Woman C.P.A.

Volume 19 | Issue 3 Article 3

4-1957

Task Force on Budget and Accounting - Hoover Commission

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TASK FORCE ON BUDGET AND ACCOUNTING — HOOVER COMMISSION

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You will probably recall that there have been two Hoover Commissions, and I think it might be well to review briefly the accomplishments of each of these.

The first Commission began its work in September 1947 and made its final report in May 1949. Its authority was limited to recommendations for the reorganization of departments and agencies. It made 273 recommendations, and some 196 of these were wholly or partially adopted by either executive or congressional action. 11 recommendations became obsolete or of diminished importance with the passing of time. This left 66 which were not acted on and many of them were referred to the second Hoover Commission for consideration.

The second Commission was authorized by Congress in July 1953. It made its final report at the end of June 1955. Its authority was enlarged to include recommendations on questions of policy. This commission appointed 19 Task Forces to carry on its studies.

At its peak, the Commission and the various Task Forces engaged a total of 525 full-time and part-time personnel. Many of these served without compensation. These Task Forces studied some 60 governmental departments and agencies, which represent about 95% of the expenditures in the Executive Department.

As a result of the studies by these Task Forces, the second Hoover Commission made 362 recommendations. Of these, 50 were of a character which might be submitted as Presidential Reorganization Plans to the Congress under the Reorganization Act of 1949, or which might be implemented by presidential executive order. A second group of recommendations totaling 145 were within the authority of the various departments and agencies to adopt if they wished. The third group of 167 recommendations were of a character that would require legislation.

The primary purpose of the Commission was to recommend methods by which savings could be made in federal expenditures. Thirteen of the Task Forces estimated savings. Five others said that savings were possible, but stated no amount. A grand total of the indicated savings would be more than $8 billion, but this is obviously an overstatement, since some of the estimates overlap. However, there was no doubt in the minds of the commissioners that the possible savings should be enough to balance the budget and in addition bring about a reduction in federal taxes. None of these savings contemplated a reduction in present defense programs, the elimination of useful public works, or a contraction of education, health and welfare programs.

In addition to these savings, the Commission pointed out that there are possibilities for recovering federal capital now invested in certain agencies which could be sold to private enterprises, such as the Federal Housing Administration, Federal Intermediate Credit Banks, Federal National Mortgage Association, Rural Electrification Administration, etc. Such recoveries might exceed $10 billion.

TASK FORCE ON BUDGET AND ACCOUNTING

The Task Force with which I am most familiar is that on Budget and Accounting, of which I was a member. The chairman of this Task Force was J. Harold Stewart, head of a public accounting firm in Boston and formerly president of the American Institute of Accountants. The other members were: Dudley E. Brown, Financial Vice President, Lockheed Aircraft Corporation; H. E. Humphreys, Jr., President and Chairman of the Board, U.S. Rubber Company; Christian E. Jarchow, Executive Vice President, International Harvester Company; Gwilyn A. Price, President, Westinghouse Electric Corp.; Kenneth C. Tiffany, Vice President, Burroughs Adding Machine Company; and J. David Wright, President, Thompson Products, Inc.

Our first meeting was with Mr. Hoover two days before Christmas 1953. Subsequent meetings were held in Washington, Chicago and New York.

Our Task Force engaged two full-time staff directors and a number of consultants.

We presented 31 recommendations (later consolidated to 25) for improvements in budgeting or accounting. We estimated that the introduction of these improvements would result in an annual saving of at least \$4 billion or $8\frac{1}{2}$ per cent of the controllable budget expenditures.

I shall not attempt to review each of the 31 recommendations, but will comment on a few of them.

First, let us talk a bit about the budget itself. It contains over 1,200 pages of detailed information—about the size of the Chicago telephone directory. In addition, schedules of personnel positions are included as a separate appendix to the document.

The budget is presented in great detail. There are many items of only \$1,000 each. While some progress has been made in program budgeting, there still remains much to be done to indicate broad programs and objectives.

