

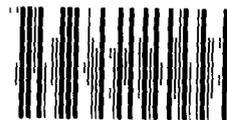
GAO

Report to the Secretary of the Army

May 1987

FINANCIAL MANAGEMENT

More Controls Needed Over Army's Obligation of Funds



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**Accounting and Financial
Management Division
B-214645**

May 14, 1987

The Honorable John O. Marsh, Jr.
The Secretary of the Army

Dear Mr. Secretary:

This is our report on a follow-up audit we made to assess the Army's efforts to prevent improper obligations of customers' operation and maintenance funds (O&M) by industrial fund activities. Such improper obligations preclude obligations for proper purposes and extend the availability of 1-year appropriations. The House Appropriations Committee has been concerned about a possible lessening of control over working capital funds such as these and other appropriated funds in the Department of Defense (DOD).

In a 1984 report¹ to the Chairman, House Appropriations Committee, we reported that the six DOD industrial fund activities we reviewed, including two Army Materiel Command (AMC) activities, carried over about \$35.7 million of O&M appropriations from fiscal year 1982 to 1983 through the improper use of industrial funds, thereby extending the life of 1-year appropriations which would have otherwise expired.

In response to our 1984 report, AMC initiated a work group to analyze conditions leading to the problems we identified. As a result of this work group's findings, AMC, in December 1985, strengthened its management controls by issuing a Letter of Instruction consolidating guidance and more clearly identifying responsibilities concerning fund obligation/deobligation. The objective of the instruction is to improve obligation procedures by addressing current and repetitive problems. As required by the instruction, AMC is monitoring the effectiveness of these changes by requiring activities to submit quarterly deobligation reports which could indicate abuses of the obligation process.

Our follow-up review at Army activities included in our prior review disclosed that, of the \$3.3 million in O&M funds carried over from fiscal year 1985 to 1986 we reviewed, \$2.9 million had been improperly obligated.

¹Improper Use of Industrial Funds by Defense Extended the Life of Appropriations Which Otherwise Would Have Expired (GAO/AFMD-84-34, June 5, 1984)

While we believe AMC's December 1985 instruction and its efforts to monitor implementation through quarterly deobligation reports should help prevent improper obligations in fiscal year 1986 and later, we believe some additional corrective actions are still needed. In particular, we believe the Army needs to take additional steps to reduce the risks associated with (1) the year-end obligation process not preventing recurring problems of improper obligations and (2) the quarterly deobligation reports not providing enough information to AMC headquarters officials to effectively monitor implementation at industrial fund activities. DOD concurs with our recommendations and plans to issue revised instructions that provide for more complete reporting of year-end obligations and for independent review of compliance with existing requirements. A complete copy of DOD's comments can be found in appendix I.

We also noted that AMC's October 1986 report to the Secretary of the Army on its evaluation of AMC's internal accounting and administrative control systems reported, as a material weakness, problems similar to those described in this report. We believe the corrective actions we have proposed should help AMC correct this weakness.

Background and Description of Working Capital Funds

A working capital fund is a revolving fund, operated as an accounting entity, under which assets are capitalized; income from its sale of goods and/or services is used to finance its continuing operations. The two basic types of DOD working capital funds are stock funds and industrial funds.

Defense industrial funds are modeled after businesslike operations except that as revolving funds they operate on a break-even basis. Industrial funds are designed to (1) provide an effective means for financing, budgeting, accounting for, and controlling costs of producing certain goods and services and (2) create a contractual (buyer-seller) relationship between industrial type activities and customers to provide management advantages and incentives for economy and efficiency. As revolving funds, they should be self-sustaining, that is, industrial fund activities should recover from customers the costs incurred in producing or contracting for goods and services ordered.

DOD uses industrial funds to finance various activities, such as maintenance depots, shipyards, and ordnance stations, that perform functions of an industrial or commercial nature. In fiscal year 1985, DOD obligated about \$25.1 billion—about 9 percent of its \$289 billion budget—through its industrial fund activities.

