

DOCUMENT RESUME

02616 - [A1612600]

Unauthorized and Questionable Use of Appropriated Funds to Pay Transportation Costs of Non-Appropriated-Fund Activities. LCD-76-233; B-148581. June 3, 1977. 15 pp. + 5 appendices (11 pp.).

Report to the Congress; by Elmer B. Staats, Comptroller General.

Issue Area: Facilities and Material Management: Federal Transportation of Things (704).

Contact: Logistics and Communications Div.

Budget Function: National Defense: Department of Defense - Military (except procurement & contracts) (051).

Organization Concerned: Department of Defense.

Congressional Relevance: House Committee on Armed Services; Senate Committee on Armed Services; Congress.

Authority: DOD Directive 7060.3.

Non-appropriated-fund activities provide members of the armed services with goods and services not furnished by the Government. These activities include post exchanges, liquor stores, clubs, and recreational facilities. The activities operate primarily with funds generated from their own operations, but the Department of Defense (DOD) gives them some appropriated-fund support. Findings/Conclusions: In addition to the support authorized by DOD, millions in appropriated funds have been spent for transportation support that should have been funded by the non-appropriated-fund activities.

Non-appropriated-fund activities did not always reimburse DOD for using the Defense Transportation System. Unreimbursed costs primarily related to the overseas transportation of foreign-made merchandise and personal property. The Navy financed overseas land transportation costs with appropriated funds, a practice inconsistent with Army and Air Force practices.

Recommendations: The Secretary of Defense should: direct the non-appropriated fund activities to reimburse the appropriation for ocean costs incurred in excess of those applicable to shipment through the port of embarkation nearest the overseas destination; institute procedures for assuring that non-appropriated fund activities are properly charged for reimbursable transportation services, considering the need for both manual and mechanical controls over the correct use of transportation account codes; recover the unreimbursed costs for improper appropriated fund support provided non-appropriated-fund activities; direct the Secretary of the Navy to stop using appropriated funds for overseas land transportation of non-appropriated-fund property; and revise the applicable DOD directive to prohibit any foreign-made merchandise shipments from receiving support. (Author/QM)

1600
02616
UNITED STATES
GENERAL ACCOUNTING OFFICE

REPORT TO THE CONGRESS

BY THE COMPTROLLER GENERAL
OF THE UNITED STATES

Unauthorized And Questionable Use Of Appropriated Funds To Pay Transportation Costs Of Non-Appropriated-Fund Activities

Department Of Defense

Post exchanges and other non-appropriated-fund activities received millions of dollars of transportation support from the Department of Defense that should not have been financed with appropriated funds. Improper routing of shipments, poor billing and review procedures, inconsistent payment practices, and failure to follow Defense's policies all contributed to the unauthorized payments.

Defense has since billed the non-appropriated-fund activities for many of the reimbursable costs. GAO is recommending that Defense recover additional costs and take action to preclude the future unauthorized use of appropriated funds.



COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

B-148581

To the President of the Senate and the
Speaker of the House of Representatives

This report describes how the Department of Defense has been providing non-appropriated-fund activities with appropriated-fund support by paying for unauthorized transportation services. It discusses Defense's need to better control appropriated funds and to recover expenditures already made.

We made our review pursuant to the Budget and Accounting Act, 1921 (31 U.S.C. 53), and the Accounting and Auditing Act of 1950 (31 U.S.C. 67).

Copies of this report are being sent to the Director, Office of Management and Budget; the Secretary of Defense; and the Secretaries of the Army, Navy, and Air Force.

A handwritten signature in cursive script, reading "James A. Stuebel".

Comptroller General
of the United States

COMPTROLLER GENERAL'S
REPORT TO THE CONGRESS

UNAUTHORIZED AND QUESTIONABLE
USE OF APPROPRIATED FUNDS TO
PAY TRANSPORTATION COSTS OF
NON-APPROPRIATED-FUND ACTIVITIES
Department of Defense

D I G E S T

Non-appropriated-fund activities provide members of the armed services with goods and services not furnished by the Government. These activities include post exchanges, liquor stores, clubs, and recreational facilities.

The activities operate primarily with funds generated from their own operations, but the Department of Defense gives them some appropriated-fund support.

GAO found that, in addition to the support authorized by the Department, millions in appropriated funds have been spent for transportation support that should have been funded by the non-appropriated-fund activities. Following are reasons for these improper payments.

The Department's policy requires that merchandise purchased in the United States be moved at non-appropriated-fund expense to the port of embarkation nearest the overseas destination. This was not always done.

Non-appropriated-fund activities saved land transportation costs by selecting ports closer to the merchandise sources, but appropriated-fund costs increased because of the longer ocean distances to the overseas destinations. (See ch. 2.)

Non-appropriated-fund activities did not always reimburse the Department for using the Defense Transportation System when appropriated-fund support was not authorized. Unreimbursed costs for the period 1964-76 totaled over \$7 million because reimbursable transportation account codes had not been assigned or properly charged.

These codes are on the shipping documents and are the basis for determining who should be billed for transportation costs.

The unreimbursed costs primarily related to the overocean transportation of foreign-made merchandise and personal property. After GAO brought the matter to Defense's attention, it billed the non-appropriated-fund activities for about \$3.6 million of these costs. (See ch. 3.)

The Navy financed overseas land transportation costs with appropriated funds. This practice was inconsistent with the Army's and Air Force's practices of not financing these costs. (See ch. 4.)

Foreign-made merchandise was shipped from New York to Hawaii by the Defense Transportation System at appropriated-fund expense. Defense permitted using these funds because U.S. customs duties and taxes had been paid on the merchandise.

