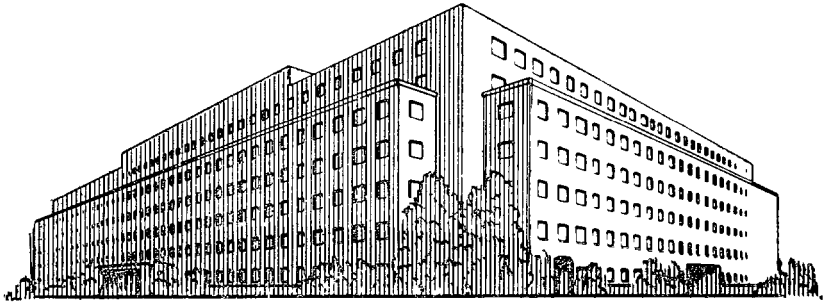




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The GAO Review



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THE GAO REVIEW

WINTER 1968

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Published quarterly for the accounting and auditing staffs of the U.S. General Accounting
Office

Protecting the Taxpayer's Dollar

721328

By Elmer B. Staats
Comptroller General of the United States

This address was made on September 26, 1967,
by Mr. Staats at the 80th annual meeting of the
American Institute of Certified Public Accountants
in Portland, Oregon.

Federal expenditures are now running at the rate of more than \$150 billion a year. This figure is about twice what it was 10 years ago. I think we all can expect the increase to continue. The General Accounting Office, which I head, plays a crucial role in the ever-present job of protecting this ever-increasing number of taxpayers dollars. I therefore welcome this opportunity to tell you, briefly, who we are, how we carry out our job, and what we see in the future.

Concept of Independent Audit

The concept of the independent and impartial review or audit of Government expenditures is deeply founded

in American and Anglo-Saxon history. Although the General Accounting Office was not established until 1921—some 46 years ago—this concept of independence was imbedded in the legislation that created it.

—While appointed by the President, the Comptroller General can be removed only by impeachment or joint resolution by the Congress.

—Both the Comptroller General and the Assistant Comptroller General are appointed for terms of 15 years.

—The Comptroller General cannot be reappointed.

**Elmer B. Staats, Comptroller
General of the United States**



—The General Accounting Office is an agency of the Congress.

—As every Comptroller General has emphasized, the GAO is a non-political and nonpartisan organization.

The GAO staff totals approximately 4,300, including about 2,400 professional accountants and auditors and 100 attorneys. In addition to the Washington headquarters there are 16 regional offices and five overseas offices.

The overall role of the General Accounting Office is to assist the Congress in carrying out its oversight responsibilities. We provide the Congress—as its agency—a multitude of services, most of which are intended to result in greater efficiency and economy in Government operations. GAO is, therefore, an important part of the management information system of the Congress.

Our Office is responsible, with limited exceptions, for auditing all programs, activities, operations, and financial transactions of the Federal Government and for making reports to the Congress containing recommendations for greater economy and efficiency in Government operations. We assist in drafting legislation, make factual investigations for congressional committees, testify before committees, and handle numerous inquiries from Members of Congress as well as from committees.

We have far-reaching responsibilities in prescribing accounting principles and approving accounting systems for Government agencies and in assisting them in developing improved financial and management information systems.

The operations of the General Ac-

counting Office are perhaps most widely known because of its audits and related reports on the activities of the departments and agencies of the Federal Government and many of its contractors. These reports to the Congress are made public.

The Government Corporation Control Act of 1945 provided that financial transactions of wholly and mixed-owned Government corporations would be audited by GAO in accordance with the principles and procedures applicable to commercial corporate transactions.

Success in auditing Government corporations, highlighted by a very bad situation in the Maritime Commission, led to the assignment of the audit of the U.S. Maritime Commission. A congressional investigation had revealed an almost complete breakdown in the agency's recording and collection of accounts receivable.

This audit was particularly significant for, among other reasons, it resulted in a reorganization of the Commission and produced large-scale refunds from the adjustment of payments to ship operators.

It did much to establish in the eyes of the Congress the value of generally accepted auditing standards carried on at operating sites.

These experiences led to the adoption of a broadened comprehensive audit program in the General Accounting Office and, soon after, the Accounting and Auditing Act of 1950. This law extended statutory recognition to the application of generally accepted principles of auditing to the financial transactions of executive agencies in general.

Our Office has made much progress

in developing techniques and experience in reviewing management performance in the Federal agencies. It has been our longstanding policy to place particular audit emphasis on functional areas of agency operations believed to require correction or improvement and on means of *effecting* the needed corrections. Congressional committees and individual Members of Congress are particularly interested in this phase of our work because it identifies opportunities for *improving Government operations* and *saving public funds*.

Some Examples

Some examples may be of interest to the many representatives here from the Pacific Northwest.

As a result of a typical management review, we reported that the Federal Aviation Agency had made separate grants to the adjacent communities of Kenai and Soldotna, Alaska, which are only about 12 miles apart, for improving their respective airports. Our review showed that each of the improved airports is capable of accommodating 100,000 air operations annually, which far exceeds the foreseeable combined traffic loads of the two airports.

The Agency's Alaskan region executed both grants on the basis that each proposed project, when considered separately, qualified for Federal assistance even though, in our opinion, it was evident that both airports, as developed by the grants, were not needed. As a result, the Government will contribute about \$233,000 for improvements to the Soldotna airport, a significant portion of which was not necessary to meet the then-

current or anticipated civil aviation needs of the area.

We believe that separate grants, in the amounts approved, would not have been made if the Alaskan region had followed the Agency's area airport policy of developing only one airport, where possible, to serve the needs of more than one community. In addition, our review disclosed that the Washington Headquarters Office had not established adequate procedures and controls to ensure compliance with the area airport policy.

A good example of the effective utilization of our work was the report we issued on July 18, 1966, on the results of our comprehensive survey of internal audit and management inspection activities of U.S. agencies operating in Vietnam. The Subcommittee on Foreign Operations and Government Information of the House Committee on Government Operations held hearings which confirmed and enlarged upon our survey findings that too little audit effort generally was being made in Vietnam by the agencies directly concerned.

Later, the committee recommended that we follow up with a review of the specific audit and inspection programs initiated in Vietnam by the responsible agencies during 1966. This review, on which we reported to the Congress in May 1967, showed significant increases in the number and scope of internal audits and management inspections since our earlier report, a result we think is directly attributable to the combined efforts of our Office and the committee.

Contract Auditing

Another area in which GAO has a continuing responsibility and consid-

erable interest is that of contract auditing.

For several years we sent numerous reports to the Congress describing negotiations which resulted, in our opinion, in unreasonably high prices for defense materials. These reports were a major factor leading to the enactment in 1962 of Public Law 87-653, the so-called "Truth-in-Negotiations" Act. We collaborated with the House Armed Services Committee and the Department of Defense in drafting this law. It was designed to safeguard the Government against inflated cost estimates in negotiated contracts and subcontracts, generally where competition is lacking. With certain exceptions this law requires contracting officials to obtain from suppliers cost or pricing data in support of their estimates *and a certificate* that the data submitted is accurate, complete and current.

It is axiomatic that a law must be properly administered in order to be effective. Therefore, our concern did not stop with the enactment of the legislation. We have closely followed the effectiveness of its administration, have issued three reports to the Congress containing numerous suggestions to this end, and have testified a number of times during congressional hearings having to do with the economy and effectiveness of Government operations.

Our followup review of 242 negotiated contracts and subcontracts indicates the widespread problems we encountered in the way this law was first administered. The 242 contracts we reviewed totaled \$600 million. Among other deficiencies we found that in 165 of the awards nei-

ther the contracting agency nor the prime contractor had records identifying the cost or pricing data submitted and certified to by the contractor.

Our most recent report concerned 237 construction contract actions negotiated since November 1964 for a total of about \$128 million. We found generally that, in negotiating construction contract and modification prices, sufficient cost or pricing data supporting the contractors' proposals were also not obtained. The reason was that Department of Defense officials believed the law did not apply to construction contracts since construction contractors' proposals are evaluated by comparing them with Government estimates. While comparing a proposal with an estimate serves a useful purpose, it is not an acceptable substitute for current and complete cost and pricing data.

When we pointed out these problems and deficiencies Department of Defense officials agreed to take steps to improve administration of the law.

As our review showed that Government estimates often exceeded available information on contractors' costs, these actions should result in significant savings.

The Joint Economic Committee and the House Armed Services Committee of the Congress have shown keen interest in our followup reviews and we plan to give continuing attention to the way the Truth-in-Negotiations Act is administered.

Internal Auditing

Internal auditing in Government agencies is a necessary part of a good management system and is becoming

of increasing value and importance in the Federal Government.

We are devoting more of our effort to reviewing the effectiveness of agency audit systems as a part of our regular audit work.

Along with the growth and strengthening of internal audit staffs in the operating agencies—a trend which has had strong support from the GAO and the Congress—there has been an accompanying decrease in the more traditional financial audit by the GAO. This type of audit now represents a relatively small portion of our activity. Commensurate with this trend, we have placed more and more emphasis in the GAO upon what is usually described as management audits, including in some cases program evaluations or reviews of Federal programs. We expect this trend to continue in the future.

As we all recognize, basic responsibility for effective, efficient and economical management lies with managers. This is well illustrated by the Department of Defense cost reduction program.

This program was launched in July 1962. It was truly a pioneering effort in Defense management. The Department has claimed monetary savings of billions of dollars as a result of this program.

But in Secretary McNamara's own words—an audit of the claimed savings should be made to be sure that they are bona fide. Under existing arrangements, internal auditors of the Department of Defense examined the claimed savings. We have agreed with Secretary McNamara that in future years we will review and test the adequacy of such internal audit work

and the criteria for measuring claimed savings.

I will not attempt to discuss all of the work of our Office but I should touch briefly on some of our other important responsibilities.

Legal Work

Our legal work extends across the whole range of activity of the executive branch and in some areas of the legislative and judicial branches. It involves problems arising under international law and laws of foreign countries as well as Federal and State statutes, administrative regulations, court decisions and other precedents.

An example of a legal case requiring consideration of the GAO is represented by a bid protest, which may be filed with our Office by any unsuccessful bidder who feels that the law or procurement regulations of the contracting agency have not been complied with.

Such a protest was filed recently by a large computer manufacturer against the selection of another leading computer manufacturer as the source of furnishing advanced computer equipment for the worldwide bases of the Air Force.

The Air Force had selected the successful bidder over three others after determining that it was the only one of the four to meet all mandatory requirements.

The runnerup's price was approximately one-half of the successful bidder's price of \$114 million. After bench mark tests the three losers were not considered further by the Air Force.

After reviewing its equipment, subsequent to the bid award, the protesting company concluded it could meet

the stipulated requirements within a short period of time by certain modifications of its equipment at relatively little additional cost.

Among other matters the protesting company asserted that the action of the Air Force in refusing to conduct further oral or written discussions with it after the bench mark tests was contrary to law.

We held that the protester should have been considered as being within the competitive range and that further discussion should have been conducted by the Air Force before selection was made.

Soon after our decision upholding the protesting company the Air Force canceled its selection and announced that it would reopen the negotiations.

Accounting and Financial Management

Another important responsibility we have is to prescribe the principles, standards and related requirements for accounting to be observed by each executive agency, to cooperate with the agencies in developing their systems, to approve those systems when they meet the prescribed principles and standards, and to review them in operation.

The first GAO comprehensive statement of accounting principles and standards was issued in 1952. It has been continuously updated and closely parallels the principles generally accepted by the profession.

The GAO is also directed by law to work with the Treasury Department and the Bureau of the Budget, to conduct a continuous program of improving accounting and financial reporting in the Government. About a year ago the Civil Service Commission was in-

vited to become a major participant in this joint program because of the great importance of qualified personnel to effective financial management systems.

Top representatives of these agencies meet from time to time with the Institute's Committee on Federal Budgeting and Accounting headed by Karney Brasfield to keep informed on problems and accomplishments in the area.

This program can claim many accomplishments during the years it has operated, not only in accounting and financial reporting, but also in improved practices that have resulted in savings of millions of dollars annually.

Still there is a long way to go. At present I have been able to approve just a little more than a third of the nearly 150 accounting systems subject to my approval.

We have found it difficult to gain general understanding and acceptance in the Federal establishment of the concept of accrual accounting and of the help good accounting can be in controlling operations and in forecasting future requirements.

Lack of understanding is due in considerable part to difficulty in communication.

For many years we have provided professional and advisory assistance to the agencies to assist in developing their accounting and financial management systems. We are devoting more attention to this important area and we believe that progress is being made in devising better accounting systems in the Federal departments and agencies even though it is not as rapid as some of us would like.

Current Trends and Possible Future Developments

Two strong forces that will certainly influence the future are apparent. One is a demand for more information and evaluation of plans. The other is the continuing demand for management performance evaluations.

It has been our policy to place particular audit emphasis on areas of agency operations thought to require correction or improvement. Most of our audit reports in recent years have concentrated on individual cases of management problems involving actual or potential losses and on making recommendations for their correction. This emphasis has resulted in substantial savings in public funds and undoubtedly has contributed to significant improvements in Federal operations.

Over the past 5 years alone benefits directly measurable in dollar terms resulting from our work have totaled over a billion dollars, or an average of over \$200 million a year.

These figures of course do not reflect the large number of GAO reports for which no dollar savings are reported—either because of the difficulty in estimating accurately the amount of the savings or because the recommendations are directed to overall management improvements which are not reflected directly in terms of budgetary savings. A good illustration is a recent report to the Congress recommending improved controls in the handling of nuclear materials made available to private industry by the AEC. Our recommendations were designed to assure full accountability for this highly valua-

ble and potentially dangerous material.

We believe that our work can be even more productive if we make more extensive inquiries into basic causes of the unsatisfactory conditions we find and include in our reports clear explanations of those causes and realistic recommendations for improvement. Our current audit work is pointed in this direction and is deliberately related more closely to the time schedules and interests of congressional committees. We think that by increasing the coverage and significance of our reports and improving their timeliness we will be providing greater assistance to Congress in carrying out its responsibilities.

In discharging our audit responsibilities as well as in carrying out our responsibilities for improvement of financial management and the approval of agency accounting systems, we are more interested in helping the agencies to discover and eliminate the weaknesses which we find than we are in publicly reporting shortcomings to the Congress.

Our broadened and responsive approach will involve the increasing use of the new quantitative techniques and methods from mathematics, statistics, electronic data processing, social sciences, and economics. The requirement that the accountant of today and tomorrow be knowledgeable in these fields has been recognized by your Institute in its highly significant and useful Common Body of Knowledge report.

Recruiting and Staff Development in GAO

To more effectively meet our broadened responsibilities we have extended

our recruiting efforts to majors in fields other than accounting such as economics, industrial management, engineering, and public and business administration. We are also sending selected staff members to educational institutions and strengthening our in-house professional training programs.

We continuously encourage our staff to join and participate in the activities of professional societies, since we recognize the significant contributions the institutes and societies make toward professional development.

I can illustrate this by the fact that 424 of our professional staff are now certified public accountants. Over 250 of these staff members obtained their experience with GAO. In addition, about 400 of our staff are preparing for the CPA examinations. About 100 will receive their certificates when experience requirements are met. About 200 of our staff are members of this Institute. Many of our professional accountants have served and are serving as officers and committee members of the AICPA and other professional organizations.

We are greatly encouraged by actions taken in the District of Columbia, the State of Pennsylvania, and the State of Michigan within the past year to recognize GAO experience as qualifying toward the CPA certificate. These accomplishments could not have been brought about without the fine cooperation which we received from the members of the American Institute and the local societies concerned. These actions will be of great assistance to the GAO and we look forward to similar actions in the few remaining States in which experience in our organization still does not qualify.

We must have the talent and knowl-

edge to meet the challenge represented by the greater sophistication of articulated accounting and management information systems resulting from ever-increasing technological capability—because the rate of increase is more likely to accelerate than slow down. The trend and the future we are preparing for are evidenced by a number of developments.

Planning, Programming, and Budgeting

One of the most important of these developments is that about 2 years ago, the President directed the development of an integrated planning-programming-budgeting system in the major agencies of the Federal Government. He placed emphasis on the importance of “high quality, business-type information system.” This system requires that realistic cost information be used in estimating future costs and in appraising current performance against approved plans. It emphasizes systems analysis and cost-effectiveness studies as a basis for decisionmaking in long-range planning, programming, and budgeting.

This is an important development in the Government’s management processes and we are taking steps to add to our own capability to make or review cost-effectiveness studies. We have also made it clear that accounting systems of Federal agencies must be capable of providing adequate support in the form of cost and other financial information for their planning, programming, and budgeting systems.

Congressional Interest in Better Information and Evaluations

Legislation now being considered by the Congress reflects its interest in

more adequate and timely information and for more management evaluations. It also provides insight into possible new responsibilities for GAO.

The proposed Legislative Reorganization Act of 1967, sometimes referred to as the Monroney-Madden bill, is indicative of this interest. This bill, if passed, will establish a standardized Federal information and data processing system for both budgeting and fiscal data. Federal programs and activities and, of course, costs and revenues would be accounted for on an articulated Government-wide basis.

GAO would be required to provide information on agencies' programs, activities, receipts and expenditures to the Congress and its Members, and to keep a scoreboard of changes in the amount of the President's budget as shown by information available in Federal agencies.

The bill would increase significantly the Congress' capability to evaluate proposed Federal programs, budget requests, and budgetary changes. It would call on the GAO for help in providing the Congress access to data needed to see how program operations compare with program plans, and to judge the effect of budgetary cuts being considered by the Congress.

Another legislative proposal is a further illustration of the direction congressional interest is taking. To enable the Congress to evaluate the results of the programs it appropriates money for, the proposed Legislative Evaluation Act of 1967 would establish a commission to conduct a thorough study of the status of evaluation of research and the Federal use of evaluating systems to measure results of Federal programs. It contem-

plates that the Comptroller General establish a system for evaluating the results of Federal programs including selecting the criteria to be used. If enacted, this law will require GAO to further increase its systems analysis capability.

Auditing the Computer

Then, of course, we have the requirement to learn how, as auditors, to live with the computer.

We are currently undertaking to conduct pilot reviews of ADP systems in which we will develop and use advanced techniques for auditing in an ADP environment, including the use of sampling and other selective approaches to auditing computer-based records and systems.

We have been interested for some time in exploring better ways of utilizing electronic computer techniques in accounting and auditing operations. We expect to become more involved in the future with the increased use of more sophisticated ADP equipment.

Conclusion

The future will certainly be influenced by these demands for more and more timely information, and for evaluations of plans as well as performance. It adds up to using our technology for greater accountability for plans, for actions, and for results.

In this climate how can the accounting profession help to protect the taxpayer's dollar?

I suggest the first step is to recognize the increasing involvement of the Federal Government with State and local governments, institutions, and private business; and that this involvement is being accepted.

This increased involvement is amply demonstrated by the growth in Federal financial assistance to State and local governments alone. Federal financial assistance is now running at about \$15 billion a year and may top \$17 billion in fiscal 1968. It is expected to rise to about \$60 billion a year by 1975.

It is estimated that Federal aid will constitute approximately 17 percent of the revenue of State and local governments by 1968.

Estimates of the number of Federal aid programs differ. The figure most frequently cited is 170; another estimate puts the number at 220. These programs are financed through 400 or more separate appropriations, administered by 21 Federal agencies through 150 major Washington bureaus and over 400 field offices.

Programs are carried on in each of the 50 States. Nearly 92,000 units of local government, each with its own taxing, planning, financing, and operating authorities, are eligible for grants in aid under one or more Federal programs.

This seemingly endless number and variety of programs has created perplexing problems. One of the more frequent criticisms of grant-in-aid programs by State and local government officials has been an inability to even keep track of the overlapping benefits for which their governments may be eligible.

This involvement means that there is a need for greater interchange of information and ideas, particularly as to how the Federal Government can achieve greater uniformity and consistency in the auditing and accounting requirements it prescribes for assistance programs.

There is also a need for cooperation in developing the principles and standards that the public accounting profession will apply in making audits of governmental programs where Federal assistance plays a part. I am sure other speakers on this program will comment further on this subject.

The public accountant's understanding of financial operations of both government and industry places him in an unusually strategic position to stimulate greater public interest in and understanding of the economic and financial issues confronting government at all levels. I was much interested in immediate past AICPA President Hilliard Giffen's remarks at the recent symposium of the Federal Government Accountants Association in Washington in which he discussed his efforts in urging CPAs to become more familiar with and involved in government problems and finances.

I was equally interested in the remarks of your new president, Marvin Stone, yesterday when he suggested that CPAs take a more active part in the framing of legislative and governmental procedures and processes.

The job of protecting the taxpayer's dollar takes many forms and it calls for the efforts and skills of everyone who has a stake in the success of our system of Government. I know that members of the public accounting profession have a vital interest in this objective. Your important work often brings to light opportunities for reducing public expenditures. We in the General Accounting Office would welcome your ideas and suggestions on achieving the objective all good managers seek—getting the most for our money.

721329

A Teamwork Venture With Public Accountants in the Audit of Tennessee Valley Authority

By Andrew F. McCall and Zane Geier

This article discusses GAO's audit of TVA over the years and describes the current procedure which places primary reliance on work done by a public accounting firm.

While TVA's broad charter and the nature of its activities have changed little since it was created in 1933, GAO's approach to the audit of TVA has changed markedly over the years. From a centralized audit of vouchers in the beginning, it progressed to a commercial type audit requiring a fairly large site audit staff of GAO auditors. Today, GAO performs its annual audit of TVA using a small staff of auditors who rely largely on audit work done by a public accounting firm. The arrangement with the public accounting firm has been successful in spite of controversial accounting questions which arise from time to time.

History and Programs

TVA was created by the Tennessee Valley Authority Act of 1933 as a Government-owned corporation for the general purpose of providing for the unified development of the Tennessee River system, including flood control in the Tennessee River and Mississippi River basins; navigation on the Tennessee River; generation of power consistent with flood control and navigation; operation of power and chemical properties at Muscle

Shoals, Ala.; reforestation and agricultural and industrial development of the Tennessee Valley; and the economic and social well-being of the people living in the Tennessee drainage basin and adjoining territory.

While the main programs have remained essentially the same since TVA was created, some noteworthy changes have occurred within these programs over the years. During World War II and the Korean conflict, fertilizer production was converted to the manufacture of phosphorus and other wartime necessities. At the same time construction of dams and steamplants was speeded up to provide electrical energy required by the Atomic Energy Commission and the defense industry, particularly aluminum production.

Low-cost power derived from the economical hydroenergy of 47 dams and large amounts of coal in or near the area has encouraged greater home use of electricity and has attracted industry. The increased power demands have in turn made TVA the largest single coal buyer in the Nation. Developments associated with the growth of TVA's power produc-

tion role have had a direct impact on GAO's audit approach and have resulted in the unique audit arrangement of today.

Early Audits and Controversy

During TVA's initial years, GAO audits were similar to those made of other Federal agencies. Most of the work was performed in Washington and consisted primarily of a desk review of vouchers received there. Visits by staff members to TVA usually involved questions raised in this voucher review.

A major controversy soon arose with TVA over GAO's right to audit and take exception to vouchers. TVA steadfastly refused to honor a large number of exceptions taken by GAO in TVA's disbursing accounts. The then Comptroller General, J. Raymond McCarl, refused to countersign warrants required for release of appropriated funds from the Treasury for use by TVA. This action precipitated hearings in 1938 before a joint special committee of the Congress in which GAO was chided for its action in thwarting congressional intent to make funds available to TVA. Congress then amended the TVA Act in 1941 to provide that "The General

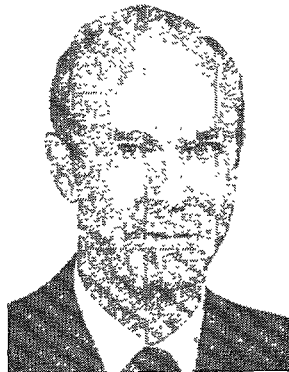
Accounting Office, in settlement of the accounts of the Treasurer or other accountable officer or employee of the Corporation, shall not disallow credit for, nor withhold funds because of, any expenditure which the board shall determine to have been necessary to carry out the provisions of said Act."

Change to Commercial-Type Audits

Aware of the need for a commercial-type audit, TVA engaged the public accounting firm of Lybrand, Ross Bros. & Montgomery to make annual audits beginning in 1938. These audits were continued until the passage of the Government Corporation Control Act in 1945 when GAO established a new, separate audit division to perform commercial-type audits of Government corporations.

In his report for the fiscal year 1945, the Comptroller General commented on TVA's accounting procedures and system of internal control including the work of the internal audit division and recognized TVA as one of the foremost Government corporations in the use of accounting in management. The report stated also that the classification of operating costs and expenses brought out clearly the operating

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results by organizational lines as well as by program. It is interesting to note that this attainment by TVA has become a primary goal of the planning-programming-budgeting system now being stressed for use throughout the Government, almost 30 years after TVA accomplished it.

GAO continued its commercial-type audits of TVA in essentially the same manner for 15 years. The annual audit involved the use of 20 to 25 staff members selected from the Washington and Atlanta offices with emphasis on continuity of experience. The audit required about 2 months and was performed at the three principal TVA offices: Chattanooga, Tenn., where power and plant operation records were maintained; Muscle Shoals, Ala., the location of chemical and fertilizer operations; and Knoxville, Tenn., where the office of the comptroller, central accounting office, and internal audit organization were located. Staff members concerned with the audit of plant records also visited accounting offices established at the sites of major construction projects. All audit work was coordinated from the Knoxville location. Interim work was limited primarily to procedures involving inventories and accounts re-

ceivable, but reviews of other TVA activities were made from time to time.

Financial Statements and Accounts

The Government Corporation Control Act requires Government corporations to submit annually a business-type budget to the Bureau of the Budget, including a statement of financial condition, a statement of income and expense, an analysis of surplus, and a statement of source and application of funds. A number of provisions in the TVA Act affect the form and substance of these financial statements. The statement of source and application of funds shows the nature and amounts of payments to the U.S. Treasury required by the act, and repayments of the appropriation investment are shown in the balance sheet.

From both operational and audit points of view, there are a number of similarities between TVA and private enterprise. The Board of Directors of TVA, directly responsible to the President and the Congress, is granted much of the flexibility and administrative freedom found among private corporations in carrying out the provisions of the TVA Act. The accounts and financial statements have much in

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common with those of commercial enterprises. The usual distinctions are made between capital expenditures and operating expenses. Depreciation is recorded and charged to the activities using the assets. Administrative and other overhead costs are allocated to the various programs on the basis of direction of effort studies. The system of accounts prescribed by the Federal Power Commission for privately owned power companies is used also by TVA. In the 1930's and again in the current decade, TVA raised powerplant construction funds using the same means as private companies, through the sale of its own bonds.

In view of the fact that funds are received from appropriations, revenues, and both long-term and short-term borrowing and are expended on various programs, of which the power program must be self-financing, the system of internal control is of particular importance. The internal audit organization is an important segment of this system and its work plays a large role in determining the nature and extent of tests performed by outside auditors.

Change in Financing and Present Audit Approach

In 1953, annual appropriations to TVA reached a peak of \$336 million. After 1954, however, appropriations were made only for the completion of existing power construction and for nonpower activities, and were less than \$17 million in 1959. By that time, the power program represented over three-fourths of the \$2.2 billion invested capital in TVA. With the need for further power construction, the Congress in 1959 amended the act to authorize TVA to again issue its own

bonds and to arrange for audits and reports on its financial condition and operations by certified public accounting firms. Unlike the earlier bonds which were sold to the Government, these bonds were for sale to private investors and were to be secured only by revenues from the sale of power without pledging the credit of the United States.

To facilitate the sale of these securities on the open market, Lybrand, Ross Bros. & Montgomery was again engaged to fulfill the attest function. GAO continued to be charged with making annual audits of TVA because it had responsibilities which went beyond the attest function associated with the corporation's financial statements.

GAO Reviews Lybrand's Work

Since information obtained in an examination of the financial accounts is a normal prerequisite in fulfilling GAO's responsibilities, the question arose as to how such required information could be obtained without duplicating the audit work of the public accounting firm. The solution agreed upon and in use today provides for GAO representatives to make a careful and detailed review of the audit program and working papers of the public accountants at the audit sites, thereby eliminating any detailed review effort by GAO except where it is believed that additional work is required in order to discharge our responsibilities.

In general, the GAO review is made by an experienced team of three or four supervisory auditors who prepare working papers consisting of notes covering their tests, observations and conclusions on the work done by

the public accounting firm. The firm's working papers are reviewed as they are completed so that any questions can be discussed with the firm's auditors and TVA as they develop. Changes in the firm's audit program from that of the prior year are given particular attention and evaluated during the audit.

In any large organization with operations as varied as those of TVA, questions arise concerning proper accounting treatment and disclosure. Such questions may tend to be controversial and involve such matters as the allocation of costs between self-financed power operations and non-power operations financed from appropriated funds; procedure for capitalizing interest for borrowed funds on construction projects; acceptability of footnote disclosure for certain long-term leases; treatment of the cost of long-lasting nuclear fuel used in atomic powerplants; values assigned to property received by transfer from other Federal agencies, etc. Through the cooperative effort of the audit staffs, questions that do arise are generally resolved in a satisfactory manner.