Congressional Concern Over Industrial Fund Operations

When reviewing the fiscal year 1983 DOD appropriation bill, the House Appropriations Committee expressed concern that the inherent flexibility in the financing techniques for working capital funds was being used to remove congressional oversight and control over some appropriated funds. The committee asked us to review DOD working capital funds and set forth several specific issues it wanted addressed. One of the committee's concerns was whether the life of appropriations was being extended through improper use of these funds.

In response to the committee's concerns, we visited six DOD industrial fund activities, including two Army activities, and reviewed \$192.5 million of the \$465.2 million in O&M funded carryover at these activities as of fiscal year 1982. Our objective was to determine if such carryover was generated by the proper use of industrial funds.

We reported to the committee in 1984 that industrial fund activities had improperly obligated customer O&M funds, thereby extending the availability of O&M appropriations beyond their 1-year life. About \$35.7 million of the \$192.5 million we reviewed had been carried over into fiscal year 1983 through such improper obligations. The Army industrial fund activities we reviewed accounted for about \$13 million of the \$35.7 million. As a result, the military services

- used and/or had available fiscal year 1982 O&M funds, which would have otherwise expired, to pay for fiscal year 1983 or later requirements; and
- inaccurately reported the true results of industrial fund operations and the status of O&M funds at fiscal year-end.

We also reported that management control problems existed in that industrial funds were improperly used because activities did not adhere to existing statutes and regulations governing industrial fund operations and the use of O&M appropriations. We concluded that DOD and the military services needed to strengthen management controls to better ensure that certain existing statutory and regulatory requirements were being met and that other requirements over industrial fund customer orders, especially at fiscal year-end, were being followed to ensure that only authorized amounts were carried over between fiscal years.

Army Industrial Fund Operations

The Army has four industrial fund groups: Depot System Command; Armament, Munitions, and Chemical Command; Missile Command; and Military Traffic Management Command. The Depot Systems Command

(DESCOM) is the largest of the four groups and was a focus of both our 1984 report and follow-up audit.

DESCOM, which reports to AMC, manages the Army's depot level maintenance program. DESCOM has 12 major depots, 7 of which are assigned maintenance as their major missions. For example, the Tobyhanna Army Depot is responsible for repairing and maintaining tactical electronic equipment, cameras, and projectors. The Sacramento Army Depot is responsible for strategic electronic and night vision equipment.

The depot system's financial structure is based on the revolving fund concept. Work on a maintenance order is started at a depot by using available capital in the industrial fund. The fund is replenished with customers' funds (for example, an Army major command, such as the Communications-Electronics Command) as work progresses and expenditures are reported. DESCOM acts as the bank—holding the customers' funds until billing is received from the depot.

Objective, Scope, and Methodology

The objective of our follow-up review was to assess the adequacy of corrective actions taken by the Army in response to our 1984 report. We conducted audit work at the following Army activities which were reviewed during our prior audit.

- U.S. Army Depot System Command (DESCOM), Chambersburg, Pennsylvania;
- U.S. Army Communications-Electronics Command (CECOM), Ft. Monmouth, New Jersey; and
- Army Depot, Tobyhanna, Pennsylvania.

At DESCOM, we determined the amount of the fiscal year 1985 O&M funded carryover for the Tobyhanna depot related to orders placed by CECOM. Of the \$29.2 million carryover amount as of September 30, 1985, we judgmentally selected eight project orders for review which accounted for \$3.3 million of this carryover amount. These eight orders were selected based on such factors as the large dollar value of each of the order's unexpended balance as of September 30, 1985, and whether each order continued to show a large unexpended balance as of April 30, 1986 (7 months after the close of fiscal year 1985). This selection criteria enabled us to (1) review a significant portion of the carryover amount (about 10 percent) and (2) select project orders where there was an indication, based on the order's large unexpended balance 7 months

after the close of the fiscal year, of some problems with the validity of the initial obligation.

