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United States General Accounting Office
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B-300480.2

June 6, 2003

The Honorable Christopher Bond
Chairman
The Honorable Barbara Mikulski
Ranking Minority Member
Subcommittee on VA, HUD, and Independent Agencies
Committee on Appropriations
United States Senate

Subject: Corporation for National and Community Service: Amount of Obligations

This responds to your request of May 20, 2003, that we review the conclusion of the Office of Management and Budget (OMB) that the Corporation for National and Community Service (Corporation) may continue to record obligations based on the Corporation's estimates of "the amount of funds [it] will actually have to pay for the [national service educational] awards that are earned and used" rather than recording its maximum potential liability. See Letter of May 2, 2003 from Phillip Perry, General Counsel, OMB, to Frank Trinity, General Counsel, Corporation for National and Community Service. OMB's position is, as you know, at variance with our prior advice on this matter. B-300480, April 9, 2003. Specifically, you asked whether OMB has offered a legal basis for the Corporation to deviate from the requirement to record obligations according to fiscal law requirements upon grant award.

As noted below, we continue to disagree with OMB's legal conclusion that the Corporation may record its obligations for education benefits on the basis of estimates of what it will have to pay when education awards are earned, i.e., its probable accounting liability, rather than according to fiscal law requirements, i.e., its maximum potential liability. At the same time, we note that Congress has provided specific statutory flexibility to address situations where certain probable accounting liabilities may likely be greater or less than the real economic costs to the government, for example, the Federal Credit Reform Act of 1990 (Pub. L. No. 101-508, title XIII, § 13201(a), i.e., credit reform. Congress may wish to provide similar flexibility to the Corporation in obligating national service education awards.

BACKGROUND

As we explained in our April 9 opinion, at the time the Corporation awards a grant, it enters into a binding agreement authorizing the grantee to enroll a specified number of new participants in the AmeriCorps program without any further action by the Corporation. Because the Corporation, at time of grant award, accepts a legal duty to cover the education benefits of the new participants, it incurs, and must record, an obligation at that time. 42 Comp. Gen. 733, 734 (1963). Since the amount of the government's obligation is under the control of the grantees and those they enroll, not the Corporation, the Corporation must obligate funds to cover its maximum potential liability. See, e.g., B-238581, Oct. 31, 1990; B-197274, Sept. 23, 1983. As more information is known, for example, when an approved participant fails to enroll or a volunteer drops out of the program, the Corporation may adjust the obligation, i.e., deobligate funds or increase the obligational level, as needed. Because funds in the Trust are available without fiscal year limitation, the deobligated funds can be reobligated and used for future education benefits. At the time of grant award, the Corporation's obligation for the education benefits is equal to the number of approved positions in a grant award multiplied by the total value of a national service educational award.

In its May 2 letter, OMB agrees that the Corporation incurs a recordable obligation at the time of grant award. OMB apparently, however, does not consider the amount of the recordable obligation for the education benefits to be defined as the maximum potential liability reflected in the grant agreement. OMB finds a distinction between obligations based on "reasonable and conservative estimates that reflect historical experience" and obligations based on what OMB calls "theoretical maximums."

OMB argues that the Corporation may use historical experience and modeling to estimate its obligation for national service educational awards because the Congress contemplated that the Corporation would record obligations based on estimates. OMB bases this argument on two provisions of the National and Community Service Trust Act of 1993, Pub. L. No. 103-82, 107 Stat. 785. The first provision is 42 U.S.C. § 12581(f), which provides that

> "The Corporation may not approve positions as approved national service positions under this division for a fiscal year in excess of the number of such positions for which the Corporation has sufficient available funds in the National Service Trust for that fiscal year, taking into consideration funding needs for national service educational awards . . . based on completed service. If appropriations are insufficient to provide the maximum allowable national service educational awards . . . for all eligible participants, the Corporation is authorized to make necessary and reasonable adjustments to program rules."

OMB argues that section 12581(f), permitting an adjustment to program rules, contemplates that the Corporation will obligate based on estimates because appropriations would be insufficient only if the Corporation underestimated the amount it would need.

The second provision on which OMB relies is 42 U.S.C. § 12603, which prescribes the value of national service educational awards. OMB argues that because this section does not provide a single "value" of an award, the Corporation must necessarily estimate its liability. We will discuss each provision separately below.

