds used for operational purposes and set administrative cost ratios to help control these costs.

The MTB exercise has not changed the funding source policy in ADS 601, which provides guidance on which appropriation account – program or operating expense – is to be used to fund the salary and support costs of the Agency's direct hire and non-direct hire personnel. MTB categorization is a separate analysis that takes place regardless of funding source as determined by ADS 601.

The goal of implementing MTB is to strategically align OE resources to program resources and ensure that we have the most efficient and effective administrative operations for the Agency. To this end, the MTB process is designed to help control costs, reduce overhead, and reduce the use of program funds for administrative expenses. This document summarizes the management framework, as well as the processes and procedures that will support MTB.

Operating Environment Defined

MTB maintains management control while providing managers greater flexibility over their overall budgets provided the operating units stay within the established budget allocations and overarching policy parameters. First and foremost, managers must comply with all human resources, budget and financial management rules as promulgated through the ADS, regulations and statute, e.g., the FS and GS hiring, assignment and promotion policies must be observed. The M Bureau will be responsible for providing overall management policy of the MTB exercise and PPC will provide the budget policy guidance.

What Managers will manage under MTB

<u>The budget for:</u>

- Salaries and benefits of direct hire employees;

- Salaries and benefits of non-direct hire employees (USPSC, FSNPSC, TCNPSC, CASU, other – PAPA/PASA/TAACS);
- Performance Pay (bonuses, spot awards, incentive and special act awards);
- Non-labor: missions – all non-labor costs (e.g., rent, non-expendable property); Washington - travel/transportation, non-mandatory training, selected IT costs, administrative support costs currently funded by the OU.
- Program funds for operational costs.

Field missions currently manage their budgets except for DH salaries, as FS hiring is done from the "center" to ensure the appropriate mix of individuals with particular skills are hired to support the various sectors across the Agency. A methodology for further delegating FS labor costs to overseas missions will be established in FY 2007 (see section on FS labor below).

What Managers will not establish or manage under MTB:

- Rate and amount of foreign service allowances;
- Rates of CS & FS salaries and benefits;
- Rates for FSN compensation (these are based on the post local compensation plan, based on prevailing practice);
- Across the board general pay increases and locality pay increases;
- USAID/W Space; and
- Funding for centrally managed IT corporate applications and infrastructure services. (See further discussion below on space and IT costs.)

MTB Pilots

Four pilot units were designated for the initial phase of MTB: M/HR, EGAT, GH, and AFR. As part of this process, the pilots have begun to sign MOUs which lay out the initial framework for the exercise. The purpose of the MOU is that it serves as the basis by which to test the implementation of the MTB concept. During this phase, PPC allocated budgets to the offices/bureau. Basically, the MOUs state that the pilot units:

- Will no longer have hiring ceilings for U.S. Direct Hire (DH) and non-DH;
- Will manage the U.S. Direct Hire Payroll; and
- Will be provided the USDH payroll budget to manage FTEs filled as of PP07, to include approved but pending personnel actions.

The pilot units were able to negotiate with PPC if any adjustments were necessary. Agency senior management will evaluate the lessons learned from the pilots for the implementation of MTB in FY 07.

Operational Parameters for MTB Exercise in FY 2007

MTB Working Groups

Eleven working groups were established to assist in developing comprehensive Agency MTB implementation procedures. These working groups have conducted initial analyses and made recommendations on how to expand the scope of MTB from the pilot stage. This is an evolving process. The primary recommendations are contained in this document. Further detail is provided in action memos that will be the basis for changes made to the ADS in the long-term. The tasks for the MTB working groups have been broken down into three broad categories – labor, other direct costs (ODC); and components required to manage MTB. The working groups responsible for FS staffing, space, incentives, information technology, data systems and report design will continue their work in FY 07 to identify additional costs that may be decentralized and create information systems to support the MTB initiative.

