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Summary of a Report--Revolving Funds: Full Disclosure Needed for Better Congressional Control. PAD-77-25(a); B-115398. August 30, 1977. 12 pp. + appendix (1 pp.).

Report to Rep. Butler Derrick, Chairman, Task Force on Budget Controllability, House Committee on Budget; by Elmer B. Staats, Comptroller General Better Congressional Control.

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Because of the way some revolving funds are currently included in the Federal budget, the total amount of Government activities is understated; for example, by an estimated \$28 billion in fiscal year (FY) 1978. Findings/Conclusions: In order for Congress to decide on budget totals and make priority allocations, it must have complete information on the total levels of Federal activities. Periodic congressional review is the best method for Congress to control revolving funds. The Office of Management and Budget (OMB) and GAO agreed that adoption of gross accounting for public enterprise revolving funds would have significant effect on Federal accounting and budgeting. Recommendations: The Director of OMB should: (1) make appropriate changes in current budget procedures which will result in the financial activities of public enterprise revolving funds being reflected in the Federal budget on a gross basis; and (2) periodically review established revolving funds in the budget to determine whether they meet established criteria and should continue to operate as revolving funds. Congress, with the executive branch, should develop and utilize common criteria for establishing and classifying revolving funds. Before establishing additional revolving funds, Congress should study the fiscal implications of each new proposal. (Author/HTW)

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REPORT TO THE HOUSE COMMITTEE ON THE BUDGET

BY THE COMPTROLLER GENERAL
OF THE UNITED STATES



Summary Of A Report-- Revolving Funds: Full Disclosure Needed For Better Congressional Control

Because of the way some revolving funds are currently included in the Federal budget, the total amount of Government activities is understated--for example, by an estimated \$28 billion in fiscal year 1978.

Inconsistent classification of budget accounts causes inconsistent reporting for essentially similar programs.

GAO recommends that revolving funds should be accounted for differently than they are now. This will cause changes in the budget process, especially in the disclosure of financial information. GAO also recommends that common criteria be established for classification of budget accounts.



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

B-115398

The Honorable Butler Derrick
Chairman, Task Force on Budget
Controllability
Committee on the Budget
House of Representatives

Dear Mr. Chairman:

In response to your request, we are reporting on various aspects of revolving funds--an important means of financing Government programs--and assessing the effects such financing techniques have on congressional control over the budget. This is a summary of a report which is the first of a series aimed at assuring consistent application of budget principles.

Our review was made pursuant to your request and under the provisions of title VIII of the Congressional Budget Act of 1974 (P.L. 93-344).

We are sending copies of this summary to the Director, Congressional Budget Office; the Secretary of the Treasury; and the Director, Office of Management and Budget.

Sincerely yours,

A handwritten signature in cursive script, reading "James B. Stacks".

Comptroller General
of the United States

SUMMARY OF A REPORT--

REVOLVING FUNDS: FULL DISCLOSURE NEEDED

FOR BETTER CONGRESSIONAL CONTROL

PURPOSE AND SCOPE OF REPORT

This report was undertaken at the request of the House Budget Committee's task force on budget controllability as part of a series of reports dealing with legislative, financial, and administrative practices that affect the ability of the Congress to control Federal spending. These studies are intended to assist the Congress in distinguishing between controllable and other programs (a distinction required by the Congressional Budget Act). In addition, they are intended to gather data and develop concepts for practical application by the Congress in improving the controllability of the Federal budget.

The extent of our review was to study the overall use of revolving fund financing throughout the Federal Government and its implications on congressional control. Although individual revolving fund accounts are cited frequently throughout the report as examples, no individual accounts were studied in depth or audited by us for this report.

The source for most of the statistics and financial information used in this report is from an analysis of "The Budget of the U.S. Government," 1977, its "Appendix," and the Office of Management and Budget (OMB) computer tape of this information. Therefore, financial data for fiscal years 1976 and 1977 are OMB estimates.

Other information in the report came from various sources, such as previous reports on revolving funds, legislative histories, and general studies on the budget process and congressional control. Numerous interviews were held with officials at OMB and Treasury and with congressional staff members from various committees.

RECOMMENDATIONS TO THE DIRECTOR, OMB

We recommend that the Director:

- Make appropriate changes in current budget procedures which will result in the financial activities of public enterprise revolving funds being reflected in the Federal budget on a gross basis.

- Periodically undertake indepth reviews of all established revolving funds in the budget to determine whether (1) they meet the established criteria for revolving funds and (2) it is necessary that the accounts continue to operate as revolving funds. The results of such reviews should be furnished to the appropriate congressional committees, the Department of the Treasury, the Congressional Budget Office (CBO), and us.