This practice is contrary to Defense's policy of promoting the sale of U.S. goods and services in overseas non-appropriated-fund activities. GAO believes this practice should be stopped. (See ch. 5.)

GAO recommends that, to correct these deficiencies, the Secretary of Defense:

--Direct the non-appropriated-fund activities to reimburse the paying appropriation for ocean costs incurred--for all past and future shipments--in excess of those applicable to shipment through the port of embarkation nearest the overseas destination. (See ch. 2.)

--Institute procedures for assuring that non-appropriated-fund activities are properly charged for reimbursable transportation services, considering the need for both manual and mechanical controls over the correct use of transportation account codes. (See ch. 3.)

- Recover the unreimbursed costs for improper appropriated-fund support provided non-appropriated-fund activities. (See ch. 3 and app. I.)
- Direct the Secretary of the Navy to stop using appropriated funds for overseas land transportation of non-appropriated-fund property. (See ch. 4.)
- Revise the applicable Defense directive to prohibit any foreign-made merchandise shipments from receiving appropriated-fund support. (See ch. 5.)

Defense concurred with GAO's first and second recommendations. With respect to the third recommendation, Defense has billed the exchanges about \$3.6 million, of which \$2 million has been collected. It has taken no action as yet to bill \$1.1 million of unreimbursed costs and does not concur that \$2.3 million spent for shipping foreign-made merchandise to Vietnam and Thailand should be billed.

Defense said the issues involved in GAO's recommendations to stop appropriated-fund support for overseas land transportation and imported merchandise were being studied.

C o n t e n t s

		<u>Page</u>
DIGEST		i
CHAPTER		
1	INTRODUCTION	1
2	IMPROPER ROUTING OF SHIPMENTS RESULTS IN MORE APPROPRIATED-FUND SUPPORT THAN THAT AUTHORIZED BY DOD	3
	Agency comments and our evaluation	4
	Recommendation	4
3	PROCEDURES NEEDED TO ASSURE REIMBURSEMENT FOR USE OF THE DEFENSE TRANSPORTATION SYSTEM	5
	Foreign-made merchandise	6
	Personal property	7
	Other services	8
	Agency comments and our evaluation	9
	Conclusion	9
	Recommendation	10
4	NAVY'S USE OF APPROPRIATED FUNDS FOR OVERSEAS LAND TRANSPORTATION SUPPORT IS INCONSISTENT WITH OTHER SERVICES' PRACTICES	11
	Agency comments and our evaluation	11
	Recommendation	12
5	TRANSPORTATION SUPPORT FOR IMPORTED FOREIGN-MADE MERCHANDISE IS CONTRARY TO DOD'S POLICY	13
	Agency comments and our evaluation	13
	Recommendation	14
6	SCOPE OF REVIEW	15
APPENDIX		
I	Summary of estimated amounts of appropriated funds erroneously used by non-appropriated-fund activities, as of December 31, 1976	16
II	Letter dated August 2, 1976, from the Assistant Secretary of Defense (Comptroller)	17

APPENDIX		<u>Page</u>
III	Letter dated March 3, 1975, from the Transportation and Claims Division, GAO	20
IV	Letter dated July 23, 1976, from the Assistant Secretary of Defense (Man- power and Reserve Affairs)	23
V	Principal officials responsible for activities discussed in this report	25

ABBREVIATIONS

DOD	Department of Defense
GAO	General Accounting Office
OMB	Office of Management and Budget

CHAPTER 1

INTRODUCTION

Non-appropriated-fund activities provide members of the Armed Forces with goods and services not furnished by the Government. From initially small operations, the activities have grown into giant systems with a combined annual sales volume in the billions.

The best known of these activities are the post exchanges; namely, the Army and Air Force Exchange Service, the Navy Resale System Office, and the Marine Corps Exchange Service. Other activities include liquor stores, clubs, and recreational facilities.

Although the non-appropriated-fund activities were created by the Department of Defense (DOD) and continue to be governed by DOD regulations, the activities are organizations technically separate from the military. They do, however, retain a status as instrumentalities of the Federal Government.

The non-appropriated-fund activities operate primarily with funds generated from their own operations. They receive appropriated-fund support for, among other things, the overocean transportation of American-made merchandise in the Defense Transportation System--a term applied to the services provided or procured by the Military Airlift Command, the Military Sealift Command, and the Military Traffic Management Command.

Although annual DOD appropriation acts have generally provided funds for welfare and recreation, they have not specifically provided funds for transportation of merchandise for resale through these activities. Also, as we pointed out in our report to the Congress "Should Appropriated Funds Be Used for Transportation Procured Specifically for Armed Forces Exchange Goods?" (E-169972, Aug. 6, 1973), we believe a reasonable interpretation of the basic statutes authorizing the use of appropriated funds for transportation of exchange goods permits such only when the goods are carried on conveyances owned, leased, or chartered by the Government, where the Government is already obligated to pay for the space whether it is used or not.

DOD, however, relies on other statutes, longstanding practice, and congressional awareness of that practice as the authority for the continued appropriated funding of

these shipments. DOD also permits the transportation of foreign-made merchandise and personal property (household goods and privately owned vehicles; of non-appropriated-fund activity employees in the Defense Transportation System but requires that the transportation costs be reimbursed by the non-appropriated-fund activity.

CHAPTER 2

IMPROPER ROUTING OF SHIPMENTS RESULTS

IN MORE APPROPRIATED-FUND SUPPORT

THAN THAT AUTHORIZED BY DOD

Non-appropriated-fund shipments are not always made from the ports of embarkation nearest the overseas destinations. As a result, millions in appropriated funds are spent annually for non-appropriated-fund shipments routed through other ports of embarkation.