To assess the validity of the eight project order obligations, we performed work at both CECOM and Tobyhanna. At both locations we interviewed officials knowledgeable about the orders and reviewed appropriate documentation to (1) determine whether O&M funds were being used to meet legitimate (generally referred to as "bona fide") needs of the fiscal year for which they were appropriated, (2) determine whether the items to be repaired were available to be worked on, (3) determine the status of work on the order, (4) identify reasons for any unexpended balance related to the orders, and (5) determine the capability of the depot to start and complete work on the orders within a reasonable period of time. Based on this information, we evaluated the eight project order obligations for compliance with Army Regulation No. 37-41, "Regulations Governing the Use of Project Orders," which prescribes policies and procedures concerning the issuance and acceptance of project orders.

We conducted our follow-up review between April and September 1986, in accordance with generally accepted government auditing standards.

Army Actions in Response to Our 1984 Report

In response to our 1984 report, the Headquarters, Department of the Army, sent a message to AMC reemphasizing existing regulations concerning the use of project orders and outlining possible causes of improper use of such orders. In addition, AMC initiated a work group to analyze conditions leading to problems with invalid obligations and improper execution of obligations.

In December 1985, based on the results of the work group findings, AMC issued a Letter of Instruction to all AMC activities who have responsibility to obligate funds. The instruction is intended to improve O&M obligation/deobligation procedures. It contains clear and detailed guidance addressing repetitive problems disclosed by past audits. For example, the instruction clearly defines such terms as bona fide need and explains such requirements as a depot having to be capable of starting a project order within a reasonable time.

As required by the instruction, AMC began monitoring improvements in the O&M obligation/deobligation area in 1986 by requiring activities to submit quarterly deobligation analyses based on a standard format.

These analyses are intended to disclose reasons for the deobligations and highlight problems requiring corrective actions.

The reason for the emphasis on monitoring deobligations was discussed in a February 1986 memorandum, signed by AMC's Deputy Chief of Staff for Resource Management, transmitting the Letter of Instruction to various Army activities. The memorandum noted that AMC headquarters had received audit reports containing findings about improper obligations. It also noted that activity commanders apparently had not sufficiently monitored the actions required by the reports' recommendations because many of the reports' findings were repetitive. The memorandum further noted that Army commanders are prone to compliment subordinates responsible for the obligation process when high obligational goals are reached, even though poor or haphazard obligation practices could have been followed to reach the goal. According to the memorandum, the validity of the original obligations will only be known when they are comprehensively reviewed at a later date.

In an August 1986 memorandum to the Army's controllers and other resource managers, the Comptroller of the Army stressed the importance of effective execution of funds appropriated for the Army. The Comptroller stated that the true measure of resource management performance is the Army's ability to deliver supplies and services when and where they are needed. According to the Comptroller, "obligations that result in follow-up deobligations rather than delivery of supplies and services are a waste of time and money."

Additional Actions Needed To Prevent Improper Obligations

Our follow-up review showed that the Army improperly obligated O&M funds and thereby extended the availability of appropriations which would have expired or been obligated properly for other purposes. Although AMC's Letter of Instruction should help prevent improper obligations in fiscal year 1986 and the future, we believe some additional actions are needed to further reduce the risk of such obligations.

Of the \$3.3 million carried over into fiscal year 1986 we reviewed at the Tobyhanna Depot, \$2.9 million was improperly obligated during previous fiscal years, thereby extending the life of O&M appropriations which would have otherwise expired or which would have been obligated for valid purposes. The improper obligations precluded the Army from making valid obligations because the O&M appropriations had expired by the time the funds were deobligated.

For example, during fiscal year 1986, the Army deobligated the total obligated amounts (about \$527,500) for three of the eight orders we reviewed and a portion of the obligated amount (about \$240,240) for two other orders. In addition, Army officials told us that they planned to deobligate the unexpended balance on a sixth order, amounting to about \$247,000. These deobligations took place or will take place after fiscal year 1985, the year in which the original obligations were made. Thus, the Army could no longer use these funds—about \$1,014,740—because the authority to obligate them had expired.

