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How Working Capital Funds Can Help Mitigate The Impacts Of Funding Instability

Irregular funding and stop-gap measures are the unfortunate reality of Federal Government appropriations today. Congress has passed continuing resolutions (CRs) to keep the government running in all but three of the last 40 years,[3,4] including multiple CRs in every one of the past 20 years. Lapses in appropriations have forced the government to shut down 4 times since Fiscal Year (FY) 2013,[5] and the last shutdown that occurred from December 22, 2018 to January 25, 2019 was the longest such event in US history.[6] Once enacted, funding is often "one-year" money, limiting the amount of time Government leaders have to utilize it prior to the end of the FY.

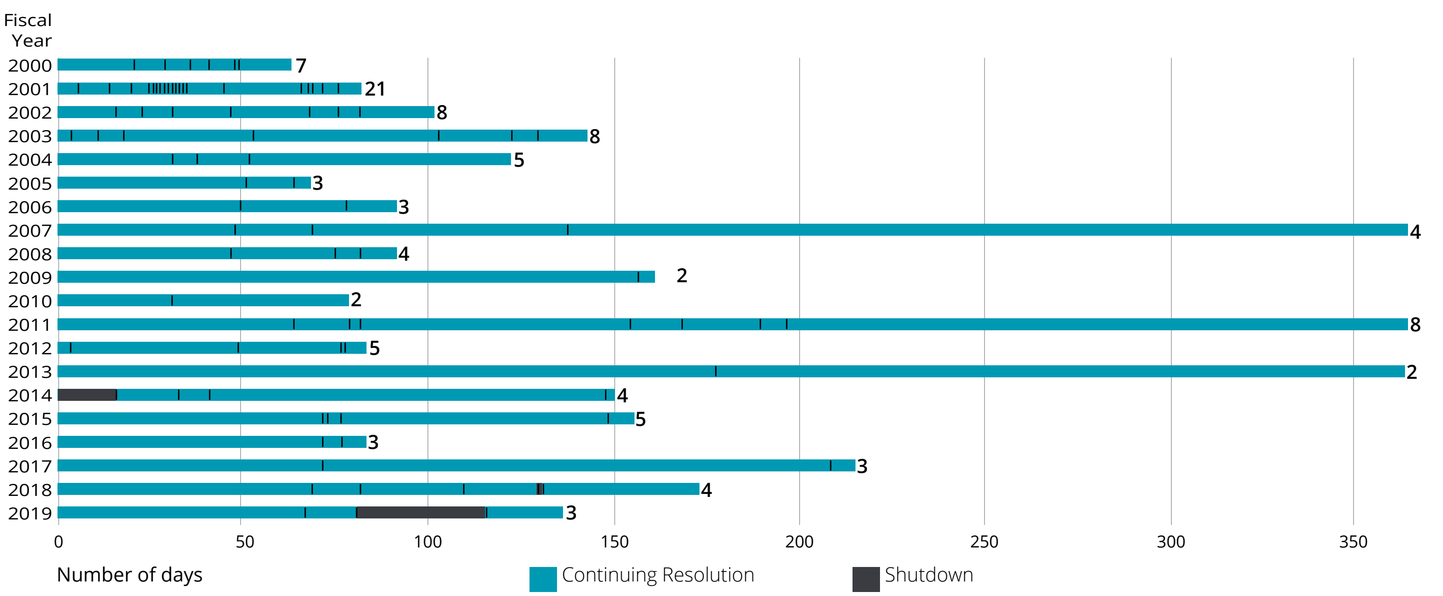
Shutdowns have a significant impact on agency missions and represent serious costs to the US Government and economy as a whole. The Office of Management and Budget (OMB) estimated the 16-day shutdown in 2013 incurred over $2 billion in costs for services that could not be performed.[8] The Congressional Budget Office (CBO) estimates that the partial shutdown from December 22, 2018 through January 25, 2019 reduced real GDP growth by $3 billion.[9]

Once enacted, time-bound limitations on funding further constrain agencies' ability to make long-term investments, which is particularly evident in government information technology (IT) spending. The Federal government plans to spend more than 80 percent of its total IT budget on Operations & Maintenance (O&M) of existing systems in FY19. This may lead to impacts on operational efficiency, increased cybersecurity risks, and limitations on administrative support needed to meet mission requirements.[10]

The Impacts of Funding Instability

CRs and shutdowns are generally detrimental to workforce stability and morale, disruptive to operations, and exceedingly costly. Agency officials reported to the Government Accountability Office (GAO) that CRs resulted in limited or delayed spending, and inefficiencies including delayed hiring and rework.[7] Depending on the length of a given CR, agency spending is constrained to a few days, weeks, or months. This often results in implementation delays, as agencies are hesitant to commit to any activities (including hiring and contractual actions, grant agreements, travel, training, etc.) that require funding beyond the date of the present CR. Additionally, the need to re-enter into contractual agreements for each CR period not only creates substantial rework, but may also impact agencies' ability to negotiate more favorable terms due to the limits CRs place on duration and funding obligations.

Duration and number of continuing resolutions (CRs): FY 2000-2019



Sources: GAO-18-368T[1] and Congressional Appropriations and Budget Data[2]

How Working Capital Funds Can Help

A Working Capital Fund[11] (WCF) is a full-cost recovery operating model where program expenses are recovered through funds collected from supported customers, both internal and external to the organization. WCFs operate more like a business than a traditional government service, offering and scaling services in response to customer demand, and securing funding through customer payments for those services. Implemented effectively, this operating model offers multiple key benefits for organizations:

- **Increased Cost Transparency and Efficiency:** Under a WCF model, customers pay the WCF for products and services consumed, and receive transparent pricing information as to their full costs. This incentivizes customers to consume only what is needed to support their mission needs and puts pressure on WCF service providers to contain costs.