The preparation of the budget begins, in some agencies, eighteen months prior to the beginning of the fiscal year to which the budget relates. The lengthy cycle required for development and enactment of the budget is a basic defect in the government's budget processes and tends to make the budget out of date before it goes into effect.

The Task Force on Budget and Accounting recommended that the length of time required for developing budget estimates should be reduced, both in the agencies and in the Budget Bureau. We also recommended that agency budgets be presented in more simplified and concise form and be better supported by factual information in order that the staffs of the Congressional Committees be able to complete their reviews in shorter time.

The federal budget is essentially a "cash" budget and is prepared on the basis of the estimated "obligations" to be incurred during the budget year.

The budget fails to take into account inventories and other working capital available at the beginning of the year which may be consumed in the programs of the budget year. Neither does it reflect working capital which may become available during the budget year and which will be carried over to a subsequent year.

Under present procedures there is no effective control over expenditures either by the Congress or in the Executive Branch. This loss of control is attributable to several factors which can be summarized as follows:

> Appropriations are enacted in terms of the obligational authority required to carry out approved programs, some of which relate to long lead time programs.

There is a tendency in Executive agencies to state the obligations incurred at the highest possible figures since this action strengthens the budget requests for the following year.

The obligation basis of appropriations produces an incentive in the agencies to use all available obligational authority prior to the date when it otherwise would lapse for obligating purposes. Such action tends to support agency budget requests for the following fiscal year.

As a result of this procedure, there is a substantial amount of unexpended appropriations carried forward annually into the following year:

(In Billions)	Amount brought forward into the year
1950	\$11.5
1951	14.1
1952	50.3
1953	68.8
1954	78.4
1955	68.0
1956 (estimated)	53.9

This carryover of unobligated authority for multiple year programs arises from the practice of making full budget provision at the outset for such programs, which funds remain available until expended.

There has been no effective post review of such appropriations by either the Bureau of the Budget or the Congress. The procedure has been to review in minute detail a new program for the budget year under consideration with little consideration of past performance. This inadequacy applies particularly to military procurement.

As a means of controlling government expenditures more directly and effectively we proposed that the present budget, which is in terms of obligational authority, be replaced by an annual expenditure budget.

Under an annual expenditure budget an agency would submit initially a properly described program showing the total funds required for its completion, projected in terms of years. The Congress, if it approved the program, would enact an annual appropriation for the estimated expenditures required for the year under consideration. In addition, the Congress would give the agencies contracting authority for the amount required during the first year for forward contracting beyond the budget year. The Executive Branch and the Congress thereafter would review the program annually from the standpoint of costs and accomplishments, both completed and projected, and grant additional authority.

For example, let us assume that the Navy is asking for legislative approval to construct a ship. The work is to be accomplished over a four-year period at a total estimated cost of $150 million, of which $20 million is to be spent in the first year.

The Department of the Navy, under the plan proposed, would furnish complete information regarding the entire project. They would ask for an appropriation of (say) $20 million for the current budget year, to cover goods and services to be received during the first year, they would request authority to make contracts for long lead items, and they would show the estimated costs to be covered by future appropriations.

Congress would pass an annual appropriation on a "goods and services received" basis of $20 million to cover the first year's estimate. In addition, the Congress would grant contracting authority in the amount needed for long lead time items. This would provide authority for the Navy to proceed with the work and enter into forward contracts.

In its annual appropriation request for the second year the Navy Department would submit experience data showing how construction is proceeding, together with latest cost information. The Department might request an annual appropriation of, say, $50 million, their estimate of goods and services to be received in the second year. However, because of a lower priority given to Naval construction in that budget year and a decision to stretch out the project, the Congress might reduce the Department's request for the second year's appropriation to $35 million.

Under present practice an appropriation for the entire $150 million would be made at the outset. Except as the Congress might rescind a previous authority, it has lost control over the rate of construction and expenditures.

We believe that adoption of the proposal for an annual expenditure budget would permit more effective control over government expenditures. It is recognized that adoption of this proposal will require administrative changes in the government's budgeting and accounting procedures, particularly in the Department of Defense.