The following table summarizes information on the eight project orders we reviewed, including why their obligations were improper.

Table I: Projects Involving Improper Obligations of O&M Funds and Carryover to Fiscal Year 1986

Item description	Project order number	Obligated amount as of 9-30-85	Unexpended balance carried over into FY 86	Amount of obligation considered improper	Reason obligation was improper
Field-operated communications station, consisting of shelters for a transmitter, receiver, and message center	IG4FN240	\$268,921	\$246,726	\$246,726	Portion of the item to be repaired could not be located
Communications shelter used in field	IG503465	114,215	114,215	114,215	No legitimate requirement for this item in fiscal year 1985 since order duplicated another project order
Ninety-six public address systems (microphones, speakers, etc)	IG500306	288,294	288,294	288,294	Depot unable to start repair work on project within reasonable time
Repair of 25 shelters	IG508850	125,000	125,000	125,000	Project order was not specific about work to be done
Three landing control radar systems	IG504662	457,524	258,009	152,508	One of the three systems to be repaired could not be located
Communications components for missile systems	IG508801	2,180,000	1,823,328	1,823,328	Project order was not specific about the work to be done and exceeded authorized limitation of \$750,000 for this type order
Communications test equipment	IG504583	204,880	204,880	61,464	Due to limited repair equipment and other workload requirements, depot was unable to complete work required by order within the projected period
Communications sets used to test navigational equipment	IG5A4429	274,050	274,050	87,744	Depot was not properly involved in accepting this order and, as a result, funds needed for repair work were overestimated
Total		\$3,912,884	\$3,334,502	\$2,899,279	

For these eight cases, the major reasons funds were obligated contrary to requirements in Army Regulation No. 37-41 were

- the depot accepted orders for work which could not be started within 90 days and/or completed within the projected completion period;
- the depot accepted orders for work and continued to keep the order open, even though the item to be worked on, or parts of the item, could not be located;
- customer orders were not specific about the work to be done and, in one instance, the obligated amount of the order exceeded the authorized limitation for this type order; and
- the order, which duplicated another project, did not meet a legitimate need in the fiscal year in which it was placed.

We also noted that AMC's October 1986 report to the Secretary of the Army on its evaluation² of AMC's internal accounting and administrative control systems reported, as a material weakness, that project orders were not supported by valid obligations and costs. According to AMC, one of the causes of this weakness was that the prescribed guidance outlined in Army Regulation No. 37-41 was not being followed. AMC indicated this weakness would be examined during an upcoming compliance review.

While we recognize AMC's December 1985 Letter of Instruction clarifies and provides more detailed guidance, which should help prevent improper obligations in the future, we are concerned that providing additional guidance alone will not be sufficient. For instance, when we attempted to determine why the obligated amount exceeded authorized limitations for one case we reviewed, CECOM officials told us they were not aware of any authorized limitations, even though regulations that existed at the time and the Army's instruction, issued over 6 months before our discussions with these officials, clearly state such limitations. Further, Tobyhanna officials we interviewed indicated certain practices were being followed, such as the depot not rejecting any work and not showing the actual completion schedule, which also violated existing regulations as well as the December 1985 instruction. These practices can continue to cause improper obligations.

We believe one reason for the improper obligation is the long-standing practice of obligating available funds at year-end. For example, the

²These evaluations are made pursuant to the Federal Managers' Financial Integrity Act of 1982 (31 U S C 3512(b) and (c)), which requires department and agency managers to identify internal control and accounting system weaknesses that can lead to fraud, waste, and abuse in government operations

Internal Review and Audit Compliance Division at DESCOM issued a report in June 1984 on its audit of unliquidated obligations and fiscal year-end closeout procedures. This audit also found that neither materiel readiness commands nor DESCOM adhered to project order regulations. The report attributed the problems to the following:

“The Materiel Readiness Commands persistently authorized funds for programs which could not be started or could not be completed because of insufficient requirements or assets. This persistence, we believe, stemmed from a lingering practice of using all available program authority. DESCOM also demonstrated a similar persistence to obligate or retain funds. Reasons were first, to ensure the depots had sufficient workload to compensate for unexpected program delays, cancellations, or curtailments, and second, because obligating funds was viewed as obtaining the maximum benefit for the Army in use of resources....”