The Department of Defense policy requires that merchandise purchased in the United States with nonappropriated funds be moved at either non-appropriated-fund or vendor expense to the port of embarkation nearest the overseas destination. Overocean transportation from this port is financed with appropriated funds.

Non-appropriated-fund activities can save land transportation costs by selecting ports close to the merchandise sources rather than distant ports that are closer to the overseas destinations. However, appropriated-fund transportation costs increase because of the longer ocean distances.

Our tests showed that improper ports were frequently being selected. For example, from July 1974 through February 1975 over \$621,000 of excess transportation costs were financed by appropriated funds because merchandise for the Army and Air Force Exchange Service outlets in the Pacific area was shipped from east coast ports of the United States.

As another example, 89 containerized shipments of liquor for Army and Air Force liquor stores were made from west coast ports of the United States to England, the Netherlands, and Germany between January and June 1975. Over \$59,000 of appropriated funds would have been saved if these shipments had been made from east coast ports.

If we had extended our review period and had reviewed additional shipments, excess transportation costs could have run into the millions. Compliance with DOD's policy would reduce considerably the expenditure of appropriated funds for transportation.

AGENCY COMMENTS AND OUR EVALUATION

The Assistant Secretary of Defense (Comptroller), in commenting on our draft report, said that a joint Office of Management and Budget (OMB)/DOD study is in progress and that some of the comments on our findings must be tentative at this time. (See app. II.)

We reviewed a draft report on this study which was published on March 25, 1977. The joint OMB/DOD report addresses only two of the issues discussed in this report; i.e., appropriated-fund support for land transportation overseas and support for imported foreign-made merchandise. (See chs. 4 and 5, respectively.) DOD's specific comments on our findings, as well as the positions taken in the OMB/DOD joint report, are discussed in the appropriate chapters.

We originally recommended that the Secretary of Defense direct the non-appropriated-fund activities to comply with DOD's policy requiring the activities to bear transportation costs to the points of embarkation nearest the overseas destinations. Since DOD felt that it is prudent to use the port of embarkation which produces the lowest overall transportation cost as long as the Government is reimbursed for any excess costs caused by this routing, we agreed and have revised our recommendation.

RECOMMENDATION

We recommend that the Secretary of Defense direct the non-appropriated-fund activities to reimburse the paying appropriation for ocean costs incurred--for all past and future shipments--in excess of those applicable to shipment through the port of embarkation nearest the overseas destination.

CHAPTER 3

PROCEDURES NEEDED TO ASSURE REIMBURSEMENT

FOR USE OF THE DEFENSE TRANSPORTATION SYSTEM

Non-appropriated-fund activities did not always reimburse the Department of Defense for using the Defense Transportation System when appropriated funds were not authorized. Procedures for assuring reimbursement are needed.

We identified over \$7 million which should have been billed to non-appropriated-fund activities during 1964-76 but was not because reimbursable transportation account codes had not been assigned or properly charged. (See app. I.) After we brought this matter to their attention, various military agencies billed the non-appropriated-fund activities for about \$3.6 million of these costs. Some costs have been refunded, some are being repaid incrementally, while others are a matter of contention.

DOD authorizes non-appropriated-fund activities to ship American-made products overocean at appropriated-fund expense. Overocean transportation covers shipments to and between ports in Europe, the Far East, Alaska, Hawaii, Panama, Guam, Puerto Rico, Cuba, and other locations throughout the world.

DOD also allows non-appropriated-fund activities to ship foreign-made merchandise and personal property of non-appropriated-fund employees overocean in the Defense Transportation System on a reimbursable basis. Under current procedures, transportation costs should be reimbursed by the non-appropriated-fund activity requesting the shipment. DOD does this by assigning reimbursable transportation account codes to the various non-appropriated-fund activities. The code is then designated on shipping documents by the shipping activity.

The Army and Air Force Exchange Service and the Navy Resale System Office are included as shipping activities in the Defense Transportation System. If an incorrect code number is used, it usually is undetected in the documentation, shipping, and billing process and thus continues throughout the system.

We found the assignment and use of transportation account codes to be highly inaccurate. Specific examples of failure to properly charge non-appropriated-fund activities follow.

FOREIGN-MADE MERCHANDISE

Although foreign merchandise was normally shipped on a reimbursable basis, in September 1970 the Army established an appropriated-fund transportation account code which, in conjunction with other Army regulations, allowed the movement of foreign-made merchandise of the Army and Air Force Exchange Service to isolated locations such as Greenland, which was not serviced by commercial transportation at a reasonable cost. In July 1974, the Army eliminated this code and again put the transportation of all foreign-made merchandise on a reimbursable basis.

We found that the transportation account code was being used to ship merchandise to locations which were not isolated, such as England and Japan, and from Japan to Vietnam and Thailand. Transportation costs of \$3.4 million were erroneously charged to this code during fiscal years 1971-74. After we brought this matter to its attention, the Army concurred and billed the Army and Air Force Exchange Service for this amount. However, the Exchange Service said these shipments were properly made at appropriated-fund expense.

We also found instances in the Far East in which foreign-made merchandise of the Exchange Service was coded and shipped as American-made products at appropriated-fund expense.

In contrast to the Army, the Navy did not establish a reimbursable transportation account code for shipments of foreign-made merchandise until July 1, 1974. During fiscal years 1973-74, shipments of foreign-made merchandise for the Navy Resale System Office were incorrectly coded as American-made products, and consequently, about \$1.1 million was erroneously charged to appropriated funds. In April 1975 we told the Navy about these charges, but it has not yet taken any recovery action.