Some of Lybrand's staff members on this audit participated in the TVA audits prior to 1945 and assisted in

improving initial procedures. Some members of the firm audit other large electric power companies and bring worthwhile experience and timetested ideas to the job.

In transmitting our report to the Congress, we acknowledge our responsibility under the Government Corporation Control Act. We state that our audit included observations and tests of the certified public accounting firm's work, and that the financial statements of TVA are incorporated in our report together with the opinion of the firm. When appropriate, we include comments on TVA operations or other matters.

At first, some of us had reservations as to whether divergent views of the two groups of auditors would make such an arrangement unworkable. Some members of the public accounting staff doubtless shared these reservations. But thus far experience has shown that both audit groups hold relatively consistent views on significant issues. Perhaps the fact that each audit group is concerned about the problems of the other has contributed much to the success of the present working arrangement, and with good communications and free interchange of information it has been a pleasant and rewarding experience.

721330

Statistical Sampling Procedures in Examination of Vouchers

By Susumu Uyeda

An act of Congress in 1964 permits Federal agencies to use statistical sampling procedures in the preaudit of disbursement vouchers. In this article, the author describes the system designed by the Defense Supply Agency to apply such procedures.

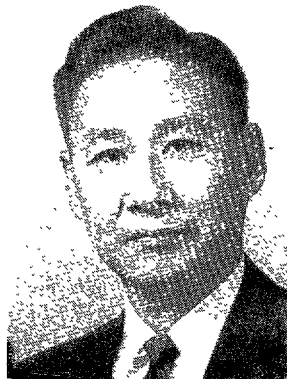
Introduction

The chance of having a straight flush in a poker game is 64,999 to 1 and of having four of a kind is 4,164 to 1. But no law of probability will convince the incorrigible cardplayer that the odds of his winning the next game are against him. Similarly, it is sometimes difficult to persuade auditors to use statistical sampling procedures and it is more difficult to convince agency officials of the accuracy of audit conclusions based on projections of statistically selected samples.

While most of us were wrestling with these mundane problems, the

Auditor General of the Defense Supply Agency (DSA) designed a procedure for using statistical sampling in examining vouchers in amounts under \$100 by the finance and accounting personnel. The proposed procedure is now being tested at a DSA installation. DSA's procedure is unique because of its simplicity and its lack of requirement for much knowledge in mathematics and statistics. The purpose of this article, therefore, is to discuss the methodology of DSA's study leading to the design of the procedure and to describe the procedure itself.

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Historical Background and Statutory Authority

During fiscal year 1963, the Departments of Agriculture and Health, Education, and Welfare tested the use of statistical sampling techniques in their voucher examination operations. These tests gave promise of worthwhile savings and a Government-wide application; but the Comptroller General, acting on a request by the Department of Agriculture, indicated that a change in legislation was needed for adopting such practices.

Before the close of the fiscal year, a team of Bureau of the Budget, Treasury Department, and General Accounting Office representatives was set up to look into this matter. The team drafted legislation that would permit Federal Government agencies to use sampling techniques in the examination of vouchers.

On August 20, 1964, the Congress enacted Public Law 88-521 (31 U.S.C. 82b-1) entitled "An Act to Permit the Use of Statistical Sampling Procedures in the Examination of Vouchers." It provides as follows:

"(a) That, whenever the head of any department or agency of the Government or the Commissioners of the District of Columbia determines that economies will result therefrom, such agency head or the Commissioners may prescribe the use of adequate and effective statistical sampling procedures in the examination of disbursement vouchers for amounts of less than \$100; and no certifying or disbursing officer acting in good faith and in conformity with such procedures shall be held liable with respect to any certification or payment made by him on a voucher which was not subject to specific examination because of the prescribed statistical sampling procedure, provided that such officer and his department or agency have diligently pursued collection action to recover the illegal, improper, or

incorrect payment in accordance with procedures prescribed by the Comptroller General.

"(b) Nothing contained in this Act shall affect liability, or authorize the relief, of any payee, beneficiary, or recipient of any illegal, improper, or incorrect payment, or relieve any certifying or disbursing officer, the head of any department or agency of the Government, the Commissioners of the District of Columbia, or the Comptroller General of responsibility to pursue collection action against any such payee, beneficiary, or recipient."

To ensure that agencies would apply adequate and effective statistical sampling procedures, the House Committee on Government Operations, in reporting favorably on the bill that was enacted into law, stated that the General Accounting Office would issue a set of principles and standards for executive agencies to follow. These principles and standards are contained in title 3 of the GAO Policy and Procedures Manual for Guidance of Federal Agencies.

Feasibility Study

Having received the GAO guidelines, the Auditor General's staff initiated a study to determine whether it is feasible for operating personnel to use statistical sampling procedures in the examination of vouchers for amounts under \$100 and whether such procedures would result in savings to the Government.

Prior to the commencement of the study, it was first necessary to have a meeting of the minds as to what is meant by terms such as "examination" and "vouchers." The GAO guidelines define examination as "the review, prior to payment, of documents assembled in support of any claim against, or any payment to be made by, the Government, to determine its

legality, propriety, validity, and accuracy." Voucher is defined as "the document authorizing a disbursement, together with all other documents necessary to support the determinations made in the examining process." Although these definitions are fairly specific, the peculiarity in the use of these terminologies in the Department of Defense and related problems precluded the meeting of the minds of those participating in the study. As a result, GAO's assistance was requested in further clarification of the definitions.

Next, it was necessary to establish the way the \$100 criterion would be applied. For vouchers representing payments to vendors and contractors, the net amounts—after deducting discounts and other allowances—were used for determining whether vouchers were for amounts under \$100. For vouchers supporting payments to employees, the gross amounts—before deducting advances, taxes, insurance, and other reductions—were used. This application of the \$100 criterion is in accordance with the GAO guidelines.

Seven DSA activities were selected for the feasibility study. At each of these activities, the monthly, quarterly, and annual volume of vouchers for amounts under \$100 were determined. The various characteristics of these vouchers were reviewed to determine whether segregation by any characteristic would be necessary prior to sampling. The characteristics subjected to review included amounts of disbursements, types of purchase documents, purposes of payments, discount provisions, "fast-pay" procedures, multiple-line vouchers, and multiple-fund disbursements. This review disclosed that only when travel

vouchers comprise a substantial portion of an activity's disbursements for amounts under \$100, should they be segregated and sampled apart from payments made to vendors. Also, at each of the activities, the cost for examining vouchers for amounts under \$100 with 100-percent examination was computed with the assistance of appropriate operating personnel.

At that time it was necessary to design a tentative statistical sampling procedure. (The details of the final sampling procedure will be described later in this article.) By following the tentative procedure, the study team was able to estimate the cost for the sampling procedure. Included in this cost were the clerical time required in the administration of the sampling procedure and the estimated amount of undetected overpayments on vouchers not examined.

The comparative analysis of the cost for the procedure in effect and the cost under the tentative sampling procedure led to the conclusions that the sampling procedure was feasible and that a composite annual saving of approximately \$43,000 would be realized by five of the seven activities studied. The study team concluded that only a nominal saving would be realized at those activities where vouchers were already being checked on a "cursory" or "spot-check" basis. Even at the latter activities, the benefits of improved control over the accuracy of disbursements may well offset the training costs required for implementing a mathematically supported procedure.

Highlights of Simplified Procedure

As the study progressed, it became obvious to the study team that a com-

plex and sophisticated statistical sampling procedure could not be implemented, because almost all finance and accounting personnel lacked sufficient background and training in mathematics and statistics. The product sought, therefore, was a procedure which would be very simple and which would meet the minimum GAO requirements.

Accordingly, a procedure was designed which made almost no reference to statistical terms, such as standard deviations, confidence levels, and sampling precision. Several reference tables were developed which could be used, after a few arithmetical calculations, to determine appropriate sample sizes, to evaluate sample results, and to estimate the total over (or under) payments in the universe. Adherence to this procedure will result in a 95-percent level of confidence that the total amount of errors is or is not within the preestablished tolerance limit. Knowing the extent of errors, management can then refer to a decision table which outlines action to be taken at different levels of error rates disclosed. Finally, a format was designed for use by the accounting personnel in computing the savings resulting from the application of the sampling procedure and in supporting the amount claimed under the Department of Defense cost reduction program. The details of the procedure are described in the following paragraphs.

Selection of Preliminary Sample

Since the sampling method is intended for estimating the dollar amount of errors (variables sampling), a preliminary sample of 50 is selected under the DSA procedure. Moreover, the samples are selected

and reviewed each day rather than held until the end of the sampling period of a month (or a quarter). Therefore, at the beginning of the sampling period, it is necessary for the accounting personnel to make a best estimate of the volume of vouchers for less than \$100. The number obtained by dividing the estimated volume (established universe) by 50 represents the selection interval for identifying samples under the systematic selection method. A randomly selected number from 1 through the selection interval will be the starting point in the selection process. In order to facilitate the selection of samples, the vouchers for amounts under \$100 are separately filed and assigned sequential numbers. An alternative to the separate file is a workpaper which cross-references disbursing officer's voucher numbers with the sequential numbers for locating the vouchers selected.

Let us assume that in a given situation the estimated universe is 6,000. The sampling interval will be 120 (universe of 6,000 divided by sample size of 50). The next step is to select the random starting point by selecting a number between 1 and 120 from a table of random numbers (or from other means if so desired). If the number 55 is selected, voucher number 55 is the first sample, the second being 175 ($55 + 120$), the third being 295 ($175 + 120$), etc. These sample vouchers, which are selected as soon as they are prepared for disbursement, are examined for accuracy during the sampling period. If 5,600 vouchers, or 400 less than the earlier estimate, were actually processed during the period, the actual number of samples selected would be only 47. In this in-

stance, three additional vouchers must be selected from the "actual universe" by using the systematic selection process.

As each sample voucher is examined, pertinent information is recorded on a worksheet. This worksheet (see illustration No. 1) will show, for each sample, the voucher number, the name of payee, the amount paid, the amount of error, the type of error, and the name of the individual responsible for the error. The worksheet, therefore, serves as: (1) A control record of the examination; (2) a tool for detecting error trends or individuals making recurring errors; (3) a documentation to indicate corrective action taken; and (4) an aid in determining the final sample size.

Determination of Final Sample Size

After the preliminary sample has been carefully examined and the results fully documented on the worksheet, the final sample size must be determined to achieve the desired degree of confidence and precision in projecting the total amount of overpayments in the universe. To accomplish this, the first step is to arrange the amounts of overpayment in the order of selection from the worksheet in five groups of 10 vouchers as follows:

Group 1	Group 2	Group 3	Group 4	Group 5
\$0.10	0	0	0	\$0.10
0	0	0	\$0.08	0
.32	\$0.02	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	.20
0	.10	0	0	0
0	0	0	0	1.94
0	0	0	.14	0

For each group the range, or the difference, between the highest value and the lowest value is obtained; then the overall average group range is calculated as shown below:

Group	Highest value	Lowest value	Group range
1-----	\$0.32	0	\$0.32
2-----	.10	0	.10
3-----	0	0	0
4-----	.14	0	.14
5-----	1.94	0	1.94
Total group range----			\$2.50
Average group range--			\$0.50

Under a normal variables sampling plan, the next step would be to estimate the standard deviation by using the appropriate "d₂ factor."¹ Also, at this time a sample reliability desired per voucher must be decided and a ratio between the sample reliability and the estimated standard deviation must be computed. With this ratio and the size of the universe in mind, statistical tables are consulted to determine the final sample size.

However, terms such as "standard deviations" and "d₂ factors" are foreign to the vocabulary of most accounting clerks. The use of such terminologies alone could create a resistance in their minds, with the result that a statistical sampling procedure would not be successfully implemented. In order to simplify this procedure, the DSA Auditor General's staff created a reference table. This table required only two basic items of information—the average group range and the size of the universe—in determining the final sample size.

¹ Factors for estimating the standard deviation from any average range are referred to as d₂ factors. These factors vary with group sizes.

Illustration No. 1

EXAMPLE OF WORKSHEET FOR SAMPLING VOUCHERS UNDER \$100

	Sampling control Nos.	Voucher No.	Payee	Voucher Amount	Amount overpaid	Amount underpaid	Other type error	Cause of money error (employee making error)	Cause of other error	Error corrected
1----	55	7933	X Co---	\$78. 25	\$0. 10	-----	None-----	Addition error (J. Doe)-----	N/A-----	X
2----	175	8234	Y Co---	98. 00	None	-----	(Incorrect approp charged).	N/A-----	Typing error (Ann Brown).	X
3----	295	8451	Z Co----	25. 00	. 32	-----	None-----	Discount not taken (B. Adams).	N/A-----	X
	*	*	*	*	*	*	*	*	*	*
47---	5, 575	20740	A Co---	65. 25	. 20	-----	None-----	Transportation charge not payable (Jane Smith).	N/A-----	X
48---	315	18781	X Co---	45. 95	None	-----	None-----	N/A-----	N/A-----	N/A
49---	2, 181	21521	A Co---	87. 32	1. 94	-----	None-----	Transportation charge not payable (Jane Smith).	N/A-----	X
50---	4, 047	26783	E Co---	66. 00	None	\$0. 16	None-----	Addition error (N. Ricc)-----	N/A-----	X
Preliminary sample totals-----				\$3, 331. 00	\$3. 00	\$0. 16	-----	-----	-----	---
				(9 vouchers)		(1 voucher)				

Followup note: Jane Smith recently acquired A Co.'s voucher preparation responsibility and was not familiar with transportation clause. All A Co.'s vouchers (19) were pulled and \$42.50 in overpayments is being deducted on voucher 20936-67. Overpayments occurred on 3 vouchers: 11,709; 13,256 and 19,743.

For all practical values of average group ranges, the estimated standard deviations were computed using the d_2 factor, and ratios between these estimated standard deviations and the desired sample reliability were predetermined. Finally, sample sizes for each combination of universe sizes and average group ranges were charted in relation to the ratios computed and this chart was the basis for the table (see illustration No. 2).

The use of this table not only simplifies the statistical sampling procedure but also expedites the determination of the final sample size. For example, using our previous example of a universe of 5,600 vouchers and an average group range of \$0.50, the accounting clerk has only to look under appropriate average range column (in this case \$0.00 to \$0.50) and, moving down to the appropriate universe line, to simply determine the final sample size to be 50. Since 50 vouchers have already been selected in the preliminary sample, additional selection of vouchers is not required. If, however, the average group range

happens to be \$0.75 with a universe of 10,000, the required final sample size is 170. Accordingly, 120 additional vouchers would be selected by using the systematic selection procedure previously discussed.

Evaluation of Sample Results

Once a complete review of all samples has been accomplished, it is necessary to evaluate the sampling results as to their reliability and creditability. One must therefore determine the degree of precision actually achieved on the basis of the final sample size. To accomplish this, the average range of errors must be determined from the final sample in groups of 10 vouchers. If the final sample size is the same as the preliminary sample size, the average range need not be recomputed. If the final sample size is greater than the preliminary sample size, a new average range should be computed by arranging the vouchers in groups of 10 in the order of selection in as many groups as possible up to a maximum of 50 groups.

Illustration No. 2

TABLE FOR DETERMINING FINAL SAMPLE SIZE

Size of universe up to:	Average group range from preliminary sample				For expanded review ¹
	\$0.00 to \$0.50	\$0.51 to \$1.00	\$1.01 to \$2.00	\$2.01 and over	
500.....	50	130	190	230	(²)
1,000.....	50	150	230	280	(²)
2,000.....	50	160	260	330	600
3,000.....	50	170	270	360	700
4,000.....	50	170	280	360	800
5,000.....	50	170	280	360	800
10,000.....	50	170	290	400	900
20,000.....	50	170	300	400	1,000
100,000 and over.....	50	170	300	400	1,000

¹ To be used only when the average rate of overpayment in the final sample is over 125 percent of the cost to examine a voucher.

² All of universe.

From this point, the normal variables sampling procedures require the following actions to determine the sample precision:

1. Divide the average range by the d_2 factor to obtain the standard deviation.
2. From statistical tables, find the sampling error in terms of multiples of standard deviation for the appropriate sample size and actual universe.
3. Multiply the standard deviation by the sampling error determined above to obtain the sampling precision per voucher.

Again, the average accounting and disbursing clerk cannot be expected to have knowledge of these computations. The Auditor General's staff, therefore, created another table (see illustration No. 3) to simplify the determination of the degree of precision achieved.

The two basic items of information essential to the use of this table are the average range value and the final sample size. Referring back to the previous example of 50 vouchers, the average group range was \$0.50. By identifying the appropriate range column and moving down to the line signifying the sample size of 50, we find that the precision is $\pm \$0.0329$ per voucher. For the 50 vouchers sampled, the total amount of overpayment was \$3 or an average of \$0.06 per voucher. It can now be stated with 95-percent certainty that the actual error per voucher is somewhere between \$0.0271 and \$0.0929 ($\$0.06 \pm \0.0329). Only when the average group range is over \$4 will the detailed mathematical computations be

required. This, of course, is expected to occur very rarely.

Action To Be Taken as a Result of Sampling

The value of the sampling procedure will be minimized unless the results of the review are used for determining what action should be taken by finance and accounting personnel. Even before the end of the sampling period, the work sheet showing sample results should be reviewed to detect trends in errors, to identify individuals making repetitive mistakes, and to emphasize the need for training.

At the end of the sampling period, a decision must be made either to accept the error rate and do no more review work or to expand the review work for the purpose of recovering all material amounts of overpayment. The original DSA procedure, which is subject to change, provided essentially the following guides:

1. If the average rate of overpayment is 75 percent or less than the cost to examine a voucher, no further sampling is necessary. A followup by management on the causes contributing to the errors detected during the review of the selected samples would be the only requirement.
2. If the average rate of overpayment is between 75 and 125 percent of the cost to examine a voucher, management will perform additional necessary reviews to establish additional trends or causes for the errors.
3. If the average rate of overpayment is over 125 percent of the cost to examine a voucher, sample sizes will be increased as prescribed. After the review, if the error rate is still over 125 percent, all vouchers in the universe should be reviewed and any substantial overpayments should be recouped from the vendors.

Illustration No. 3

LIMITED TABLE OF SAMPLING PRECISIONS PER VOUCHER, 95 PERCENT CONFIDENCE

Final sample sizes	Average ranges—															
	\$0.00 to \$0.25	\$0.26 to \$0.50	\$0.51 to \$0.75	\$0.76 to \$1.00	\$1.01 to \$1.25	\$1.26 to \$1.50	\$1.51 to \$1.75	\$1.76 to \$2.00	\$2.01 to \$2.25	\$2.26 to \$2.50	\$2.51 to \$2.75	\$2.76 to \$3.00	\$3.01 to \$3.25	\$3.26 to \$3.50	\$3.51 to \$3.75	\$3.76 to \$4.00
Sampling precision per voucher																
50	0.0110	0.0329	0.0548	0.0768	0.0986	0.1206	0.1425	0.1645	0.1864	0.2083	0.2303	0.2522	0.2741	0.2961	0.3180	0.3399
130 .....	.0065	.0195	.0325	.0454	.0584	.0714	.0844	.0974	.1104	.1233	.1363	.1493	.1623	.1753	.1883	.2012
150 .....	.0060	.0179	.0298	.0418	.0537	.0656	.0775	.0895	.1015	.1133	.1253	.1372	.1491	.1611	.1730	.1849
160 .....	.0058	.0173	.0289	.0404	.0519	.0635	.0750	.0866	.0981	.1096	.1212	.1327	.1443	.1558	.1674	.1789
170 .....	.0056	.0167	.0279	.0390	.0502	.0613	.0725	.0836	.0948	.1059	.1171	.1282	.1394	.1505	.1617	.1728
190 .....	.0052	.0156	.0259	.0363	.0467	.0570	.0674	.0778	.0882	.0985	.1089	.1193	.1297	.1400	.1504	.1608
230 .....	.0048	.0143	.0238	.0333	.0428	.0524	.0619	.0714	.0809	.0904	.1000	.1095	.1190	.1285	.1380	.1476
260 .....	.0047	.0140	.0233	.0326	.0420	.0513	.0606	.0699	.0793	.0886	.0979	.1072	.1166	.1259	.1352	.1445
270 .....	.0046	.0137	.0228	.0319	.0410	.0501	.0592	.0683	.0774	.0865	.0956	.1047	.1138	.1229	.1320	.1411
280 .....	.0044	.0133	.0222	.0311	.0400	.0488	.0577	.0666	.0755	.0844	.0932	.1021	.1110	.1199	.1288	.1376
290 .....	.0044	.0133	.0222	.0310	.0399	.0487	.0575	.0664	.0753	.0841	.0930	.1018	.1106	.1195	.1284	.1372
300 .....	.0044	.0132	.0221	.0309	.0397	.0485	.0574	.0662	.0750	.0838	.0927	.1015	.1103	.1191	.1280	.1368
330 .....	.0042	.0127	.0211	.0295	.0380	.0464	.0548	.0633	.0717	.0802	.0886	.0970	.1055	.1139	.1223	.1308
360 .....	.0040	.0121	.0201	.0282	.0362	.0443	.0523	.0604	.0684	.0765	.0845	.0926	.1006	.1087	.1167	.1248
400 .....	.0038	.0113	.0188	.0264	.0339	.0414	.0490	.0565	.0640	.0716	.0791	.0866	.0942	.1017	.1092	.1168
600 .....	.0030	.0089	.0149	.0209	.0268	.0328	.0387	.0447	.0507	.0566	.0626	.0686	.0745	.0805	.0864	.0924
700 .....	.0028	.0084	.0141	.0197	.0253	.0310	.0366	.0422	.0479	.0535	.0591	.0648	.0704	.0760	.0817	.0873
800 .....	.0027	.0080	.0133	.0186	.0239	.0293	.0346	.0399	.0452	.0505	.0559	.0612	.0665	.0718	.0771	.0825
900 .....	.0026	.0078	.0129	.0181	.0233	.0284	.0336	.0388	.0439	.0491	.0543	.0594	.0646	.0698	.0750	.0801
1,000 .....	.0025	.0075	.0125	.0175	.0225	.0275	.0325	.0375	.0425	.0475	.0525	.0575	.0625	.0675	.0725	.0775

Further, finance and accounting personnel are required to document the basis for all decisions, the findings disclosed during the reviews, and the corrective action taken.

In addition, they are required to compute and report the savings resulting from the application of the statistical sampling procedures. Very briefly, the computation requires the comparison of costs for 100-percent examination with costs required under the sampling procedure. The costs for the sampling procedure include the costs for reviewing the total number of samples selected, the estimated amount of undetected overpayments, and the costs of administering the sampling review. The costs of administering the sampling review consist of costs for annotation sampling control numbers, making required work sheets and reports, selecting samples, determining final sample sizes, and computing the degree of precision achieved.

Conclusion

The DSA's test application of statistical sampling technique in examining vouchers in amounts under \$100 is unique from a simplicity standpoint; but, most significant, it does save

money and it gives management information on the relative accuracy of its disbursements. Further refinements and improvements may be made to DSA's procedure. For example, a further critical look at the procedure may show that the "average rate range" intervals in the table for selecting final sample size may be too great. It may be noted that the table for determining sample precision, by not distinguishing the size of universe, may distort the precision as much as 1 or 2 percent.

No doubt, by emphasizing simplicity, DSA's procedure has sacrificed precision to a small degree. However, a disbursing officer's function is different from that of a scientist. Certainly we must recognize that the same degree of precision is not required for paying a \$10 voucher as for sending a man to the moon. That the procedure may require further refinements and improvements does not diminish the credit that should go to DSA for developing this technique. Such work is evidence that there is great opportunity for creative imagination, for bold ingenuity, and for productive application of mathematics and new technology in the field of financial management.

721331

The United States Commercial Import Program as an Economic Weapon in Viet Nam

By Irving Martin

The author discusses some of the economic implications of programming U.S. assistance to Viet Nam, with particular reference to the commercial import program.

The commercial import program is a major instrument of U.S. economic assistance to Viet Nam. From inception of such assistance in fiscal year 1954 through fiscal year 1967, a total of \$2.2 billion was obligated for the program. This represented 60 percent of the \$3.6 billion obligated for all economic assistance to that country during this period.

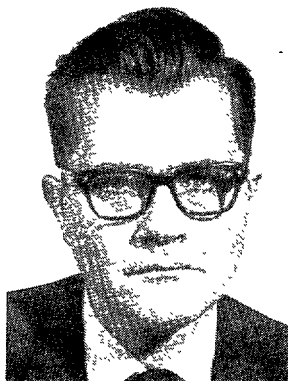
In October 1966, the General Accounting Office undertook a survey of the Viet Nam commercial import program giving recognition both to the magnitude of the program and to the fact that, by its very nature, it is particularly subject to abuse. The current size of the program was indicated by the fact that fiscal year 1966 obliga-

tions of the program—\$397 million—represented about 15 percent of the worldwide obligations of the Agency for International Development. Our report to the Congress, released in August 1967, focused upon the broader aspects of program management (Survey of the Agency for International Development's Management and Operation of the Commercial Import Program for Viet Nam, B-159451, Aug. 24, 1967).

In planning the job, we established a chronological sequence of checkpoints to examine into. These points encompassed four broad areas around which the report to the Congress was organized.

1. *Program formulation*—The

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manner in which the size and commodity content of the program are established.

2. *Program implementation*—Controls exercised from the point in time that funds are released until goods arrive in Viet Nam.
3. *The Saigon port situation*—The problem of getting goods into Viet Nam.
4. *Surveillance activities*—Actions by U.S. agencies to ensure proper use of the U.S.-financed commodities.

We did not expect to run into anything really surprising since we had been “down the commercial import program road” before in a number of other countries and were aware that there were unusual problems in regard to the port situation and surveillance activities in Viet Nam. We encountered surprise number one, however, when we found that there was no formal program formulation process for the Viet Nam commercial import program, at least not in any sense we had encountered before. Rather, Vietnamese importers determined the size and content of the program. For one to appreciate this, a little background will be helpful.

How the Program Operates

The concept of a commercial import program is not new in the array of U.S. programs of economic assistance, having first been instituted under the Marshall Plan in 1948. Through the ensuing years, it has been employed, to a greater or lesser extent, in practically all countries receiving U.S. economic assistance. Essentially, it entails U.S. financing of commodity imports into a recipient's economy. Thus, the U.S. role in a given trans-

action is that of an international banker—paying to the supplier the cost of the commodities bought by the importer, with the transaction itself carried on through international trade channels. The importer is an individual or business entity in the recipient country or an agency of the country itself. The supplier is similarly an individual, a business entity, or a governmental agency in the “source” country.

Immediately after the supplier ships the goods, the importer or his bank pays for them in local currency. These funds are ultimately deposited into a bank account, known as the “counterpart account,” in the recipient country. Counterpart funds are owned by the recipient government but can only be used for purposes mutually agreed upon between that government and the United States. A portion of these funds is generally made available for U.S. use. For example, 10.5 percent of the local currency (piasters), generated by the commercial import program in Viet Nam during fiscal year 1966, was made available for the Agency for International Development's local support costs within that country.

Normal Program Formulation Process

A commercial import program generally serves three purposes.

1. *Budgetary support* for the recipient government by generating sufficient counterpart funds to make up the difference between governmental outlays and governmental revenues.
2. *Foreign exchange support* by providing U.S. financing of imports.

3. *Combating inflation* by absorbing the surfeit of purchasing power within an economy through the infusion of imported goods.

Budgetary deficits, shortages of foreign exchange, and inflation have been and still are symptomatic of developing countries, and a commercial import program will contribute toward remedying all three of these problems. However, the overall size and the commodity content of any commercial import program will be greatly influenced by the particular objective on which U.S. strategists place primary emphasis.

Ordinarily, the size and content of a commercial import program are based on readily determinable program standards and related monetary ceilings. Thus, a forward-going calculation of a recipient's budgetary deficit is made as the basis for a budgetary support program. This methodology was followed by the United States during fiscal years 1955-59 to establish the size of the Viet Nam program.

A calculation of foreign exchange needs serves as the basis for a program designed to lend support to a recipient's balance-of-payments. This procedure was employed in Viet Nam during fiscal years 1960-65.

In either case, the associated program formulation process within the Agency for International Development involves a detailed justification of both the size and content of the proposed program by the field. Similarly detailed reviews and justifications are required in AID's Washington offices before submission of the agency's annual budgetary request to

the Congress. The extensive lead time between initial program formulation in the field and subsequent program implementation, generally about 18 months, requires further justification and review to reflect interim program adjustments in connection with the allocation of program funds.

The Viet Nam Variation

In mid-1965, inflationary pressures in Viet Nam started to get out of control as a result of a sharp increase in the amount of purchasing power in the economy. There were no offsetting changes in the capacity of the economy to absorb the increased purchasing power through corresponding increases in the availability of goods or through other absorptive means, such as increased tax collections. Several factors contributed to the creation of this situation, notably:

1. Increased budgetary deficits by the Government of Viet Nam (GVN), occasioned by a large wartime budget, its limited capacity to enforce taxation, and the absence in Viet Nam of a public tradition of tax compliance.
2. The infusion into the Vietnamese economy of an ever-increasing amount of money by U.S. elements, occasioned by our buildup in response to increased Communist aggression.