The Comptroller of the Army's August 1986 memorandum emphasized the importance of proper obligation practices and stressed that resource managers should not simply obligate funds at year-end to reach obligation targets.

We believe the Army needs to take additional actions to prevent improper obligations. One solution is to require an independent observer of the year-end obligation process at the depots to help ensure regulatory requirements are met. AMC's Letter of Instruction recommends, but does not require, that this independent observer be a representative from the Internal Review and Audit Compliance Division. We believe this is an excellent recommendation and that it should be made a requirement.

The Army's requirement that activities submit quarterly deobligation reports should also help to detect and correct improper obligations. We believe, however, that this process needs to be strengthened. For example, our review of DESCOM's deobligation report for the first quarter of fiscal year 1986, prepared in February 1986 as a result of the December 1985 Letter of Instruction, shows AMC's instruction was not completely followed. For instance, although AMC's instruction for the deobligation reports requires that explanations of deobligations explicitly identify why a deobligation occurred, DESCOM's report did not do so. DESCOM's report cited “assets did not materialize” (that is, the item to be repaired was not available) as an explanation for several deobligations even though AMC's instruction specifically cited this as an example of a poor explanation. Unless AMC strongly enforces its requirement regarding explanations of deobligations, these reports will be of little value.

Further, we believe AMC needs more information in the deobligation reports to enable it to effectively use the reports to monitor compliance with its instruction. For example, although activities are required to report deobligations by program year, AMC does not require the activity to indicate the date the initial obligation was made nor the date the deobligation was made. We believe AMC needs such information to help detect problems resulting from deobligations. For example, if AMC required activities to indicate the date of the initial obligation, it could readily detect whether a substantial number of deobligations were resulting from year-end obligations. If this proves to be the case, AMC could initiate corrective actions.

Conclusions

Our follow-up review disclosed that Army O&M funds at Tobyhanna were sometimes improperly obligated, thereby (1) causing deobligations of funds that could not be used for valid purposes because the authority to obligate the funds had expired and (2) extending the life of 1-year appropriations which would have otherwise expired.

While the Army has taken positive actions to correct some of the management control problems causing improper obligations, some additional actions are needed. We believe a major cause of improper obligations is the long-standing practice at year-end of obligating all available resources. To help correct this problem, we believe the Army needs to strengthen its year-end obligation process.

AMC's requirement that activities submit quarterly deobligation reports should also help to detect and correct obligation problems. However, we believe the Army needs to strengthen this process further to better ensure its effectiveness.

Recommendations

We recommend that the Secretary of the Army direct AMC to take the following actions to improve management controls over its obligation process:

- revise the December 1985 Letter of Instruction on O&M obligation/deobligation procedures to require an independent observer of the year-end obligation process to help ensure all regulatory requirements are met;
- reject any deobligation reports submitted by activities that do not adequately explain why deobligations were made; and

- review information currently required for deobligation reports to determine what additional information, such as the date of the initial obligation, is needed to better monitor the deobligation process.

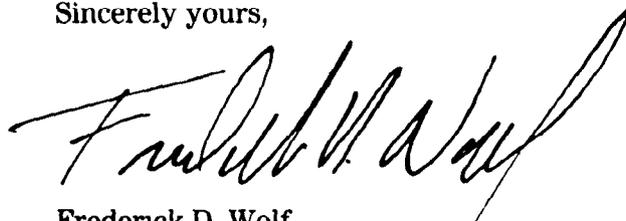
Agency Comments

In commenting on a draft of this report (see appendix I), DOD concurred with our recommendations and stated that the Army will revise its instructions and reporting requirements to provide for independent review of the year-end obligation process, better explanation of reasons for deobligations, and additional information needed to better monitor compliance.