There also were coding problems with transportation of foreign-made liquor and wine. In Europe, the Air Force and Army operate non-appropriated-fund retail liquor stores, known as Class VI stores.

The Air Force did not establish a reimbursable transportation account code for foreign-made liquor and wine shipments until November 1974. During the 10 years preceding that date, the Air Force Class VI Agency received

\$629,000 of appropriated-fund support for the transportation of these products. The Class VI Agency was to repay this amount over a 3-year period ending February 1977.

The Army Audit Agency identified \$350,000 of appropriated-fund support for the transportation of foreign-made liquor and wines for the Army Class VI Agency between fiscal years 1966-70, when there was no reimbursable transportation account code for shipments of foreign-made liquor and wine. The Class VI Agency agreed to reimburse \$221,000 and did so in August 1971.

We checked the coding of shipments made after the reimbursable code was established in 1971 and found that the appropriated fund code continued to be charged quite frequently. We identified \$41,000 of unreimbursed costs for shipments of foreign-made liquor and wines between July 1971 and October 1973. The Army Class VI Agency repaid this amount in March 1974.

The cost of shipping Canadian liquor from the United States to the Army Class VI Agency in Europe was incorrectly charged to an appropriated-fund transportation account code between November 1973 and December 1974. The Agency refunded these incorrect charges of \$12,000 in July 1975.

In Japan the Army operates a non-appropriated-fund wholesale liquor activity, known as the Far East Locker Fund. Before 1975 an appropriated-fund transportation account code was charged for shipments of locker fund foreign-made liquor from Japan to Korea, Taiwan, and Okinawa because a reimbursable code had not been established. Between 1965 and 1974 nearly \$393,000 of appropriated funds was used for this transportation.

In May 1975 we told the Army that a reimbursable transportation account code was needed for locker fund foreign-made liquor shipments and suggested that action be taken to recover earlier transportation charges. In June 1975 DOD published a reimbursable code, and in December 1975 the locker fund made its first monthly payment for the charges incurred before 1975.

PERSONAL PROPERTY

Some shipments of personal property of employees of the Army and Air Force Exchange Service were incorrectly charged to the appropriated-fund transportation account code used to transport American-made merchandise sold at exchange outlets

overseas. For example, our review of 903 shipments made between January 1971 and July 1972 showed that 388 shipments of personal property had been incorrectly assigned an appropriated-fund code.

In other cases the proper code was charged but the Exchange Service did not pay DOD for the shipments. The Army Finance and Accounting Center thought reimbursements were being made at the origin ports, while the ports thought reimbursements were being made at the Accounting Center. As a result, DOD was not being reimbursed.

We estimate that between fiscal years 1966 and 1975, about \$902,000 was erroneously spent from appropriated funds to ship personal property of Exchange Service employees. The Exchange Service has paid this amount. In January 1975 the Army issued instructions requiring that transportation costs for shipments of personal property be paid in advance.

Shipments of personal property of employees of the Navy Resale System Office also were incorrectly charged to an appropriated-fund transportation account code used for merchandise sold at exchange outlets overseas. We told the System Office of this, and in November 1974, it reimbursed the appropriated fund \$78,000.

OTHER SERVICES

Merchandise for exchanges generally is moved from the United States to overseas locations in containers known as seavans. DOD policy provides that costs resulting from delays in unloading seavans at inland destinations be paid by the non-appropriated-fund activities.

In Hawaii and Guam we found that seavan-delay costs incurred between July 1972 and September 1974 for Exchange Service shipments had been improperly paid from appropriated funds due to incorrect use of a transportation account code. In March 1975 a \$52,000 collection action was processed against the Exchange Service, but reimbursement had not been received as of February 1977.

Seavan-delay costs incurred for Navy Resale System Office shipments also were improperly paid from appropriated funds because a transportation account code was incorrectly used. We identified \$103,000 of such costs and the System Office made full reimbursement in September 1975.

AGENCY COMMENTS AND OUR EVALUATION

The Assistant Secretary of Defense (Comptroller) by letter of August 2, 1976, concurred in our findings and conclusions. He noted actions taken by the Army and Navy to restructure transportation account codes and by the Military Sealift Command to establish a unit level billing system. (See app. II.)

The Assistant Secretary of Defense (Manpower and Reserve Affairs) responded separately to the matter of shipments of foreign-made merchandise to Vietnam and Thailand during fiscal years 1971-74. (See app. IV.) In his July 23, 1976, letter, the Assistant Secretary said DOD believed that the Army and Air Force Exchange Service should not have to pay for shipments of foreign-made goods to Vietnam and Thailand before 1974. This belief is based not only on whether reasonable ocean shipping costs existed before 1974, but on the unusual conditions at the time, such as costs associated with warehousing, pilferage, and damage incident to commercial shipping. DOD also said that when adequate commercial shipping at reasonable cost had become available to transport foreign-made goods to these locations, Army policy was changed to discontinue use of appropriated funds.

We know of no significant changes in commercial transportation to, or warehousing in, those areas in 1974 that were not available before. We also know of no significant changes in the security afforded these shipments after 1974. The foreign-made goods were, for the most part, shipped on commercial vessels under contract to the Military Sealift Command at reasonable costs.

In our opinion, both Vietnam and Thailand were adequately served by commercial transportation at reasonable cost and shipping charges to those destinations should have been borne by the Exchange Service and not the military services. Furthermore of the \$3.4 million involved, about \$1.1 million represents shipments of foreign merchandise to other overseas locations such as Korea, Taiwan, the Philippines, England, and Germany. These costs should be collected.