There is another situation which leaves Congress little control of the budget. This arises when Congress enacts legislation for undertakings which leave the appropriations committees little discretion as to the amounts to be appropriated.

For example, in fiscal year 1955 there were major programs aggregating $15.3 billion or 24% of the total budget; which were relatively uncontrollable. This included $6.6 billion for interest which, of course, is based on the size of the debt and the applicable interest rates; $3.5 billion for veteran compensation, pensions, and benefit programs; $2.2 billion for agriculture price support; $1.4 billion for grants to states for public assistance; and $0.6 billion for Federal-aid highway grants; and approximately $1.0 billion for nine other programs of like character.

Generally, this type of basis legislation either commits the Federal Government to specified expenditures or prescribes formulae which automatically determine the amounts of the appropriations required. Agricultural legislation, for example, requires that prices shall be supported at certain levels, which in turn depends upon the state of the markets for agricultural products. Legislation granting funds to the states for public welfare assistance prescribes the rates at which assistance shall be provided to claimants, and appropriations are governed by the number of claimants. Similarly, veterans legislation establishes rates for readjustment allowances, and expenditures under such programs depend upon the number of qualifying veterans.

Through the enactment of such authorizing legislation which involves commitments, the Congress has diluted effective control over an important area of government spending. Therefore, the burden of making adjustments in budget expenditures tends to fall upon the more controllable programs.

We recommend that whenever legislation was passed committing the government to continuing expenditures for special programs which are not susceptible to the usual budgetary control, it be enacted for a limited term in order to obtain periodic Congressional review of its usefulness. Also, that the Bureau of the Budget keep such programs under continuing review, and the President's budget contemplate amendments to them when their operation conflicts with current budgetary policy.

Let's discuss another situation regarding government expenditures. When Congress passes appropriations and grants the funds needed, the responsibility for budget execution lies within the agencies and the Bureau of the Budget.

The Bureau's control over appropriated funds is based upon a system of agency financial reports. It operates primarily through the apportionment of funds, the establishment of reserves, review and approval of agency regulations governing control of funds, analysis of audit reports, and such specialized measures as regulations designed to discourage excessive year-end purchasing ("June buying").

The rate at which appropriations may be obligated by the agencies is regulated by apportionment of obligational authority (usually on a quarterly basis) after consideration of agencies' requests. These apportionments are further subdivided by the agencies into allotments to their organizational subdivisions. Depending upon the complexity of an agency's organization, the allotments are further divided and suballotted to lower levels. This results in a multitude of pockets of obligational authority, and each allotment constitutes a ceiling of expenditures which cannot be exceeded.

In the Department of Defense, it is impossible to obtain readily a reliable estimate of the number of allocations, allotments, suballotments and administrative subdivisions of allotments which are in active use and for which accounts are kept. At a minimum there were over a hundred thousand in that department alone.

There was a tendency in the government to attempt management control through this device of controlling funds. The allotment system in itself does not usually provide management with the financial information required for measuring the efficiency and economy with which funds are used. Actually, the allotment system places emphasis on the ability to live within allotments rather than the usual management criterion of performance in terms of cost. Another defect in the allotment system is the inherent incentive to spend all allotted funds in order to support succeeding allotment requests. A more positive approach is needed under which an appraisal of both good and poor performance can be brought to light.

This system of multiple allotments creates another condition. Under the Anti-Deficiency Act, whenever an allotment is exceeded the agency must render an immediate report to the President, through the Director of the Bureau of the Budget, and to the Congress.

This necessitated the reporting to the President and the Congress of a large number of technical violations where administrative divisions and subdivisions of allotments have been exceeded. These violations are attributable to the unnecessarily complicated and detailed allotment structure.

Now for another phase of this problem. Officers responsible for the disbursement of funds are personally liable to the government for proper performance of their financial duties. This personal liability attaches to any violations of statutes, even though they be unintentional and even though the officer himself did not make the mistake which resulted in the violation.