The head of a federal agency is required by 31 U.S.C. 720 to submit a written statement on actions taken on our recommendations to the Senate Committee on Governmental Affairs and the House Committee on Government Operations no later than 60 days after the date of this report and to the House and Senate Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of this report.

We are sending copies of this report to the Director, Office of Management and Budget; to the Secretary of Defense; to interested congressional committees; and to other interested parties. Copies will be made available to others upon request.

Sincerely yours,



Frederick D. Wolf
Director

Comments From the Department of Defense

Note A GAO comment supplementing those in the report text appears at the end of this appendix



COMPTROLLER

ASSISTANT SECRETARY OF DEFENSE

WASHINGTON D C 20301

MAR 20 1987

Mr. Frederick D. Wolf
Director, Accounting and
Financial Management Division
United States General Accounting Office
Washington, D.C. 20548

Dear Mr. Wolf:

This is the Department of Defense (DoD) response to the General Accounting Office (GAO) Draft Report entitled, "FINANCIAL MANAGEMENT: Army Needs To Take Additional Actions To Prevent Improper Obligations Of Industrial Funds," dated February 2, 1987 (GAO Code 903081, OSD Case 7221).

The DoD basically concurs in the draft report. However, the title of the report and certain statements within the report create a misleading impression that the improper obligations occurred within the Army Industrial Fund rather than within the appropriation issuing project orders to the industrial fund. A more appropriate title would be, "FINANCIAL MANAGEMENT: Army Needs To Take Additional Actions To Prevent Improper Obligations Of Industrial Fund Customer Orders."

Detailed DoD comments on the findings and recommendations are included in the enclosure. Thank you for the opportunity to comment on the draft report.

Sincerely,

Enclosure

John R. Quetsch
Acting Assistant Secretary of Defense
(Comptroller)

See comment

GAO DRAFT REPORT - DATED FEBRUARY 2, 1987
(GAO CODE 903081) OSD CASE 7221

"FINANCIAL MANAGEMENT: ARMY NEEDS TO TAKE ADDITIONAL ACTIONS
TO PREVENT IMPROPER OBLIGATIONS OF INDUSTRIAL FUNDS"

DEPARTMENT OF DEFENSE COMMENTS

* * * * *

FINDINGS

- FINDING A: Congressional Concern Over Industrial Fund Operations: GAO 1984 Report. The GAO explained that a working capital fund is a revolving fund, operated as an accounting entity, under which assets are capitalized and income from its sale of goods and/or services is used to finance its continuing operations. The GAO observed that the two basic types of DoD working capital funds are stock funds and industrial funds. The GAO reported that in FY 1985, the DoD obligated about \$25.1 billion through its industrial fund activities, which represented about 9 percent of the \$289 billion Defense budget. The GAO noted that the House Appropriations Committee, when reviewing the FY 1983 DoD appropriation bill, expressed concern that the inherent flexibility in the financial techniques for working capital funds was being used to remove congressional oversight and control over some appropriated funds. One of the committee's specific concerns was whether the life of appropriations was being extended through improper use of Defense working capital funds. In response to the committee's concerns, in 1984 the GAO visited six DoD industrial fund activities, and found that industrial funds had, in fact, been improperly obligated, thereby extending the availability of Operations and Maintenance (O&M) appropriations beyond their 1-year life (OSD Case 6442). Specifically, the prior GAO report found that about \$35.7 million of the \$192.5 million reviewed had been carried over into FY 1983 through the improper obligation of industrial funds, with the Army industrial fund activities accounting for about \$13 million of the \$35.7 million. The GAO further found that as a result, the Services (1) used and/or had available FY 1983 O&M funds, which would have otherwise expired, to pay for FY 1983 or later requirements, and (2) inaccurately reported the true results of industrial fund operations and the status of O&M funds at fiscal year-end. The GAO also found that management control problems existed in that industrial funds were improperly used because activities did not adhere to existing statutes and regulations governing industrial fund operations and the use of O&M appropriations. In the 1984 report the GAO,