These two factors, coupled with uncertainties regarding the course of the war, resulted in a deterioration of the piaster and released the natural tendency of the populace to convert piasters to goods as rapidly as possible and thereby to provide some measure of protection against continued monetary depreciation. An inflationary

cycle was thus ignited. For example, the cost of living in Viet Nam showed an annual increase of only 4.6 percent between 1960 and 1964, whereas living costs rose 40 percent during 1965.

U.S. officials decided that inflation could not be contained through such measures as the establishment and enforcement of price controls or improved tax collections. It thus came down to a case of the United States finding a means for containing inflation. But what means? The commercial import program was chosen on the grounds that the fastest way to absorb excess purchasing power was through a major infusion of goods into the economy.

With the emphasis on the word "fastest," the next set of questions evolved—whether AID could use its time-consuming program formulation process, whether adequate data to forecast commodity needs were available, and whether forecasts based on such data would be of any value, considering the fluidity of economic factors in Viet Nam.

AID met this head-spinning dilemma by forgetting about program formulation in the traditional sense and letting the size and commodity content of the commercial import program be determined by the law of supply and demand. The United States made sufficient dollar funds available to pay for commodities needed to meet the market demand as determined by the Vietnamese import community. This manner of functioning fulfills AID's basic premise that the importation of goods, per se, is deflationary and that the interplay of market forces, as reflected in Vietnamese requests for financing of imports, would

be the most feasible way to counter inflation.

Controls Exerted by AID

Notwithstanding AID's apparent hands-off policy, it employs two devices which tend to control the size and commodity content of the program.

1. *Determination of commodity ineligibility*—This is really a negative control whereby AID designates commodities which it will not finance. Any commodity not so designated can be financed. Moreover, there are no limitations imposed on quantities of eligible commodities. Items are designated as ineligible for a variety of reasons:
 - They should be financed with Viet Nam's own foreign exchange.
 - They are luxury items.
 - Similar goods are produced within Viet Nam.
 - They are commodities susceptible to unauthorized use and/or use by the enemy.

For example, in March 1967, 18 broad commodity categories were declared to be ineligible, on the grounds that needs for them should be met first through the use of the GVN's own foreign exchange reserves. These reserves have increased significantly in recent years—from \$135.9 million in January 1965 to \$351.9 million in February 1967. These commodities represented 23 and 24 percent of the transactions financed under the commercial import program during fiscal years 1966 and 1967, respectively. The transfer

of these commodities had the following noteworthy sidelights:

- a. The transfers to the GVN were consummated only after lengthy and intricate inter-governmental negotiations even though AID had the *de jure* right to declare any commodity ineligible for program financing.
- b. The transfers included two commodities—cement and broad spectrum antibiotics—as to which AID has been criticized because of (1) evidence of hoarding and other devices used by Vietnamese importers to create artificial shortages of cement and drive up its price, and (2) circumstantial evidence that significant quantities of broad spectrum antibiotics were being diverted to the Viet Cong and to Communist-bloc countries. The GVN will now finance the importation of these commodities with its own foreign exchange.

As indicated above, it was found necessary to negotiate with the GVN in order to exercise the unilateral right of the United States to declare all of these commodities ineligible for commercial import program financing. This exemplifies the extreme sensitivity of the “sovereign nation” climate in which efforts to purify the commercial import program are conducted. On the other hand, AID’s effort to prevent the importer abuses by declaring cement and broad spectrum antibiotics ineligible

for commercial import program financing was largely nullified by the GVN undertaking the financing. Moreover, the availability of GVN foreign exchange for other needs will be reduced to the extent it is used to finance those commodities, with consequent increase in the burden on the United States to finance needed imports.

2. *Constructive interference*—AID has hired a number of commodity analysts to perform statistical studies of commodity needs in Viet Nam. The agency hopes to use the studies to influence the decision of the Vietnamese import community as to what will be imported. The importers will not, however, be bound by the studies. A data and a data reliability gap, coupled with a shortage of experienced U.S. personnel, and linguistic difficulties represent major impediments toward performing these studies.

The Inflationary Gap Analysis

Although there is not, in the traditional sense, a commercial import program formulation process in Viet Nam, AID does maintain continuing analyses of available data regarding factors that bear on inflation and thus affect the estimated size of the program. Top management is thus in a position to exert influence on conditions affecting these factors.

One of the analyses is the so-called “inflationary gap analysis” which compares the aggregate of monetary input, or inflationary factors—i.e., GVN and U.S. expenditures, expansion of credit, etc.—to the aggregate

of monetary absorption, or counter-inflationary factors—i.e., tax revenues, imports, etc. For example, for calendar year 1966, the “gap,” 17.8

billion piasters, represented a 37-percent increase in the monetary supply. This increase came about from the following factors:

Inflationary gap—1966¹

	Values assigned to gap factors (in millions)	
	Piasters	Dollar equivalent ²
Monetary creating factors:		
GVN expenditures.....	\$VN61, 900. 0	\$524. 6
U.S. expenditures.....	39, 200. 0	332. 2
Credit expansion.....	7, 800. 0	66. 1
Other.....	7, 700. 0	65. 2
Total.....	\$VN116, 600. 0	\$988. 1
Monetary absorption factors:		
GVN revenues.....	\$VN37, 100. 0	\$314. 4
Imports (GVN- and U.S.-financed).....	53, 000. 0	449. 2
Other.....	8, 700. 0	73. 7
Total.....	\$VN98, 800. 0	\$837. 3
Inflationary gap.....	\$VN17, 800. 0	\$150. 8

¹ The author would be reluctant to certify the accuracy of the individual figures, particularly GVN revenues and expenditures. The overall “gap” figure, however, is believed to be reasonably accurate, as are the other components of the equation.

² Vietnamese money is calculated at 118 piasters to 1 U.S. dollar.

The gap analysis is an application of the proposition that a change in money supply determines changes in price. The chart on page 34 depicts the relationship between changes in money supply and retail prices in Viet Nam (actually only Saigon).

As the chart shows, price changes in recent years have closely paralleled changes in money supply, except in mid-1966. At that time, prices started rising much more rapidly than money supply. To a great extent, this can be attributed to the devaluation of the piaster in June 1966¹ and the psycho-

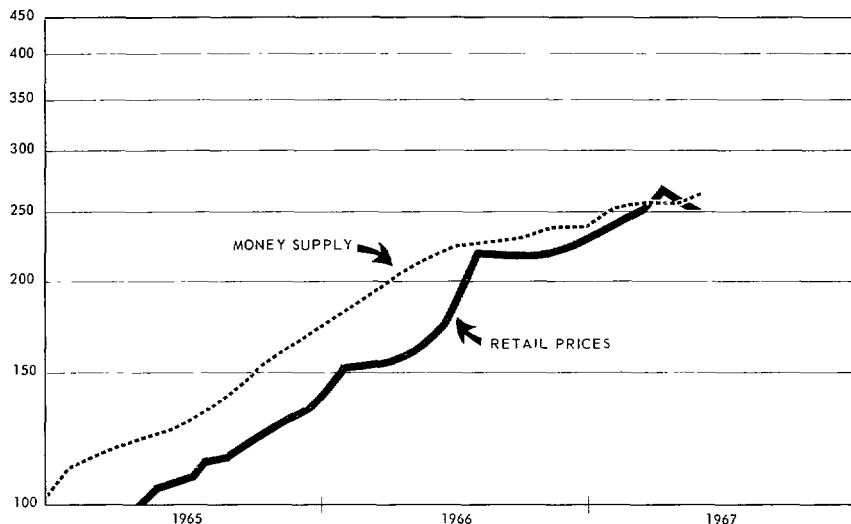
logical scare factors that the devaluation set off in the economy. Such post-devaluation jumps are symptomatic of any currency devaluation.

The gap analysis is an imperfect measure of inflation in that it does not take into account such things as changes in the level of domestic production of goods, changes in the willingness of people to hold money as liquid assets, and changes in the use of barter rather than money in payment for goods and services. The analysis is, however, the “best game in [Saigon] town” since other means of measuring inflationary pressure are unavailable. For example, national in-

¹ The devaluation, from 60 piasters to the dollar to 118 piasters to the dollar, resulted in almost doubling the cost of import transactions.

VIET NAM MONEY SUPPLY AND RETAIL PRICES

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come statistics are impossible to compile with any reasonable degree of reliability.

All in all, one can easily conclude that predicting the next move in the Vietnamese economy is a tricky business.

Perhaps the most important application of the gap analysis is that it focuses attention on the factors accelerating or retarding inflation, and thus it permits U.S. officials to act on these factors within their control. For example:

1. The monetary absorption potential of increasing imports was central in the United States decision to use the commercial import program as a counterinflationary device starting in 1965.
2. Because of the inflationary effect of U.S. expenditures, a ceiling was imposed upon such spending for 1967.

Economic Effect of the Commercial Import Program

The foregoing discussion serves to focus attention on the interaction of the various economic factors involved in the inflationary syndrome. For example, inputs of U.S. troops and the related logistics support mean more money being pumped into the Vietnamese economy. The resultant increase in inflationary pressures will make it more difficult to win the economic struggle unless offsetting countermeasures are adopted. This points up the necessity of giving continuous attention to the devising of means such as the commercial import program to counteract the inflationary forces being exerted in Viet Nam to the extent that such forces cannot be fully controlled. In the words of the U.S. official responsible for direction of AID's economic stabilization program in Viet Nam, "a 10-piaster in-

crease in the price of rice will bring more mobs into the streets than any Buddhist demonstration.”

It would appear that uncontrolled expansion of the monetary supply, if stemmed only by forced input of goods, ultimately could reach the stage of commodity market saturation. How many cigarette lighters will the consumer buy after satisfying his basic need? By the same token, however, it should be evident that the availability of sufficient quantities of

goods to satisfy demands created by an increased money supply is a significant factor in the effort to combat inflation. It seems clear, therefore, that the commercial import program, although not a panacea, can be a strong weapon in combating inflation, particularly if used in combination with improvement in the use of other money absorption devices, such as tax collections and in the exercise of controls over the monetary expansion factors.

721332

Development of a Congressional Committee Assignment

By Frederick R. Cross, Jr.

This article describes how an observation made by the writer on one audit assignment led to a congressional committee request. It also describes the writer's participation in all phases of the work performed as a consequence of the request.

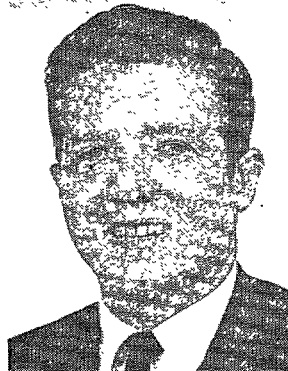
Ordinarily congressional committee requests to GAO are received at the Washington office, and in most cases field office personnel, particularly the journeyman auditors, are far removed from the origin of such requests. The writer, however, had a unique experience in which a congressional committee assignment resulted from an observation he made while reviewing another matter. The writer was able, as a result of further survey work and through joint participation with the Washington audit staff, to follow his initial observations through the complete development of the matter, including preparation and processing of the draft report to the agency and the final report to the congressional committee.

Background

As part of a nationwide review of Atomic Energy Commission (AEC) research contracts awarded to educational institutions, the Boston Regional Office was requested to review selected contracts awarded to educational institutions in the Boston area.

During our review at one of the educational institutions, it was noted that AEC and the school had entered into a cost-sharing arrangement for the enlargement and modernization of a building housing a cyclotron facility. The contractual terms seemed to be rather unique, and, since inquiry into such terms was not one of the objectives of the review, a note of this observation was made for later followup.

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The observation was subsequently discussed with the audit manager and with the regional manager. It was decided that a preliminary survey into this area would be made and the Washington AEC audit group was advised of the decision.

Results of Preliminary Survey

The cost-sharing construction contract terms provided that the school contribute not less than \$250,000 toward the cost of the project and that AEC contribute not more than \$333,000 of the estimated project cost. The AEC contract further provided that the Government's share of the cost of building, as defined by AEC operating manuals, not exceed \$100,000.

The school had issued a contract to a construction firm for the building at a price that appeared to be in excess of the building cost limitation if the total contribution of project costs by the school was considered as being applicable to the cost of building. An examination of the final cost report showed, however, that the school, after advice from AEC, had revised its report to exclude from building costs a portion covering such items as air-conditioning systems, building ventilation systems, electrical systems, plumbing systems, etc., and had reclassified these costs as reactor and accelerator equipment. We were advised that this was done because the contractor's proposal had listed these as "special purpose" items.

We noted that the services of an architectural and engineering (A/E) firm had been used to prepare the proposal. The A/E firm told us that, if it had been aware of AEC's definition for cost of building, in all probability

the subject costs would have been designated as building costs.

The next step was to ascertain which appropriation was used by AEC to finance its portion of the project costs. We found that the agency had used general plant projects (GPP) funds which were designated for general maintenance and upkeep of AEC facilities and for small unexpected construction projects that were required to facilitate the agency's programs. The appropriation act provides that the total costs of a general plant project not exceed \$500,000 and that the total building construction costs of any one project not exceed a limitation of \$100,000. No definition of building cost was provided in the act.

Since the cyclotron construction and modernization program was planned for some time prior to its initiation, it appeared that the Government's share of the program could have been financed with funds specifically appropriated by the Congress rather than with GPP funds.

We discussed our observations with responsible officials of the AEC operations office involved. We were informed that the operations office applied the same concept in using GPP funds for construction of facilities at other educational institutions. It appeared from our discussions that the definition of building costs in the AEC manual was subject to different interpretations. We therefore requested the operations office to provide us with its views on this matter, in writing. It seemed evident, from the views received and an evaluation of the information we had gathered, that similar situations might exist at other AEC contractor locations. We summarized

the information obtained during the preliminary survey and submitted it to the Washington assistant director for consideration.

Expansion of Survey Within Operating Region

Our survey summary received immediate attention from the Washington operating group. The case was discussed in further detail with Washington staff personnel and with officials at AEC headquarters. We learned during these discussions that the AEC used a decentralized management concept for administering general plant projects. Thus, for the most part, AEC headquarters representatives were not specifically knowledgeable as to the administrative determinations being made in the field regarding the use of GPP funds.

The Washington AEC audit group decided that we should perform additional work in the AEC operations office where we had made our preliminary survey so that we might further define the extent that GPP funds had been used for large building construction programs. A supervisory accountant from the Washington operating group was assigned to work with me in this phase of our work. We found that a substantial amount of GPP funds had been used at another educational institution for the construction of buildings.

During the week after our visit to the AEC operations office, members of our Washington AEC audit group met with the executive director and other officials of the Joint Committee on Atomic Energy to apprise them of our observations. As a result of this conference, GAO was requested by the executive director of the com-

mittee to determine whether similar cases existed, and to provide the committee with an informational report within 3 months to be used in the forthcoming 1968 fiscal year appropriation authorization hearings. As a consequence, this assignment now had reached the stage where it was in a top priority category.

Expansion of Survey to Other Regions

By examining data at the agency headquarters, it was determined that three other regional offices of the AEC were also using substantial amounts of GPP funds in their programs. The cognizant GAO regional offices were requested to inquire into the use of the funds at the AEC locations in their regions and to provide the Washington AEC audit group with the results of their survey as soon as possible. The writer was assigned to actively participate in this review as a member of the Washington AEC operating team. It was believed that the background knowledge gained during the preliminary survey would substantially decrease the time that would normally be required to obtain the information needed.

A Washington supervisor and I visited a second educational institution to inquire into the use of GPP funds for financing building construction programs. After initiating the survey work and obtaining a portion of the required information, the Washington supervisor left the site to accompany the assistant director in charge in a visit to the other regional offices that were selected to participate in the survey. His responsibilities were to

assist the assistant director and review the work being done by the audit staffs on this assignment.

At the second location, we found that AEC was using GPP funds to finance a long-range, planned construction expansion program. In some instances, this construction had been planned 3 to 5 years in advance by the school and the agency. It was also noted in several instances that the buildings were being constructed in stages as separate projects. Under this procedure, the cost of each individual project did not exceed the statutory limitation.

For example, an initial story of a building would be constructed the first year as one project and then a second story to the same building would be added a second or third year hence as a separate project. The first story of the building was structurally designed to accommodate a second story which had been initially planned by the contractor.

Instances were noted during the expanded survey where one-story structures were constructed in phases in recognition of the statutory limitation imposed upon general plant projects. Thus, it would take as long as 2 or 3 years to complete the construction of a single-story building. It was noted that extreme care was exercised by the agency to ensure that, in the construction programs, the building costs for each phase did not exceed \$100,000 in reconciliation of the AEC interpretation of the laws, even though the total overall cost of the building would eventually exceed the \$100,000 statutory limitation.

Participation at Washington Level

After the expanded survey work was completed, the writer, as a member of the Washington team, was involved in assembling the data obtained and in performing further work at AEC headquarters. After this was done, a proposed report was drafted. As portions of the report were prepared, they were referenced to the supporting working papers by an independent referencer. The proposed report was forwarded to the agency for comment just 1½ months after we received the survey request from the Joint Committee.

Because of the urgency of providing the Joint Committee with the survey report, we requested the agency to return its comments within 10 days. The agency was able to provide us with its comments on our proposed report in about 15 days. The agency comments were resolved and a report on our survey was issued to the Joint Committee 3 months after the committee had requested GAO to expand the survey and report back to them.

Nature of Report

Our 75-page report presented our observations to the Joint Committee on Atomic Energy on (1) the use of GPP funds for planned expansion programs; (2) the effect and uneconomical nature of certain practices employed by the AEC to comply with funding or statutory limitations; and (3) the interpretations being placed on the statute relating to the limitation of building costs.

Extensive use of graphic illustrations was made in our report to support the observations reported. The use of illustrations enabled us to

demonstrate much more clearly our observations concerning the use of GPP funds in the construction of buildings.

Action Taken

The Joint Committee on Atomic Energy report on the 1968 fiscal year appropriation authorization for AEC (H. Rept. 369, 90th Cong., 1st sess.) dated June 19, 1967, refers to its request to GAO and our report on selected aspects of the administration of GPP funds by AEC. The committee report stated that, as a result of GAO's review, AEC established revised procedural requirements and proposed an amendment to the standard language used to establish limitations on the use of GPP funds. The new proposed language will give the Commission the authority to exceed the \$100,000 limitation on the cost of any one building within a project if the Commission determines that it is necessary in the interest of efficiency and economy.

The committee's report also stated that it is the committee's intent that the Commission establish written pro-

cedures for implementing the proposed new statutory authority and that such procedures provide for prior review and approval by appropriate AEC headquarters officials of any use of the new authority. In addition, the Commission is required to report on the use of GPP funds to the Joint Committee on Atomic Energy and the appropriations committees after the close of each fiscal year. Such reports must identify each project for which the proposed new authority has been utilized.

Printed copies of the hearings on AEC authorizing legislation for fiscal year 1968 before the Joint Committee on Atomic Energy (Feb. 28 and Mar. 2 and 3, 1967, p. 3) contain a comprehensive statement by AEC about its authority and its practices relating to general plant projects. This statement included the comment that "In our view the GAO survey and reporting was constructive and of significant help to us, with the result that our administration of GPP funds has been strengthened."

Supervisory Review of Working Papers

721333

By John A. Dowell

The author discusses a very important supervisory audit responsibility and suggests a number of specific points to be considered in reviewing working papers.

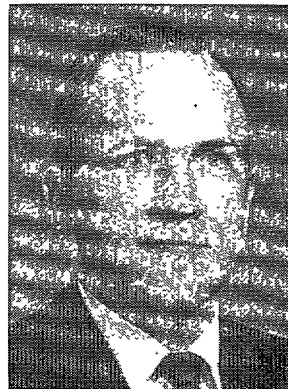
The General Accounting Office has reason to be proud of its long history of significant contributions to improvements in Government operations and its proficient staff which makes these contributions possible. These achievements are the result of effective recruiting and training of staff, hard work by employees at all levels, and a system of internal control to ensure that the audit work and related reports consistently conform to high standards of quality.

The supervisory review of working papers is one of the more critical quality control processes used by GAO to ensure that these high standards are met. The review process also provides an excellent means for the supervisor to evaluate the performance of staff

members and to provide needed training and counseling. It is through this day-to-day supervision and counseling that capable auditors and supervisors are developed and attain the degree of technical proficiency contemplated under the auditing standards of the Office.

When reviewing working papers, the supervisor must ensure that the audit objectives adopted for the assignment were met, the necessary steps were performed, the papers were adequately prepared, and all matters were properly considered and developed. While timely completion is desirable, a supervisor must not accept substandard work at any time to expedite the completion of an assignment. When he accepts substandard work, the

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supervisor not only compromises prescribed standards but also hinders the continuing development of his staff.

Responsibility for Review

Working papers are usually reviewed by at least three staff members, the first of which is the individual who prepares the memorandum. During preparation and at completion of a working paper, or series of working papers, the staff member reviews and evaluates them to ensure they represent his best effort, releasing them to the site supervisor only after he is satisfied with them.

Each time the site supervisor reviews the papers, he should prepare review notes and discuss them with the staff member, giving constructive suggestions on how to improve the auditor's performance. After satisfying himself that the papers are adequately prepared, the audit program has been complied with, the conclusions reached are valid and reasonable and the papers represent a professional product in all respects, the site supervisor should sign the working papers. The signing-off by the site supervisor means that he has found them to be in conformity with Office standards and that he is in agreement with the conclusions and recommendations.

After the site supervisor completes his review, the audit manager, during the course of the audit, reviews the working papers and prepares review notes when appropriate. This review generally is not as extensive as that of the site supervisor. For example, the audit manager may be satisfied, after reviewing a portion of the papers, that the auditor and site supervisor have done a good job and limit

the scope or depth of his review. Regardless of the extent of his review, the audit manager will also sign off on the working papers, signifying that he has found them to be in conformity with Office standards and that he agrees with the conclusions and recommendations.

Timeliness of Review

Working papers should be reviewed promptly. Generally, working papers, or a series of working papers, should be reviewed by the site supervisor within 2 or 3 days after completion.

The timely review of working papers may result in significant changes in audit plans. For example, the supervisor may learn from his review that the original audit plans cannot be followed and that an alternate approach must be devised. His review may also show that considerable additional work at other locations is necessary at an early date to enable prompt reporting. At times, he may learn that evidence gathered by the auditor shows that the finding is not as significant as originally thought or that there is no finding at all, in which event the assignment should be discontinued before more time is expended. He may also find that the auditor is not following the program or is devoting too much time to insignificant matters. Unless the supervisor stays on top of the job through timely supervision and review of the working papers, considerable audit effort may be wasted.

Prior to completion, certain working papers may be reviewed several times by both the site supervisor and the audit manager. For instance, in the case of an inexperienced staff member, the supervisor may discuss

the format of a schedule before any work is performed. After limited data is scheduled, he may review the schedule to ensure that the auditor is preparing it as agreed. Near or at completion of the schedule he may again review it to determine if the information obtained will suffice.

Working papers may also be reviewed after completion of certain schedules but before preparation of the summary. After summaries are completed and the papers indexed, another review will be performed, and at this time, the working papers usually will be accepted by the supervisor.

Depth of Review

The auditing standards of the General Accounting Office require the exercise of due professional care on all assignments. While some assignments vary in significance as to potential report matters, the work performed during all assignments must meet the high Office standards. Accordingly, on each assignment, regardless of its nature and size, all working papers must be carefully reviewed.

The supervisor's review of working papers involves more than scanning the papers to see if they are neat. It is expected that the supervisor will become thoroughly familiar with the activity under audit, including a knowledge of the organization, staffing, procedures, and types of records maintained. In other words, the supervisor is expected to expose himself to the "muck and mire" of the job and be in a position to make informed judgments, based on his personal knowledge of the activity and a careful analysis of the information gathered by his subordinates.

In reviewing the working paper summaries, the supervisor must ensure that all statements are factual and fully supported by working papers and that conclusions reached are valid and reasonable based on the work performed and evidence obtained. During the report preparation process, the working papers which have a bearing on the findings should again be reviewed. Certain inconsistencies may appear at this time and these should be resolved.

Points To Be Considered

Due to the nature of our work, it is not possible to prepare an all-inclusive list which can be used by supervisors in reviewing working papers. There are, however, some points which should be considered on all assignments. These are:

1. Have the working papers been prepared in accordance with Office policies and practices? Is security information clearly and properly labeled?
2. Are the headings, legends, and sources clearly and properly stated? Are the purposes clear? Are the papers and summaries easy to follow and sufficiently cross-indexed?
3. Have computations and footings been independently verified?
4. Has the auditor complied with the program by meeting the audit objectives and by carrying out all required work steps? Have review notes been cleared?
5. Does the summary convey a convincing story? Are the conclusions and recommendations clear, valid, and reasonable in view of the facts presented? Have all pertinent facts been considered, including those points which may tend to mitigate the condition?
6. Has the auditor completely developed the report matter by considering all important aspects of the problem, including a proper identification of the underlying causes?

Summary

The review of working papers is a responsibility which cannot be taken lightly by the supervisor. It is one of the control processes used to ensure that the audit work and related reports meet high standards of quality. In addition, and perhaps of greater im-

portance in the long run, the supervisor must critically review the work of all staff members and make appropriate suggestions for improvements to provide the on-the-job training needed to supplement formal training programs.

The Role of the Supervisor

721334

By Lester C. Farrington, Jr.

The theory and practice of supervision is discussed in this article, with particular emphasis placed on the attributes of a good supervisor.

There is no doubt that the supervisor plays a vital role in every organization. A good supervisor not only should be interested in and knowledgeable of the work being performed but also must be able to assign work and motivate his staff. Within the General Accounting Office, a supervisor is responsible for the work performed and the results achieved on a particular audit assignment.

The importance of the supervisor has been brought out nicely, I believe, by Spriegel and Schulz in the statement which follows:

“More and more the supervisor, provided with staff specialists, is becoming a manager of men, a specialist himself in handling men, in dealing with and guiding human effort. The successful supervisor today must be a practical industrial psycholo-

gist, versed in guiding, developing, and controlling the actions of men. But his skill in his specialized field must be built on a sound foundation of knowledge—knowledge of his own organization, its objective and pattern, its policies and methods; knowledge of the tasks of organizing, deputizing, and supervising; knowledge of his duties and responsibilities and their delegation.”¹

The supervisory attributes which are discussed in the following paragraphs are not intended to be all-inclusive and many more probably can be added. However, upon the basis of my experience in the General Accounting Office, I believe that they are the attributes which have been most effectively applied. When dis-

¹ W. B. and W. R. Spriegel and Edward Schulz. “Elements of Supervision,” p. 10. John Wiley & Sons, Inc., New York, 2d ed., 1965.

Mr. Farrington is a supervisory auditor in the Boston Regional Office. He holds a B.S. degree in business administration from Suffolk University, Boston, Mass., and has been with GAO since 1964. Prior to July 1967 he worked in the New York Regional Office.



cussing supervisors, I am referring to onsite supervisors rather than to audit managers, regional managers, or other levels of supervision.

Motivation and Productivity

A supervisor must be able to motivate his subordinates to do a good job. Proper motivation should result in optimum productivity and morale. David L. Korb, Bureau of Programs and Standards of the U.S. Civil Service Commission, has stated that supervisors can increase productivity by:

- Making better use of employee energy and effort.
- Organizing the assignment and flow of work to facilitate output.
- Training employees to work efficiently.
- Getting to understand employees as individuals.
- Building a group attitude of cooperation to stimulate each employee to do a better job.
- Developing an understanding of the employee's desire to do a good job.
- Giving proper recognition for good ideas and superior performance.
- Giving employees full opportunity to demonstrate their worth.²

Although these guidelines may be more adaptable to supervision within a manufacturing or production operation, I believe that they are applicable to some extent to our work.

The supervisor on a GAO assignment must be genuinely interested in and concerned about the work performed and the results achieved by all members of his staff. Ideas and opin-

ions on current and future audit areas should be solicited from all staff members, including trainees. The supervisor should make a concerted effort to obtain these thoughts and should weigh the prospective merits of each accordingly.

The supervisor must also have the respect of his staff since it is this attribute that will motivate the staff to follow his suggestions and recommendations eagerly and enthusiastically. Even the most menial tasks should not be deemphasized. The supervisor should attempt to make such tasks attractive by explaining how these minor functions are an important aspect of the overall assignment and contribute to its success.

In addition to the above, a supervisor's own motivation has a substantial effect on his staff. A display of eagerness by the supervisor in developing information on an area under review may provide extra incentive and initiative for the staff.

Knowledge of the Job

The supervisor should be thoroughly familiar with GAO policies and procedures and with the entire audit assignment from inception to end. This is necessary because he is responsible and held accountable for the output generated by the staff and must be able to render guidance and to train the staff to do the job, when necessary.

The supervisor may be able to gain a good deal of insight to the job not only by reviewing workpapers and summaries prepared by the staff but by having short daily discussions with staff members. By doing this, he could keep abreast of the work currently being performed and any problems

² American Management Association, "Leadership on the Job," p. 167. New York, 1957.

being experienced. This may be particularly beneficial when there is a large staff assigned at a given location.

A supervisor may also increase capability to evaluate the work being done through efforts related to his self-development. For example, many books and articles dealing with the use of learning curves, statistical sampling, and program evaluation and review techniques have been written. By studying subjects such as these for his self-development, a supervisor may gain necessary background data and knowledge directly related to his GAO job assignments.