Program versus Operational Costs

Under the MTB process, the nature of all activities funded in acquisition and assistance instruments must be categorized as either program or operational costs. This new requirement is in addition to the ADS 601 analysis for determining the appropriate funding source – program or OE. The basic consideration for MTB purposes is whether particular costs, regardless of funding source, are program-oriented in support of host country implementation activities (i.e. direct development interventions) in support of USAID's operations and programs.

To determine the appropriate MTB cost category, Operating Units (OUs) should pose the threshold question: "Are the costs to support Agency operations and programs or for the direct benefit of the host country programs?" If the costs are incurred to support Agency operations or programs and/or to accomplish work that would traditionally be done by Agency staff, the costs are considered operational in nature. Some examples of operational costs include:

- Final and stand alone evaluations;
- Program design;
- Studies, analysis and assessments for policy development, decision-making, or other management purposes; and
- Training that is provided to USAID employees.

Except where specifically noted in other sections of this guidance, all assistance awards are generally considered programmatic and should not be reported as part of the MTB exercise. (See discussion below regarding categorization of labor costs.) When an acquisition award includes both programmatic and operational costs, and the costs are easily discernable in the award budget, the operational costs should be reported as part of the MTB exercise. Additional guidance will be provided to Contracting Officers.

Labor and Administrative Costs

As described above, there are numerous types of operational costs that the Agency incurs in conducting its day-to-day business. When labor and labor-associated administrative costs are incurred in support of USAID operations and programs, the costs are operational. These operational costs are in contrast to labor and administrative costs embedded in program implementation contracts that are part of the direct program implementation for the benefit of host countries, which are categorized as programmatic costs. An example of such a direct program implementation cost includes contractor salaries and overhead. MTB requires each OU to capture all of its operational costs. In doing so, OU's are required to count operational costs, which include the following:

- Direct-hires
- Personal Services Contractors (PSCs)
- Participating Agency Service Agreements (PASAs)
- Resources Support Services Agreements (RSSAs)
- Participating Agency Program Agreements (PAPAs)
- Cooperating Administrative Support Units (CASUs)
- Fellows
- Institutional Manpower/Support Contracts*

  * **Note:** For MTB purposes, an Institutional Support Contractor is defined as a non-personal service contractor, funded by USAID to support Agency operations and/or to augment the Agency's direct hire and personal services staff. Institutional Support Contractors are commonly referred to as "manpower" contracts. Personnel employed by an Institutional Support Contractor may be physically located within USAID space, space rented by or on behalf of the Agency, or in the Institutional Support Contractor's space. Institutional Support Contractors may be funded by either program funds or operating expense funds, in accordance with ADS 601. However, by definition Institutional Support Contractors are operational costs and must be classified within the 2500 series EOCC codes.

For MTB purposes, all of the categories of labor noted above and their associated administrative costs, even if properly program-funded pursuant to ADS 601, are considered operational and should be captured under MTB. When an Institutional Support Contract is broader than the definition above and includes both manpower/support personnel and direct development intervention activities, OUs should use their best efforts to disaggregate the costs and report the number of individuals and operational costs.

Non-direct Hire Labor Trade-off Considerations

When applying MTB concepts, missions and Operating Units should carefully consider both the legal/policy issues associated with the various labor categories and the associated costs. The first step is to identify the various direct hire or non-direct hire labor mixes that will meet the manager's needs. When determining this labor mix, some of the legal/policy issues that arise include the following:

- Will the position involve Cognizant Technical Officer (CTO) duties?—for example PSCs can be CTOs.

- Is there existing authority for the position?—for example PSCs are allowed under special authority.
- Are the duties required inherently governmental or unique?—for example interagency agreements can be used for inherently governmental needs.
- Are the duties readily provided in the commercial sector?—for example contractors provide commercial services.

Once the proper category or categories of labor are identified, managers must then identify any cost trade-offs in selecting one labor mix over another. Examples of cost issues to consider when determining the labor mix include:

- Interagency agreements (e.g., PASAs/PAPAs) include the overhead/operational costs of the other federal agency which typically range from 10% to 30%.
- Federal agencies contracting out for USAID (e.g., Franchise funds/CASUs) typically include a management fee (e.g., 4%) or the overhead costs of the agency (e.g., 10-30%) plus the overhead costs and profit of the firm supplying the personnel.
- Contracts include overhead or other indirect costs (can vary significantly and may range from 30%, 50% to 100% of direct-labor costs) and profit (up to 10%).