RECOMMENDATIONS TO THE CONGRESS

We recommend that the Congress,

- together with the executive branch, develop and utilize common criteria for establishing and classifying all revolving funds; and
- before establishing any additional revolving funds, study the full financial implications of each new proposal and incorporate the findings in the appropriate reports and documents on the legislation.

AGENCY COMMENTS

OMB

OMB disagreed with our recommendation for gross accounting for a number of reasons:

1. The present system of accounting and budgeting for public enterprise funds conforms to the precepts laid down by the President's Commission on Budget Concepts. This recommendation runs counter to those precepts.
2. It is not necessary for the budget summary information to disclose the gross accounting for collections and outlays of public enterprise funds in order for the Congress to decide on budget totals or make priority allocations among functions.
3. It is not appropriate for gross collections and outlays to be used as the basis for making priority allocations among functions.
4. Such a change would affect the current appropriations process and agency accounting for the individual accounts.

5. Since this recommendation applies only to public enterprise funds, it applies different accounting and budget presentation rules to public enterprise funds from those for intragovernmental revolving funds.

OMB stated that, while it has no objection to the reviews required by our second recommendation, it would be more appropriate for the administering agency of the executive branch to conduct the reviews and propose appropriate amendments to the authorizing legislation.

OMB agreed with our recommendation for common criteria. OMB noted that in the past it has at times been hampered when technical financial terms are used imprecisely in authorizing legislation. In addition, OMB believed that if the Congress were to adopt uniform criteria as proposed in our recommendation, there would be no need for the reports called for in our fourth recommendation other than on an exception basis.

Department of the Treasury

Treasury stated:

"Better disclosure for the Congress is a must--however, we feel that before any major changes are made in the present methods of reporting and disclosing the financial results of Federal activities, time is needed by Treasury, OMB, and GAO to thoroughly evaluate the full effects of such a proposal. Also, the idea of whether or not to include the trust revolving funds and the intragovernmental revolving funds, as well as the public enterprise funds, is something that should be looked at more closely."

Congressional Budget Office

CBO suggested that the concept of accounting for public enterprise revolving funds on a gross basis merits serious consideration, but pointed out that adoption of this concept would require CBO and the Budget Committees to review the scorekeeping procedures now in effect.

House Committee on Appropriations

The House Committee on Appropriations stated, "The recommendation that a common set of criteria be developed to determine the proper circumstances for revolving fund status is a good one." They pointed out that the development of such criteria will raise a number of questions which will need further study and coordination.

OUR EVALUATION

We disagree with OMB's statements on our recommendation for gross accounting. The budget process, especially since enactment of the Congressional Budget Act of 1974, is a dynamic, evolving process. While the recommendations of the President's Commission on Budget Concepts were valid and needed when they were made, times have changed and the Congress has demanded a stronger voice in the budget process.

We believe that for the Congress to decide on budget totals and make priority allocations among functions under the new budgetary process, it must have complete information on the total levels of Federal activities. With full disclosure (gross accounting for receipts and outlays in the budget), the Congress will be better able to use the budget information in establishing aggregate financial targets by functional category. We fail to understand why the Congress should have to consult the individual public enterprise accounts in the budget appendix to obtain their gross activities. We believe it is more logical that these activities be included in total as part of the functions in the Federal budget.

We disagree with OMB that the appropriations process for the revolving funds will be changed. There is nothing in our report or recommendations that would alter in any manner the current appropriations process. On the contrary, as we point out in our conclusion, we believe periodic congressional review through the appropriations process is the best method for the Congress to control revolving funds.

We agree with OMB, Treasury, and CBO that adoption of the concept of gross accounting for public enterprise revolving funds will have significant effect on Federal accounting, budgeting, and scorekeeping systems. Details of implementing this proposal will require extensive study and coordination between congressional committees, CBO, OMB, Treasury, and us. 1/ We believe that this effort can best be done by a task force made up of representatives of the aforementioned entities. We will assist in the task.

1/App. I contains examples of how the change to gross accounting would affect the budget presentation for an individual public enterprise revolving fund account.

We also recognize, as both OMB and Treasury point out, that accounting for public enterprise revolving funds on a gross basis will be inconsistent with budget treatment for similar transactions. Therefore, additional studies of similar financial transactions need to be conducted to see if budget treatment for offsetting receipts, direct loans, guaranteed loans, etc., are consistent with present congressional budget information needs. We plan to undertake the necessary reviews and to report to the Congress and the executive branch on the results of those reviews.