Assigning Work

The assignment of work is closely affected by the way a supervisor communicates, orally or in writing, with his staff. For example, the supervisor may understand the nature of the work to be accomplished in relation to the specific objective; however, when assigning work to others via instructions he must in some way convey this knowledge. Therefore, instructions should be as clear and complete as possible to avoid misinterpretations and misunderstandings.

The supervisor has the responsibility of conveying to members of the staff knowledge of how their particular assignments relate to the overall objectives of the review. If this is not done, the work being performed loses significance and meaning to the staff member assigned to each specific segment. In addition, the supervisor should assure himself that each staff member is given assignments commensurate with his ability. In making these assignments, the supervisor should clearly define the staff members' responsibilities.

Other Qualities

A supervisor should possess, among other qualities, the ability to:

- Establish realistic time estimates for specific segments of an assignment.
- Stand behind his men when problems arise (where warranted).
- Be objective when preparing staff ratings.
- Create an atmosphere in which staff members are at ease in discussing problems and progress experienced on assignments.
- Make decisions.
- Maintain good relations with his staff and with agency and contractor personnel.
- Communicate fully not only with his staff but also with his supervisors.

Extent of Supervision

The above discusses some of the attributes and qualities one should possess to be a good supervisor. A question that may arise is whether very close or very limited supervision is to be given on an assignment.

A very limited amount or a general lack of supervision during an assignment may lead to an individual not being assured that he is doing an adequate job in fulfilling the assigned tasks and specific objectives. The supervisor will therefore have to exercise judgment concerning the extent of supervision to be given to the staff. The overall and individual initiative, capability, and resourcefulness of the staff should be considered in making the determination.

As a member of the American Management Association has said, however, a good supervisor does not supervise too closely. He tells his sub-

ordinates what is wanted, teaches them how, and checks the results. His job is to guide, to stimulate, to encourage—to release the creative energy of his work group.³

I have found that close supervision, except for newly hired employees, tends to restrict and limit initiative within the person being supervised. The employee may begin to lose confidence in himself and to feel that he cannot be relied upon if the above situation exists. I have found also that, at the beginning of a job, fairly close supervision may be warranted; however, once an individual shows that he can do the work adequately, expeditiously, and thoroughly, direct supervision can be given to a more limited degree.

Supervision Received by Writer

On many of my audit assignments with the General Accounting Office, I have been a staff assistant receiving supervision from a senior. The supervision received, in most cases, was effective in creating good morale and providing optimum output. For example, both oral and written instructions given me have, for the most part, been clear, concise, and complete. Audit programs and other instructions have contained sufficient information on the subject matter for review to enable me to know and understand: (1) The objective; (2) the audit steps; and (3) the work previously done by other audit groups.

In addition, if I encountered a problem relating to my work, I could discuss it freely and openly with my supervisor and he in turn would do everything possible to help me solve the problem. Conversely, supervisors

have sought my thoughts and ideas on a particular audit area. When my ideas were considered and subsequently used, I was given proper credit and recognition by the supervisor.

I have also worked for supervisors who made available to me written materials accumulated by them on previous assignments, which directly related to the subject matter being considered or currently under review. This has provided me with a better understanding of and deeper insight into the audit area than would have been possible had I not been made aware of such material.

Need to Expand Training Program

Even though I have been exposed to supervision that has, in my opinion, been effective, I believe that a certain amount of formal training in the theory and practice of supervision should be given to an individual prior to or shortly after he becomes a supervisor. This is the time, early in one's career, when such training is most needed and when the foundation for good supervision can and rightfully should be instilled within the individual. Any formal training will be supplemental to the training received on the job since, as discussed above, the attributes displayed by a good supervisor are the best means of conveying to an individual the qualities that he should have as a supervisor.

The importance of the onsite supervisor cannot be emphasized enough. He is a key man in our operation and contributes greatly to the success of our organization. As previously mentioned, he motivates, trains, and instructs the staff; assigns work; and reviews results. In effect, he is respon-

³ Ibid. p. 172.

sible for getting work done through the efforts of others.

A successful onsite supervisor certainly applies some of the principles that have been set forth in this article. I believe that an awareness of these, through formal training, can and should improve a supervisor's performance. It is therefore my opinion that GAO should devote more emphasis to this important function in its formal in-house training programs. I am not advocating that a separate training program on supervision be developed. I believe, however, that a certain amount of time in our intermediate training course could be devoted to a discussion of supervision and a review of case study material. Some of the areas that could be highlighted are:

- Supervisory theory and practice.
- Supervision as it applies to our work and requirements of a good supervisor in GAO.
- Problems that have arisen in GAO and possible solutions to these problems.
- Relationships between supervisors (all levels) and subordinates and what each should expect from the other.

Case studies could be developed for discussion to confront the training group with actual and/or hypothetical problems. The objective would be to analyze the situation in order to arrive at the means by which these problems could have been avoided through effective supervisory practices.

New Budget Concepts

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By Ellsworth H. Morse, Jr.

This article presents a brief résumé of the recommendations of the President's Commission on Budget Concepts which completed its work in October 1967.

On October 18, 1967, the President's Commission on Budget Concepts released the report on its study of how to make the Federal budget a more understandable and useful instrument of public policy and financial planning.

The Commission had been appointed by President Johnson in March 1967 to review existing budget concepts and make recommendations for improvement (see *GAO Review*, Spring 1967, p. 80). In a period of about 6 months, the Commission made its study and produced a comprehensive and impressive report with numerous far-reaching recommendations on a very complex subject.

The Commission had 16 members consisting of prominent representa-

tives of private business, the press, and academic institutions; Members of the Congress; and high Government officials, including the Comptroller General of the United States (see opposite page).

It was assisted by a small but able staff whose work was supplemented by assistance from staff members of the Bureau of the Budget, the Treasury Department, the General Accounting Office, and other Government agencies; various congressional committees; the Board of Governors of the Federal Reserve System; and The Brookings Institution.

It seems likely that all or most of the Commission's recommendations will be adopted in time. The President has accepted the Commission's recom-

**Ellsworth H. Morse, Jr., Director,
Office of Policy and Special
Studies.**



COMMISSION MEMBERSHIP AND STAFF

- Mr. David M. Kennedy, Chairman of the Board, Continental Illinois National Bank and Trust Company of Chicago.
- The Honorable Robert B. Anderson, New York City (Secretary of the Treasury, 1957-60).
- The Honorable Frank T. Bow, Ranking Minority Member, Committee on Appropriations, U.S. House of Representatives.
- The Honorable Henry H. Fowler, Secretary of the Treasury.
- The Honorable Carl Hayden, Chairman, Committee on Appropriations, U.S. Senate.
- Mr. Winthrop C. Lenz, Executive Vice President, Merrill, Lynch, Pierce, Fenner & Smith, New York City.
- The Honorable George H. Mahon, Chairman, Committee on Appropriations, U.S. House of Representatives.
- Professor Paul W. McCracken, The University of Michigan.
- The Honorable Charles L. Schultze, Director, Bureau of the Budget.
- Professor Carl S. Shoup, Columbia University.
- Mr. Leonard S. Silk, Editorial Page Editor and Chairman of the Editorial Board, Business Week.
- The Honorable Elmer B. Staats, Comptroller General of the United States.
- Mr. Robert M. Trueblood, Chairman of the Policy Group, Touche, Ross, Bailey & Smart, Chicago (President, American Institute of Certified Public Accountants, 1965-66).
- Professor Robert C. Turner, Indiana University (Assistant Director, Bureau of the Budget, 1961-62).
- Dr. Theodore O. Yntema, Oakland University, Rochester, Michigan.
- The Honorable Milton R. Young, Ranking Minority Member, Committee on Appropriations, U.S. Senate.
- Staff:**
- Robert P. Mayo, Staff Director.
 - Wilfred Lewis, Jr., Research Director.
 - Ronald W. Johnson, Research Assistant.
 - Jeffrey M. Wiesen, Research Assistant.
 - Roselle Smith, Administrative Assistant.

mendations as to the basic concepts of the Federal budget. On December 14, 1967, the Director of the Bureau of the Budget, Charles L. Schultze, announced that virtually all of the basic changes recommended by the Commission, and which could feasibly be undertaken in time, would be incorporated in the budget for the fiscal year 1969, to be submitted to the Congress early in 1968.

The entire subject of the Commission's report is important to the work and the functions of the General Accounting Office. A good understanding of the structure and processes of the Federal budget is necessary on the part of GAO staff members if they are to have an adequate perspective of the complex field of overall Federal management within which their work is performed. The purpose of this article is to present a résumé of the Commission's proposals with commentary, where applicable, as to any special significance they may have from the standpoint of the General Accounting Office.

Major Recommendations

The essence of the Commission's major recommendations is that:

- There should be a single Federal budget concept for all purposes.
- The budget should include all programs of the Federal Government and its agencies.
- Receipts and expenditures should be stated on the accrual basis.
- Loans, after deduction of any subsidy elements, should be segregated in the budget from all other expenditures.
- Sales of participation certificates in loan pools should be treated

as a method of financing rather than as a deduction from expenditures.

- Receipts which are enterprise or market-oriented should be treated as offsets to expenditures to which they are related.

The Commission recommended strongly against a capital budget under which a separate financial plan for capital or investment expenditures would be presented.

Unified Budget Concept

The Commission's most significant recommendation is that a unified budget concept be adopted and that it be constantly adhered to in:

- The President's budget submitted to the Congress annually in January.
- Publications revising budget estimates or reporting year-end results.
- Monthly financial reports from the Treasury on actual budget results.
- Estimates of overall budget results.

The Commission's recommendation was made in light of the evolution in recent years of three different budget concepts, namely:

- The administrative budget which excludes trust funds administered by the Federal Government.
- The consolidated cash budget which includes trust fund transactions.
- The national income accounts budget which includes all funds but excludes loan transactions.

The Commission was also concerned that the bases of reporting ex-

penditures for each of these budgets differed. It concluded that there should be a unified budget which would put an end to competing measures, and it urged adoption of the accrual basis for stating both budget receipts and expenditures.

The Commission's report pointed out, perhaps somewhat hopefully, that adoption of its recommended, unified concept would make such terms as *administrative budget*, *consolidated cash budget*, and *national income accounts budget* obsolete.

The Commission also recommended that:

- The budget be thought of as part of a broad financial plan, which would present—in addition to appropriations, receipts, expenditures, and net lending—the means of financing a budget deficit (or use of a surplus) and information about borrowing and loan programs of the Government and its agencies.
- More prominence be given in the budget presentation to the actions requested of the Congress, such as appropriations and revenue legislation.
- The budget include all programs of the Federal Government and its agencies.

These several recommendations were the basis for the Commission's proposal as to overall structure or initial summary tabulation for the budget presentation. Such structure was suggested as shown on page 54. The proposal was designed to produce in simple form the figures needed for an analysis of the economic impact of the budget (net lending excluded) and the aggregate figures (net lending included) to provide:

- A summary of agency and program amounts used in deciding the appropriate allocation of resources to be used by the Government.

- An accurate measurement of the scope of overall Government activity.

In announcing on December 14 the decision to incorporate the recommended concepts into the Federal budget, the Budget Director stated:

The 1969 presentation will require some adjustment in public thinking about Government finances. For many years emphasis was placed on the single "administrative budget" which excluded social security funds, the highway trust funds and other earmarked accounts whose receipts and expenditures exceed \$45 billion. The new concept is much more comprehensive. It includes all the funds administered by the Federal Government. The totals of both receipts and expenditures in current and past years will, therefore, be significantly higher under the new concepts.

The Commission recognized that no single budget summary could adequately serve all the different purposes of various users of the Government's financial data. It noted that specialized tabulations of Federal receipts, expenditures, and appropriations are required for many purposes but urged that all such tabulations be treated as subordinate to or explanatory of, and not competitive with, the basic budget.

Importance of Appropriations and PPB

In explaining its recommendations, the Commission carefully emphasized the importance of the congressional appropriation process. It noted that the making of appropriations is, and will continue to be, the actual point of basic choice in allocating resources among Government programs. Of interest is its strong endorsement of the Planning - Programming - Budgeting System approach to budget preparation and review, which is intended to

RECOMMENDED SUMMARY OF THE PRESIDENT'S BUDGET AND FINANCIAL PLAN

- I. Budget appropriations:
 - Proposed for action by the Congress
 - Not requiring action by the Congress
 - Total appropriations
- II. Budget receipts, expenditures, and lending:
 - Receipt-expenditure account:
 - Receipts
 - Expenditures (excluding net lending)
 - Expenditure account surplus or deficit ¹
 - Plus: Loan account:
 - Loan disbursements
 - Loan repayments
 - Net lending
 - Equals: Total budget:
 - Receipts
 - Expenditures and net lending
 - Budget surplus or deficit
- III. Means of financing:
 - Borrowing from the public
 - Reduction of cash balances, etc.
 - Total budget financing
- IV. Outstanding Federal securities and Federal loans, end of year:
 - Federal securities:
 - Gross amount outstanding
 - Held by the public
 - Federal credit programs:
 - Direct loans outstanding
 - Guaranteed and insured loans outstanding

¹ In any discussion of the economic impact of the budget where net lending is excluded from expenditures, the Commission cautions that the full heading "expenditure account" preceding the term "surplus or deficit" should be used to identify the item as a subtotal of section II of the table. Otherwise, the use of the term "surplus or deficit" would be confusing and misunderstood. Whenever the term "budget surplus or deficit" is used, it refers to the total budget, including net lending.

improve the mechanics of choice among alternative programs and approaches in meeting public needs and purposes. It also observed that PPBS is concerned with total costs and benefits to the Nation and not merely with Federal revenues and expenditures. Thus, although PPBS analyses should be used in the allocative process, the budget is a financial plan for the Government and the budget totals should not include total social costs and benefits.

Another principle enunciated by the Commission—and one that has long been of interest to the GAO—was that the budget presentation should provide all the information needed for making sound program decisions. While the budget document itself would not include all the detailed information, it should provide the setting for a full presentation of the alternatives considered and their evaluation. This presentation and evaluation should be made by the agencies during hearings before the legislative and appropriations committees on proposed legislation and appropriation requests.

The Commission took note during its study of the trend in recent years toward including more understandable and analytical business-type financial statements in the appendix to the budget. It expressed endorsement of this trend.

Coverage of the Budget

The Commission pointed out that, to work well, the Government's budget process should embrace the full scope of Federal programs and transactions. It accordingly recommended that the budget comprehend the full range of Federal activities, including:

- Federal trust funds.
- Borderline agencies and transactions except where there are exceptionally persuasive reasons for their exclusion.

Trust Funds

In reaching its conclusions, the Commission encountered the problem that the boundaries of the Federal establishment are not always easy to draw.

One of the most important budget boundary questions studied by the Commission was the area of the trust funds, representing, in theory, funds not owned by the Government but for which it acts as trustee. Sizable programs accounted for under trust fund activities include:

- Old-age and survivors insurance.
- Unemployment insurance.
- Federally aided highway construction.
- Medicare.
- Civil service retirement.

The Commission noted the growth in magnitude, both relative and absolute, of trust fund activities in total Federal operations and concluded that current surpluses of trust funds had to be considered in calculating the effect of Federal Government activities on the level of income and employment, in managing Treasury cash balances, in deciding on Treasury cash borrowing needs, and in program evaluation.

It therefore recommended that the Federal budget include receipts and expenditures of the trust funds. In making this recommendation, the Commission also made it clear that it was not advocating the elimination of separate trust fund accounting. It

recognized the need to respect the integrity of trust funds and that to do so requires separate accounting of trust fund transactions and balances.

The inclusion of trust fund transactions is the principal difference between the present administrative budget (which excludes them) and the consolidated cash budget and the national income accounts budget.

Government-Sponsored Enterprises

Another boundary question encountered by the Commission concerned the Government-sponsored enterprises as to which attention centered on:

The Federal Home Loan Bank System:

The 12 Federal home loan banks.

The Federal Farm Credit System:

The 12 Federal land banks.

The 12 banks for cooperatives.

The 12 Federal intermediate credit banks.

The Federal Deposit Insurance Corporation.

With respect to these enterprises, the Commission concluded that:

- The Federal land banks and the Federal home loan banks should be *excluded* from the Federal budget on the basis that they are now completely privately owned.
- The banks for cooperatives and the Federal intermediate credit banks should be *included* in the Federal budget as long as Federal capital is invested in any of them.
- The Federal Deposit Insurance Corporation should continue to be *included* in the budget on the ground that it carries out a Federal insurance program and cannot be said to be privately owned since it no longer has any equity capital.

For those enterprises suggested for exclusion, the Commission stated that

their transactions should not be sheltered from public scrutiny. It specifically recommended that the budget document include data on the volume of outstanding loans of such enterprises. It also recorded itself in favor of including financial statements of such enterprises in the budget appendix.

Federal Reserve System

The Commission recommended that the receipts and expenditures of the Federal Reserve System continue to be *excluded* from the budget although the payment to the Treasury of excess profits from operations would continue to be included as a Federal budget receipt.

The Commission characterized the System as "clearly a Federal Government operation" but noted that inclusion of the Federal Reserve banks in the Federal budget might jeopardize the flexibility and independence of the monetary authorities. It also noted that forward projections of the System's operations did not appear to be "feasible at the present time" and that the nature and economic significance of Federal Reserve bank receipts and expenditures differed from those of most other Government programs and activities. Accordingly, the Commission endorsed the treatment given the System under existing budget concepts.

District of Columbia Government

The Commission recommended that receipts and expenditures of the District of Columbia Government be *excluded* from the Federal budget on the basis that it is a local, and not a national, function. The Federal payment to the District of Columbia

would of course be included as a Federal budget expenditure.

The treatment recommended is the same as that followed in the present administrative budget and the national income accounts budget. However, the consolidated cash budget includes the financial transactions of the District of Columbia.

International Monetary Fund

The Commission recommended that subscriptions, drawings, and other transactions affecting the United States position with this Fund be *excluded* from budget receipts and expenditures.

The Commission viewed the International Monetary Fund as a bank to help finance the international payments positions of member countries. The United States net position with the Fund was considered as a foreign exchange asset comparable to gold or convertible foreign currencies owned by the Treasury.

Deposit Funds

The Commission endorsed an analysis being made by the Bureau of the Budget and the Treasury Department of the great number of deposit funds used in the Federal accounting system. In general, deposit funds are used for banking type transactions or for accounting for amounts held in suspense pending determination as to proper disposition.

The purpose of the analysis being made is to identify items which should be reclassified more in keeping with their true character. Generally, transactions affecting deposit funds should not be reflected in budget totals stated on the accrual basis. Since the Commission's report was issued the Gen-

eral Accounting Office has also been participating in the analysis of these funds used by the Federal agencies.

Loan Programs

The Commission's recommended top summary of the budget calls for a separation between receipts and expenditures on the one hand and net lending transactions on the other, although the totals of these two "accounts" are to be added in determining the budget surplus or deficit.

It was felt that such a separation between loans and other expenditures was important because of the fundamentally different nature of such outlays, largely from the standpoint of economic analysis. In making this separation, certain loan programs are to be excluded on the basis that they are more in the nature of expenditures. Foreign loans made on noncommercial terms and nonrecourse loans on farm commodities made by Commodity Credit Corporation were the principal examples cited by the Commission of loans to be left in the expenditure account.

Another exclusion from the loan account recommended by the Commission is the subsidy element in loans made. The principal element of subsidy identified by the Commission on Federal loan programs is the difference between the interest paid by the Government on borrowed funds and the interest collected from borrowers. The Commission characterized such differences as "in part grants or transfer payments rather than loans."

The Commission suggested that the interest subsidy be measured on a capitalized basis over the life of the loan and be disclosed as an expenditure in the period in which the loan is made.

Adoption of this recommendation will mean that accounting procedures of agencies administering loan programs will have to be extended to accommodate the required additional analyses of loan disbursements and repayments. The impact of this recommendation on loan accounting procedures will require additional study by the GAO, the Bureau of the Budget, the Treasury Department, and the lending agencies concerned before the recommendation can be implemented.

The Commission also suggested disclosure in the expenditure account of allowances for estimated losses on loans as representing a further subsidy growing out of the fact that Federal loans involve a larger element of risk than Treasury borrowing.

In making these recommendations, the Commission was not taking a position on the existence or the extent of loan subsidies. Its stated purpose was to promote bringing them "out in the open as a matter of essential budget information needed for adequate policy formulation." Separate appropriations were not suggested. Further, it observed that the importance of stating the amount of loan subsidies was not so much in disclosing the dollar effect as in providing a better measuring stick for helping policymakers decide on the relative merits of allocating resources among competing direct loan programs or between direct loans and grants-in-aid or direct expenditures.

Participation Certificates

Most of the members of the Commission regarded the procedure of selling certificates of participation in Federal loans as a means of obtaining funds and not as a reduction of

expenditures. In adopting this view, it was noted that the Government still "owned" the loans, incurred the servicing costs, and assumed all risks of default by individual borrowers. Net sales of participation certificates currently amount to over \$4 billion a year.

The only stated dissent by any of the members from the Commission's recommendations related to the recommendation that participation certificates be treated as a means of financing and not, as has been the practice, as an offset to expenditures.

Three members, including the Secretary of the Treasury and the Budget Director, did not agree with the recommendation. Despite their dissent on this point, however, these officials recommended to the President that the Commission's recommendations be adopted as a whole. Thus it is planned to incorporate the revised treatment in the 1969 budget.

Offsetting of Receipts and Expenditures

The Commission urged more consistent practice in offsetting receipts against expenditures for budget presentation purposes. Its main recommendation on this score was that receipts from activities that are essentially governmental in nature which involve regulation or compulsion should be classified as receipts. On the other hand, receipts from business-type operations or those that are market-oriented should be offset against related expenditures.

Examples of receipts derived from governmental functions include taxes, customs duties, social insurance premiums, patent and copyright fees, and

immigration, passport, and consular fees.

Examples of receipts from business-type or market-oriented activities include receipts from Government enterprises, permits, hunting and grazing licenses or fees, interest, dividends, royalties, sales of products or other property, etc.

No changes in funding arrangements were contemplated by this recommendation. The analysis of present receipts and the identification of those to be shown gross and those to be netted will probably be carried out as a joint project of the Bureau of the Budget, the Treasury Department, and the General Accounting Office.

Other Recommendations

The Commission's report contains numerous other recommendations for improving the way in which Federal budget information is presented.

Without commentary, the more important of these are:

1. The President's budget message should give more prominence to new legislation and appropriations being requested of the Congress.
2. The concept currently referred to as "new obligational authority" should be used by both the executive branch and the Congress. This concept should be renamed "appropriations" which would include contract authorizations and authorizations to spend debt receipts.
3. When the term "budget surplus or deficit" is used, it should refer to the total budget (expenditure account and loan account). The President's budget presentation should not include surplus or deficit figures calculated on the basis of the present administrative budget.
4. The budget document should present a means-of-financing statement in a prominent place showing the major ways in which a budget deficit is financed or a surplus used.

5. New debt concepts should be adopted consistent with the Commission's definitions of receipts and expenditures. Securities issued by all Federal agencies in the budget should be included to produce a concept of "gross debt outstanding." From this total, Treasury and agency securities held by the Federal agencies in the budget and in Federal trust funds would be deducted to produce "Federal securities held by the public." Both amounts should appear in the budget summary.
6. Seigniorage ("profits" on coinage operations) should be treated as a means of financing rather than as budget receipts.
7. The budget summary should disclose outstanding guaranteed and insured loans as well as data on total direct loans.
8. Communication of budget information to the Congress and the public should be:
 - More frequent by providing within-year revisions of January estimates.
 - More detailed by breaking down budget figures into quarterly on semiannual units.
 - More comprehensive by making estimates which extend further into the future.

Accrual of Receipts and Expenditures

To provide a better measure of the impact of Government activities on the economy, the Commission recommended that budget receipts and expenditures be stated on the accrual basis instead of the present cash basis.

Recognizing the difficulties involved, the Commission noted that the accrual of individual income taxes would require further study. However, in general, it advocated reporting all receipts on the accrual basis as soon as possible, including corporation income and other taxes and miscellaneous receipt items.

The Commission's recommendation for reporting budget expenditures on the accrual basis is the most important of its recommendations from the standpoint of the functions of the General Accounting Office. For this reason, the nature and significance of this recommendation will be analyzed in a separate article in a later issue of the *Review*.

Interesting Request

The following evidence of intensifying interest in the operations of the General Accounting Office was recently received:

Gentlemen:

Would you please send me one copy of the General Accounting Office for the past 4 years.

Planning of Health Programs in El Salvador

By Jack Wild

The author describes some of our assistance projects in this Central American country, the GAO audit work, and personal aspects of the assignment.

Since being assigned to the audit of the Agency for International Development (AID), I have had an opportunity to travel to many parts of the world. One assignment involved El Salvador which I found to be one of the more pleasant and interesting countries of the many in which I have worked.

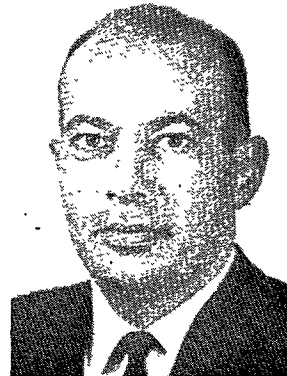
The audit was an offshoot of a survey trip made to four Central American countries, to determine whether a more detailed examination of the foreign assistance program in these countries would be in order. While in El Salvador we became aware of numerous problems in U.S.-assisted health programs. Through an examination of records and documents and discussions with AID officials, we found indications that some AID-assisted

health projects were not being properly implemented. On the basis of these observations and further preliminary work in Washington, we concluded that more work should be performed. As a consequence, we scheduled a detailed review of the U.S.-assisted health programs in El Salvador.

Nature of Aid Program

Our fieldwork consisted mainly of examining (1) pertinent agreements between the Government of the United States and El Salvador; (2) correspondence and documents relative to the administration of the projects; and (3) internal audit reports of AID. We also inspected certain health project facilities and supplies and equipment and discussed the projects with appropriate U.S. and host country officials.

Mr. Wild is a supervisory auditor in the International Division and has been with GAO since 1956. He is a graduate of Rider College in Trenton, N.J., where he received his bachelor's degree. Mr. Wild is a Certified Public Accountant in the State of New Jersey where he was engaged in public accounting before coming to the GAO.



The United States has been providing financial and technical assistance to health projects in El Salvador since 1942. The Cooperative Health Service was established then as an autonomous operating organization to serve as an administrative device for carrying out health projects jointly funded by the United States and El Salvador. The projects carried out by the Cooperative Health Service were in such areas as health education, rural sanitation, construction of rural water supplies, development of facilities for nursing education, and construction of health centers.

Beginning in fiscal year 1963, AID started to channel its assistance through various branches of El Salvador's Ministry of Public Health. Between fiscal years 1963 and 1966, the United States provided \$2.1 million in health program assistance, mostly for the following projects:

- Malaria eradication.
- Nursing education.
- Construction and equipping of permanent health units and posts in rural communities.
- A mobile rural health project.
- A civic action medical clinic project for rural areas, participated in also by the Department of Defense.

The emphasis on health assistance in rural areas is not surprising; two-thirds of El Salvador's population is rural.

Results of Review

In February 1967 we reported our findings on these five projects to both the Administrator of the Agency for International Development and the Secretary of Defense. No significant

management weaknesses were noted as to the malaria eradication and nursing education projects. The construction of health units and posts had not started at the time our work was completed. However, serious problems, attributable primarily to poor planning, persisted in the remaining two projects.

The purpose of the mobile rural health project was to create an immediate, wide-range impact to gain interim support for the slower, long-range economic goals of the Alliance for Progress. The project was to accomplish this by providing basic medical care and health services to the rural population of El Salvador. Initiated in December 1962, the project was to be in full operation by June 1963. It wasn't.

Up until fiscal year 1965, AID had a team of six advisers in Central America, one each in the fields of medicine, nursing, health education, field support, sanitation, and community development, to assist in implementing mobile rural health projects. The team was to cover the entire area. As a consequence, it spent a considerable amount of its time traveling between countries and was unable to render full-time advice in any one country.

In El Salvador, AID personnel, such as the executive officer and the controller, were responsible for the project at various times during the first 18 months of its operation. This absence of properly qualified full-time personnel resulted, among other things, in extremely poor planning. For example, mobile units were set up and ready to go into the rural areas

except for one important ingredient—medical supplies.

As a consequence, implementation of the project was delayed a year and much of the immediate and favorable impact it could have achieved for the Alliance for Progress was lost. Certain U.S.-financed commodities or equipment were also ineffectively utilized. For example, all the ambulances were in the city of San Salvador rather than in the rural areas for which they were intended.

The civic action medical clinic project was funded with U.S. assistance of about \$300,000 under both the U.S. economic and the military assistance programs. Under the economic assistance program, AID provided medicines and drugs and, under the military assistance program, the Department of Defense provided ambulances, medical equipment and supplies, and training to an El Salvador Army Medical Company which was responsible for the operation of the project.

Poor planning again typified this undertaking, since the major impediment to the project's success was a shortage of doctors. This could have been foreseen by U.S. officials at the time the project was being planned. Failure to do so, and thus to implement this project, resulted in the ineffective use of most of the \$300,000 worth of U.S.-financed equipment, supplies, and services which our Government provided.