- **Improved Mission Delivery:** The efficiency of the WCF business model drives organizations to align resources with mission requirements, driving proactive customer engagement, detailed cost analysis, and informed demand forecasting. These activities help increase coordination between mission and support functions, enabling WCF entities to better serve their customers, maintain an agile support environment, and identify cost reduction and containment approaches that have the least mission impact

- **Improved Ability to Make Long-term Investments**: Under the full-cost recovery model, WCFs must finance all expenses through customer agreements. Subject to the terms of these agreements, this may include planning and capitalizing long-term investments in improvements to the WCF, including but not limited to IT and cybersecurity improvements.

  In compliance with applicable reprogramming law, an agency's existing transfer authority, and Appropriations Committee guidelines,[12] agencies with WCFs established under the Modernizing Government Technology Act[13] may reprogram and transfer funds to the WCF, including cost savings achieved through IT upgrades and funds originally designated for the O&M of existing systems. Such funds are available for obligation within three years, encouraging agency leadership to identify and utilize this funding to invest in multi-year IT and cybersecurity improvements..

- **Increased Continuity of Operations:** Service level agreements with customers provide WCFs the budget authority to operate and collect reimbursements from customers. Subject to the authorizations within these customer agreements, WCFs may maintain continuity of operations in times of uncertainty, continuing to provide and/or finance authorized services by managing cash flow and operating reserves. This flexibility is generally greatest when executing non-severable, fully-funded orders for customers, as the WCF's authority to operate is defined by an agreement which may span multiple CRs or FYs.

  Agreements with severable services may be more constrained, as the terms of the customer agreement (and thus the WCF's authority to provide services) will be affected by funding instabilities like CRs and shutdowns. Further, agreements with customers external to the WCF's host agency are subject to the Economy Act,[14] requiring that any funds that remain unobligated at the end of the FY be returned to these external customers.

  Subject to these constraints, common agency-level guidance is that WCFs with positive cash balances and budget authority via customer orders may continue to operate until cash reserves are insufficient,[15] allowing them to operate through a shutdown and mitigate many of the challenges identified above. To conserve cash reserves WCF will generally look to non-essential activities. While these will vary agency to agency, some of the common tactics are to delay trainings, minimize or eliminate travel, reduce the procurement of supplies, reduce vendor support for administrative related contracts, furlough federal staff in more administrative support roles, and temporarily suspend upgrade projects that are not critical to the current mission.

Striking the Right (Cash) Balance

Maintaining an appropriate cash balance is a critical component of any WCF, and it is particularly important when dealing with funding uncertainty. Key considerations include:

- **Reserve Limits:** When planning and managing cash levels, WCFs must strike a suitable balance between planning for uncertainty and exceeding responsible maximum cash requirements. In most cases, there are limits placed on WCFs in terms of reserves, as these revolving funds are designed to be 'break even' over time. Therefore, the WCF program must carefully calculate uncertainty premiums each year and maintain a plan for addressing excessive reserves.

- **Demand Forecasting:** Effective cost and demand forecasting is fundamental to maintaining cash balances within minimum and maximum requirements. WCFs need to closely examine data elements that may provide insights into annual demand curves. Analyzing historical data in conjunction with forward-looking customer consumption trends will aid in calculating unit prices that will yield a 'break even' recovery.

- **Reporting:** Effective cash management largely depends on managers receiving accurate and timely data on cash balances, collections, and disbursements. To that end, well-run organizations will conduct status of funds checks against their WCF on a regular basis. This helps fund managers understand how long the fund can operate under in situations of funding uncertainty.

Considerations for Establishing a WCF

It is important to note that a WCF operating model may not be an appropriate fit for all organizations. Establishing a WCF requires statutory authorization from Congress and may take years from the inception of the idea to implementation. When discussing both internally and with Congress as to whether or not to establish a WCF, agencies should consider a number of key scoping and readiness factors. Please see the following articles for perspectives on leading practices dedicated to this subject:

Federal CFO: Considerations for Using Working Capital Funds[16]

Making the Most out of the Modernizing Government Technology Act[17]

Making a Working Capital Fund Work for You

In today's evolving landscape, Federal CFOs are under increased pressure to improve operational efficiencies and provide an additional degree of strategic planning capability. Meeting these objectives is often complicated in periods of funding uncertainty, including CRs or government shutdowns. In these situations, agencies may struggle to support changing mission needs due to limits in available funding. These realities often require leaders to make difficult decisions about program funding which limit the ability to take a strategic approach towards investment planning thus stifling modernization efforts.

Through full-cost recovery, WCFs provide Federal CFOs with the ability to recover long-term investment costs through customer agreements by capitalizing these costs over time. For example, WCFs established through the Modernizing Government Technology Act[18] may facilitate long-term investments in IT and cybersecurity improvements across the host agency. These attributes contribute to an environment in which Federal CFOs can take a significantly more strategic approach towards investments.

A function of being less dependent on direct appropriations is the additional level of flexibility an organization has when faced with a CR or shutdown. Subject to the nature of their customer agreements, WCFs may be able to continue to operate on cash reserves. While WCFs do not represent a silver bullet solution to funding uncertainty, they may enable some agencies to operate with fewer limitations during these periods.

Federal CFOs should consider the strategic and operational advantages that WCFs can provide to their organizations. While WCFs do come with additional burdens around management and reporting, their design helps leaders operate more strategically and may provide additional degrees of flexibility when faced with funding uncertainty.

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11. As used in this document, "Working Capital Fund" refers collectively to intragovernmental revolving funds, which depending on the agency may also be labelled as Franchise Funds, Supply Funds, Building Funds, etc.
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