CONCLUSION

Transportation services have been improperly charged to appropriated funds. The improper charges resulted from the failure to either establish or correctly designate a reimbursable transportation account code.

Contributing to the inaccuracies were human error, the complexity of the coding system, and the absence of reviews for the validity of codes.

Procedures are needed to assure that reimbursable transportation account codes are charged for services not authorized for payment from appropriated funds. Proper training of personnel responsible for assigning codes and reviews of codes as merchandise passes through the system would help.

Mechanized controls could be instituted to preclude the erroneous use of appropriated-fund codes. To some degree, the Navy recently implemented such controls for checking personal property codes. Its computerized program matches transportation account and commodity codes. It rejects shipments which have a personal property commodity code that are charged to a retail merchandise transportation account code. The exceptions are manually investigated to determine the proper coding.

RECOMMENDATION

We recommend that the Secretary of Defense institute procedures for insuring that non-appropriated-fund activities are properly charged for reimbursable transportation services, considering the need for both manual and mechanical controls over the correct use of transportation account codes. DOD should also recover the unreimbursed costs for improper appropriated-fund support provided non-appropriated-fund activities, particularly those identified in appendix I of this report which have been outstanding for some time.

CHAPTER 4

NAVY'S USE OF APPROPRIATED FUNDS FOR OVERSEAS LAND TRANSPORTATION SUPPORT IS INCONSISTENT WITH OTHER SERVICES' PRACTICES

The Navy's practice of financing overseas land transportation costs with appropriated funds is inconsistent with the Army's and Air Force's practices of not financing these costs. This land transportation support for the Navy exchange exceeds \$300,000 annually.

Army and Air Force regulations provide that appropriated funds can be used for overocean transportation of American-made non-appropriated-fund merchandise. Navy regulations have similar provisions and authorized paying overseas land transportation costs from the overseas port to the inland destination.

The overseas land transportation costs can be considerable. In Hawaii \$44,000 of appropriated funds were used for land transportation of Navy exchange cargo during the 12-month period ended November 1974. The Navy also has overseas exchanges in Japan, Spain, Italy, Scotland, and other countries where appropriated funds are used for land transportation.

On July 24 1975, we wrote to the Secretary of Defense about the inconsistencies among the military services in funding overseas land transportation costs. In a March 9, 1976, letter, the Assistant Secretary of Defense (Comptroller) acknowledged the inconsistency and agreed that it was inappropriate for the Army, Air Force, and Navy exchanges to receive different levels of appropriated-fund support.

The Comptroller said that a major effort to detect and correct all such inconsistencies had begun. However, he did not say how the inconsistencies would be resolved.

We believe the Army's and the Air Force's practices should be adopted. Neither of these services uses appropriated funds for overseas land transportation nor suffers any apparent ill effects.

AGENCY COMMENTS AND OUR EVALUATION

DOD's comments on this matter were tentative, since they related to issues to be resolved in the joint OMB/DOD study. The tentative comments state, however, that if the rationale

for paying overocean costs from appropriated funds is to equalize sales costs to the overseas service member, then the cost of overseas land transportation should also be absorbed by appropriated funds as representing an added cost of doing business overseas. (See app. II.)

Furthermore, a review of a draft of the OMB/DOD study report indicates that this rationale is being accepted, and rather than having the Navy conform to the Army and Air Force policies, increased appropriated fund support will be provided to the Army and Air Force exchanges for overseas land transportation.

We believe a new interpretation of legislative intent by DOD which would provide payment for even more transportation services overseas for non-appropriated-fund shipments is unwarranted. If additional appropriated-fund support is contemplated, it should be specifically authorized by the Congress.

RECOMMENDATION

We recommend that the Secretary of Defense direct the Secretary of the Navy to stop using appropriated funds for overseas land transportation of non-appropriated-fund property.

CHAPTER 5

TRANSPORTATION SUPPORT FOR IMPORTED FOREIGN-MADE

MERCHANDISE IS CONTRARY TO DOD'S POLICY

DOD's practice of providing appropriated-fund transportation support for shipment of foreign-made beer because U.S. customs duties and taxes are paid hinders its policy of encouraging the sale of U.S. products overseas.

DOD Directive 7060.3 states that DOD's policy is to promote the sale of U.S. goods and services in overseas non-appropriated-fund activities. The policy's objective is to aid in achieving a more favorable balance of payments. The directive specifically provides that no appropriated funds be used for transshipping foreign-made merchandise.

Between March 1972 and August 1974 about \$88,000 of appropriated funds was spent to ship foreign-made beer from New York to Hawaii, which DOD considers an overseas area for transportation purposes. Military clubs in Hawaii bought the beer through a commercial broker. The beer originated in the Netherlands and was shipped to New York at the clubs' expense.

After the beer reached New York, customs duties and taxes were paid and the beer was turned over to the Defense Transportation System for transshipment to Hawaii at appropriated-fund expense. By paying about \$850 in customs duties and taxes for each container of beer, the clubs received about \$1,200 worth of appropriated-fund support in the form of transportation. Although we specifically cite foreign-made beer, this situation could occur just as easily with future shipments of other foreign-made goods.

AGENCY COMMENTS AND OUR EVALUATION

The DOD Office of General Counsel has determined that the payment of customs duties and other applicable U.S. taxes makes foreign merchandise eligible for ocean transportation, at appropriated-fund expense, on the same basis as American-made products. This same position has also been taken in the joint OMB/DOD draft report on funding support for morale, welfare and recreation activities.