Adherence to Department of Defense and the Agency for International Development policy guidelines for project planning would have precluded these deficiencies. We therefore recommended in our report that steps

be taken to reemphasize to operating personnel the need to ensure that U.S. funds not be obligated for projects until adequate financial, management, and technical resources necessary to operate them are available. Both the Agency for International Development and the Department of Defense concurred and advised that appropriate corrective action had been initiated. The effectiveness of these actions will probably be followed up at a later date.

Personal Aspects of the Assignment

El Salvador is the smallest of all the Latin American republics and lies in Central America between Guatemala and Honduras. The country is about the size of Massachusetts and is the most densely populated in the Western Hemisphere. Almost all the populace are a fusion of Spanish and Indian parentage.

During our review we were headquartered in San Salvador, the capital, with a population of about 300,000 people. San Salvador is what one would expect to find in this part of the world; it is rambling and provincial with low buildings in deference to the earthquakes which occur from time to time and which have destroyed the city sufficiently often to have obliterated most of the old colonial flavor. Parts of the city are quite modern and have the type of modern houses seen in southwestern United States.

Working in a small country like El Salvador has the distinct advantage of permitting one to visit nearly all parts of the country within a few hours from the capital. On this assignment it was possible to make all

our field trips on a day-by-day basis, returning each night. Since we were staying at a hotel that is considered to be the best in Central America, this made our assignment quite pleasant.

The hotel, located at the foot of an extinct volcano, has all the attributes of a luxury hotel—a swimming pool with an abundance of bikinis, a miniature golf course, air-conditioned rooms with balconies lending a spectacular view of both the city and the volcano, and an exquisite restaurant and nightclub with top-flight food and entertainment.

Easily reached from the city is Lake Ilopango. This beautiful lake, of volcanic origin, is a favorite resort for the people of San Salvador. I was fortunate to spend a few weekends at a country club, located at the lake, which had an impressive clubhouse, an 18-hole golf course, a large swimming pool, a restaurant and bar, and tennis courts. On the lake shore are a picnic area, bathhouse, pier, and beach. Motor boating, small boat sailing, and water skiing are also available.

The American colony in El Salvador held its Independence Day celebration ceremonies at the lake. This

was an all-day affair and most impressive. Being in a foreign country makes one listen more intently to Independence Day speeches, watch the color guard with emotions, and just be downright proud to be an American. Believe me, it's an emotion you have to experience to appreciate.

During our fieldwork, we made trips into the rural areas and were able to see firsthand how people in these remote areas live. In just a few hours drive from the modern capital city, we saw villagers in colorful native dress, pyramids which dated back to the sixth century A.D. scattered among sugarcane fields, and an inactive volcano.

One of our staff members had the opportunity to attend the inauguration of a public sanitation facility in a local village which was financed with funds donated by the United States. The inauguration ceremony, consisting of speeches by local officials, the raising of the American and the Salvadoran flags, and the presentation of certificates to those who worked on the project, concluded with a ribbon-cutting ceremony, with GAO doing the honors.

National Association of Accountants Conference Report

Denver, Colo., hosted the 48th annual conference of the National Association of Accountants, June 25 to 28, 1967, which provided an outstanding technical program coupled with social activities marked by genuine western hospitality. More than 1,400 members attended the conference.

The National Association of Accountants is an organization of over 61,000 men and women representing a wide variety of occupations in nearly every field of economic endeavor. The association is an educational organization devoted to the service of its members who are interested in the problems of accounting and related aspects of business management.

The following four GAO staff members attended the conference in Denver:

- A. T. Samuelson, director, Civil Division.
- Max Neuwirth, assistant director, Civil Division.
- Jack L. Mertz, assistant to the director, Civil Division.
- Donald M. Mutzabaugh, assistant to the director, Civil Division.

The 1967 conference program was of special interest to GAO accountants and auditors because the topics covered a wide range of subjects which concern today's accounting profession—from management controls in government, management information systems, and line-of-business report-

ing to flexible budgets. Comments on specific sessions follow.

Management Controls When There Is no Profit Motive

Presiding: Robert I. Dickey, professor of accounting, University of Illinois.

Speaker: Robert N. Anthony, Assistant Secretary of Defense.

Mr. Anthony discussed the past, current, and future problems of financial control in the Department of Defense and what has been and is being done to meet them. He compared the structuring of the Defense Department budget in World War II, the Korean war, and the present Vietnam conflict, noting that the Korean war budgets were so overstated that as late as 1955 the Defense Department continued to be financed in part by funds appropriated under these budgets. For the Vietnam conflict, however, provisions in budgets through 1967 were not made for the uncertainties associated with the continuance of the war. As a result, the public, Members of the Congress, and the press accused the Department of Defense of a \$10 billion "goof" when a large supplemental appropriation request became necessary because of the escalation of the war effort. Mr. Anthony then described the basis of the 1968 budget which he said contemplated the continuance of the Vietnam conflict for periods of 2 and 3 years.

Mr. Anthony compared industry with Government by citing the semi-automatic warning system and the yardstick in industry served by the profit system and the profit motive. In Government, he said, no danger signal flashes of the kind that exists in industry when profits go down, and no yardstick comparable to profit exists in Government. He said that, ironically, Government needs a better management control system than does industry—one that measures and signals deterioration in efficiency, effectiveness, and economy.

Mr. Anthony noted the potential of extending the competitive environment to Government through, for example, the creation of service centers, the quantification of operations, and the comparison of unit costs between centers—equating the effectiveness of the center managers. He added, however, that Government has a long way to go to develop effective control mechanisms and an even longer way to go to develop managers who can and will use financial data in managing their operations.

Mergers and Acquisitions

Presiding: Bertram J. Belda, partner, Ernst & Ernst, Cleveland.

Speaker: Robert E. Healy, partner, Price, Waterhouse & Co., New York.

Mr. Healy, who is in charge of acquisition and merger activities in his firm, stressed the planning and investigation essential to a successful acquisition program and described the effective participation therein by financial managers and accountants. He noted the painstaking detail of the review in every aspect of a company's operations, which is required to reach

useful evaluations for the decision makers on acquisitions or mergers. He warned that companies that are rich in assets but are selling below real value and have limited management ownership are likely targets for takeovers and should therefore develop their own acquisition programs or be prepared to promptly consider compatible upstream merger partners. He also discussed the methods by which companies can avoid takeover bids, frustrate corporate raiders, and defend themselves when cash tender offers are made.

Corporate Financial Reporting: The Developing Debate on Line of Business Disclosure

Presiding: Dr. Morton Backer, professor of accounting, University of Massachusetts.

Speakers: Monte J. Gordon, Bache & Co., New York; Andrew Barr, Securities and Exchange Commission, Washington; Robert J. Brockmann, Wallace & Tiernan, Inc., East Orange, N.J.; and Dudley E. Browne, Lockheed Aircraft Corp., Burbank, Calif.

Mr. Gordon presented the investment analysts' viewpoint by discussing the need for line-of-business information in making investment decisions. He noted the very heavy reliance that is placed by the analysts on public information that permits the analyst to perceive trends. He said that the appearance of conglomerates has highlighted the problem of the analyst but that the need for product-line reporting extends to many corporations that have diversified product lines but are not normally considered as conglomerates.

Mr. Barr discussed criteria for line-of-business reporting. He stated that, while the Commission favored voluntary and evolutionary development of criteria, it has a study underway of the reporting practices of conglomerates and companies with diversified operations which may lead to the issuance of regulations by the Commission. He said that the Commission has prepared an exposure draft on criteria which is expected to be submitted to the Financial Executives Institute and other organizations for comment before proceeding to develop new regulations.

Mr. Brockmann discussed the research and soul searching that preceded the decision of his company—a conglomerate having chemicals, industrial equipment, and pharmaceuticals as product lines—to adopt line-of-business reporting.

Mr. Browne discussed some objections to line-of-business reporting. He made a comparison between the present-day effort to ensure the rights of the individuals and the trend to restrict the rights of corporations by the Government. He concluded with an appeal for a corporate bill of rights and a plea to proceed cautiously so that the trade-offs that emerge will truly improve financial disclosure.

Technical Sessions

Technical sessions on seven subjects of significant interest to GAO staff members were held concurrently on the final day of the conference:

- Educational needs for management accountants of the 1980's.
- Developments in management information systems.
- Inventory management.
- Flexible budgets.

Statistical techniques for cost control and variance analysis.

Measuring and reporting pension costs.

Lease or buy decisions.

The sessions on the first two subjects drew the largest groups and apparently stimulated the liveliest discussions. Of particular interest to GAO staff members is the fact that the conclusions of the discussion leaders on educational needs coincide with the philosophy and programs of our Office of Policy and Special Studies—Staff Development.

Educational Needs for Management Accountants of the 1980's

Speakers: Professor Robert K. Mautz, University of Illinois; Elmer G. Beamer, partner, Haskins & Sells, Cleveland; and Robert G. Luckey, Controller, Sandia Corp., Albuquerque.

Professor Mautz centered his discussion around a series of questions. Will accounting continue to be a separate subject in colleges or universities? Will there be a major in accounting? Will accounting continue to be taught and, if so, where will it be taught? He noted that educators have differing viewpoints and philosophies on these questions.

Professor Mautz predicted that accounting education at universities (and perhaps also at the advanced levels in high schools) will shift largely if not entirely to the concepts of accounting so that the graduates will have a broad conceptual knowledge and understanding of accounting theory useful for application in a modern business operation. In this connection he expects that, for teach-

ing purposes, business education and accounting education will be brought together, because accounting is the language of business. Moreover, he believes that management accounting will be emphasized in the accounting education. He concluded that the management accountant of the future would have a university degree with a general business education and a conceptual accounting background.

Professor Mautz further predicted that technical schools will emerge for the training of accounting specialists and for the teaching of specific techniques, including the training of those who want to become certified public accountants. He recognized that this development would result in later graduation, thus shortening the working life of those who follow this course of action.

Mr. Luckey stated that business managements need broad-based individuals to develop and use the tools that help the decision makers. He expressed reservations on lengthening the time for formal education for technical training, stating that technicians rarely have the opportunity to talk to management.

Mr. Luckey discussed various definitions of accounting. He noted that there is a trend in accounting toward conceptual education that would include much more than an education in accounting concepts. He said the business world was looking for re-

cruits with broad college educations, good common sense and, above all, the ability to communicate. Although he believes that the basic education for accounting will not change, he believes that an accountant's education should include a liberal arts program.

Mr. Beamer suggested that more education in mathematics, statistics, and probabilities would be a valuable addition to the education of management accountants. He described the accountant of the future as more of an administrator who would have to understand and motivate people and know how to differentiate the requirements of one task from another in order to manage an organization. He recommended that the profession insist that its prospective members obtain a better knowledge of grammar along with the ability to communicate, because the management accountant must be able to talk—both conversationally, in conducting meetings, and formally.

Mr. Beamer generated a lively discussion on his observation that on-the-job training was on the way out—an observation in which Mr. Luckey seemed to concur. It was their view that it is the job of the university to prepare a man for the business world and the responsibility of business to give the graduate an assignment commensurate with his training—an assignment that will test and challenge him.

American Institute of CPAs—Annual Meeting

Notes

The 80th annual meeting of the American Institute of CPAs was held in Portland, Ore., September 24–27, 1967. As in prior years, several members of the accounting and auditing staff from the Washington and regional offices were authorized to attend this meeting because of the direct concern and interest of the General Accounting Office in the work, problems, and future of the public accounting profession.

Of especial interest to GAO staff members is the fact that the Comptroller General addressed the technical session devoted to accounting for the Government. Mr. Staats spoke on "Protecting the Taxpayer's Dollar." His remarks are published in this issue of the *Review* beginning on page 3.

Other speakers for the session on accounting for the Government were Lee C. White, Chairman, Federal Power Commission, and James F. Kelly, Assistant Secretary, Comptroller, Department of Health, Education, and Welfare. The session was chaired by Karney A. Brasfield, partner of Touche, Ross, Bailey & Smart. Two other members on the panel were Herman W. Bevis, senior partner of Price Waterhouse & Co. and William Freitag of Peat, Marwick, Mitchell & Co.

One Regulator's View of the Accounting Profession

Mr. White emphasized the role that the public accounting profession can

play in the regulatory process. He stated:

In the Federal Power Commission we have an excellent example of the constructive role which can be played by the accounting profession in the work of regulatory agencies. Prior to 1962, our rate examiners, auditors, and engineers frequently spent many months examining accounts and records of companies involved in rate cases under the Natural Gas Act. In 1962, however, as a part of revised procedures to expedite rate cases, we required companies to submit an opinion by an independent public accountant on specific aspects of the submitted data. This procedure was worked out in a series of meetings between our staff, industry representatives, and the independent public accountants. * * *

Our performance will be more effective and the public will be better served if we have the required data available on a firm, fair and consistent basis and if we can use our limited resources in constructive rather than duplicative effort.

* * * Under the new procedure, our rate accountants and engineers have relied on the work of the independent accountants so that if a field examination is required, it covers specific matters of special interest to ratemakers rather than the entire range of data presented. I am glad to report that the new procedures have worked very well and have significantly contributed to more efficient regulatory operations by our agency.

Another illustration of assistance the accounting profession can render regulatory agencies can be found in a proposed rulemaking recently issued by the Federal Power Commission. The proposed rulemaking sets forth a tentative requirement for each company subject to the Commission's jurisdiction to submit, together with its annual report to the Commission, an attesta-

tion by independent certified public accountants to the effect that the company has complied, in all material respects, with the requirements of the Federal Power Commission's Uniform System of Accounts.

The Government's Growing Reliance on CPAs

Mr. Kelly of the Department of Health, Education, and Welfare stated that:

There is probably no other program that relies as much as Medicare on the independent public accountant for the verification of costs. In order to promote effective and economical administration, we adopted audit policies to authorize the use of the existing audit arrangements of the intermediaries for the audit of costs claimed by the more than 10,000 providers of service participating in the program. As a result, the intermediaries have entered into about 100 subcontracts for audit work with 65 individual, independent CPA firms. Based on the estimated audit cost represented by these contracts HEW will spend approximately \$16 million for audit services in 1968 for the Medicare program alone.

Mr. Kelly also suggested some ways in which the public accounting profession could extend its efforts to improve the conduct of Government programs and strengthen important institutions in our society. He stated:

The responsibility for safeguarding the use of Federal funds should not, and of course does not, belong to the Federal Government alone. Recipients of Federal funds such as State and local governments and other private and nonprofit organizations must also concern themselves with proper management and accounting for this stewardship. The success of the Federal Government's efforts depends to a very large extent upon the management abilities of the fund recipients. Since most of our programs are administered by non-Federal organizations, we are very much dependent upon them. Since they often turn to CPAs for accounting and auditing services, we are also dependent upon you.

Our responsibility, yours and mine, is to assist recipients of Federal funds in strengthening their capabilities for good financial management. Accounting systems in States, localities, colleges, and universities run the gamut from the most sophisticated automated business type systems with effective cost accounting and cost finding capabilities to the most rudimentary systems of fund accounting. To date little has been done to promote more effective financial management, particularly at the State level. The establishment of Federal requirements has given little consideration to the needs of the grantee institutions or to their capability to meet the requirements without the establishment of otherwise unneeded special arrangements. Federal requirements have been established by different agencies and different programs with little or no consideration of each other's approach and demands. It would not be wise to try to impose a single system of accounting, reporting, or cost finding. However, it would be worthwhile to develop acceptable principles, alternative approaches to various aspects of the problem, and some model systems which could be applied by those seeking improved management. At the same time, we should review Federal requirements with a view to making them byproducts of an adequate management system, achieving as much uniformity as possible, and, in general, reducing the burden of Federal reporting requirements.

Doing this will require innovation from all parties. The traditional audit reports submitted to regulatory agencies and other Federal departments will not meet the need for strengthening institutions receiving grants and contracts from HEW. Consequently, it is not enough to report and comment on historical transactions. It is not enough to make recommendations that affect only the past. Auditors will always have a responsibility for reporting amounts which have been illegally or imprudently spent. But audit reports will have to go far beyond that if they are to play a role in fostering better management. Consequently, audits should be made with a view not only in reporting the past, but helping to make a better future. The reports should include specific recommendations as to the steps that need to be

taken to strengthen the institutions' financial management controls. Emphasis must be placed on the management system not merely on a particular event in its past operation.

This sort of thing is not completely new to the public accounting profession. However, this type of service is usually undertaken as a special audit engagement under the heading of "management services." I suggest that recommendations to strengthen institutions should be part of the normal or regular audit engagement for those clients involved with Federal grant programs. This would be a fairly new role for the independent accountant.

The Measurement Challenge Facing Accountants

Mr. Robert V. Hansberger, president of the Boise Cascade Corp., presented the attending accountants with perhaps the most provocative of the numerous challenges made during the meeting. His speech on September 26, which bore the label "Creativity in the Profit Center and Beyond," underscored the need for "new yardsticks, new evaluation systems, new accounting techniques" for measuring the consequences of decisions involving non-material objectives.

Passages of special interest to GAO staff members which bear on this theme are quoted below:

There is another new challenge for accountants being provided by social change. This has been, and indeed it still is, a materialistic world. Through the ages man contended against a materialistic environment with a scarcity of tools. Efficiency of choice and accuracy of choice were, therefore, critically important. Man could ill afford wasteful mistakes. But the alternatives cast up by a prolific technology began to enormously complicate his choices. Fortunately, a convenient yardstick was available with which to evaluate choice. Since man's greatest needs seemed to be material, his principal choices were among material alternatives.

His yardstick became money, or its equivalent.

These choices then became relatively simple and existed within fixed environmental limits. Money became the all-important common denominator of choice. More than the mere distinction between success or failure, it provided a measure of the *degree* of either. And so man's material values came to be measured with a fairly high degree of precision. Man devised accounting systems to tell him his costs, both fixed and variable; to determine return on investment, gross and net margins, return on sales, and growth or shrinkage of capital; to help evaluate risks; and to recognize distinctions in quality and scarcity. Today these choices can be analyzed by computers, and the best of many alternatives can be selected in seconds. In a world and in a country of increasingly scarce resources, these techniques have performed extremely well. They have minimized waste and duplication. And they have helped assign priorities in their proper order.

In addition, they have provided the basis for much of man's motivation. When there is material scarcity, then material things motivate. Our accounting systems measure degrees of value added, and thereby supply the basis for individual and collective rewards—all in dollar values, of course. Our economic reward system embraces increased investment values, increases in salaries and wages, bonuses, stock options, and countless fringe benefits. If there are other kinds of rewards involved, they seem to be either well concealed and overshadowed by the dollar value rewards, or ignored if they can't be measured in dollar values. Our unique standard of living in the United States, achieved in the amazingly short period of less than two centuries, is clear testament to the effectiveness of materialistic measuring and control devices in an environment of material scarcity.

* * * * *

With our machines we have obviously made great strides toward winning the contest with our environment. Now our people are suddenly deluged with new choices. Not choices where the final judge is an unfor- giving Nature. Not choices where the answers are determined by standard account-

ing practices. But choices for which we have no simple measuring system. Our world has suddenly and dramatically exploded into a supermarket of choices.

Now a higher standard of living fosters competition among a horde of new alternatives such as travel, recreation, higher education, political service, the Peace Corps, science and many many others. There is no present accounting system designed to value the consequences of the decisions we make among these things; nor will environment, as it did in the days of scarcity, eventually provide the proper answer.

Often the investment or input values of the new choices can be measured by our old dollar value standards, but we have no yardsticks with which to measure the returns or output. Yet we need these yardsticks, and need them badly. The dollars we allocate to the "Race to the Moon" are dollars we cannot spend on our Poverty Program. The money and food we ship to poverty stricken nations to alleviate suffering and starvation are values unavailable for our own poor. Is America rich enough to do all these things? Far, far from it. The fact that we can wrestle from Nature all of our basic needs with less than all of our time and effort does not mean that we can also feed all of the world. Nor can we freely allocate between material and nonmaterial alternatives. We are still dealing with scarce resources.

* * * * *

We need new systems for evaluation of the important intangibles that do not yield to dollar measurements. Certainly one of the great byproducts of our American system of competitive free enterprise has been its elaborate and precise accounting system which quickly quantifies results fast enough for decision adjustments. But what do we use when choices must be made among alternatives which commit huge quantities of dollars, but for which the results cannot be measured by dollars? Where is the accountant in this world of allocation? How do we evaluate the results of \$25 billion per year spent to defend a principle in Vietnam? We make huge and increasing commitments in dollars to help the aged. The Peace Corps and the poverty programs absorb big slices of our productivity. Now,

how do we relate their results to the economic benefits of a new dam?

The yardsticks of the accountant, the yardsticks he has so carefully taught the economist, the educators, and the politicians to use, no longer have complete relevance here. In fact, they have less every day. Many nonbusiness sectors of society have only just now begun to understand and accept the equations of value which have been so successful in business. Now we find them woefully inadequate to measure nonmaterial things—things which must be fueled with material resources. We face the paradox that business techniques may have obsoleted themselves by their very efficiency. They have faced environment on every front and met the test. Moreover, they have pushed it back and enriched our choices. But, we now need new yardsticks, new evaluation systems, new accounting techniques. Whether business, with its vast experience with the integration of specialties into systematic decisions, can incorporate into its techniques the new alternatives of choice it has provided is one of the great challenges of our time. The success or failure of free enterprise as a worthwhile institution in the future may depend on how successful we are in quantifying and qualifying these many new choices.

* * * * *

Clearly we cannot finance unlimited costs for all of these alternatives (problems of the cities, pollution, poverty, education, and leisure time) and the new ones of the future. Therefore, we must choose. Profit and loss techniques of today will not provide us with the answers.

The *principle* of cost and result can, however, and nowhere in our society is there a better experience in dealing with cause and effect than in the business sector and the accounting profession. To deal objectively with these new alternatives the businessman, including accountants of tomorrow, must enlarge his spectrum of values. He must think in terms of a new type of accounting that effectively embraces the new, intangible aspirations of his society.

Perhaps accounting periods must be lengthened—if not in annual reports, at least in our own thinking. Certainly we must recognize new human values not di-

rectly convertible into dollars: time, emotion, quality of life or living, creativity, and intellect. Government recognizes and is struggling with these problems we have been discussing. And time after time it is reaching out for help to the experience of the business community—an experience with systems and integrated solutions to complex problems, experience with balanced judgments involving cost relationships between commitment and consequence.

This is an exciting new challenge to businessmen and particularly to the new measurement experts of business—the accountants.

Thinking About Future Social Development

Joseph M. Goldsen of the Rand Corp., beamed a number of observations and suggestions on this subject at the accounting profession. For example:

In social development, “costs” and “benefits” are not adequately measured by such manageable criteria or dollars or units of output.

Many of our major national and local efforts proceed, in great earnestness and sincerity, knowing neither what the programs are expected to accomplish * * * nor how to evaluate the consequences in order to modify programs, or goals, or both.

Social audits and social accounting are visible needs and in principle represent con-

cepts analogous to your own professional auditing functions.

As citizens and responsible policy advisors, don't sit on your status quo by leaving social development to those whose job description so prescribes. Don't just moan and groan about those bureaucrats, those professors, those politicians. Their problems are yours, and more yours than the mass population's.

I should think that you could accumulate the resources to analyze in detail your city's problems and develop combined public-private programs which would pay off in more ways than one.

Some of you in this professional society might right now form a Committee on Social Development—not just a discussion body but a serious working group, teamed up with carefully chosen professional research staffs, to compete with public planning groups in the search for better futures.

For members of the financial accounting community to participate in a serious effort at social accounting would put yourselves into the business of acting constructively on the future instead of nervously trying to anticipate and to adjust to a world you never made.

Mr. Goldsen's address is printed in full in the Congressional Record for October 12, 1967 (p. S14740).

State of Federal Accounting

On October 4, 1967, the Wall Street Journal published an editorial labeled "No-Account Federal Accounting" which attracted considerable attention on the part of individual Members of Congress and private citizens. While the facts cited in the editorial were correct, it did not correctly reflect the level of improvement activity now going on in the Federal agencies. For this reason, the Comptroller General sent a letter on November 15 to the editor of the Journal in explanation of current efforts to improve Federal accounting.

The text of the editorial and of the Comptroller General's letter, a portion of which was printed in the Journal for November 27, follow:

FROM WALL STREET JOURNAL OCTOBER 4, 1967

No-Account Federal Accounting

Eleven years ago Congress took a look at all the money the Government was spending, and at the antiquated, helter-skelter accounting systems most Federal agencies were using. Alarmed by what it saw, it amended the Budget and Accounting Act to require the agencies to adopt up-to-date, cost accounting systems.

At the time, in 1956, annual Federal expenditures totaled about \$66 billion and the public debt stood at \$273 billion. This fiscal year, spending is expected to reach about \$143 billion and the debt may exceed \$335 billion.

However, of the 173 Federal agencies subject to the law requiring them to set up Government (sic) Accounting Office-approved, modernized accounting systems, only 61 have complied. And most of those are small agencies with small budgets.

The big agencies are still dragging their feet, for the most part using what are called obligation accounting systems. These show the amount of

money agencies are authorized to spend, but fail to show the actual costs of particular programs or operations.

Properly designed cost accrual accounting systems, on the other hand, provide not only better control over funds but also up-to-date cost data on operations. They help to determine whether money is being spent wisely and used efficiently, and whether results justify the costs. Adequate cost accounting systems, says the U.S. Comptroller General, are "basic and fundamental to the whole operation of the Federal Government."

If that is so, perhaps it helps to explain some of the deficiencies evident in Federal agency operations. The Health, Education, and Welfare Department, for instance, has 12 accounting systems subject to GAO approval; the number so far approved is zero. HEW has been found, by GAO, to be guilty during fiscal 1966 of inefficient recordkeeping and property management.

The Agriculture Department has 15

accounting systems subject to approval; only five have been approved. Interior has 17 systems with six so far approved. And Treasury, which surely ought to be setting an example, has only four approved systems out of 18.

Rep. Jackson Betts of Ohio is lead-

ing a move in the House to compel all agencies to speed up the accounting reforms they were obligated by law to adopt 11 years ago. Since no-account Federal accounting tends to breed no-account Federal programs, that move deserves full Congressional support.

COMPTROLLER GENERAL'S LETTER TO EDITOR

Your editorial of October 4, 1967, on "No-Account Federal Accounting" has attracted widespread attention. We are aware of the interest that this editorial created from calls we have received from Members of Congress for further information and from letters forwarded to us for our attention. We perforce agree with your interest and concern.

The statistics noted in the editorial apparently originated in data we furnished the subcommittee of the House Committee on Government Operations during hearings held in July 1967. As far as they go, these statistics present accurately the number of systems subject to our approval and those which we have approved. Cold, hard statistics, however, are not really the measure of the status of Federal accounting nor do they give an accurate indication of the intense activity now going on to improve accounting and the progress being made toward meeting our required standards.

It is my opinion that there is more interest being shown by Federal agencies and more effort being exerted to improve their accounting and financial management systems than has been evident for many years. The energy being displayed and the efforts being made to improve the accounting situation in the Federal Government are very encouraging to me and all

others concerned about the lack of progress over the years. This outburst of energy to bring about improvements in the Government's financial management can be attributed to several sources. The Congress itself has displayed a deep and continuing interest in this subject, as evidenced by the series of hearings held by subcommittees of the House Committee on Government Operations beginning in July 1964, continuing in September 1966, and the last one in July 1967.

The President himself has also expressed concern about the accounting problem in the Government and on May 24, 1966, he issued a memorandum to the heads of departments and agencies indicating his strong and continuing interest in the development of businesslike financial systems throughout the Federal Government.

On assuming the position of Comptroller General in March 1966, I devoted much time and attention to the status of accounting in the Federal Government and, among other things, I have increased the staff efforts of the General Accounting Office in this field by severalfold.

All of these efforts now seem to be bearing fruit. Some agencies which several years ago were considered to be hopeless laggards in accounting improvement efforts have now become leaders. On the whole, the picture is

very encouraging. The latest information we have shows that practically all agencies will have their accounting systems developed to the point where they can present them to us for approval within 2 years. This includes the three agencies named in your editorial. It includes even the Department of Defense, which has tremendous problems but is also exerting tremendous efforts to modernize its accounting.

One important reason today for not being able to reach desired goals sooner is the shortage of qualified personnel. The efforts of the Civil Service Commission have been enlisted under the Joint Financial Management Improvement Program being conducted by the Treasury Department, Bureau of the Budget, and General Accounting Office, to provide more training in this critical field and facilitate recruitment from outside the Government of people who can contribute in this area. Consultant firms have been employed by several agencies to give expert assistance. In short, we are leaving no stone unturned to speed the development and installation of systems which can be approved by our Office.

Your editorial mentioned a bill introduced by Rep. Jackson E. Betts (R) of Ohio, for the purpose of imposing restrictions on agencies that do not have approved accounting systems. We are in hearty accord with Mr. Betts' objectives but we have some strong reservations concerning some of the methods he proposes. During the hearings on accounting systems in September 1966, the chairman of the subcommittee requested us to consider what sanctions might be imposed

on laggard agencies. We considered various alternatives and eventually proposed a reporting system similar to the one that Mr. Betts proposes in his bill. We did not feel that further restrictions on agency operations would be appropriate. With the very evident interest being displayed by agency managers in improving their accounting systems and the momentum that has now been achieved, we believe that imposition of any sanctions at this time might be counterproductive rather than otherwise. It is my view that consideration of new legislation on the subject should be held in abeyance until a further review of the situation can be made, possibly sometime during the coming year. Then, if necessary, a further study should be made as to the appropriate means of assuring that adequate attention is given to this important matter.