Now pages 2 to 3
See comment.

therefore, concluded that the DoD and the Services needed to strengthen management controls to better ensure that certain existing statutory and regulatory requirements were being met and that other requirements over industrial fund customer orders, especially at fiscal year-end, were being followed to ensure that only authorized amounts were carried over between fiscal years. (pp. 3-5/GAO Draft Report)

DOD RESPONSE: Partially concur. The statements in the report that "industrial funds had, in fact, been improperly obligated" and carryover occurred "through the improper obligation of industrial funds" are not correct. The statements should be corrected to state that the O&M appropriation, rather than the industrial fund, had been improperly obligated.

- **FINDING B: Army Actions In Response to GAO 1984 Report.** The GAO observed that in response to its 1984 report, the Headquarters, Department of Army, sent a message to Army Materiel Command (AMC) reemphasizing the existing regulations concerning the use of project orders and outlining possible causes of improper use of such orders. The GAO found that the AMC initiated a work group to analyze conditions leading to problems with invalid obligations and improper execution of obligations. The GAO further found that in December 1985, based on the results of the work group findings, the AMC issued a Letter of Instruction to all AMC activities having responsibility to obligate funds. The GAO specifically noted that the instruction contains clear and detailed guidance addressing repetitive problems disclosed by past audits. The GAO learned that, as required by the instruction, the AMC plans to monitor improvements in the O&M obligation/deobligation area by requiring activities to submit quarterly deobligation analyses based on a standard format, which is intended to disclose the reasons for the deobligations and highlight those problems requiring corrective actions. In addition, the GAO reported that in an August 1986, memorandum to the Army controllers and other resource managers, the Comptroller of the Army stressed the importance of effective execution of funds appropriated for the Army, stating that the true measure of resource management performance is the Army's ability to deliver supplies and services when and where they are needed. The GAO concluded that while the new AMC letter of instruction and the AMC effort to monitor its implementation should help prevent improper obligations in FY 1986 and later, some additional corrective actions are still needed. (p.2, pp 8-9/GAO Draft Report)

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and 6

DOD RESPONSE: Concur.

- **FINDING C: Follow-up Review At Army Activities.** The GAO conducted a followup review to assess the adequacy of corrective actions taken by the Army in response to the 1984

GAO report to prevent improper obligations of industrial funds that preclude obligations for proper purposes and extend the availability of 1-year appropriations. Based on its recently completed followup review, the GAO found that the Army continued to improperly obligate O&M funds and thereby extended the availability of appropriations, which would have expired or been obligated properly for other purposes. The GAO found, for example, that of the \$3.3 million carried over into FY 1986 at the Tobyhanna Depot, \$2.9 million was improperly obligated during previous fiscal years, thereby extending the life of O&M appropriations, which would have otherwise expired or which would have been obligated for valid purposes. The GAO observed that, for the eight project orders it reviewed, the following were the major reasons funds were obligated contrary to requirements in Army Regulations:

- the depot accepted orders for work that could not be started within 90 days and/or completed within the projected completion period; and
- the order, which duplicated another project, did not meet a legitimate need in the fiscal year in which the order was executed.

The GAO noted that in the October 1986 report to the Secretary of the Army (on its evaluation of the internal accounting and administrative control systems within AMC), the AMC cited as a material weakness, problems similar to those the GAO found in its followup review. The GAO concluded that the improper obligations continued to preclude the Army from making valid obligations because the O&M appropriations had expired by the time the funds were deobligated. (p. 2, pp. 9-12/GAO Draft Report)

DOD RESPONSE: Partially concur. The statement in the report that Army corrective action taken was "to prevent improper obligations of industrial funds" is not correct. The corrective actions taken were to improve obligation/deobligation procedures within the O&M appropriation.