DISCUSSION

Obligation of Appropriations

The federal government generally operates on an obligation basis. This means that an agency first takes some action that creates the legal liability to pay–that is, the agency "obligates" itself to pay–and the actual disbursement of money typically follows at some later time. An agency can incur a legal liability, i.e., a claim that may be legally enforced against the government, in a variety of ways, such as by signing a contract, grant or cooperative agreement, or by operation of law. Collins v. United States, 15 Ct. Cl. 22 (1879). A general definition of an obligation is "a definite commitment that creates a legal liability of the government for the payment of goods and services ordered or received." B-116795, June 18, 1954[1]. For the concept to be meaningful for funds control purposes, we have not limited the definition solely to agency actions that create legally enforceable claims against the government, but also have extended the definition to include a legal duty on the part of the United States which could mature into a legally enforceable claim by virtue of actions on the part of the other party beyond the control of the United States. 42 Comp. Gen. 733, 734 (1963); see also McDonnell Douglas Corp. v. United States, 37 Fed. Cl. 295, 301 (1997).

As we explained in our April 9, 2003, opinion, understanding the concept of an obligation and properly recording obligations are important because an obligation serves as the basis for the scheme of funds control that Congress envisioned when it enacted such fiscal laws as the Antideficiency Act. 31 U.S.C. § 1341(a); B-237135, Dec. 21, 1989. Under that act, an agency may not incur an obligation in excess of the

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[1] When an agency enters into a contract, the agency incurs and must record an obligation for the value of the goods and services it has ordered. An accrual accounting system does not recognize the transaction until it becomes probable that there will be a future expenditure of funds. Therefore, the recognition of obligations generally occurs earlier and in some cases will be in amounts greater than what would be recognized as the probable future accounting liability. FASAB Statement of Federal Financial Accounting Standards No. 5.

amount available to it in an appropriation unless authorized by law. 31 U.S.C. § 1341(a).

The Antideficiency Act evolved over a period of time, in response to various abuses. As late as the post-Civil War period, it was not uncommon for agencies to incur obligations in excess of or in advance of appropriations. Some agencies would spend their entire appropriations during the first few months of the fiscal year, continue to incur obligations, and then return to Congress for appropriations to fund these "coercive deficiencies." Hopkins & Nutt, The Anti-Deficiency Act (Revised Statutes 3679) and Funding Federal Contracts: An Analysis, 80 Mil. L. Rev. 51, 56-58 (1978); Louis Fisher, Presidential Spending Power 232 (1975). The congressional response to abuses of this nature was a series of enactments collectively known as the Antideficiency Act, which prescribes a set of funds control and financial management procedures regarding the obligation and expenditure of agency funds.

In addition, an agency is required to properly record its obligations. The standards for the proper recording of obligations are found in 31 U.S.C. § 1501(a). Congress enacted this statute because it "did not have reliable information in the form of accurate obligations on which to determine an agency's future requirements." Senate Committee on Government Operations, Financial Management in the Federal Government, S. Doc. No. 11, 87th Cong., 1st Sess. 85 (1961).

Today, the revised Antideficiency Act serves as the primary foundation for the government's administrative control of funds systems. In its current form, the law prohibits, among other things:

1. Making or authorizing an expenditure from, or creating or authorizing an obligation under, any appropriation or fund in excess of the amount available in the appropriation or fund unless authorized by law (31 U.S.C. § 1341(a));
2. Involving the government in any contract or other obligation for the payment of money for any purpose in advance of appropriations made for such purpose, unless the contract or obligation is authorized by law (31 U.S.C. § 3324(a)).

For purposes of identifying the amount of the obligation, an agency must first identify whether it is the agency or the contractor (or grantee) that controls the costs. 59 Comp. Gen. 518 (1980); 47 Comp. Gen. 155 (1967). If the amount of payment is under the control of the grantee, not the government, the government should obligate funds to cover its maximum potential liability. See, e.g., B-238581, Oct. 31, 1990; B-197274, Sept. 23, 1983. In regard to the national service educational benefits, the Corporation must obligate the maximum potential liability because the amount of the Corporation's obligation is under the control of the grantees and

those they enroll. Otherwise, the Corporation may violate sections 1341(a) or 3324(a). We now address OMB's interpretation.