Another recent development is the issuance by the President's Commission on Budget Concepts of its report that includes a recommendation that budget expenditures and receipts be reported on an accrual basis instead of the present cash basis. The Commission concludes that this can be done for expenditures and for most income taxes and certain other receipts beginning with the President's budget for fiscal year 1971. If this recommendation is adopted, and I believe that there is great probability that it will be, it will have a tremendous effect on accelerating improvements in Federal Government accounting.

Sincerely yours,

(S) ELMER B. STAATS,
*Comptroller General
of the United States.*

Budget and Accounting Act, 1921

Of special historic interest to GAO staff members is the Budget and Accounting Act, 1921, which created the General Accounting Office as an agency independent of the executive branch of the Federal Government. The same act established the Bureau of the Budget, to be located in the Treasury Department.

Some Legislative History

The bill which ultimately became the Budget and Accounting Act, 1921, was originally introduced in the House of Representatives in October 1919 (66th Congress). It had been prepared by the Select Committee on the Budget, a House committee which had been appointed to study the budget system of the Federal Government. The committee, chaired by Representative James W. Good of Iowa, held hearings in September and October 1919 and took testimony from numerous authorities in the field of Government finance, legislators, and others.

The House passed the bill on October 21, 1919, and the Senate passed its version on May 1, 1920. President Wilson, however, vetoed the act because of the provision preventing the removal of the Comptroller General and the Assistant Comptroller General for any cause except by impeachment or concurrent resolution of the Congress. The President took the position that this restriction was unconstitutional since the power to appoint officers of the Government carried with it the power to remove them.

New bills to provide a national budget system and an independent audit of Government accounts were introduced in the next Congress, the 67th, in April 1921. The Senate bill received very speedy action. It was introduced, referred for committee action, reported, considered, amended, and passed all within 2 days' time. The House bill was considered and passed early in May. On June 10, 1921, the act became law when it was signed by President Harding who did not question the provisions concerning removal of the Comptroller General.

Birth of the General Accounting Office

The *Review* is indebted to *Margaret L. Macfarlane*, Chief, Legislative Reference Services, Office of the General Counsel, for the following account of the birth of the General Accounting Office in 1921, the appointment of its first leaders, and some of the competing news events of that year.

During the first 10 days of June 1921, the enrolled enactment S. 1084, 67th Congress, a bill to become the Budget and Accounting Act, 1921, and to establish the General Accounting Office under the direction of a Comptroller General of the United States, lay on President Harding's desk for his approval. A year earlier a similar bill had passed the legislative hurdles but had been vetoed by President Wilson not because he was not in sympathy with the objects of the bill but because he believed that the provision for removal of the Comptroller General and Assistant Comptroller by concurrent resolution of the Congress was unconstitutional and in violation of the

CHIEF CLERK
 JUN 10 1921
 DEPARTMENT OF STATE

BUREAU OF ROUTE & CLERK
 JUN 30 1921
 DEPARTMENT OF STATE

Sixty-seventh Congress of the United States of America,

At the First Session,

Began and held at the City of Washington on Monday, the eleventh day of April, one thousand nine hundred and twenty-one.

AN ACT

To provide a national budget system and an independent audit of Government accounts, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

TITLE I -- DEFINITIONS

SECTION 1. This Act may be cited as the "Budget and Accounting Act, 1921."

TITLE III. -- GENERAL ACCOUNTING OFFICE.

SEC. 301. There is created an establishment of the Government to be known as the General Accounting Office, which shall be independent of the executive departments and under the control and direction of the Comptroller General of the United States. The offices of Comptroller of the Treasury and Assistant Comptroller of the Treasury are abolished, to take effect July 1, 1921. All other officers and employees of the office of the Comptroller of the Treasury shall become officers and employees in the General Accounting Office at their grades and salaries on July 1, 1921, and all books, records, documents, papers, furniture, office equipment and other property of the office of the Comptroller of the Treasury shall become the property of the General Accounting Office. The Comptroller General is authorized to adopt a seal for the General Accounting Office.

SEC. 302. There shall be in the General Accounting Office a Comptroller General of the United States and an Assistant Comptroller General of the United States, who shall be appointed by the President with the advice and consent of the Senate, and shall receive salaries of \$10,000 and \$7,500 a year, respectively. The Assistant Comptroller General shall perform such duties as may be assigned to him by the Comptroller General, and during the absence or incapacity of the Comptroller General, or during a vacancy in that office, shall act as Comptroller General.

SEC. 303. Except as hereinafter provided in this section, the Comptroller General and the Assistant Comptroller General shall hold office for fifteen years. The Comptroller General shall not be eligible for reappointment. The

SEC. 318. This Act shall take effect upon its approval by the President: Provided, That sections 301 to 317, inclusive, relating to the General Accounting Office and the Bureau of Accounts, shall take effect July 1, 1921.

J. A. Sullist

Speaker of the House of Representatives.

Charles McNary

Vice President of the United States and President of the Senate.

Approved

June 10, 1921,

Warren G. Harding

President's power of appointment and removal.

President Harding was perturbed that the new session of Congress convened to carry out the President's campaign promises on taxation and the tariff had not gotten down to business on these matters. The President was still in the process of making initial appointments to executive positions. On June 6, he named Albert D. Lasker to be Chairman of the U.S. Shipping Board, Mr. T. L. Dangan to be the purchasing agent for the Post Office Department and Mr. Adolph A. Hochling, a prominent Washington attorney, to be an Associate Justice of the Supreme Court replacing Justice Ashley M. Gould recently deceased.

Throughout the Government service there was great anxiety and apprehension about the plans for reduction in Government personnel. Newspapers carried the headlines, "Many Ex Service Men Will Face Dismissal" because of failure of Congress to provide compensation beyond June 30, "New Fiscal Year to Bring Anxiety—Demand for Economy from People Means Reduced Personnel July 1," "War Department Will Dismiss 1,938 Because of Reduced Appropriations." Inasmuch as the bill on the President's desk would abolish the position of Comptroller of the Treasury held by Mr. Walter Warwick since 1915 and the six auditor positions, there was apprehension among the employees in the Treasury Department too.

On June 4, 1921, Will P. Kennedy, in one of a series of articles on Government reorganization, discussed the accounting features of the new proposal which was awaiting the President's signature. He stated that the

"Comptroller-Auditor General Independent Office Proposed Would Take Over Duties of Comptroller of Treasury, Six Auditors, Bookkeeping and Warrants Division.

"The organization of the proposed Office of Comptroller and Auditor General suggested by the Comptroller of the Treasury in his annual report of 1920 is quoted. Briefly it provides (1) a legal department; (2) an auditing department; (3) a bookkeeping department; and (4) an inspection department. This position of the Con-

troller was endorsed by Secretary Carter Glass in his annual report.

"The third of the changes in the handling of the accounting operations of the Government in addition to that of setting up an independent office of comptroller and auditor general, mentioned as essential in putting this important branch of public administration upon a proper basis, is that of making this office responsible for keeping the general accounts of the Government and of rendering the reports showing the financial condition and operations of the Government.

"Emphasis is laid upon the duty defined in the budget measure of the comptroller general to give information to Congress and aid it in taking those steps that will be necessary to make the administration of the financial affairs of the Government more efficient.

"Under this new system, Congress will automatically get much of the data it has sought through investigating committees. When special information is desired it can be readily furnished at a minimum expense and trouble by the comptroller's office. The new Committee on Appropriations will always have at its right hand an officer possessed of full knowledge of governmental conditions and practices and independent of all party, administrative or Congressional pressure, to aid it in performing its important duty of passing upon the estimates of expenditure needs as contained in the President's budget."

The national and international crises in those first days of June 1921 with which the new Harding cabinet was concerned included the demands for the removal of outspoken Gen. Billy Mitchell, the refusal of Mexico's Obregon to sign the U.S. treaty for recognition, the proper disciplinary action to take against Rear Admiral Sims for a speech made in London against the Irish and the amount of Government aid to meet the flood disaster situation in Colorado.

On the day prior to the day the President signed S. 1084 to establish the General Accounting Office, the Secretary of the Navy saved the C and O Canal by placing an order for coal to be shipped to the proving grounds at Indian Head via the Canal thereby continuing the Government's sup-

port of the ancient waterway. On the same day a pageant on enfranchisement for the District of Columbia—a vision of the future—was presented before the Members of Congress.

June 10, 1921—this significant day for the GAO—was a Friday, a fair and warm day with high temperature of 81 degrees predicted. If there was a signing ceremony around the President's desk as we know them today, there was no mention of it in the news. However, coincident with the signing, the Chairman of the Appropriations Committee, House of Representatives, Mr. James W. Good of Iowa, who had led the fight for the adoption of the national budget system as proposed in S. 1084 and who was a veteran of 12 years in the Congress, announced his resignation from the Congress to practice law in Chicago.

The afternoon of the day our act was signed, Mrs. Harding and Mrs. Calvin Coolidge, wife of the Vice President, were entertained by Mrs. Edwin Denby, wife of the Secretary of the Navy on a short cruise down the Potomac. The news also carried the item that the court had refused Peggy Hopkins money to investigate her husband Stanley Joyce's conduct in connection with a suit against him for \$100,000 a year alimony.

On the same day, in the sports world, Jack Dempsey who was to fight Carpentier on July 2, became weary of training camp routine and decided to take the day off and motor to Camden, N.J., 60 miles from his camp to bring back his Belgian police dog which was left in the care of the veterinarian. The article hastened to add that all of Jack's sparring mates had headaches because of Jack's paralyzing rabbit punches.

Serialized in the Washington Evening Star was E. Phillips Oppenheim's "The Avenger," a tale of political intrigue and private revenge.

As the signed enrolled enactment went from the White House over to the State Department where the Statutes Section personnel assigned it Public Law No. 13, and paginated it as 42 Stat. 20, President Harding drove to the Chevy Chase Club to play golf.

In the business news of the week a deficit was noted in the financial picture of the

Columbia Graphophone Company and Wall Street announced a sagging tendency in bonds. Georgetown University Law School announced at its graduation ceremonies that in October it would become the largest law school in the city by the inauguration of day classes.

On June 15, 1921, the President announced the annulment of a contract to sell surplus U.S. Army harnesses. The Attorney General held that the contract was illegal because it was in violation of the prohibition against officers and employees participating in such transactions.

Since the new budget and accounting system was to take effect on July 1, the beginning of the new fiscal year, there was speculation as to who would be appointed to fill the four new positions created by the act. On June 20, the Evening Star indicated that officials were worried about the President's delay in naming the officers. The story indicated that

"Many of the employees of the present controller's office are becoming restless to know whether they will be among those whose official heads will be lopped off.

"Controller Warwick is unable to give them any information for the reason his authority ends and as a controller of the United States has not been appointed there is no one with whom he can confer concerning the situation."

Eight days before the beginning of the new fiscal year the President appointed Charles Gates Dawes to be the first Director of the Bureau of the Budget under the authority in section 207 of Public Law No. 13. The day of this appointment, Mr. Berryman depicted in the Star cartoon Uncle Sam offering Mr. Dawes the Budget post with the caption "Here's a Hell and Maria Job Just Suited to You." The selection of Mr. Dawes was pleasing not only to the GOP but to the public as well. From 1898 to 1901 Mr. Dawes had been Comptroller of the Currency in the Treasury Department and had distinguished himself in the military service during World War I.

An announcement that President Harding was going to New Jersey on July 1, to the summer home of Senator Joseph S. Frelinghuysen to spend the Fourth of July holiday served to heighten the anxiety about

whether the President would name appointees for the position of Comptroller General and Assistant Comptroller General prior to his trip. On June 26, there was a headline story about the President's failure to appoint a "Controller General" to the new \$10,000 post. The same day the newspaper announced that the Washington Nats, then under the managership of Ty Cobb and George McBride, would begin a sizzling series with the Yankees on Babe Ruth Day; that Samuel Compers had been reelected head of the AFL; and that all U.S. employees who really wanted to work would be retained.

Finally on June 27, 1921, 3 days before the effective date of the Budget and Accounting Act, 1921, President Harding nominated Mr. J. Raymond McCarl of McCook, Nebraska, as Comptroller General of the United States. Mr. McCarl had been Secretary of the GOP congressional campaign committee during the recent presidential election. Prior to that time Mr. McCarl, who was a graduate of the University of Nebraska Law School, served as secretary to Senator George W. Norris of Nebraska.

On July 1, 1921, the effective date of the new Budget and Accounting Act, 1921, General Pershing was named Chief of Staff and Ex-President J. Howard Taft's ambition of a lifetime was realized when President Harding appointed him Chief Justice of the United States. Also in the news was an item that Lady Churchill died leaving a son Winston Spencer Churchill.

While the Budget Director started his administration with a meeting of over 500

Government officials in the Department of the Interior auditorium where he jumped off the platform in order as he said "to get mentally closer" to his audience and reprimanded Secretary of State Charles Evans Hughes and Secretary of the Treasury Andrew Mellon for their failure to appoint budget officers, the administration of the General Accounting Office began with very little fanfare. The Evening Star reported on July 1, 1921, that

"There was not a hitch in the establishment of the Office of the Comptroller General of the United States which takes the place of the Controller of the Treasury and six departmental auditors. J. R. McCarl as Comptroller General and L. R. Ginn, Assistant Comptroller General, were sworn in before 9 o'clock this morning and when the hour arrived for the formal starting of the governmental business these two officials were at their desks going over the appropriation measures and preparing the papers necessary for a smooth running of the Government's financial machinery. When this work is completed Comptroller McCarl said he would tackle the reorganization of his office and expects to have it completed in about a week."

From this businesslike approach the Comptroller General of the United States and the General Accounting Office under his direction began as the right arm of the Congress in the field of expenditure control to insure that public funds are utilized in accordance with the law.

Court of Appeals Decision on the Hewlett-Packard Case

In the Fall 1966 issue of the *GAO Review*, Robert F. Keller, General Counsel of GAO, discussed this case which involved a dispute over the right of access by GAO auditors to contractor records. Suit was instituted by the Justice Department on behalf of GAO to require Hewlett-Packard Co., the contractor, to make the records available for audit. In his discussion, Mr. Keller reported on the ruling in favor of the Government by the Federal district court in San Francisco in June 1966.

Hewlett-Packard appealed the case and on November 15, 1967, the U.S. Court of Appeals for the Ninth Circuit affirmed the district court's ruling. Because of the importance of this decision to the contract audit work of the General Accounting Office, the court's decision is printed in full in this issue.

UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

No. 21,323

HEWLETT-PACKARD COMPANY, a corporation;
DAVID PACKARD; and WILFRED F. CAVIER, *Appellants*

vs.

UNITED STATES OF AMERICA, *Appellee*.

[November 15, 1967]

Appeal from the United States District Court for the Northern District of California, Southern Division.

Before: CHAMBERS, HAMLEY and HAMLIN, Circuit Judges
HAMLEY, Circuit Judge:

The United States brought this action against Hewlett-Packard Company, a corporation, to enforce the Government's asserted right under 10 U.S.C. § 2313 (b) (1964) to examine certain books and records of the company.¹ Plaintiff sought declaratory and injunctive relief. After defendants filed a responsive pleading the parties stipulated as to the relevant facts and filed cross motions for summary judgment. The district court granted the motion of the United States, denied that of Hewlett-Packard, and entered a judgment substantially as prayed for in the complaint. Hewlett-Packard appeals.

Hewlett-Packard is a manufacturer of electronic test and measurement equipment designed for general use where great precision in measurement is required. During the period from March, 1959 to January, 1961, the United States Department of the Air Force awarded to Hewlett-Packard four negotiated firm fixed-price contracts for equipment. The parties are agreed that, for the purposes of this case, the two contracts referred to below may be regarded as typical.

One of these, designated No. AF 33(604) 22221, was executed on March 16, 1959. It provided for the sale, to the United States, of standard commercial items of equipment then sold by Hewlett-Packard in substantial quantities to the general public. With one exception, each such item had been included in Hewlett-Packard's regularly published catalog for the previous three years or more.

¹ David Packard and Wilfred F. Cavier, President and Vice-President-Finance of Hewlett-Packard, respectively, were also named defendants, but it will not be necessary to make further reference to them in this opinion.

The catalog listed items for sale to the public at indicated prices. Each item qualified as a standard commercial article as defined by the Renegotiation Act of 1951, 65 Stat. 7, added by 70 Stat. 790 (1956), 57 U.S.C. App. § 1216(e) (1964), and was therefore exempt from renegotiation.²

In the contract of March 16, 1959, the contract price was determined upon the basis of the listed catalog prices of the particular item of equipment, less a volume discount. The Government's Request for Proposal which was incorporated into the contract contained a form statement of additional terms and conditions, but only the clauses check by the Government were to be applicable. One clause, entitled "Cost Data Information," called for the seller to provide the Government with detailed data concerning such cost items as material, labor and overhead. However, this clause was not checked and was therefore not applicable. Hewlett-Packard did not supply to the Government any information as to the costs of production or profit margins upon any of the items listed in this contract.

The other contract which the parties regarded as typical, designated No. AF 33 (604)-31882, was executed on January 30, 1961. This contract related to only one item of equipment, namely Hewlett-Packard instrument Model No. 620A. This was a standard commercial item then sold by the company in substantial quantities to the general public. The item had been included in Hewlett-Packard's regularly published catalog since 1952, for sale to the public at a catalog list price. The price had remained unchanged since the original date of introduction of the item.

At the date of execution of this contract, this item of equipment qualified as a standard commercial article as defined by the

² Under this section the provisions of the Renegotiation Act were made mandatorily inapplicable to amounts received or accrued in a fiscal year under any contract or subcontract for a standard commercial article. In Senate Report 643, July 25, 1953, U.S. Code Cong. & Admin. News (1954), p. 3880, the committee gave the following reasons for making this exemption mandatory rather than permissive:

"The committee believes that in the case of standard commercial articles there is in most cases no basis or need for renegotiation since cost and pricing experience has already been acquired and prices made in a competitive market."

Renegotiation Act of 1951, as amended, and was therefore exempt from negotiation. The contract price was determined upon the basis of the listed catalog price, less a volume discount. Hewlett-Packard did not supply to the Government any information as to any of the company's costs of production or profit margins upon this contract item.³

All four contracts were negotiated pursuant to chapter 137, Title 10, U.S.C. §§ 2301-14, entitled "Procurement Generally." A subsection of that chapter, 10 U.S.C. § 2313(b), provides that each contract negotiated under chapter 137 shall provide that the Comptroller General and his representatives are entitled for a period of three years after final payment, to examine any books, documents, papers or records of the contractor, or any of his subcontractors:

"that directly pertain to, and involve transactions relating to, the contract or subcontract."

Consistent with this statutory provision each of the four contracts referred to above contained a clause 10, giving the Comptroller General and his representatives for a period of three years after final payment, access to and the right to examine:

"any directly pertinent books, documents, papers, and records of the Contractor involving transactions related to this contract."⁴

Purporting to exercise rights accorded by clause 10 of these contracts, representatives of the Comptroller General commenced an

³ In a memorandum dated January 4, 1961, prepared by employees of the Air Force, setting forth facts as to the negotiation of this contract, the following statement was made:

"2. The Field Analyst was not contacted to evaluate subject proposal due to urgency (AOCP) of this proposal and the fact that competition was involved. In addition, subject item is listed in contractor's catalogue."

An agency regulation pertaining to firm fixed-price contracts, and an agency statement of contract pricing policy, appear to recognize that production costs need not be inquired into in connection with the purchase of items having an established catalog or market price. (32 C.F.R. § 3.403.1 (1955), now 32 C.F.R. § 3.404.2 (1964), Defense Procurement Circular No. 5, May 12, 1964.)

⁴ The parties seem to be agreed that clause 10 in the four contracts in question was intended to give the Comptroller General the same rights of examination as specified in section 2313(b).

examination of the books and records of Hewlett-Packard in September, 1962. During this examination the company permitted access to books and records relating to sales prices of various instruments and parts sold under the four contracts. The representatives of the Comptroller General then requested all books, documents, papers or records of Hewlett-Packard:

“relating to the pricing and cost of performance, support for prices charged to the Government, and such other necessary information which would permit such Representatives to review the reasonableness of the contract prices provided for in the aforesaid contracts.”

This request was refused by Hewlett-Packard upon the ground that cost of production information was not directly pertinent to these contracts. In this suit, which the United States then instituted, the trial court disagreed with Hewlett-Packard, and judicially declared that the company's costs of direct material, direct labor and overhead costs in producing the items furnished under the contracts, directly pertain to, and involve transactions relating to, those contracts. The court further declared that the Comptroller General and his representatives have the right to examine the books, documents, papers and records of the company relating to or otherwise disclosing these production costs. Defendants were ordered to make this information available to the Government.³

Hewlett-Packard argues that the decision of the district court gave no effect to the words of limitation contained in 10 U.S.C. § 2313(b), and reflected in clause 10 of each contract.

The words of limitation to which the company refers limit the records which may be examined by the Comptroller General and his representatives to those “of the contractor, or of any of his subcontractors, *that directly pertain to, and involve transactions relating to, the contract or subcontract.*” (Emphasis supplied.) Hewlett-Packard asserts that the district court has, in effect, placed a period after the word “subcontractors” in the quoted clause, and

³ The trial court stayed the injunctive provisions of the judgment pending disposition of this appeal.

has thus given no practical effect to the words of limitation.

A mere reading of the judgment indicates that this is an overstatement. If, in its decree, the district court had placed a period after the word “subcontractors,” then the Comptroller General and his representatives would have been authorized to examine the books of the company without limitation. Instead, the court declared that the Comptroller could examine any such records

“relating to the cost of producing the items furnished by Hewlett-Packard Company under the aforesaid contracts, including costs of direct material, direct labor and overhead costs. . . .”

It is therefore clear that the district court sought to give effect to the words of limitation. The question is whether it gave full effect to those words. This depends upon the meaning to be attached to those words.

The key word in the limitation clause is “contract.” If that word is used in section 2313(b) only with reference to the terms and conditions of an agreement and the procedures whereby those terms and conditions were formulated, then the district court failed to give full effect to the limitation clause. As Hewlett-Packard correctly points out, under the stipulated facts summarized above, production costs were not taken into consideration in arriving at the terms and conditions of the contracts in question. Thus data pertaining to production costs could not be said to directly pertain to, and involve transactions relating to, the contract, as so defined.

In our opinion, however, the word “contract,” as used in this statute is intended to have a broader meaning, embracing not only the specific terms and conditions of the agreement, but also the general subject matter. The subject matter of these four contracts is the procurement of described property by the Government.

Production costs directly pertain to that subject matter, because if out of line with the contract price, the contract may have been an inappropriate means of meeting this particular procurement need of the Government. While this appraisal could

not affect these particular contracts, it could lead to the use of other methods of meeting future procurement needs. Production costs involve transactions relating to the contract, because they encompass business arrangements made by the contractor in obtaining the materials, labor, facilities and the like required by it in fulfilling its commitment with reference to the subject matter of the contract.

Hewlett-Packard contends, in effect, that the sole purpose of the examination right accorded by section 2313(b) and clause 10 of these contracts, is to enable the Comptroller General to find out whether the particular contracts which gave rise to the examination had been performed in accordance with their terms and whether

the contracting officer had been defrauded or misled in entering into the contract.

We find nothing in the words of the statute, its legislative history, or administrative interpretation, or in the impact of other statutes, which supports this view. On the contrary, it seems to us that if such a limited scope of examination had been intended by Congress it would have found the means to so indicate. The term "contract" could have been given a restricted meaning, or the scope of the permissible examination could have been specifically limited to lines of inquiry relevant to the legality and faithful performance of the particular contract giving rise to the examination.

Affirmed.

NEWS and NOTES

Public Service in a Period of Change

The Comptroller General, *Elmer B. Staats*, was the featured speaker at the 13th annual merit and service awards ceremony of the Securities and Exchange Commission in Washington on November 1, 1967.

The following excerpts are from his address which was devoted to the subject of public service in a period of change.

What does a career in Government mean to an individual? Why does he deliberately choose it, say, instead of a business career? There are many reasons as I will try to show. One of the reasons that a career in public service has its appeal, I think—and I am speaking here particularly of Federal service—is that there is nothing else quite like it. There are, for example, hundreds of companies selling stocks but only one Securities and Exchange Commission; hundreds of American corporations doing business in many parts of the world but only one U.S. Bureau of International Commerce; hundreds of universities and colleges but only one National Science Foundation; many electrical power companies but only one Federal Power Commission and one Atomic Energy Commission; countless commercial banks with foreign departments but only one Export-Import Bank. And, if you will pardon family pride, there are thousands of accounting firms serving business well throughout the country but only one U.S. General Accounting Office.

* * * * *

What I am attempting to say—and why I feel it appropriate to say it on this occasion—is that we as Government servants run the risk of being tied too much to the past. We tend to do things in the traditional ways. We fail to question why it cannot be done better, or we may fail to realize that situa-

tions have changed which call for new solutions or new ideas. But, above all, the challenge is to do our job better, to find ways of improving our own capabilities.

It is not enough to be judged good at doing our daily work—that we had a satisfactory performance rating. We want to be able to look back and know that the public service is better because *we* were there. This will be done only in proportion to our efforts to broaden our understanding of the role which we play, in improving our skills, and in knowing how our efforts relate to the changing role of the agencies in which we work.

* * * * *

Innovation, change, education—these are familiar words describing our reaction to this changing environment. We cannot avoid change, nor would we want to if we could. But just as nuclear energy must be controlled and carefully channeled to be useful, so must change be guided through social institutions and organizations to meet the goals and objectives which history and past experience dictate as meeting the moral and ethical needs of society. Government—which you and I represent—is probably the most important of these institutions.

We have people with that kind of understanding in this room. Government in the coming years will need as many people as possible with that kind of vision. In solving the complicated governmental problems that are arising in our mass society—rising costs of education, public health, and welfare; rebuilding of the cities; reducing poverty to its lowest possible level; developing in our society a higher sense of unity—in solving these immense problems even partially we will need all that kind of understanding.

This is the challenge of Government at all levels. In one way or another it has always been so and I suppose always will.

Public service is more than an occupational category. It runs with the discovery, as Harold Laski put it long ago, that men serve themselves only as they serve others.

Could any of us give a better reason why many men choose careers in the Government service?

Defense Procurement Notes

On October 31, 1967, *Frank H. Weitzel*, the Assistant Comptroller General, addressed the 1967 procurement pricing conference of the Department of Defense in Hershey, Pa. Of especial interest are the following remarks from his address:

We are giving increasing attention to advance procurement planning. It is apparent that crucial decisions or lack of such decisions during this phase of your work have the greatest impact on pricing. They significantly influence the production costs as well as the supply, operation, and maintenance effort over the life of the new weapon or item being procured. Among the areas and management disciplines required by your Defense Directives which we expect to review are:

- The cost effectiveness evaluations which determine what should be procured;
- The contract definition phase, where you perform the necessary contractual and technical definition and the management planning sufficient for design and procurement award;
- The selection of the method of procurement, whether it be multiyear procurement, two-step formal advertising, or the increasing trend toward total package procurement;
- The source selection; and
- The contract negotiation and award.

We also plan to direct our efforts to the special incentive arrangements utilized in some procurements to motivate the contractor to meet or even exceed his contractual commitments. In this connection, one of the most significant steps taken in advance procurement planning during the 1960s, in our opinion, has been to discourage buy-in bidding during the initial acquisition phase of a weapons system, by including as part of the contractor's subsequent contractual commitments the weapons performance, delivery, and cost which the contractor promised at the time of the competitive award. This should help to minimize the performance

disappointments that invariably go along with buy-in bidding as well as to aid you in achieving more realism in the competition for your major defense programs. Better pricing and performance will result and we commend you for taking this step.

Our future reviews in the area of advance procurement planning will, in part, be directed toward determining whether the prescribed management disciplines are being followed in actual practice. Initially, however, we will obtain more background on these management disciplines and observe how they work in practice. We think that the results of our work will ultimately provide the Congress with a better understanding of your procurement processes and problems.

* * * * *

We believe it is basically the responsibility of the contractor, when business is done with the Government in a noncompetitive environment, to develop good methods and procedures for estimating cost on a realistic basis and to manage the preparation of the proposals so that this will be accomplished. We feel that if the average contractor recognizes what is expected of him in this area more acceptable proposals will ultimately be submitted and that this will tend to relieve the burdensome review and negotiation process.

The best way to get at this problem, we believe, is through the total visibility that can be obtained at the contractor's plant—

- Where all the cost and pricing data in its original environment can be found;
- Where the proposal itself is prepared;
- Where the estimating system, the connecting link between the cost and pricing data and the proposal, can be evaluated;
- Where proper interpretation of the data in the proposal can be found from technical, estimating and management personnel; and, finally
- Where in many instances you have a resident team of pricing technical and audit personnel who are familiar with the contractor's practices.

* * * * *

Still in the audit area, one recommendation we had made in an earlier report to the Congress was adopted in March 1966

when the Defense Contract Audit Agency established a program for regularly scheduled postaward audits of selected contracts to determine whether pricing data submitted under Public Law 87-653 are deficient.

Just recently, the Department decided, as we had recommended previously, that when it is necessary to provide assurance that defective cost or pricing data were not submitted, audits should be conducted of actual costs incurred after contracts are consummated. To this end, there will be included in all noncompetitive, firm fixed-price contracts involving certified cost or pricing data, a contractual right to have access to the contractors' actual performance records.