In our opinion, using appropriated funds and the Defense Transportation System for the transshipment of foreign-made merchandise is contrary to DOD's policy of encouraging the

sale of American-made products overseas. Although using appropriated funds may be technically permissible, it is contrary to the intention of the directive. The provision of "free" Government transportation gives the foreign-made merchandise advantages of both cost and visibility it would not otherwise have.

RECOMMENDATION

We recommend that the Secretary of Defense revise DOD Directive 7060.3 to prohibit any foreign-made merchandise shipments from receiving appropriated-fund support.

CHAPTER 6

SCOPE OF REVIEW

We made our review to find out (1) the extent to which appropriated funds were being used to support non-appropriated-fund activities and (2) whether adequate reimbursement was being made by these activities.

Work was done at the following major activities and subordinate offices:

- Military Traffic Management Command
Falls Church, Virginia
- Military Sealift Command
Washington, D.C.
- Army and Air Force Exchange Service
Dallas, Texas
- Navy Resale System Office
Brooklyn, New York
- United States Army Finance and Accounting Center
Indianapolis, Indiana
- Naval Supply Systems Command
Washington, D.C.
- U.S. Air Force Class VI Agency
Mainz-Kastel Air Station, Germany
- U.S. Army Class VI Agency
Heidelberg, Germany
- Far East Locker Fund
Camp Zama, Japan
- Various military clubs and exchanges in Japan, the
Philippines, Thailand, and Hawaii

We discussed our findings with officials of the Offices of the Assistant Secretaries of Manpower and Reserve Affairs, Comptroller, and Installations and Logistics, and various military representatives of the Department of Defense.

We obtained statistical data for shipments from billing and shipping records of the Military Traffic Management Command and the Military Sealift Command.

SUMMARY OF ESTIMATED AMOUNTS OF APPROPRIATED FUNDS
ERRONEOUSLY USED BY NON-APPROPRIATED-FUND ACTIVITIES

AS OF DECEMBER 31, 1976
(notes a and b)

Agency	Services received at appropriated fund expense	Approximate cost to appropriated funds	Amount collected from agency	Balance outstanding
Army and Air Force Exchange	Shipment of personal property \$ 902,000 Shipment of foreign merchandise 3,400,000 Delay charges on seavans 57,000	\$ 902,000 3,400,000 57,000	\$ 902,000 0 0	\$ 0 3,400,000 52,000
USAFE Class VI Agency (note d)	Transportation of foreign liquor	621,000	556,000	73,000
USAREUR Class VI Agency (note e)	Transportation of foreign liquor	1/274,700	274,000	0
Far East Locker Fund	Transportation of foreign liquor	133,000	131,000	262,000
Various clubs and messes in Hawaii	Transportation of foreign liquor	88,000	0	88,000
Various clubs and messes in the Pacific	Transportation of foreign liquor	42,000	42,000	0
Navy Resale System Office	Transportation of personal property 78,000 Shipment of foreign merchandise (estimated) 1,100,000 Seavan-delay 103,000	78,000 1,100,000 103,000	78,000 0 103,000	0 9/1,100,000 0
Total (note b)		\$7,061,000	\$2,086,000	\$4,975,000

a/All figures rounded.

b/Summary does not include land transportation support costs described in chapter 4.

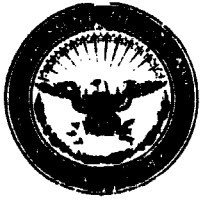
c/DOD does not incur that \$2.3 million of this amount should be billed. See page 9.

d/United States Air Force, Europe.

e/United States Army, Europe.

f/The Army Audit Agency identified and collected over \$221,000. An additional \$53,000 was identified and collected during our review.

g/The Navy has taken no action to recover these costs. See page 6.



COMPTROLLER

ASSISTANT SECRETARY OF DEFENSE
WASHINGTON, D.C. 20301

August 2, 1976

Mr. Fred J. Shafer
Director, Logistics and
Communications Division
U.S. General Accounting Office
Washington, D. C. 20548

Dear Mr. Shafer:

This is in response to your letter dated May 20, 1976, which requested comments on a draft report titled, "Unauthorized and Questionable Use of Appropriated Funds to Pay Transportation Costs of Nonappropriated Activities." (OSD Case #4373)

The draft report expresses your concern that appropriated funds have been improperly expended for transportation support that should have been funded by nonappropriated fund activities.

Since the President has directed that a study be completed concerning the use of appropriated funds to support nonappropriated fund activities and the study is in progress, some of our comments must of necessity be tentative at this time. This study is a joint OME/DoD effort and is scheduled for completion in September 1976. The objectives of this study are to:

- Identify the amount of appropriated and nonappropriated funds used in support of NAF activities.
- Evaluate the effectiveness and equity of the current policies governing that support.
- Develop alternative plans to modify any deficiencies or inefficient policies.

Our comments on the issues raised in your report follow:

Chapter 2: Improper Routing of Shipments Resulting in More Appropriated Fund Support Than Authorized by DoD

We concur that shipment through a farther distant port of embarkation (POE) increases the cost to DoD. However, we feel that it is prudent to use the POE which produces the lowest overall transportation cost, whether the beneficiary of the resultant savings be the Government or the nonappropriated fund activity. Therefore, we suggest the recommendation be revised to indicate "the Secretary of Defense direct the non-appropriated fund activities to reimburse the paying appropriation for ocean costs incurred in excess of those applicable to shipment through the port of embarkation nearest the overseas destination."

Chapter 3: Procedures Needed to Assure Reimbursement for Use of the Defense Transportation System

Concur with findings, conclusion and recommendation. As noted in the draft report, both Army and Navy have taken action to restructure Transportation Accounting Codes (TAC) to properly segregate costs for identification and reimbursement purposes. Concurrently, the Military Sealift Command is taking steps to establish a unit level billing system, which will materially enhance the Service's ability to obtain proper reimbursement.