Therefore, accountable officers frequently seek advice as to the application of laws to the facts in a particular case in which he is called upon to make a payment. The natural tendency is for them, in self-protection, to request an advance decision from the General Accounting Office with respect to any case in which they have the slightest question as to the legality of a payment. They are, in consequence, overcautious in the performance of their duties. As an example, the Claims Division of the General Accounting Office received about 29,000 vouchers under open appropriations from the military's accountable officers during fiscal year 1954, which, according to a GAO analysis, did not involve any doubtful or complex matters.

It is unduly harsh to hold an officer liable where he has acted in good faith and shown reasonable diligence. Moreover, the expense involved in investigating and disposing of exceptions involving alleged violations is not warranted.

We, therefore, recommended that accountable officers be relieved of financial liability except where losses resulted from their gross negligence or fraud.

In the field of governmental accounting there is much to be done. The systems used in some departments are antiquated by industrial standards. Accounting in the Federal Government is still mainly concerned with cash transactions and has not kept pace with the needs of management arising from increasing complexity of government operations. There is a great deal of duplication in record keeping. For example, the Treasury Department maintained about 7,000 detailed accounts which duplicated in large measure similar records maintained in other agencies.

In 1950 Congress passed the Budget and Accounting Procedures Act which provided, among other things, that . . . "The Comptroller General of the United States, the Secretary of the Treasury, and the Director of the Bureau of the Budget conduct a continuous program for the improvement of accounting and financial reporting in the Government."

While a means of coordination was thus provided, there was in fact no central guidance or control in the Executive Branch over accounting performance.

The essence of the problem as we saw it, was what form of organization is needed to bring about improvements in government accounting and where should it be placed, preferably without setting up a new agency?

This function did not belong in the Treasury Department where there is enough to be done in fiscal accounts without assuming responsibility for central direction of accounting in all other agencies. Neither did it belong in the General Accounting Office. The Comptroller General is the auditor and critic of the accounting and financial management of the Executive agencies. The General Accounting Office is an independent agency in Legislative Branch of the Government, having wide powers of examination and reporting directly to the Congress. This independence should not be diluted. The Comptroller General should not be directly involved in the administration of the Executive agencies.

The logical place for this function, we felt, was in the Bureau of the Budget. The Bureau had four principal staff offices, each under an Assistant Director, namely:

Office of Budget Review
Office of Legislative Reference
Office of Statistical Standards
Office of Management and Organization

In order to meet his accounting responsibilities we proposed that there be established under the Director of the Budget a fifth staff office headed by an Assistant Director for Accounting and that such office be named "Office of Accounting".

This Assisant Director for Accounting should be an accountant well qualified by training and experience to perform this function. He should have ability and reputation such as will gain respect and enlist cooperation throughout the Executive agencies.

His duties should be:

1. To develop an overall plan for accounting and reporting for all of the departments and agencies, consistent with broad policies and standards prescribed by the Comptroller General.
2. To assist in the introduction of modern accounting methods in the Executive agencies.
3. To set reasonable but definite time schedules for performance and to watch progress.
4. To stimulate the building of competent accounting and auditing organizations in the Executive agencies and to assist actively in the selection, training and retention of capable personnel.
5. To report at least annually to the Director of the Bureau with respect to the status of accounting in each of the Executive agencies.

The performance of these duties would require him to maintain close cooperation with the General Accounting Office and the Treasury Department in the development of Government accounting problems. It would also require him to maintain a small but select staff of well-qualified assistants to operate with the various Executive agencies.

In this connection, our Task Force also recommended the appointment of a competent comptroller in each of the important departments and agencies.

Under our concept of comptrollership, he would occupy an advisory role in management. While he would not make management decisions, the comptroller should be invaluable as an adviser and interpreter to management. As a result of his intimate knowledge of the financial facts, the comptroller can assist management in reaching sound decisions.