In announcing this decision, Deputy Defense Secretary Nitze said:

I wish to make it clear that the purpose of any postaward cost performance audit, as provided herein, is limited to the single purpose of determining whether or not defective cost or pricing data were submitted. Access to a contractor's records shall not be for the purpose of evaluating profit-cost relationships, nor shall any repricing of such contracts be made because the realized profit was greater than was forecast, or because some contingency cited by the contractor in his submission failed to materialize—unless the audit reveals that the cost and pricing data certified by the contractor were, in fact, defective.

I realize that industry, as well as some of you here, will be concerned at the implications of this decision. Reassurance should be found not only in Mr. Nitze's carefully worded directive but in the professional approach which the Defense Contract Audit Agency is taking toward its new responsibilities. Defense Contract Audit Agency auditors have been given very complete and careful instructions as to when something is *not* defective pricing as well as when it is. Also, seminars are being held around the country to assure that these audits will be approached in a sensible way.

Defense Contract Audit Agency

On July 28, 1967, the Military Operations Subcommittee of the

House Government Operations Committee held a hearing on the functions of this audit agency. The Comptroller General, the Assistant Comptroller General, and other GAO officials testified. The printed hearing record presents a considerable amount of information about the organizations and functions of DCAA and its relationships with the General Accounting Office. In addition, the appendix to the hearing record includes six GAO reports pertaining to examinations into defense contract pricing and related matters.

GAO Findings Pertaining to Contract Pricing

On September 25, 1967, *Charles M. Bailey*, deputy director, Defense Division, testified at length before the Subcommittee for Special Investigations of the House Committee on Armed Services on GAO findings relating to reviews made of the administration of Public Law 87-653, the so-called "Truth in Negotiations Act."

The various types of deficiencies discussed by Mr. Bailey based on GAO examinations are summarized below.

Need for improvements in contractors' submission of cost or pricing data in support of proposed prices—

Lack of records identifying cost or pricing data submitted and certified by contractors.

Failure of Department of Defense regulations to require contractors to submit prior cost experience even when not used as a basis for contractors' estimates of costs.

Incomplete cost and pricing information submitted by contractors in support of proposed costs.

Failure of contractors to disclose information that became available between the time the proposals are submitted and the time of price negotiations.

Need for improvements in evaluation of contractors' proposals by agency officials—

Inadequate technical evaluations of cost estimates.

Inadequate auditing and reporting on contractors' price proposals.

Need for postaward defective pricing data audits and right of access to contractors' records to perform such audits.

Need for evaluations of subcontract price estimates included in prime contract price proposals.

Need for improvements in actions by contracting officers for establishing reasonable negotiated prices—

Failure to request preaward audits.

Failure to adequately consider and/or document negotiation files on consideration given to findings and recommendations contained in advisory reports.

Failure to recognize the need for and to request postaward audits.

Questionable determinations by contracting officials that proposed prices are based on adequate price competition or catalog prices and that cost or pricing data need not be obtained.

M-16 Rifle Program

In October 1967, the House Committee on Armed Services released a report on the inquiry made by its special subcommittee into the development, history, distribution, sale, and adequacy of the M-16 rifle now in use by the Armed Forces. This rifle is manufactured by Colt's, Inc. The ammunition for it is produced by Olin Mathieson Chemical Corp.

The report lists numerous conclusions concerning the performance and procurement of this rifle and the ammunition; two of the recommendations were directed to the GAO:

Conduct an audit and investigation of the contracts awarded to Olin Mathieson for ball propellant loaded in both 5.56-mm. and 7.62-mm. ammunition and the justification for sole-source procurement over the past 26 years.

Conduct a complete audit of Colt's military contracts to determine actual profit rates experienced, the adequacy of their accounting system and whether provisions of Public Law 87-653 were circumvented.

Management of Research Equipment in Government Laboratories

The Fall 1967 issue of the *Review* contained an article by *Harold H. Rubin*, associate director, Defense Division, which summarized the results of a GAO survey relating to scientific research equipment management problems and techniques in Government laboratories.

Hearings were held on this subject by the Research and Technical Programs Subcommittee of the House Government Operations Committee in August 1967. The printed record of the hearings subsequently released by the committee includes the full text of the GAO survey report which was issued in June 1967.

The Lybrand Newsletter for November 1967 took notice of the recommendations for improved management practices included in the GAO report in the printed hearing record as follows:

Business may be able to pick up some useful pointers for greater efficiency and cost savings from findings of a recent General Accounting Office (GAO) survey on equipment management and purchasing in Government laboratories.

The official report of the House Government Operations Committee on its inquiry, entitled "Better Management of Research Equipment and Utilization in Federal Laboratories," was released October 30, 1967 (H. Rept. 867, 90th Cong., first sess.). It contains several recommendations for achieving greater economy and efficiency in Federal

laboratory equipment management; these recommendations are directed to the Bureau of the Budget, the General Services Administration, and the Department of Defense.

Distribution of Selected Audit Reports

The following audit reports issued by the Comptroller General to the Congress in recent months were selected for distribution to a list of over 400 interested college and university faculty members:

Compilation of General Accounting Office Findings and Recommendations for Improving Government Operations, Fiscal Year 1966—8-23-67.

Review of Inventory Accounting Systems for Aeronautical Equipment, Department of the Navy—9-29-67.

Actions to Improve the Financial Management System of the U.S. Army Tank-Automotive Command, Warren, Mich., Department of the Army—10-31-67.

Administration of Research Grants

The ninth report of the Committee on Government Operations to the 90th Congress (H. Rept. 800), dated October 20, 1967, is concerned with the administration of research grants in the Public Health Service. The report is based on a study by the Intergovernmental Relations Subcommittee and contains a series of recommendations designed to improve such administration.

GAO provided assistance to the committee in its study by making a review and reporting on certain aspects of indirect cost allowances on selected research project grants awarded by the Public Health Service. The GAO report (B-114836, June 30, 1966) on this work is printed in the

appendix to the committee's published report.

The Assistant Comptroller General has advised the chairman of the subcommittee that the committee's report "merits the full and careful consideration of responsible officials in the Department of Health, Education, and Welfare" and that in continuing reviews of the activities of the Public Health Service, GAO will be "particularly alert to the weaknesses highlighted by the report and the adequacy of corrective actions taken by the agency."

Congressional Policy on Accounting Improvements in the Department of Defense

Congressional concern with the accounting improvement program in the Department of Defense, particularly Project PRIME (see *GAO Review*, Summer 1966, p. 47; Fall 1966, p. 51) resulted in the decision to have the Comptroller General, representing the legislative branch, review the Department's proposed program and advise the Congress as to its adequacy. The decision was reflected in an amendment to the 1968 Defense appropriation bill (Public Law 90-96, approved Sept. 29, 1967).

The amendment which became section 640(b) of the appropriation act provides that the Department may not use its funds to install or utilize any new "cost-based" or "expense-based" systems of accounting until 45 days after the Comptroller General reports to the Congress that in his opinion such systems are designed to:

1. Meet the requirements of all applicable laws governing budgeting, accounting, and the administration of public funds and

the standards and procedures established pursuant thereto.

2. Provide for uniform application to the extent practicable throughout the Department of Defense.
3. Prevent violations of the anti-deficiency statute (R.S. 3679).

Financial Management Improvement in the Department of Agriculture

The Secretary of Agriculture recently reminded the heads of offices in his department of some very important tenets for successful financial management improvement programs. In a memorandum dated October 18, 1967, he stated:

For the most part, it appears that the responsibility for the work to date has been left to financial management people within the agencies. They cannot do this job alone. They cannot make final decisions on the kind of financial data agency heads and other program administrators need. Program administrators should play a part in this determination. As a minimum, the responsibility for guiding and coordinating financial management improvement efforts should not be delegated below the level of Deputy or Assistant Administrator for Management.

It is not enough to merely modify existing procedures so that the accounts will provide monthly accrued cost information, or to meet other technical requirements of the General Accounting Office. Agencies should make a comprehensive review of their internal financial management requirements to be sure that the system is efficient and that obsolete records and reports are eliminated.

Further emphasis was given in this Department to the need for operating officials to become involved in financial management improvement programs when a Department-wide meeting of about 90 top management and fiscal officials was held on December 7, 1967. The Secretary of Agriculture participated in the meeting which was

addressed by the Comptroller General, *Elmer B. Staats*. Mr. Staats spoke on the importance of improving agency accounting systems.

An Air Force View of GAO

In the October 1967 issue of the *Air Force Controller* appears an article about GAO which takes a somewhat different twist than most published articles about our operations. The article in question is entitled "The GAO Rep Can Help You * * * Toward Better Management" and was written by Col. Frank E. Johnson, assistant for GAO matters, in the office of the Comptroller of the Air Force.

His theme, reflected in the title, is that Air Force management officials have much to gain from GAO audit, investigative, and advisory services. Of especial interest are remarks such as the following:

* * * A better understanding of GAO may bring the realization that the product of this organization could be utilized to your advantage.

* * * Any critical examination of a job undertaken and performed in good faith, even from one's own "family," is somewhat unpalatable. It follows that when a "stranger" makes an examination and comes up with adverse remarks about one's performance or operation even stronger resentment may follow.

Notwithstanding this quite normal reaction to external criticism, the Air Force, as well as all other executive agencies, has an obligation to the citizens of the United States for the most efficient management of resources possible.

* * * Pride in operations should not extend to the point that we automatically reject constructive criticism and suggestions for better utilization of resources from outside sources.

* * * the Air Force should utilize, to the maximum extent, GAO's product. By intelligent application of all information made available regardless of source, the Air Force

can enhance its management improvement effort and achieve maximum effectiveness and minimum waste.

* * * Don't resist the GAO representative when he has a job to do. Don't treat him as a stranger * * * help him out and use his considerable investigative skills to your own advantage.

GAO Cooperative Assistance

The Acting Comptroller and Director of Programs of the U.S. Army Materiel Command has expressed in writing his appreciation for GAO assistance provided in developing systems and procedures for extending the Army Industrial Fund under project PRIME in the Department of Defense during the period from January to June 1967. The communication stated:

The material contribution made by the following representatives of your office was outstanding and is a tribute to the professional competence, ability and dedication of each of the individuals concerned:

James S. Rodgers II, Philadelphia regional office.

Mas Yoshioka, San Francisco regional office.

James Marbutt, Atlanta regional office.

Accounting for Human Assets

Writing on the subject of reality in management in the November 1967 issue of the *Michigan Business Review*, Dr. George S. Odiorne of the University of Michigan Graduate School of Business Administration made the following very interesting remarks about the possibility of expanding the scope of accounting to account for human assets. He stated:

The idea that human capital is an asset which should be carried on the corporate books, depreciated, and maintained like other assets is one possible for the economist or psychologist, but as yet is not permissible with the tax man, the accountant, or the vice president of finance.

Conceptually the idea is both necessary and correct. The route to its full utilization will require more than attitude surveys and interviews to achieve, however. It will call for changes in law, accounting, and accounting conventions, and numerous procedural matters must be worked out. The tax courts, for example, have set precedent in certain defense contracts that return on investment might take into account the prior expense of gathering certain kinds of engineering talent together in estimating rate base. Utility companies have begun investigating the possibilities of including human assets in calculating rate base—other evidence that the idea is one that will gain acceptance.

Audit Provisions for New Corporation for Public Broadcasting

The Public Broadcasting Act of 1967 (Public Law 90-129, approved Nov. 7, 1967) amends the Communications Act of 1934 in several respects to authorize Federal assistance for educational television and radio broadcasting. The law also provides for establishing a nonprofit corporation to be known as the Corporation for Public Broadcasting. This corporation will not be an agency or establishment of the U.S. Government.

The law provides for annual audits of the accounts of the corporation in accordance with generally accepted auditing standards by independent CPAs or independent licensed public accountants. It also authorizes an audit by the General Accounting Office of the financial transactions of the corporation, for any fiscal year during which Federal funds are available to finance any portion of its operations.

Reporting of Contingent and Unfunded Liabilities

Section 402 of Public Law 89-809, approved November 13, 1966, requires the Secretary of the Treasury

to make an annual report to the Congress as of June 30 each year setting forth the contingent and unfunded liabilities of the Government and of each department, agency, and instrumentality thereof.

The Treasury Department has amended its circular No. 966 to prescribe the instructions to be followed by the Federal agencies in submitting financial information to the Treasury which will enable it to comply with this statutory requirement (Amendment No. 1, Sept. 13, 1967).

Report of President's Commission on Budget Concepts

In March 1967, the President appointed a 16-member commission to make a study of existing concepts pertaining to the Federal budget and to make recommendations for improvement. The Commission released its report on October 18, 1967. The report contains numerous recommendations designed to make the Federal budget a more understandable and useful instrument of public policy and financial planning.

The 100-page report contains much useful information about the overall financial operations of the Federal Government. Copies have been made available in all GAO offices for use of staff members. Starting with this issue (p. 50), the *Review* will present from time to time analytical articles about the Commission's recommendations and problems and progress in implementing them.

Published Article on GAO

The November 1967 issue of Reader's Digest contains an article bearing the title "GAO: The Taxpayer's Best Friend" written by Alfred Steinberg.

This article was printed in full in the Congressional Record for November 9, 1967. Senator Proxmire requested that it be printed in the Record with the following comments:

Mr. President, the General Accounting Office does a superlative watchdog job for Congress and for every American taxpayer. Unfortunately, this difficult, complicated work of investigating the vast Federal Government has been largely unheralded.

Recently, the Reader's Digest published an excellent article entitled "GAO: The Taxpayer's Best Friend," written by Alfred Steinberg. The article concisely spells out some of the achievements of the good right hand of Congress.

Program Planning Staff

The Program Planning Staff, established on July 7, 1967, by Comptroller General's Order 2.15, has been organized and staffed as shown below. It is located in Room 7310 of the GAO Building, telephone extension 5501.

Director:

Harry C. Kensky

Program Planning:

Paul C. Newell
Abraham Yalom
Anthony Gabriel
Francis P. Degnan

Management Information System:

Edwin Y. Rodda
William E. Parker
J. Richard Berman
Williston B. Cofer

As set forth in the Comptroller General's Order, the staff is responsible for performing specific functions related to: (1) The development and review of programming, scheduling, and reporting systems with regard to accounting and auditing activities; (2) the review and analysis of program proposals for, and conduct of, accounting and auditing work; and

(3) the development of an office-wide management information system.

Glossary of PPBS and Systems Analysis Terms

The systems analysis group of the Office of Policy and Special Studies, GAO, has prepared a booklet setting forth a glossary of terms relating to planning, programming, and budgeting operations and systems analysis.

New Joint Program Booklet

A revised edition of the pamphlet entitled "The Joint Financial Management Improvement Program in the Federal Government of the United States" has been published. The pamphlet is organized in question and answer form and is designed to explain the scope, objectives, and methods of this Program which has been in operation for over 18 years.

PPB Interest Group

A special meeting sponsored by the Washington Operations Research Council (WORC) and the National Institute of Public Affairs (NIPA) on November 15, 1967, at the Marriott Motor Hotel, Washington, D.C., produced a large turnout of representatives from a wide range of executive departments and agencies who met to organize a PPB Interest Group to help foster better planning, programming, budgeting and systems analysis in the Federal Government.

WORC is the first professional association to form a group which will deal exclusively with matters relating

to PPBS. WORC also holds regularly scheduled meetings dealing with the application of operations research and systems analysis techniques which are often useful in the field of PPBS.

Some of the ways in which this group plans to help advance the state-of-the-art for PPBS and systems analysis are listed below:

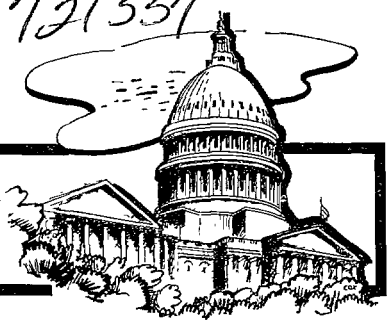
- Present reports and hold exchanges about experiences of successes and failures in applying PPBS theory.
- Discuss common system development problems and possible solutions to them.
- Serve as a sounding board for legislators and others interested in PPBS matters.
- Develop examples and case studies showing how PPBS contributes to sound financial management practices.
- Develop illustrations showing how agencies use PPB systems and systems analysis techniques; the nature and form of good PPB systems; and good and bad practices.
- Identify sources and provide materials for agency training programs and university courses which focus on PPB and systems analysis.

A series of monthly meetings will be held on PPBS and systems analysis starting January 17, 1968, at the Marriott Motor Hotel. The theme for these meetings will be: "The Planning-Programming-Budgeting System: Progress and Potential."

Further information may be obtained from *Edward E. Winchester*, OPSS, telephone 202-386-5319, who is acting chairman for the PPBS Interest Group.

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HEARINGS *and* LEGISLATION



By MARGARET L. MACFARLANE

Chief, Legal Reference Services, Office of the General Counsel

Legislation enacted during the first session of the 90th Congress has brought the GAO into the field of international organizations to a greater extent than ever before.

Audits of Inter-American Development Bank

Annual audits of the financial statements of this Bank, the capital stock of which is owned by the United States and about 20 Central and South American countries, are made by a large firm of CPAs.

Reflecting congressional interest in having more comprehensive audits made of the operations of the Bank, an amendment to the Inter-American Development Bank Act was passed by the current Congress to require that such audits be proposed. This amendment, known as the Selden amendment, grew out of a report of a special study mission to Latin America last year undertaken by the Subcommittee on Inter-American Affairs chaired by Congressman Armistead Selden, Jr., of Alabama. The mission's report recommended that a full review of the Social Progress Trust Fund, which is administered by the Bank for the United States, be made by GAO.¹

Since the Bank is an internationally owned organization, the United States cannot unilaterally arrange for expanded audits. Thus the law authorizing U.S. participation in the Bank, as now amended by Public Law 90-88, approved September 22, 1967, contains the following somewhat unusual provisions which include assigning certain new functions to the Comptroller General:

The Secretary of the Treasury is directed to instruct the U.S. Executive Director to propose the establishment of "a program of selective but continuing independent and comprehensive audit" of the Bank in accordance with terms of reference prescribed by the Bank's Board of Executive Directors.

The Comptroller General is directed to prepare for the Secretary of the Treasury "the scope of the audit and the auditing and reporting standards" for use in formulating the terms of reference.

Reports to the Congress made by the National Advisory Council on International Monetary and Financial Policies are to include an appraisal of the effectiveness of the implementation and administration of loans made by the Bank based on reports of audits made.

The Comptroller General is directed to review the audit reports and report to the Secretary of the Treasury and the Congress suggestions for improving the scope

¹ H. Rept. 219, 90th Cong., first sess.

of the audit work or the auditing and reporting standards of "the independent auditing firm, group, or staff."

Foreign Assistance Act of 1967

In a related but entirely separate action the Congress included in the Foreign Assistance Act of 1967, enacted as Public Law 90-137, approved November 14, 1967, the following provision which also affects the Inter-American Development Bank:

"In any case in which a fund established solely by the United States contributions under this or any other Act is administered by an international organization under the terms of an agreement between the United States and such international organization, such agreement shall provide that the Comptroller General of the United States shall conduct such audits as are necessary to assure that such fund is administered in accordance with such agreement. The President shall undertake to modify any existing agreement entered into before the date of enactment of this subsection to conform to the requirements of the preceding sentence."

At the present time the largest fund that is wholly financed by the U.S. Government and administered by an international organization is the Social Progress Trust Fund, a one-half-billion-dollar fund administered by the Inter-American Development Bank.

In addition to the audit provision, the Foreign Assistance Act of 1967 is significant for the inclusion of an additional control mechanism to correct a deficiency in the capital assistance programs of the Agency for International Development, which deficiency was highlighted over the years in GAO reports to the Congress.² Congressman John S. Monagan and Congressman John E. Moss, who serves as chairman of the Foreign Operations and Government Information Sub-

committee of the House Government Operations Committee, sponsored the capital assistance amendment. This provision is to the effect that for capital assistance projects over \$1 million the head of AID must obtain and take into consideration a certification, from the head of the AID mission in which the project is located, as to the capability of the country (both financial and human resources) to effectively maintain and utilize the project taking into account among other things, the maintenance and utilization of projects in such country previously financed or assisted by the United States.

Atomic Energy Commission— General Plant Projects

Another law enacted during the first session of the 90th Congress containing provisions resulting from GAO recommendations was the Atomic Energy Commission authorizing legislation approved by the President on July 26, 1967.³ On January 31, 1967, at the request of the Joint Committee on Atomic Energy a report was made on selected aspects of general plant project funds.⁴ As a result of the review an amendment to the Commission's statutory authority to establish building cost limitations on the use of general plant project funds was proposed.⁵ The effect of the new language would give the Commission added flexibility to protect the Government's investment in the project and keep the Congress advised as to the use of the general plant project funds.

² Public Law 90-56, July 26, 1967, 81 Stat. 124.

³ B-160731. See article beginning on p. 36 of this issue of the *Review*.

⁴ H. Rept. 369, 90th Cong., first sess., pp. 52-53.

⁵ B-161882, September 1967, being the latest report.

Vietnam Refugee Program

The Subcommittee to Investigate Problems Connected with Refugees and Escapees of the Senate Judiciary Committee, chaired by Senator Edward M. Kennedy, invited representatives of GAO to testify concerning the GAO inquiry into the refugee program and the civilian health and casualty program in Vietnam. *Oye V. Stovall*, Director, International Division, presented a statement outlining the program difficulties. (Other GAO participants included *Messrs. Johnson* and *Martin*.)

Civil Service Retirement System

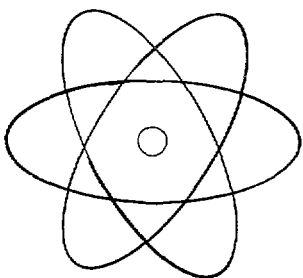
The Comptroller General was invited by the Subcommittee on Retirement, Insurance, and Health Benefits of the House Committee on Civil Service and Post Office to present views on H.R. 10912, which would provide improved financing of the retirement

system. Mr. Staats invited the subcommittee's attention to the differences between the proposed bill and the alternative approach suggested in the GAO report to the Congress last spring.⁶ (Other GAO participants included *Messrs. Smith, Ahart*, and *Fenton*.)

Procurement and Supply

The Subcommittee on Economy in Government of the Joint Economic Committee asked the Comptroller General to be the leadoff witness and the concluding witness during the second phase of its inquiry into procurement and supply matters. Mr. Staats presented statements on November 27 and December 8, 1967. (Other GAO participants included *Messrs. Weitzel, Newman, Bailey, Hammond, Fasick, Welch*, and *Ahart*.)

⁶ B-130150.



AUTOMATIC DATA PROCESSING

20th Annual International Systems Meeting

The annual systems meeting of the Systems and Procedures Association was held in Detroit, Mich., on October 1-4, 1967. The overall theme of the meeting was "Blueprint for the Future." *Edward J. Mahoney*, associate director, Office of Policy and Special Studies, attended the meeting and provides the following comments on the proceedings.

The meeting this year, as for the past several years, was heavily oriented toward the use of computers in business systems. Much emphasis was placed on the subject of overall management information systems and possible approaches to using ADP techniques in the design of such systems.

Many of the topics covered during the meeting, relating to the use of computers in advanced management systems, involved presentations and discussions on techniques that have evolved from military efforts in the command and control area and other advanced techniques that are being used in the development of integrated data processing systems in industry.

In addition to the discussions on advanced systems development, technical sessions were devoted to such topics as:

- Direct access computer file techniques.
- Simulation and model building.
- Information retrieval.
- Compatibility of third generation hardware and software.
- Use of decision tables.
- Computer time-sharing.
- Computer software problem areas.

Those attending the meeting were presented with a copy of a book entitled "Ideas for Management" which was published by the association. This book is available for reference use by GAO staff members who are interested in inquiring into the various matters covered at the conference.

ADP Equipment Procurement Authority of GSA

The General Services Administration is preparing a regulation designed to implement its authority to act as the single purchaser for all general-purpose ADP equipment used by Federal agencies. This regulation is based on the interpretation of Public Law 89-306 (the Brooks bill) enacted in 1965 that GSA have exclusive authority to do such purchasing.

The Administrator, GSA, requested the opinion of the Comptroller General on this interpretation. In an opinion dated November 21, 1967 (B-

151204/157587), the Comptroller General confirmed the GSA interpretation. The opinion stated:

Accordingly, you are advised that we concur in your construction of section 111 of the Federal Property and Administrative Services Act of 1949, as added by Public Law 89-306, as providing exclusive authority to GSA to procure all general-purpose ADPE and related supplies and equipment for use by other Federal agencies.

Selected Readings in Automatic Data Processing

The latest set of selected readings in ADP was distributed by the Office of Policy and Special Studies in November 1967 to other GAO divisions and offices. The following booklets were included:

Published by U.S. Air Force Auditor General—

Flexible Audit Selection Technique

Selecting Audit Transactions Electronically

Utility Program for Selecting Data

Published by the Defense Contract Audit Agency—

Time-Shared Computer Applications in Contract Audits

GAO staff members are encouraged to utilize these publications as one means of keeping informed of developments in the field.

More on Auditape

At the Comptroller General's invitation, the accounting firm of Haskins & Sells conducted a second Auditape demonstration on November 28, 1967, in the GAO auditorium. The primary purpose of this demonstration was to explain the potential usefulness of the system to GAO personnel. Over 200 persons attended, including the Comptroller General, regional managers, staff members of GAO divisions and offices, and visitors from other Government agencies.

AEC Receives World's Largest Computer Storage Device

A photodigital storage device was recently delivered to the Atomic Energy Commission by the IBM Corp. More than 1 trillion bits of information can be stored in this system at one time. The system was installed as part of a vast time-sharing computer network at the Lawrence Radiation Laboratory in Livermore, Calif. Data is stored in files in stacks of trays which can be accessed by the computer system. Each tray holds a number of plastic cells containing data recorded by an electron beam in pieces of high-resolution film. The information is recorded in binary language for computer processing.

Recent Staff Designations

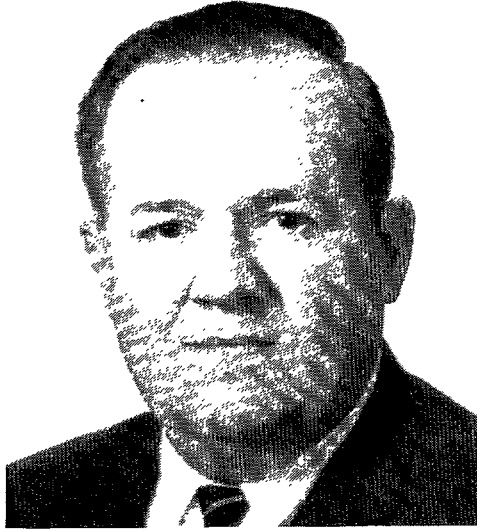


Harold C. Barton

Harold C. Barton was designated as assistant regional manager of the Dallas Regional Office, November 5, 1967.

Mr. Barton received a bachelor of science degree (accounting) from the University of Alabama. He attended the Stanford Executive Program, Stanford University, in 1963. He is a CPA (Alabama and Louisiana) and a member of the American Institute of Certified Public Accountants and the Federal Government Accountants Association. Mr. Barton received the GAO Meritorious Service Award in 1967.

Prior to joining GAO in 1953, Mr. Barton was associated with a firm of certified public accountants in Montgomery, Ala. He served in the U.S. Army Air Corps from 1941 to 1945.



Baltas E. Birkle

Baltas E. Birkle was designated an assistant director in the Civil Division, September 24, 1967. He is in charge of the accounting, auditing, and investigative work at the Veterans Administration.

Mr. Birkle served in the U.S. Navy from 1953 to 1956. He received a bachelor of science degree in accounting and a masters of arts in economics from the University of Maryland in 1951 and 1953, respectively. In 1964 he attended the Program for Management Development of the Harvard University Graduate School of Business Administration.

Mr. Birkle is a CPA (Maryland) and a member of the American Institute of CPAs and the District of Columbia Institute of CPAs. He is an honorary member of Beta Alpha Psi.

Other than in the Civil Division, which he joined in 1956, Mr. Birkle's service in the General Accounting Office included an assignment in the Office of Policy and Special Studies from 1961 to 1963.



Donald G. Boegehold

Donald G. Boegehold was designated an assistant director in the Defense Division, September 24, 1967. In this position he will be concerned with the planning and direction of GAO work relating to the acquisition, training, pay and allowances, utilization and distribution of manpower in the Department of Defense.

Mr. Boegehold joined the Defense Division of GAO in October 1957. In November 1962, he was assigned to the Far East Branch and returned to the Defense Division in January 1965.

Mr. Boegehold attended Cornell University and Columbia University and received his B.S. and M.S. degrees in business administration from Columbia University in 1949 and 1950. He is a CPA (Texas) and a member of the American Institute of CPAs.