Chapter 4: Navy's Use of Appropriated Funds for Overseas Land Transportation Is Inconsistent with the Other Services

The recommendation in this chapter relates to issues to be resolved in the joint OMB/DoD study. However, in considering the issues involved, it is important to recognize that the cost of land transportation overseas may equally be considered an added cost of doing business overseas, since the cost to the nonappropriated fund activity of delivery to the CONUS POE would equate to the cost of delivery to the CONUS sales/consumption activity. Therefore, if the rationale for paying over-ocean cost from appropriated funds is to equalize sales cost to the overseas service member, then the cost of overseas land transportation should also be absorbed by appropriated funds as representing an added cost of doing business overseas.

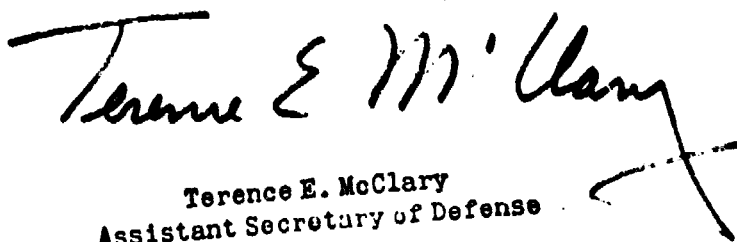
Chapter 5: Transportation Support for Imported Foreign Made Merchandise Is Contrary to DoD Policy

Our Office of General Counsel has determined ". . . that foreign made merchandise which has properly entered the United States and on which all required custom duties and other applicable United States taxes have been paid may be transported on the same basis as United States made products." Therefore, the use of appropriated funds to support ocean costs from the United States to another foreign country incurred in the transportation of such merchandise must be resolved as part of the overall issue of appropriated fund support of nonappropriated fund activities.

[See GAO note]

We appreciate this opportunity to comment on your draft report.

Sincerely,

A handwritten signature in black ink that reads "Terence E. McClary". The signature is written in a cursive style with a long horizontal line at the top and a large, sweeping flourish at the bottom right.

Terence E. McClary
Assistant Secretary of Defense

GAO note: Deleted material relates to data in our draft which has been deleted from the final report.

COPY

APPENDIX III

Page 1

TC-OD-G-607

Deputy Chief of Logistics
Department of the Army
The Pentagon 20310

MAR 3 1975

Attention: DALO TSP - C

Dear Sir:

During our work under assignment codes 46216, 43223, 43216, and 43219 we have become aware of a situation on which we would like to receive your comments. The Army and Air Force Exchange Service (AAFES) has been moving foreign made merchandise to Thailand and Vietnam at appropriated fund expense. We feel these movements should have been charged to AAFES in accordance with DOD Directive 7060.3 para VA(3) which states that no appropriated funds will be used for the trans-shipment of foreign-made goods between nonappropriated fund activities. The policy guidance does allow appropriated funds to be used to move foreign made goods to isolated locations where adequate commercial transportation is not available at reasonable costs.

AR 230-4 indicates that Vietnam and Thailand are isolated locations and the AAFES officials in Honolulu are using this regulation as their authority for moving foreign merchandise to Vietnam and Thailand at appropriated fund expense.

On September 17, 1970, AR 37-23 established transportation account code (TAC) A-216 (an appropriated fund TAC) and AAFES began using this code to fund shipments of foreign merchandise to Vietnam and Thailand. We disagree with AAFES' position on this matter. We have identified these shipments and intend to bill AAFES' retroactively from September 17, 1970 until July 1, 1974 at which time Department of the Army directed that AAFES reimburse Army Operations and Maintenance funds for all foreign merchandise shipments made against TAC A-216.

We feel that Vietnam and Thailand are adequately served by commercial transportation at reasonable cost. Attached for your reference is an analysis of the MSC's commercial rates between various countries in the Pacific and we find no appreciable difference between the rates to Vietnam or Thailand and those to other countries in the area such as Taiwan, Philippines, or Hong Kong.

COPY

TC-OD-G-607

Prior to our processing collection actions against AAFES for these shipments we would appreciate receiving your views on the provisions of AR 230-4 relied upon by AAFES.

We are available to meet with you or your staff to discuss this problem in more detail. Questions should be directed to Mr. Paul F. Dinsmore telephone 386-6378.

Your cooperation is appreciated.

Sincerely yours,

R. E. West

For/ T. E. Sullivan
Director

Attachment

COPY

Schedule of Low Cost Carrier Rates
of Pacific Interport Shipments
of General Cargo

<u>Between</u>	<u>MSC Rate Guides Effective</u>			
	<u>1/1/73</u>	<u>1/1/74</u>	<u>7/1/74</u>	
Japan	Vietnam	1720	1875	2670
	Thailand	1675	1725	2600
	Korea	1250	1480	1846
	Okinawa	1200	1260	2050
	Taiwan	1375	1375	2000
	Hong Kong	1435	1480	2105
	Philippines	1700	1730	2347
	Guam	2500	2500	3117
Korea	Vietnam	1725	1725	2717
	Thailand	1750	1775	2905
	Japan	1250	1480	1846
	Okinawa	1485	1627	2244
	Taiwan	1500	1625	-
	Hong Kong	1435	1600	-
	Philippines	1700	1480	-
	Guam	3000	3000	-
Okinawa	Vietnam	1725	1850	2100
	Thailand	1665	1600	2905
	Taiwan	1250	1500	2100
	Hong Kong	1250	1275	-
	Philippines	1300	1260	2100
	Guam	3000	3000	-
Taiwan	Vietnam	1627	1760	2400
	Thailand	1805	1597	2905
	Hong Kong	1250	1260	-
	Philippines	1350	1350	2200
	Guam	3000	2520	-
Hong Kong	Vietnam	1627	1627	-
	Thailand	1670	1625	-
	Philippines	1325	1600	-
	Guam	2500	2500	-
Vietnam	Thailand	1325	1325	2000
	Philippines	1627	1760	2400
	Guam	3000	3000	-
Thailand	Philippines	1745	1650	-
	Guam	3000	3000	-