OUs are advised to consult with their Contracting Officers for additional assistance in determining the cost tradeoff for non-direct hire hiring mechanisms.

Foreign Service Overseas Staffing

The following specifically applies to OE funded overseas Foreign Service staffing. OE funded Washington Foreign Service staffing will be handled in the same manner as civil service staffing under MTB. Currently, missions manage and control significant parts of both their program and OE budget. Thus, to a great extent, they already manage to budget. Further, missions are responsible for and manage the support costs of much of their direct and non direct hire labor pools, as well as managing all costs related to their Foreign Service Limited (FSL) appointees. Missions also have the authority to create and abolish Foreign Service positions given their OE budget levels and/or changes to mission programs. M/HR will continue to monitor overseas positions and will continue to approve all OE funded USPSCs and most program funded PSCs in accordance with the General Notice dated February 14, 2006. The major budget items that the missions do not directly manage and/or control are the OE salary/benefits costs for members of the Foreign Service assigned to their missions. Additionally, they do not directly control the position grade of the assigned FS personnel or their family size and support costs.

Under MTB, missions will, for the first time, be provided the actual costs for the salary/benefits of their OE funded FS employees. However, given the need to hire and assign from Washington, to maintain an adequate number of overseas FS positions, to adhere to the tenets of the Foreign Service Act, and to develop MTB procedures to address these and other issues regarding OE funded overseas positions, FS overseas OE funded salaries and benefits will be controlled centrally in Washington. It is anticipated that the issues impacting MTB relating to the cost of salaries/benefits for overseas OE funded FS employees will be identified, with an implementation plan for resolution by September 30, 2006.

Space (Washington Only)

Space management will remain centralized in the Management Bureau during FY 2007 because (1) a space reconfiguration/reallocation project is underway to maximize the equity and efficiency of space in the Ronald Regan Building and (2) there would be no immediate cost benefit in providing managers authority for space management since space is currently a fixed cost for the Agency. However, over the course of FY 2007, the following actions will be undertaken to facilitate decentralization of space management in FY 2008:

- Space costs attributable to each OU will be reported to responsible managers and the senior leadership.
- The Office of Administrative Services in the M Bureau will work with bureaus to maximize the efficiency and equity of space allocations as the space reconfiguration plan is implemented during FY 2006 and FY 2007. A primary objective of the plan is to unite fragmented work units in contiguous space and to establish space standards.
- The data collection systems and processes related to space utilization will be refined and strengthened.
- The "seat tax" – or Agency implemented space cost recovery which imposes a tax for program funded staff occupying space in the building – will continue to be imposed for program funded staff, an area where managerial decisions impact program funds used for administrative purposes.

IT Infrastructure, Systems and Services

While the Office of Information Resources Management (M/IRM) will continue to centrally manage the Agency's budget for corporate applications and infrastructure services, OUs will manage funds for the following information technology costs in FY 07:

- Voice over IP (VOIP) calls (field missions)
- Cellular telephones and monthly service fees
- Blackberries and service fees
- Video-conferencing equipment and related costs
- Special software and hardware beyond base configurations
- ClassNet equipment
- Personal computer and hardware beyond that provided in the technology refresh cycle unless there is a compelling need or new employee

.

M/IRM will approve and procure the equipment/services for Washington operating units to ensure consistency with Agency standards and economies of scale. Missions must still receive technical approval from M/IRM for all IT hardware and software purchased for installation on the Agency network.

Cost Centers/Capital Investment Funds (CIF)

To date, the Agency has had cost centers and/or CIF funds for IT, Personnel Support, Staff Training and General Support. As part of the MTB exercise, the cost centers and CIF accounts will be examined line by line and a determination made as to which costs must be centrally managed and which costs can be allocated to the various offices/bureaus. This process will be concluded by November 30, 2006. When this analysis is completed, appropriate costs will be allocated by PPC to the individual OU's budget.