We recommended that the comptroller should be directly responsible to the head of the agency in order to assure independence and objectivity in the performance of his duty. He should also be responsible to the Assistant Director for Accounting in the Bureau of the Budget for the observance of the standards and policies laid down by him. He should be a principal officer whose duties are, as they would be in private industry:

1. To set up adequate accounting and auditing systems.
2. To recruit, train and develop qualified accounting personnel.
3. To point out opportunities for economies.
4. To furnish reliable financial reports for the management of the agency, for Congress, and for other Executive departments.
5. To interpret and advise upon significant aspects of the financial reports.
6. To direct the preparation and execution of budgets in the agency.

Agency accounting has been limited in most cases to accounting for cash expenditures. We recommended that modern accounting systems be installed and maintained on the accrual basis. Such systems should permit the preparation of periodical financial statements for each agency showing what it owns and what it owes, as well as the current costs of the various operations within it.

While it would always be necessary to account for expenditures of appropriated funds, a system of accrual accounting would also make possible a record of the dollar value of inventories, of real estate and other property, as well as their application to costs.

Until all of the departments have adequate accounting systems under competent supervision, it will not be possible to know the real costs of operating the Federal Government or to prepare reliable combined reports for the entire government showing the accrued receipts and expenditures of the Federal Government, the fixed assets owned by it (real estate, buildings, equipment, etc.), the inventories and other working capital of the government, as well as the obligations payable by the government. In other words, if we expect to produce the kind of financial statements which every modern business institution must have, we felt it would be necessary to modernize the government accounting systems so as to know the accrued revenues and costs, as well as assets and liabilities of the Federal Government.

As for the saving of $4 billion set out in our report, it is not possible to pinpoint this saving and indicate in detail where it may be accomplished. Necessarily, much of it must come in the Department of Defense, but we did not contemplate any reduction in the defense program. The saving can be brought about by better methods, better control, elimination of duplication in effort, reduction of excessive stocks of goods, greater efficiency and better organization.

So much for the work of our Task Force on Budget and Accounting. You are naturally interested in what has happened since our report was presented in June 1955.

A great deal has been accomplished since then—some by legislation, some by executive order, and some by voluntary adoption by the agencies.

The legislation passed included, among other things, the adoption of accrual accounting, but it did not provide for the adoption of accrual expenditure appropriation procedure. President Eisenhower has announced that he will recommend to the next Congress additional legislation to accomplish this further step.

A new staff office of accounting under the Director of the Bureau of the Budget has been set up, headed by an assistant Director for Accounting. It is under the direction of Percy Rappaport, formerly in public accounting for many years, and a very able person. He and his staff are hard at work and have already brought about worthwhile improvements.

Meanwhile many of the agencies have selected competent comptrollers and progress is being made there as well.

A few months ago our committee met with representatives of the Bureau of the Budget, General Accounting Office, Treasury Department and Defense Department, and I was encouraged with the accomplishments to date and the spirit with which this whole program was being pursued. Obviously, the program will take a lot of time —it cannot be done overnight, but I am very hopeful about the eventual outcome.

In closing, I should like to pay tribute to the Chairman of the Commission, Mr. Herbert Hoover. He is a most remarkable man of tremendous capacity. It was amazing to see what an intimate knowledge he had of the problems we were dealing with, as well as the overall problems arising out of the functional organization of the entire Federal Government. He has made a great contribution toward better government.

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(Continued from page 4)

"With respect to increasing knowledge about the effective development and utilization of womanpower . . .

1. Universities, foundations, and government encourage and support research dealing with the impact of the increased employment of women upon family life, the rearing of children, and the self-development of women; upon the process of occupational choice among both younger and older women; upon the prosperity of the economy and living standards; and upon the availability of volunteer workers for community service functions
2. The Secretary of Labor initiate a comprehensive study of the maximum use which could be made of the actual and potential resources of womanpower in the event of a national emergency
3. The Secretary of Labor take the initiative in establishing a commission to review, in the light of recent changes in technology and the economy and in the composition of the female labor force, the consequences and adequacy of existing Federal and state laws which have a direct bearing on the employment of women."