Regarding OMB comments on our recommendation for periodic reviews of existing revolving funds, we believe such reviews should be under OMB's general supervision, although they will certainly require input from the administering agency. Conducting periodic indepth reviews of all established revolving funds, along with the study and reporting on the financial implication of each new revolving fund proposal, will be a major step toward restoring the recommendations of the President's Commission on Budget Concepts concerning consistency in Federal accounts and budget reporting.

Development of common criteria, as mentioned in our third recommendation, will require an extensive and technical undertaking similar to that required for the changing from net to gross accounting. This should not, however, deter from its undertaking. Accepted common criteria form the cornerstone upon which all questions regarding revolving funds must be based. We will actively participate in developing such criteria. OMB's criteria would be a good starting point. We believe that this effort must involve the appropriate congressional committees as well as OMB, the Department of the Treasury, and the Congressional Budget Office.

Our final recommendation regarding study of full financial implications of proposed revolving funds and reporting on these studies was questioned by OMB as being unnecessary except on an exception basis. We disagree that such reports be made on an exception basis only. We believe that it is necessary, when a new account is proposed, to draw the Congress' attention to the potential loss of congressional control, together with all other financing arrangements which are outside of the appropriations process. Such studies may be done by Federal entities that the responsible congressional committees deem appropriate.

SUMMARY OF CONTENTS OF REPORT

The Congress establishes revolving funds to finance Federal programs which carry on a businesslike cycle of operations. Receipts from program operations are earmarked for future operations of the fund. Revolving funds became popular during the 1930s when many of the large Government corporations were founded. Although there has been no recent growth in the number of funds, there has been dramatic growth in revolving fund financial transactions during the last several years. "The Budget of the U.S. Government" for fiscal year 1977 lists 185 revolving fund accounts with projected receipts of \$70.6 billion and gross outlays of \$75 billion--approximately 20 percent of the total Federal receipts and outlays projected for the year. Revolving funds are divided into three major groups:

- Public enterprise. Business conducted primarily with customers outside the Government. These funds have the greatest impact upon congressional control.
- Intragovernmental. Business conducted primarily within and between Federal agencies. These funds do not greatly affect congressional control since their receipts generally come from other account appropriations and thus their financial activity has already been accounted for in the budget. To the extent these funds are used to conduct business outside the Government, however, congressional control is affected in a way similar to public enterprise funds.
- Revolving trust. Business conducted by earmarked receipts held by the Federal Government in a fiduciary (trust) capacity. There is little budgetary control possible over these accounts because most are entitlements (required by law to be furnished to all who meet the qualifications) and U.S. Government funds are not often involved.

The following table shows the number of revolving funds by category (together with their receipts and gross outlays) included in the fiscal year 1977 budget.

Scope of Revolving Funds

for Fiscal Year 1977

(in billions of dollars)

	<u>On-budget</u>		
	<u>No.</u> <u>accounts</u>	<u>Receipts</u>	<u>Gross</u> <u>outlays</u>
Public enterprise	87	\$27.3	\$33.6
Intragovernmental	a/84	37.7	37.5
Trust revolving	<u>14</u>	<u>5.1</u>	<u>3.9</u>
Total	<u>185</u>	<u>\$70.6</u>	<u>\$75.0</u>

a/Includes 43 management funds with receipts and gross outlays of \$1.4 billion. All analysis includes management fund figures.

In 1967, the President appointed a commission to review Federal budget concepts and recommend appropriate changes to the Federal budget process. The commission made two recommendations which have had a direct and lasting impact on revolving funds and their inclusion in the budget: (1) financial activities of public enterprise revolving funds should be included in the budget totals on a net outlay basis and (2) there should be a consistent classification of revolving fund accounts in the budget. These recommendations were subsequently put into effect. Since enacting the Congressional Budget Act of 1974, the Congress has become more involved in the Federal budget process, especially in setting priorities among Federal functions. Because of the major changes in the budget process brought about by the act, we recommend that the commission's recommendation concerning net outlay accounting for public enterprise revolving funds be revised to provide the Congress with the most complete information with which it will be better able to make its budget decisions. Steps should also be taken to reinforce the commission's recommendations for consistent application of revolving fund criteria.

Revolving fund transactions are currently accounted for in the budget totals on a net basis (i.e., receipts are offset against gross outlays with only the net outlay figure being brought forward for inclusion in the budget totals). It is the gross outlay figure, however, which is the best indicator of the level of financial activity carried on by revolving funds. As the result of netting, of the \$33.6

billion of financial activity projected to be conducted by the Federal Government with the public through public enterprise revolving funds in fiscal year 1977, only \$5.8 billion was included in that year's budget outlays totals. The \$27.8 billion of receipts was deducted from the \$33.6 billion gross outlays and was not included. This \$27.8 billion in outlays was, in effect, treated as if it were "off-budget."