Operational Budget Guidance

Following is a summary of the operational budget request guidance issued for FY 2007 and 2008. This includes both Operating Expense funding (OE) and Program Funding for Administrative Costs. The complete budget guidance is provided as an attachment.

Budgeting under MTB

- Operating units are defined as missions, independent offices, and bureaus.
- Operating units that manage program funds must prepare comprehensive operational budgets that include program-funded operational expenses in addition to administrative expense accounts.
- In general, OUs that do not manage program funds should prepare only an OE budget.
- The Agency will now conduct a comprehensive review of all operational expenses to set budget allocations. Under this approach, **managers must justify all expenses**, as opposed to only explaining increases over the prior year's budget.

Operational Cost Ratios

- As part of the ongoing planning for the Agency-wide roll-out of the Manage-to-Budget initiative in FY 2007, PPC requested data on FY 2006 program-funded operational expenses from all operating units.
- PPC analyzed the data submitted to develop operational cost ratios. The percentages identified below reflect the baseline analysis, represent an average across OUs, and include USDH salaries and benefits.
- As a guideline, regional bureaus and missions can request no more than 6% of their annual program new obligation authority (NOA) for program-funded operational

expenses. Their total operational costs (OE and program-funded) cannot exceed 12% of their annual NOA.

- As a guideline, pillar bureaus can request no more than 14% of their annual program NOA for program-funded operational expenses. Their total operational costs (OE and program-funded) cannot exceed 17% of their annual NOA.

- Although the operational cost ratios are set as a percentage of new obligation authority, operating units can use their annual OYB, which includes NOA, carryover, and recoveries, to fund their program-funded operational expenses.

- For example, if mission X has an FY 2007 NOA of $30 million and FY 2007 OYB of $40 million, it can spend no more than $1.8 million (6% of $30 million) on program-funded operational expenses in FY 2007.

- OUs that request budget levels exceeding these ratios must justify their needs.

- OUs that do not manage program funds are not subject to these ratios.

<u>Operational Budget Requests</u>

- OUs should assume their FY 2007 program levels equal the FY 2007 CBJ levels. For FY 2008 program levels, missions, Washington and overseas regional programs should consult with their regional bureaus for the latest program levels from the F country core teams. Pillar bureaus should use the latest F FY 2008 program levels.

- Requests should contain four brief narrative justifications: (1) 10% reduction from the FY 2006 OE operating year budget allocation for both FYs 2007 and 2008 (target levels); (2) requirements above the target for both FYs 2007 and 2008 (above-target levels); (3) program-funded operational expenses, if applicable, not exceeding the operational cost ratio for both FYs 2007 and 2008 (target) and requirements above the ratio for both FYs 2007 and 2008 (above-target levels); and (4) workforce.

- Target requests should discuss how they factor shifting program priorities, efforts to improve efficiency, proposed realignments in resources, and captured savings (e.g., lease savings resulting from co-locations). They should also discuss the negative implications of a reduced budget, including the:

  - impact of anticipated growth in program levels or responsibility;
  - curtailment of current operations required to cover increased fixed costs, such as inflation in personnel costs, rent increases, etc.; and
  - Agency's increased operational vulnerability.

- Above-target requests should describe and quantify the request in terms of:

  - maintenance of current operations;
  - changes to/expansion of programs managed;

- Staff/items/activities previously program-funded; and
- Other (trust fund situations, co-locations, regionalization, mission opening/closing, etc.)

- Managers should consider and address the following criteria when requesting their workforce levels (end-of-year on-board levels):

  - All work performed is essential.
  - The organizational structure reasonably balances efficiency and effectiveness.
  - The organizational structure is sound from a human resources management viewpoint.
  - The organizational structure enhances communication, decision-making, and responsiveness.
  - Positions and organizational structure are sound from a motivational viewpoint.