ASSISTANT SECRETARY OF DEFENSE

WASHINGTON, D. C. 20301

MANPOWER AND
RESERVE AFFAIRS

July 23, 1976

Mr. T. E. Sullivan
Assistant Comptroller General
U. S. General Accounting Office
Washington, D. C. 20548

Dear Mr. Sullivan:

This is in reply to your letter of March 3, 1975 to the Deputy Chief of Logistics, Department of the Army, regarding retroactive billing of the Army and Air Force Exchange Service (AAFES) for shipments of foreign merchandise to Vietnam and Thailand at appropriated fund expense from September 1970 through June 1974. The Assistant Secretary of the Army (Financial Management) has asked that I reply to your letter.

During the time period addressed, DoD policy authorized the use of appropriated funds at isolated locations where adequate commercial transportation was not available at reasonable cost.

A review of the matter indicated that the provisions of AR 230-4, exempting Vietnam and Thailand from appropriated fund restrictions, were based on valid consideration, competent authority, and in consonance with DoD policy. The authorization for use of appropriated funds was based, not solely on the cost of commercial ocean shipping referred to in your letter, but rather, on the unusual conditions surrounding shipments to Vietnam and Thailand at the time. It was the large attendant costs associated with warehousing, pilferage, and damage incident to the use of commercial shipping that prevented the use of such shipping at reasonable costs.

When it was determined in 1974 that adequate commercial transportation at reasonable cost had become available for transporting foreign

merchandise to remote locations, the Army policy was modified to discontinue financing such transportation from appropriated funds. Pursuant to this revised policy, nonappropriated funds, henceforth, were used to pay transportation costs of all AAFES foreign merchandise shipments.

Accordingly, it is felt there should be no retroactive billing of the AAFES for these shipments.

Sincerely,

David P. Taylor.

PRINCIPAL OFFICIALS
RESPONSIBLE FOR ACTIVITIES
DISCUSSED IN THIS REPORT

<u>Tenure of office</u>	
<u>From</u>	<u>To</u>

DEPARTMENT OF DEFENSE

SECRETARY OF DEFENSE:

Dr. Harold Brown	Jan. 1977	Present
Donald H. Rumsfeld	Nov. 1975	Jan. 1977
James Schlesinger	July 1973	Nov. 1975
William P. Clements, Jr. (acting)	Apr. 1973	July 1973
Elliot L. Richardson	Jan. 1973	Apr. 1973
Melvin R. Laird	Jan. 1969	Jan. 1973
Clark M. Clifford	Mar. 1968	Jan. 1969
Robert S. McNamara	Jan. 1961	Feb. 1968

DEPUTY SECRETARY OF DEFENSE:

Charles W. Duncan, Jr.	Jan. 1977	Present
William P. Clements, Jr.	Jan. 1973	Jan. 1977
Kenneth Rush	Feb. 1972	Jan. 1973
David Packard	Jan. 1969	Dec. 1971
Paul H. Nitze	July 1967	Jan. 1969
Cyrus R. Vance	Jan. 1964	June 1967

ASSISTANT SECRETARY OF DEFENSE
(INSTALLATIONS AND LOGISTICS):

Dale R. Babione (acting)	Jan. 1977	Present
Frank A. Shrontz	Feb. 1976	Jan. 1977
Arthur I. Mendolia	June 1973	Feb. 1976
Hugh McCullough (acting)	Jan. 1973	June 1973
Barry J. Shillito	Feb. 1969	Jan. 1973
Thomas D. Morris	Sept. 1967	Feb. 1969
Paul R. Ignatius	Dec. 1964	Sept. 1967

DEPARTMENT OF THE ARMY

SECRETARY OF THE ARMY:

Clifford Alexander	Feb. 1977	Present
Martin R. Hoffman	Aug. 1975	Jan. 1977
Howard H. Callaway	June 1973	Aug. 1975
Robert F. Froehke	July 1971	June 1973
Stanley R. Resor	July 1965	June 1971

Tenure of office
From To

DEPARTMENT OF THE NAVY

SECRETARY OF THE NAVY:

W. Graham Claytor, Jr.	Feb. 1977	Present
J. William Middendorf II	Apr. 1974	Jan. 1977
John W. Warner	Apr. 1972	Apr. 1974
John H. Chafee	Jan. 1969	Apr. 1972
Paul R. Ignatius	Sept. 1967	Jan. 1969
Charles F. Baird (acting)	Aug. 1967	Sept. 1967
Robert H. B. Baldwin	July 1967	Aug. 1967
Paul H. Nitze	Nov. 1963	July 1967

DEPARTMENT OF THE AIR FORCE

SECRETARY OF THE AIR FORCE:

John Stetson	Apr. 1977	Present
Thomas C. Reed	Jan. 1976	Apr. 1977
James W. Plummer (acting)	Nov. 1975	Jan. 1976
Dr. John J. McLucas	July 1973	Nov. 1975
Dr. Robert C. Seamans, Jr.	Jan. 1969	May 1973
Dr. Harold Brown	Oct. 1965	Jan. 1969