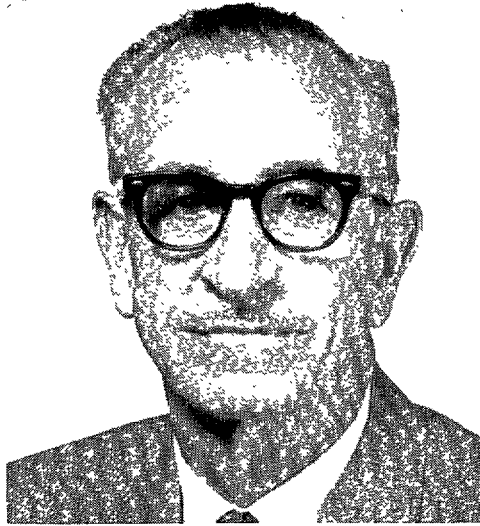
He served in the Army (Infantry) from 1942 to 1946 and in the Air Force (Auditor General) from 1950 to 1953. Prior to joining the General Accounting Office, Mr. Boegehold had extensive public accounting experience with Arthur Andersen & Co., and with his own public accounting firm.



Kyle E. Hamm

Kyle E. Hamm was designated as assistant manager of the Atlanta Regional Office, November 5, 1967.

Mr. Hamm graduated from Duke University with a bachelor of science degree (accounting) and joined the Civil Division of the General Accounting Office in 1951. In 1961 he transferred to the Atlanta Regional Office. In 1964, he completed the Executive Development Program at the University of Michigan Graduate School of Business Administration. He received the Meritorious Service Award of the General Accounting Office in 1967. He is a CPA (Maryland), a member of the Federal Government Accountants Association, and has recently applied for membership in the American Institute of CPAs.



Alpierre R. Horton

Alpierre R. Horton was designated an assistant regional manager of the Kansas City Regional Office, September 24, 1967.

Mr. Horton received a bachelor of science degree from the University of Colorado in 1933. He was employed in public accounting in Denver, Colo., and San Francisco, Calif., until 1950. During the next 4 years he was with the San Francisco Regional Office, Army Audit Agency, first as assistant chief, contract audit branch, and later as chief, internal audit division. He joined the General Accounting Office in 1954, serving as regional manager of the Denver Regional Office until 1962, and as an assistant director of the Civil Accounting and Auditing Division until 1963.

Mr. Horton holds a CPA certificate in the States of Colorado and California. He is a member of the American Institute of Certified Public Accountants and of the California Society of Certified Public Accountants.



Victor L. Lowe

Victor L. Lowe was designated an associate director in the Civil Division, October 8, 1967. He is in charge of the accounting, auditing and investigative work at the Department of Agriculture.

Mr. Lowe served in the U.S. Navy from 1945 to 1946. He received a bachelor of business administration in accounting from the University of Georgia in 1949. In 1960 he completed the Program for Management Development of the Harvard University Graduate School of Business Administration.

Mr. Lowe is a CPA (Georgia) and a member of the Federal Government Accountants Association. Other than in the Civil Division, which he joined in 1949, Mr. Lowe's service in the General Accounting Office included an assignment as an assistant director in the International Division from 1963 to 1966.



Donald C. Pullen

Donald C. Pullen was designated an assistant director in the Civil Division, October 8, 1967. He is in charge of the accounting, auditing, and investigative work at the Department of Commerce.

Mr. Pullen received a bachelor of science in accounting from Rider College in 1955. He is a CPA (Virginia) and a member of the American Institute of CPAs, the District of Columbia Institute of CPAs, the National Association of Accountants, and the Federal Government Accountants Association.

Since joining the General Accounting Office in 1955, Mr. Pullen's service has been in the Civil Division. He received a GAO Superior Performance Award in 1961.



Joseph P. Rother, Jr.

Joseph P. Rother, Jr., was designated as an assistant director in the Civil Division, October 8, 1967. He is in charge of the accounting, auditing, and investigative work at the Social Security Administration.

Mr. Rother served in the U.S. Army from 1946 to 1947 and from 1950 to 1951. He received a bachelor of science in accounting from King's College in 1952 and also received an award from the Pennsylvania Institute of CPAs in the same year.

Since joining the General Accounting Office in 1952, Mr. Rother's service has been in the Civil Division.



Stanley S. Sargol

Stanley S. Sargol was designated an assistant director in the Civil Division, October 8, 1967. He is in charge of the accounting, auditing, and investigative work at the Housing Assistance Administration of the Department of Housing and Urban Development.

Mr. Sargol served in the U.S. Army Air Corps from 1943 to 1946. He received a bachelor of science in business administration from King's College in 1951. He was awarded the Countess Elena Dandini de Sylva Medal for Highest Scholastic Achievement and the Accounting Award for Highest Scholastic Achievement in accounting in 1951. Mr. Sargol is a CPA (Virginia).

Since joining the General Accounting Office in 1951, Mr. Sargol's service has been in the Civil Division. He received a GAO Meritorious Service Award in 1961 and 1962.

Professional Activities

Office of the Comptroller General

The Comptroller General, *Elmer B. Staats*, addressed the following groups in recent months:

Northwest Universities Business Administration Conference, Sali-shan Lodge, Gleneden Beach, Oreg., October 20, on "The Growing Interdependence of Business and Government."

Securities and Exchange Commission's 13th Annual Merit and Service Awards Ceremony, November 1, on "The Public Service in a Period of Change."

Public Personnel Association, November 8, on "New Developments in the GAO."

National Capital Area Chapter of the American Society for Public Administration, November 15, on "The GAO's Growing Role in Management Improvement."

Ceremonies marking Dean's Day at New York University, December 2, on "The Role of the General Accounting Office in Business-Government Relationships."

The *Financial Executive* for December 1967, published by the Financial Executives Institute, carries an article by Mr. Staats entitled "Information Systems in an Era of Change." The article is based on the address given by Mr. Staats on September 20 before the Washington Chapter, National Association of Accountants.

The Assistant Comptroller General, *Frank H. Weitzel*, addressed the following groups:

National Security Industrial Association Procurement Symposium, held at the Shoreham Hotel, September 27. Mr. Weitzel spoke on "Industry Motivations for Maximum Performance."

George Washington University-Bureau of Employment Security (Department of Labor) Seminar, held at Willard Hotel, on October 26, on financial management.

Department of Defense Pricing Conference at Hershey, Pa., on October 30, on "An Opportunity Not to be Missed."

Financial Management Round Table, Washington, D.C., on October 31 on "More Support for Management Decisions."

Navy Graduate Financial Management Class at George Washington University on November 13 on "The Role of the General Accounting Office."

Los Angeles Chapter of FGAA on December 13 on "Current Trends in Federal Financial Management and in GAO Audits."

Office of the General Counsel

J. Edward Welch, deputy general counsel, participated as a panelist at the Government Construction Contracts Conference in November sponsored by George Washington Uni-

versity in cooperation with Federal Publications, Inc.

Mr. Welch also addressed the BNA/FBA Briefing Conference on Government-Industry Patent Matters, Washington, D.C., on November 30, 1967.

Stephen P. Haycock, assistant general counsel, was a panelist at the annual conference of the National Institute of Governmental Purchasing, Inc., September 26, 1967, Shoreham Hotel, Washington, D.C., on the subject of legal aspects of public purchasing.

Mr. Haycock also spoke before the Electronic Industries Association in November 1967, Los Angeles, Calif., and Santa Barbara, Calif.

Melvin E. Miller, assistant general counsel, spoke before the Defense Procurement Management Course, Fort Lee, Va., on October 17, 1967, on "The Role of GAO in Defense Procurement."

Paul Shnitzer, attorney, was a panelist at Government/Aerospace Industries Association of America, Inc., joint session of the annual meeting in October 1967 of the Procurement and Finance Committee, New Orleans, La.

James E. Masterson, attorney, participated on October 27, 1967, in the Department of Agriculture Graduate School program on "Grants." He spoke on the "Role of GAO in Overseeing Grant Expenditures."

Vincent LaBella, attorney, addressed 75 senior students at Phelps Vocational High School on October 24, 1967, on "Right of Privacy" sponsored by Younger Lawyers Committee, FBA.

Michael B. Schwed, attorney, spoke to about 100 students at Dunbar High

School on October 24, 1967, on "Right of Privacy" sponsored by Younger Lawyers Committee, FBA.

Seymour Efros, attorney, lectured on October 25, 1967, on "Functions of the General Accounting Office" at the Department of Agriculture School.

Civil Division

Ronald Calabria, Raymond Kunkel, J. Dexter Peach, James Rosini and Richard Sampson, auditors, participated in the Federal Career Opportunities Conference, on December 27 and 28 in the Civil Service Commission Building, Washington, D.C. The program was designed to present the gamut of Federal career opportunities available in Washington.

Defense Division

William A. Newman, Jr., director, participated in a panel discussion before the Electronic Industries Association, third annual meeting, Government Procurement Relations Department, Santa Barbara, Calif., on November 15. The subject of Mr. Newman's talk was "Current Problems under Public Law 87-653."

Charles M. Bailey, deputy director, took part in a panel discussion at the November 16 meeting of the Washington, D.C., chapter of the Federal Government Accountants Association. The theme of the discussion was the differences in accounting for costs as between Government contracts and commercial work. Mr. Bailey presented a history and background of Government contract cost principles.

Daniel Borth, associate director, Management Control Systems group, addressed the New Orleans, La., chapter of the Federal Government Accountants Association on September

28. His topic was "What's Ahead in Management Accounting in Defense."

Mr. Borth was appointed to the National Publication Policy Committee of the Federal Government Accountants Association. He is also serving as a consulting editor of the *Federal Accountant*.

Donald L. Eirich, assistant director, Management Control Systems group, attended an 8-week course on "Management Program for Executives," at the University of Pittsburgh, September-November 1967.

Guy A. Best, assistant director, Management Control Systems group, spoke on the subject of "Management Control and Direction" before two different groups of students at the Industrial College of the Armed Forces, Washington, D.C., on September 28.

James H. Hammond, associate director, Procurement group, spoke before the Electronic Industries Association, third annual meeting, Government Procurement Relations Department on November 15 at Santa Barbara, Calif. The topic of Mr. Hammond's talk was "Controls over Government-owned Property in the Possession of Contractors."

Mr. Hammond also spoke on the "Requirements of Public Law 87-653" before the meeting of the National Association of Accountants, Electronic Manufacturers Discussion Group on October 30 in Washington, D.C.

Hyman S. Baras, assistant director, Procurement group, was one of the speakers on December 11 at the Procurement and Contract Management Review Seminar held in Washington, D.C. The seminar was sponsored by the Department of Defense. Mr. Baras'

subject was "The General Accounting Office Plans for Auditing Defense Procurement."

Ralph VanKirk, audit manager, Procurement group, was a guest lecturer before the Defense Procurement Executive Refresher Course conducted by Harbridge House, Inc., in Washington, D.C., on November 16. He spoke on the organization and activities of the General Accounting Office.

Edwin C. Eads, audit manager, Procurement group, attended the Defense Procurement Executive Refresher Course in Washington, D.C., conducted by Harbridge House, Inc., during the week of November 27 to December 1, 1967. He also addressed the class on the organization and activities of the General Accounting Office.

Felix E. Asby, assistant director, Supply Management group, was guest lecturer at the Army Logistics Management Center, Fort Lee, Va., on September 1 and September 22. Mr. Asby discussed GAO activities in the area of Defense supply management.

International Division

Charles D. Hylander, deputy director, attended the Advanced Management Program at the Harvard University Graduate School of Business Administration, September-December 1967.

John Milgate, assistant director, recently completed the Management Program for Executives at the University of Pittsburgh.

Frank C. Conahan, supervisory accountant, represented the president of King's College at the dedication of the Anne Arundel Community College at Arnold, Md., on November 3, 1967.

James A. Duff, assistant director,

lectured on GAO audit activities at the Military Assistance Institute on December 7, 1967.

Field Operations Division

Zane Geier, supervisory auditor, Atlanta, has been elected first vice president of the Atlanta Chapter of FGAA for fiscal year 1968.

Howard G. Cohen and *Gustave A. Johanson*, supervisory auditors of the Hartford office, Boston region, have been elected to serve as officers of the Hartford Chapter of FGAA for fiscal year 1968. Mr. Cohen will serve as vice president and Mr. Johanson as director.

Orlaf B. Hylle, auditor-in-charge of the St. Paul suboffice, Chicago region, participated as a member of the panel on *Finance and Accounting* at a Career Day held on November 2, 1967, at Mankato State College, Mankato, Minn.

W. J. Schad and *D. L. McCafferty*, supervisory auditors, Cincinnati, spoke at the October meeting of the Accounting Society, Villa Madonna College, Covington, Ky., on the subject "The Responsibilities and Functions of GAO."

D. J. Heller, supervisory auditor, Cincinnati, has been elected to serve as president of the Dayton Chapter of FGAA for fiscal year 1968.

At the University of Dayton, Mr. Heller participated in an Accounting Careers Council meeting held on October 11 and in the Accounting Careers Seminar conducted by the Accounting Club on November 29, 1967.

Herbert Larson, supervisory auditor, New York, has been elected director of communications and publicity of the Long Island Chapter of FGAA for fiscal year 1968.

Irwin M. D'Addario, assistant regional manager, Seattle, spoke at a Beta Alpha Psi meeting held on October 31, 1967, at the University of Washington. His subject was "Functions and Responsibilities of the General Accounting Office."

Charles L. Perry, auditor-in-charge of the Portland suboffice, Seattle region, has accepted an invitation from Portland State College to participate as a member on a council to advise the accounting faculty on curriculum, communications between faculty and community, special noncredit programs, and other related topics.

Leo H. Kenyon, supervisory auditor of the Portland suboffice, participated in an AICPA-sponsored seminar on "Horizons for a Profession" and its impact in accounting curriculums at Oregon colleges and universities. The seminar was conducted at the University of Oregon on November 3, 1967. Mr. Kenyon also spoke on November 28 to the Ashland, Oreg., Lion's Club concerning the mission of GAO.

Robert A. Higgins and *Leo Kenyon*, supervisory auditors of the Portland suboffice, have been elected to serve as officers of the Portland Chapter of FGAA for fiscal year 1968. Mr. Higgins will serve on the board of directors and as program chairman. Mr. Kenyon will serve as vice president.

Wendell A. Deadmond and *Paul W. Bryant*, supervisory auditors of the Anchorage suboffice, Seattle region, have been elected to the board of directors of the Anchorage Chapter of FGAA and will serve as research chairman and membership chairman, respectively, for fiscal year 1968.

D. L. Scantlebury, regional man-

ager, Washington region, addressed the members of the Air Force Advanced Management Program at George Washington University on December 7, 1967. The subject of his address was "The Organization and Functions of the General Accounting Office."

Transportation Division

On October 21, *Thomas E. Sullivan*, director, addressed the annual meeting of the Household Goods Forwarders Association at Frankfurt, Germany, on GAO's payment audit and field reviews of military household goods shipping activities.

Joseph P. Normile, deputy director, and *Walter L. Lohfeld*, staff assistant to the assistant director (audits), attended a meeting of the Government Traffic and Defense Liaison Committee, Regular Common Carrier Conference, American Trucking Associations, Inc., at Chicago, Ill., October 14. Mr. Normile spoke to the committee on the administrative problems for carriers and the Government in handling the rapid growth in Government transportation and what GAO is doing to simplify forms and procedures.

T. C. McNeill, assistant to the director, addressed the Southeastern Ac-

counting Conference of the Association of American Railroads at New Orleans, La., October 5 and 6, with particular emphasis on controversial rate issues involving railroad claims and paid bills. Mr. McNeill also participated in the meeting of the Freight Revenue Committee, Accounting Division, Association of American Railroads in St. Louis, Mo., November 13-15.

E. B. Eberhart, staff assistant to the assistant director (audits), attended the semiannual meeting of the Cargo Revenue Committee and the Passenger Revenue Committee of the Airline Finance and Accounting Conference, Air Transport Association, at Seattle, Wash., September 18-20. Mr. Eberhart addressed the meeting on the extension of the short form Government bill of lading to all modes of transportation, its planned use by civil agencies as well as military agencies, and the support required on airline bills for truck-air shipments.

On October 2, *Paul E. Lynch*, traffic manager, and *Charles C. Loomis*, chief of the motor audit branch, addressed the Defense Advanced Traffic Management Course at Fort Eustis, Va., on the GAO central audit of transportation payments and field reviews of agency traffic management operations.

New Staff Members

The following professional staff members joined the accounting and auditing divisions and reported for work during the period September 16, 1967, through December 15, 1967.

Civil Division	Elliott, Allen R.	Fayetteville State College
	Holliman, Clementine O. (Miss)	Atlanta University
	Lewis, Paul B.	Duquesne University
	Reddan, John A.	Benjamin Franklin University
	Slotsky, Joel L.	Duquesne University
Defense Division	Fixman, Kent L.	U.S. Merchant Marine Academy
International Division	Toxopeus, Douglas P.	American University
REGIONAL OFFICES		
Atlanta	Knight, Creighton W.	Florence State College
Detroit	Jellison, Theodore C.	Husson College
	Starr, Gilbert M.	Wayne State University
Kansas City	Baxter, John W.	Rockhurst College
Los Angeles	Kennedy, Terry L.	California State College at Los Angeles
	Williams, James G.	University of California at Los Angeles
	Yoder, Anna R. (Miss)	University of Albuquerque
New York	Calhoun, Bernice (Miss)	Atlanta University
Philadelphia	Alberts, Robert I.	Pennsylvania State University
	Walter, Harry J.	East Carolina University
San Francisco	Hansen, Hans	Golden Gate College
	Watanabe, Terry M.	Golden Gate College
Seattle	Jones, Scott N.	University of Minnesota
Washington (Falls Church)	Blanchette, Harry A.	University of Hartford

Readings of Interest

The reviews of books, articles, and other documents in this section represent the views and opinions of the individual reviewers, and their publication should not be construed as an endorsement by GAO of either the reviewers' comments or the books, articles, and other documents reviewed.

Congressional Control of Administration

By Joseph P. Harris; The Brookings Institution, Washington, D.C., 1964, 306 pp., hardback \$5.75.

Also published in softback by Anchor Books, Doubleday & Co., Inc., Garden City, N.Y., \$1.45.

In this book which was published in 1964, Mr. Harris discusses the various controls which the Congress of the United States applies to the administration of the departments and agencies of the executive branch of the Federal Government. He is concerned with what the controls are, how they work, and how they might be improved. Mr. Harris contends that the present system of control has developed more as an accidental byproduct of the legislative functions of Congress than by design. In his opinion, the responsibility for oversight of the individual departments and agencies is divided among numerous congressional committees and results in a large amount of duplication and overlapping and the lack of any clear responsibility. He concludes that a joint committee of the Congress or a joint legislative-executive commission is needed to reexamine the meaning of the oversight responsibility placed on Congress by the Constitution and to

conduct a searching inquiry into the legislative control of administration, the various forms it has taken, and its effect on executive action and responsibility.

Mr. Harris discusses the legislative controls under the following headings:

Control of executive organizational structure and programs.

Control of the purse.

Control through the audit.

Congress and the Civil Service.

The legislative veto.

Control by investigation.

Each section is presented in a similar manner—a brief discussion of the legislative control; a chronology tracing the evolution of the procedure; a discussion of the present usage of the control; an evaluation of the propriety, effectiveness, and shortcomings of the control; and suggestions for improvement. In discussing improvements, the author makes frequent reference to the legislative controls in existence in Great Britain. Overall, he seems to feel that the British system is superior to our own.

Of especial interest to the professional staff is the section on control through the audit. The section deals with the functions and performance of the General Accounting Office and

with what, in the author's opinion, are the shortcomings of our work.

Mr. Harris asserts that a regular audit of the expenditures of the executive agencies is potentially one of the strongest means of legislative control. In establishing criteria by which to judge the present system, the author lists the following conditions as essential to an effective auditing system:

1. The auditor must be independent of the executive and responsible only to the legislature.
2. It must be a post-audit; as a corollary, the auditor should not have responsibilities requiring him to take any part in decisions or transactions which he is subsequently to audit.
3. It should be comprehensive in scope, as intensive as necessary, and prompt so that the results of the audit will be laid before the legislative body while they are still timely.
4. The legislative body must be suitably organized to receive, consider, and act on the audit reports.

The author maintains that the auditing system in the Federal Government deviated in important respects from the above conditions and that Congress has never had fully effective use of this means of legislative control.

Mr. Harris argues that conditions (2) and (4) are not met in the present auditing system and that condition (3) is met only in part. A summarization of the author's criticisms and recommendations in these areas follows.

Post-audit

According to Mr. Harris, the failure to meet this condition is the most

serious weakness in the present auditing system. The heart of the power of the Comptroller General lies in his statutory authority to audit and settle the accounts of executive officers, including the making of legal interpretations incidental thereto, with his determinations final and conclusive upon the executive branch. This power of settlement and disallowance virtually forces the departments to go to the Comptroller General for preliminary discussion and advance approval of any types of expenditure about which there can be a question. As a result, the Comptroller General is a party to transactions of uncertain validity. This system weakens executive responsibility and denies Congress a truly independent post-audit. Congress would be better served if the Comptroller General confined his activities to auditing and reporting to Congress any failure on the part of the departments to account for funds entrusted to them, any expenditure or activity not authorized by law, any shortcomings in the accounting system, any financial practices that are not suitable or adequate, and any wasteful or improper uses of public funds.

Comprehensiveness, Intensity, and Promptness

In the author's view, the Comptroller General has appropriate freedom to make his inquiries as broad and as deep as necessary, but he tends to extend the scope of his audits to comprehend matters of departmental policy and organization that have little if anything to do with either probity or efficiency in the use of public funds. These areas are beyond the scope of an auditor's training and should be avoided by the GAO.

The GAO has improved the promptness of its audits, but many reports contain matters which the departments *claim* to have taken care of long ago (italic supplied). Instead of the present method of issuing reports at intermittent intervals, GAO should submit prompt reports on the state of accounts of each agency for each fiscal year (similar to the audit reports on Government corporations).

Organization of Congress

Mr. Harris believes that the Congress is not suitably organized to receive, consider, and act on audit reports. There is no single point of responsibility in either House for supervising the Comptroller General's work and systematically following up on his reports. Although the two Committees on Government Operations are the most important in this respect, the GAO also has close relations with the Appropriations Committees, does a great deal of work for individual Members, and from time to time works with various subject matter committees. Consequently, the resources of GAO are frequently used on investigations for the specialized and highly political purposes of committee chairmen and senior legislators, while the more prosaic but highly important jobs of reviewing audit reports, holding executive officers accountable, and considering improvements in financial management are neglected.

In the chapter on the audit, the author also presents a concise, informative, and interesting (though not unbiased) discussion of the British system of governmental auditing.

The reviewer makes no attempt to rebut any of Mr. Harris' contentions beyond presenting the following statement from the "Foreword" to the book.

"* * * The Honorable Joseph Campbell, Comptroller General of the United States, graciously read and criticized the chapter on the audit, though differing fundamentally with its findings and conclusions. * * *"

This book is interesting reading for GAO staff members not only for its presentation of a political scientist's views on the GAO but also for the information it contains on the appropriations process and on the workings of Congress in general.

Richard E. Chervenak,
SUPERVISORY AUDITOR,
CIVIL DIVISION.

EDITOR'S NOTE.—For a comparative analysis of national audit systems in which GAO fares better, see *The Accountability and Audit of Governments* by E. L. Normanton, a British civil servant, published in 1966 and reviewed in *The GAO Review*, Summer 1967, p. 115.

The Weapons Acquisition Process: An Economic Analysis

By Merton J. Peck and Frederic M. Scherer, Harvard Business School, Division of Research, Soldiers Field, Boston, Mass., 1962, 736 pp., \$10.

This book is the first published volume resulting from a 3-year study at the Harvard Business School on the development of advanced weapons. The purpose of the study, called the Weapons Acquisition Research Project, was stated as follows:

"* * * to determine the nature of the relationships between the government and

weapons contractors in the acquisition of advanced weapons and to analyze the effects of these relationships on weapons performance and the speed and cost of their acquisition * * *

Based primarily on case studies, including 12 weapon system programs—missiles and aircraft—and seven commercial product developments, this volume describes and analyzes the management structure and problems in planning, approving, and executing weapons programs.

The broad scope of the subject is indicated by the definition of the title. As defined by the authors: “weapons acquisition” includes the conception, development, and early production phases of technically advanced weapon systems and subsystems through fabrication and test of operational prototypes, detailed design and engineering for production and concurrent with the production phase, tactical version testing and modifications to improve performance and reliability; “process” emphasizes the flow of decisions and activities of Government agencies and defense contractors; and, “economic analysis” is the probing into how this process affects the quality, time, cost, and value outcomes of weapons programs.

Part I discusses the special features affecting the Government-industry relationship: the constant technical and strategic uncertainties; the difficulty of making accurate cost, development time, and quality predictions: and the nonmarket environment. In part II, the authors deal with the overall Government-industry structure within which the weapons acquisition process takes place.

The actual acquisition process is discussed in part III. Generally follow-

ing the sequence of activities in a weapons program, this part covers: the demand for, feasibility, and choice of a new weapon system; initiating a weapons program, technical uncertainties, and source selection; system optimization and tradeoffs between acquisition time, cost, and performance / reliability / maintainability objectives; subcontracting and make-or-buy decisions; the factors contributing to significant variances between the original predictions and the actual time, cost, and quality outcomes of development programs; the varying importance of the time, cost, and quality objectives in motivating effective Government and contractor performance.

The authors' primary objective for this volume is to create an understanding of the problems of Government-business relationships in weapons acquisition. Consequently, they do not present sharply drawn conclusions and recommendations. They reach a general conclusion that there is a need for improved in-house competence in gathering and analyzing data and in optimizing the time, cost, quality, and military value variables of a weapon system. But, in this volume, they do not examine in depth the operating-level instruments for directing and administering the weapons acquisition process. Their observations should, however, provide the reader with an overall understanding of the structure and process and some insight into certain basic problems and alternatives.

A brief description of two problems, as examples, and a partial listing of other problems should suffice to show the pertinence of the discussions to the work of the General Accounting Office.

1. The authors discuss the Government's difficulties in selecting new development products and sources, i.e., deciding which of the many weapons systems and subsystems merit development and objectively choosing between competitive contractor proposals. They note that the value of contractor-furnished information may be impaired by a lack of objectivity. This, they point out, may be due to the mixture of advocacy with the contractors' interpretations of factual data and their competitive optimism and exaggerations resulting in "science fiction" proposals to "buy into" new programs. Recognizing their inability to resolve technical questions, agency officials have sought help from scientific consultants and nonprofit contract organizations. The authors feel that the "think tanks" may be useful in state-of-the-art and technical feasibility matters but are of doubtful value in decisions required to control cost overruns and schedule slippages.

2. A common problem is the phasing of development and production, i.e., deciding when in the development program to commit funds to long lead-time tooling and components so that full-scale production can start as soon as the development is completed. The authors suggest basing the decision on careful consideration of these factors: (1) The military value of lead-time savings; (2) the probability of further technical changes; and (3) the additional cost of the overlapping and possibly wasted effort. Related to this problem is the authors' observation of intraorganizational conflicts and disparity of objectives among the military functional groups—the research

and development, procurement and production, and field service groups—and the need for an effective system of conflict identification and resolution.

3. Other problems probed by the authors include: (a) Establishing technical specifications too early in the development effort; (b) the large number of instances where "new" weapons are acquired on an "evolutionary" basis—basically the same technical concept and design approach—and provide only limited increments in value, rather than exploiting new concepts afforded by technological advances; (c) military agencies discouraging realistic cost estimates because their current budgets are inadequate to support a new program; (d) the tendency to develop quality and features beyond actual need; (e) the inability of program decision makers to quickly terminate a weapon acquisition when dictated by changes in military need or the greater feasibility and value of alternative weapons.

The authors' analyses of and observations on these and other problems make this volume,¹ in my opinion, interesting reading for those of us concerned with the effectiveness of expenditures of billions of dollars a year for new weapons.

David S. Glickman,
AUDIT MANAGER,
DEFENSE DIVISION.

¹ A second volume, published in 1964 and entitled "The Weapons Acquisition Process: Economic Incentives," examines the effects of competitive and contractual incentives on contractor behavior. Future plans are to conclude publication with a third volume which will discuss technical and financial administration problems and the suitability of Government arsenals and nonprofit corporations as substitutes for or supplements to the industrial contractor approach. It is anticipated that the third volume will contain conclusions on the study as a whole and recommendations on specific improvements.

Annual Awards for Articles Published in the GAO Review

The Comptroller General has approved the making of two \$250 cash awards for each calendar year for the best articles written by GAO staff members and published in the *GAO Review*. These awards will be presented during the awards program of the General Accounting Office held annually in June.

One award will be available to contributing staff members who are 31 years of age or under at the date of publication. The other award will be available to staff members who are over 31 years of age at that date.

Members of the staff in grade GS-16 or above are ineligible for these awards.

The awards will be made based on recommendations of a panel of judges selected by the Comptroller General. The judges will evaluate the articles

published from the standpoint of the excellence of their overall contribution to the knowledge and professional development of the GAO staff, with particular concern with such factors as:

- Originality of concepts.
- Quality of expression and organization of thoughts.
- Evidence of individual research performed.
- Pertinence to GAO operations and performance.

The first awards will be for the calendar year 1967, to be presented at the GAO awards program in June 1968.

This award will be known as the GAO Award for Significant Contribution to Financial Management Literature.

STATEMENT OF EDITORIAL POLICIES

1. This publication is prepared for use by the professional staff members of the General Accounting Office.
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