Although fiscal year 1977 budget data is used throughout this report, the conclusions and recommendations presented would not change if fiscal year 1978 budget data were used. For example, the level of outlays treated as if it were off-budget, using fiscal year 1978 budget estimates, would be \$28.1 billion instead of the \$27.8 billion noted above.

A significant aspect of accounting for revolving funds on a net outlay basis is that when new programs are enacted or an existing revolving fund grows, budget outlays do not increase as rapidly as they would if accounted for on a gross basis. Changing an established account to a revolving fund gives the appearance that budget outlays are declining, even though the rate of expenditure may remain the same or even increase. Using revolving fund financing might help to reduce budget totals by changing fund structure without changing fund purposes. Therefore, accounting for revolving funds on a net basis has an adverse effect upon setting spending priorities by function (under the provisions of the Congressional Budget Act of 1974) by giving certain functions with many revolving funds an advantage over other functions which do not have as many revolving funds.

Changes in the level of net dollar transactions within public enterprise funds can have a direct and significant effect on the budget deficit which the Congress has attempted to control under the Congressional Budget Act of 1974.

Revolving funds, which are often removed from the direct control of the Congress, are very volatile in nature with large unpredictable swings in net outlays of funds. For example, when the fiscal year 1975 budget was proposed, total public enterprise net outlays were estimated to be about \$3.4 billion. The actual net outlay for these funds (2 years later) was \$7.6 billion. This was an increase of \$4.2 billion, or 124 percent.

Revolving funds are not established by the Congress on the basis of any uniform criteria as to when revolving fund

financing is necessary or appropriate. Moreover, authorizing legislation does not always clearly provide that a revolving fund is to be established. GAO, Treasury, and OMB provide different criteria for the classification of accounts as revolving funds. Some accounts classified as revolving funds do not meet the written criteria. For instance, although the criteria specifies that an activity should be self-financing, outlays often exceed receipts by large amounts in many public enterprise revolving funds. When this happens, the funds must receive some form of additional budget authority through appropriations acts. Other programs, with operations similar to revolving fund programs, have not been established as such by the Congress.

These actions are contrary to the recommendations of the President's Commission on Budget Concepts. Furthermore, the accuracy of account classification is important because of (1) the way certain funds are treated under the Congressional Budget Act of 1974, (2) application of laws restricting receipt or expenditure of certain funds, (3) analyzing trends in certain accounts, and (4) budget reporting and accounting requirements, especially net versus gross reporting in the budget.

By authorizing a program to finance its operations through revolving funds, the Congress relieves the Appropriations Committees' responsibility for limiting spending authority for the program. Since the program's use of receipts is often authorized without need for further congressional action, determination of the size of the activity tends to pass to the agency. The activity tends to escape congressional oversight so long as the account can generate sufficient revenues to match its operating expenditures.

While this lessening of congressional control is the general result of revolving fund financing, this does not always have to be the case. During our analysis of revolving funds, we found many examples of the Congress taking specific legislative steps to establish controls over individual revolving funds or over revolving funds as a general category.

REVOLVING FUNDS

Any of our opinions, suggestions, or objections on the use of revolving funds are usually governed by the Congress weakening its control over a program's activities by authorizing the use of this funding mechanism. The Congress, along with the executive branch, should control Federal activities. Over the years we have applied the standard that the public

interest is best served when congressional control over activities is exercised through regular (usually annual) reviews and affirmative action on planned programs and financing requirements through the appropriations process.

It has been our opinion that departure from the above standard should be permitted only when it can be fairly shown that an activity cannot be successfully operated in the public interest within the congressional appropriation process.

Departures from this standard should not be allowed unless it can be plainly demonstrated that:

1. Hindrances to effective management exist.
2. The change in financing method will remove, or help to remove, existing hindrances.
3. Other alternatives within the regular appropriation structure are inappropriate.
4. The demonstrated advantages attributable to the departure clearly outweigh the disadvantages of lessened congressional control, preferably with a congressional expression to that effect.

We believe it is necessary that the Congress be fully aware of the cumulative effect revolving funds have on congressional control, especially budgetary control, before authorizing additional revolving funds. Now, as in the past, the establishment of revolving fund accounts usually is done on an ad hoc basis by the Congress.