<u>Budget Review Process</u>

- PPC will lead operational budget teams with members from the bureaus and the Office of Human Resources in reviewing the requests and recommend allocations to the Administrator by September 22, 2006.

  - The budget teams will consider the following in making initial budget recommendations:
    - Workforce Planning Model recommended allocations;
    - Comparison of ratios against Agency norms;
    - Description of activities supported; and
    - Program level and composition.

- PPC will provide OUs with their initial FYs 2007 and 2008 allocations by October 13, 2006. Operating units can request the Administrator reconsider their initial levels, including workforce level assumptions, by October 20, 2006. An initial OYB will be set by October 27, 2006.

- The payroll estimate used to make the allocation will be based on the budget team's recommendation on workforce levels regardless of the current on-board level. It should be noted that although this level will not be adequate to support 100% of the positions at any given time, it will support the recommended number of positions given Agency-wide standard vacancy rates (lapse rates).

Note: Also included in the budget guidance are the standard templates for each Bureau/office to use for the OE submission. One template is for the budget numbers and the second is for the budget narrative justifying the request.

Incentives for MTB

Managing to budget requires comprehensive and systematic information about operational costs; accurate and timely data on performance, results, and effectiveness; and useful and practical tools for implementing management and budget decisions. Just as important, managing to budget requires appropriate incentives that motivate managers to use available resources more efficiently and effectively, while eliminating disincentives that undermine the MTB effort. The Agency is in the process of developing an incentives structure for MTB which will implement the following types of incentives:

- **Personal Incentives** that reward particular individuals (with bonuses, compensatory time, recognition, etc.) who manage to budget effectively or who are able to improve morale, effectiveness, customer service and results within existing budgets; and

- **Organizational Incentives** (such as increased budget resources or flexibility) that reward missions, offices, and other organizational units for operating effectively and efficiently.

Detailed guidance for managers will be issued after the FY 2007 budgets have been set. A system is being developed in which OUs will receive a percentage of the savings realized over the fiscal year, for incentive awards and other costs, while the remainder will be returned to the Agency to use in enhancing our programs and increasing benefits to countries that we are assisting. We will also survey other government and private organizations to learn the best practices.

Data Requirements

A sample of an Operational Budget template for tracking MTB costs are provided at Attachment 2. The Data Systems Support and Report Design working group are currently conducting an inventory of data elements needed for MTB and then mapping them to current systems to determine what other data systems are needed. As part of this process they are also refining a US direct hire payroll tool to help managers manage their payroll, developing other tools to help managers track their OE expenses, as well as exploring current systems for adaptability for MTB. It is estimated that required data systems for MTB should be implemented by October 1, 2007.

Communications

The MTB steering committee has established a website at http://inside.usaid.gov/M/MTB where all information related to MTB can be found. Also posted (and attached) is the communication strategy which details major milestones for the project.

Training

Trained facilitators will deliver traditional instructor-led classroom training that will be composed of presentation slides and scenarios based on USAID-specific procedures. In addition to instructor-led training, facilitators will provide training materials that will include examples and screen shots of the MTB tools. The classroom training will employ actual work scenarios that will allow the learner to understand how to use MTB. Following are important dates related to training:

Key milestones:

Training Materials completed	August 10, 2006
Train the Trainer Begins	August 24, 2006
Training Classes Begin (Washington)	August 29, 2006
Training classes Begin (overseas audience)	September, 2006

Performance Assessment

In an effort to assess the impact of MTB, operating units will be required to track their progress and report on a quarterly basis the following information: 1) Changes to personnel composition, for example changes in grade structure or conversion of categories of employees (e.g. PASA to PSC); 2) Shifts between payroll and non-payroll costs; and 3) Organizational structure changes. This information should be provided to PPC. Other centrally maintained information will also be used in the assessment, including progress of spending against payroll estimates.

Attachments:

1. Operational Budget Request Guidance for FYs 2007 and 2008
2. Sample of Operational Budget Template