- **FINDING D: Additional Actions Needed To Prevent Improper Obligations.** While the GAO recognized that the new AMC Letter of Instruction clarifies and provides more detailed guidance, which should help prevent improper obligations from occurring in the future, the GAO nonetheless found that providing the additional guidance alone will not be sufficient. The GAO cited, as an example, that when it [GAO] attempted to determine why the obligated amount exceeded authorized limitations for one of the cases reviewed, officials of the U.S. Army Communications-Electronics Command (CECOM) stated they were not aware of any authorized limitations, even though regulations in existence at the time and the Army's new AMC instruction

Now pages 1 and 6 to 8

See comment

(issued over 6 months before the discussions with these officials) clearly set forth such limitations. The GAO further found that one reason for the improper obligations is the longstanding practice at year-end to obligate available funds. The GAO observed that the August 1986 Comptroller of the Army memorandum emphasized the importance of proper obligations practices and stressed that resource managers should not at year-end simply obligate funds to reach obligation targets. While the new Army requirements for activities to submit quarterly deobligation reports should also help to catch and correct improper obligations, the GAO observed that this process needs to be strengthened. The GAO cited, as an example, that its review for the U.S. Army Depot System Command (DESCOM) deobligation report for the first quarter of FY 1986 (prepared in February 1986, as a result of the new instruction) shows that the AMC instructions were not completely followed. In addition, the GAO found that the AMC needs more information in the deobligation reports to enable it to effectively use the reports to monitor compliance with its new instruction. The GAO observed that although activities are required to report deobligations by program year, the AMC does not require the activity to indicate the date the initial obligation was made or the date the deobligation was made. The GAO generally concluded that while the Army has taken positive actions to correct some of the management control problems causing improper obligations, some additional actions are needed. In particular, the GAO concluded that the Army needs to take additional steps to reduce the risks associated with (1) the year-end obligations process not preventing recurring problems of improper obligations (i.e.-- requiring an independent observer of the year-end obligation process at the depots), and (2) the quarterly deobligation reports not providing enough information to AMC headquarters officials to effectively monitor implementation at industrial fund activities (i.e.-- indicating the date the initial obligation was made or the date the deobligation was made). (p. 2, pp. 13-15/GAO Draft Report)

Now pages 2 and 8 to 10

DOD RESPONSE: Concur.

RECOMMENDATIONS

- **RECOMMENDATION 1:** The GAO recommended that the Secretary of the Army require the AMC to revise its December 1985 Letter of Instruction on O&M obligation/deobligation procedures to require an independent observer of the year-end obligation process to help ensure all regulatory requirements are met. (p. 16/GAO Draft Report)

Now page 10

DOD RESPONSE: Concur. The Letter of Instruction will be revised to task internal review and audit compliance

representatives at all AMC activities to observe the year-end obligation process. These changes are anticipated to be published and distributed by the end of March 1987.

- RECOMMENDATION 2: The GAO recommended that the Secretary of the Army reject any deobligation reports submitted by activities that do not provide adequate explanation of reasons for deobligations. (p. 16/GAO Draft Report)

DOD RESPONSE: Concur. The Letter of Instruction will be revised to require rejection and return of any incomplete deobligation reports to respective commanding officers for adequate completion. These changes are anticipated to be published and distributed by the end of March 1987.

- RECOMMENDATION 3: The GAO recommended that the Secretary of the Army review information currently required for deobligation reports to determine what additional information (such as the date of the initial obligation) is needed to better monitor the deobligation process. (p. 16/GAO Draft Report)

DOD RESPONSE: Concur. The Letter of Instruction will be revised to include expanded reporting requirements to insure that the dates of obligation and deobligation are reported. These changes are anticipated to be published and distributed by the end of March 1987.

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Now page 11

The following is GAO's comment on the Department of Defense's letter dated March 20, 1987.

GAO Comment

We agree that the funds improperly obligated were O&M funds, and we have revised the wording throughout our report to more precisely reflect this fact.

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