The Requirements of the National and Community Service Trust Act

In our view, 42 U.S.C. § 12581 does not support OMB's interpretation that section 12581(f) contemplates that the Corporation may estimate the amount to deposit in the Trust. Subsections (a) through (d) of section 12581 provide the Corporation with percentage allocations to distribute grants and approved national service positions to states, Indian tribes, federal agencies, and other applicants. The first sentence of subsection (f) says no more than that the Corporation must have adequate funds in the Trust to cover education awards for the total number of approved national service positions allocated by the previous subsections. If, however, adequate budget authority is not available, the second sentence of subsection (f) permits the Corporation to adjust "program rules" to ensure that the Trust will not be overobligated.

There is nothing in the statute or in the related legislative history that indicates that adjustment to "program rules" refers to adjustments to long-established fiscal law requirements for recording obligations. The National and Community Service Trust Act defines the term "program" as applying to eight specific programs created by the Act. 42 U.S.C. § 12511(9). This definition includes national service programs. However, the definition of "program" does not cover or define the amount of funds deposited into the National Service Trust to be disbursed as education benefits. 42 § U.S.C. 12572(a). Congress stated that its purpose in inserting the second sentence of subsection (f) was "[t]o ensure that the Act is not considered as an entitlement program." 139 Cong. Rec. S9282-01 (1993) (Unanimous consent agreement). Section 12581 emphasizes Congress' direction to the Corporation to fully obligate the funds necessary to cover the education awards for the total number of approved positions.

In its May 2 letter, OMB provided examples of three statutes that specifically instruct agencies to use "estimation methodologies to determine the amount of funds to be obligated," rather than fiscal law requirements, namely the Federal Credit Reform Act of 1990 (Pub. L. No. 101-508, title XIII, § 13201(a), 104 Stat. 1388-609)[2]; the

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[2] Congress enacted the Federal Credit Reform Act to allow policymakers to make more informed decisions about credit programs. Prior to the enactment of credit reform, the real economic costs of direct loan programs were overstated and the real economic costs for loan guarantee programs were understated. The Credit Reform Act requires an agency to estimate the long-term cost to the government associated with a loan or loan guarantee and record this as an obligation against available budget authority appropriated to cover these costs in the year the loan or guarantee is made. 2 U.S.C. § 661c(b). See, e.g., U.S. General Accounting Office, Department of

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Department of Defense Education Benefits Fund (10 U.S.C. § 2006)[3]; and the multiyear contract authority provided in the Federal Acquisition Streamlining Act of 1994 (Pub. L. No. 103-355, § 1072, 108 Stat. 3243, 3270).[4] In each of these statutes, Congress has modified for specific purposes, to some degree, established fiscal law requirements for recording obligations. Each is an exception to the general rule for recording obligations and authorizes agencies to record estimated probable accounting liabilities as budgetary obligations. Rather than supporting OMB's argument, these statutes illustrate that when Congress wishes to give an agency authority to record estimated probable accounting liability as obligations it does so explicitly. In fact, these statutes illustrate that Congress has not provided the Corporation with the explicit authority to estimate its future probable accounting liabilities for purposes of recording its obligations, as OMB claims.[5]

The second provision on which OMB bases its argument is 42 U.S.C. § 12603. The National and Community Service Trust Act requires that the Corporation calculate the value of its obligations for education benefits based on approved national service

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Education: Key Aspects of the Federal Direct Loan Program's Cost Estimates, GAO-01-197 (Washington, D.C.: Jan. 12, 2001).

[3] The Department of Defense Education Benefits Fund is "used for the accumulation of funds in order to finance armed forces education liabilities on an actuarially sound basis," and specifically authorizes defense agencies to record obligations on the basis of estimates of their probable accounting liability rather than on the basis of fiscal law requirements for recording obligations.

[4] The multiyear contracting authority provided through the Federal Acquisition Streamlining Act permits an agency to enter into a multiyear contract using fiscal year funds if the agency obligates funds for the full period of the contract. 41 U.S.C. § 254c. This statute also authorizes incremental funding for some contracts by permitting the agency to obligate the full costs for the first fiscal year plus estimated termination costs. The requirements to obligate the full amount of the contract or the full costs for the first year plus estimated termination costs upfront are designed to protect the government from future claims in excess of available budget authority.

[5] Congress could, if it deems appropriate, authorize the Corporation to estimate its probable liability for purposes of recording obligations. It is important, however, that the agency have the necessary systems and controls in place to properly estimate, monitor, and control its budgetary requirements. In its audit of the Corporation for National and Community Service's Fiscal Year 2002 Financial Statements, KPMG reported that the Corporation approved more positions in fiscal year 2002 than what was estimated as supportable by the National Service Trust. Audit Report 03-01 at 23, KPMG, Feb. 4, 2003. The Corporation has stated that it is in the process of implementing new oversight and enrollment procedures; it is too soon, however, to evaluate their effectiveness.

positions. Section 12571(c) of title 42, United States Code, requires the Corporation to deposit into the Trust "an amount equal to the product of — (A) the value of a national service educational award under section 12603 of this title; and (B) the total number of approved national service positions to be provided." Section 12603 provides values for (a) full-time national service, and (b) part-time national service, and instructs the Corporation to provide a pro-rated amount for (c) partial completion of service. OMB argues that because different values apply, in order to determine the "value" for section 12571(c), "the Corporation must necessarily rely on robust estimates, based on historical experience, of the extent to which volunteers complete their service and, when service is not completed, the extent to which they receive pro-rated awards."

We disagree. Section 12571(c) begins by stating that the Corporation must deposit into the Trust the value specified in section 12603 multiplied by the total number of approved national service positions. At the time of grant award, the Corporation knows the total number of full- and part-time national service positions it is approving. Pursuant to 12571(c), the Corporation is required to multiply the total number of approved positions by the appropriate categories in section 12603. At the time of grant award, this will be either the full-time value or 50 percent of the full-time value. For example, if the Corporation approves 50 part-time and 50 full-time positions in a grant award, the Corporation is required to multiply the 50 full-time positions by $4,725, which is the maximum education benefit a full-time participant can earn, and multiply the 50 part-time positions by $2,362.50. See 45 C.F.R. § 2527.10. The sum of these amounts is the Corporation's obligation according to current fiscal law requirements. Congress' instructions to provide a pro-rated amount for the partial completion of service allows the Corporation to adjust the amount of its obligation and deobligate excess funds when a participant leaves national service without completing his or her term of service.

CONCLUSION

Accordingly, we find no reason to change our opinion with regard to the amount of funds that must be obligated at the time the Corporation authorizes a grant recipient to fill positions. Because the Corporation, at time of grant award, accepts a legal duty to cover the education benefits of new participants, it incurs, and must record, its maximum potential liability at that time. As we stated in our April 9 legal opinion, to ensure compliance with the Antideficiency Act, 31 U.S.C. § 1341, and other fiscal laws, the Corporation should be recording and tracking its obligations as the value of an educational award multiplied by all approved positions. This requirement to record the maximum potential liability does not undermine, however, the value of the Corporation's estimating its probable future liability for accounting purposes, which is intended to represent the best estimate of the Corporation's probable future liability for financial statement purposes. We note that the Corporation could seek legislation that would permit it to use an estimation model for recording its

obligations. (This model could be similar to the process that would be used to determine the Corporation's accounting liability.) If you have any questions, please contact Susan A. Poling, Associate General Counsel, at 202-512-5644.

Anthony H. Gamboa
General Counsel

DIGEST

As we stated in our April 9, 2003, legal opinion, because the Corporation for National and Community Service, at time of grant award, accepts a legal duty to cover the education benefits of new participants, it incurs, and must record, its maximum potential liability at that time. To ensure compliance with the Antideficiency Act, 31 U.S.C. § 1341, and other fiscal laws, the Corporation should be recording and tracking its obligations as the value of an educational award multiplied by all approved positions. As more information is known, for example, when an approved participant fails to enroll or a volunteer drops out of the program, the Corporation may adjust the obligation, i.e., deobligate funds or increase the obligational level, as needed. Because funds in the Trust are available without fiscal year limitation, the deobligated funds can be reobligated and used for future education benefits. B-300480, April 9, 2003.