As shown in this report, the way revolving funds are accounted for in the budget (netting) understates Government financial activities by billions of dollars each year and excludes these activities from the process by which the Congress establishes priorities and allocates resources. When the Congress passes legislation authorizing revolving funds, we must assume that the Congress has in most cases decided to relax its control over the activity. It would be preferable if the Congress took this action after giving explicit consideration to the advantages and needs justified in each case in relation to the lessening of congressional control. The Congress, through annual appropriation action, should pass on the agency's financial and operating plans before they are consummated. Often legislation provides that funds may be used for various purposes "within such

limitations as may be included in appropriation acts." While this would recognize the appropriations acts as a method for the exercise of congressional control, this is a permissive approach which does not require positive action by the Congress to impose limitations on the use of funds and does not necessarily result in detailed reviews by the Congress of activities financed by the revolving fund. The need for positive action (appropriations process) requires the Congress to evaluate the need for limitations and for assuring that funds provided are applied to the purpose for which the Congress intends.

ALTERNATIVES TO REVOLVING FUND FINANCING

The alternative to revolving fund financing which would establish the strongest congressional control over both individual programs and budget outlays is to finance these programs through annual appropriations (i.e., authorize these programs as "general fund" accounts). In the past, there have been a number of reasons put forth as to why revolving funds cannot be under yearly appropriations constraints. Among the more widely used reasons were the need for (1) flexibility, (2) cost awareness, (3) complexities of financing common use items, and (4) better accounting, budgeting, and reporting. When reviewing individual cases, these arguments are not always valid, and viable alternatives exist which preserve these special benefits of revolving fund financing. For example, the most widely used argument for creating a revolving fund is the need for flexibility.

In most instances, it is suggested that the appropriations process cannot work fast enough to meet the fund's needs. There are, however, various other alternatives that may be used. Besides the alternatives discussed in detail in the full report which exert congressional controls over specific revolving funds, the Congress could specify a stated amount as a permanently available, separate "emergency fund." The fund could be replenished in the amounts disbursed therefrom by annual appropriations. This would allow flexibility while retaining firm congressional control over normal operations (i.e., renewal action on individual programs, inclusion of full program outlays in budget resolutions, allocations, etc.). This alternative appears fully consistent with the present appropriations process.

CONCLUSIONS

The fundamental objective of the Congressional Budget Act of 1974 was to establish a process through which the

Congress could systematically consider the total Federal budget and determine priorities for the allocation of budget resources. We believe this process achieves its maximum effectiveness when the budget represents as complete as possible a picture of the financial activities of Federal agencies.

For example, accounting for public enterprise revolving funds in the Federal budget on a net outlay basis, whereby the accounts receipts are offset against gross outlays with only the difference being included in the budget figures, is misleading. It understates the true magnitude of Government activities as well as the impact of individual revolving fund programs. The Federal budget should disclose the magnitude of Federal activity in such a way as to provide a basis for estimating the impact of Government activity on the economy as a whole.

In the past, the Congress has established revolving funds where their use did not seem appropriate. Moreover, OMB and Treasury have classified accounts as revolving funds which in some instances did not meet their criteria. Therefore, there is no assurance that accounts presently accounted for as revolving funds should or need to be so classified.

EFFECT OF INCLUDING PUBLIC ENTERPRISE REVOLVING FUNDSIN THE BUDGET TOTALS ON A GROSS VERSUS NET BASISBY FUNCTION FOR FISCAL YEAR 1977

(in millions of dollars)

Function	No. accts.	Net outlays (as presently accounted for in budget)	Gross outlays (as GAO recommends accounting for in budget)	Difference between gross and net outlays a/ (amount change would increase budget totals)
National defense	6	\$ -7	\$ 22	\$ 28
International affairs	5	1,278	3,996	2,718
General science, space, and technology	-	-	-	-
Natural resources, en- vironment, and energy	7	1,263	3,679	2,516
Agriculture	4	352	6,347	5,995
Commerce and trans- portation	26	1,950	12,069	10,120
Community and regional development	15	1,348	3,433	2,084
Education, training, employment, and social security	2	104	182	79
Health	5	26	104	78
Income security	3	-15	649	664
Veterans benefits and services	8	-403	950	1,353
Law enforcement and justice	-	-	-	-
General government	4	-1	1	2
Revenue sharing and general purpose fiscal assistance	1	0	2,100	2,100
Multiple functions	1	*	101	101
Total Budget accounts	87	\$5,810	\$33,647	\$27,837
Off-budget accounts	6	2,219	17,386	15,167
Total	93	\$8,028	\$51,033	\$43,004

a/Difference between gross and net outlays equals the receipts of the revolving fund. Functional figures may not add up to total budget account figures due to rounding.

*Less than one million.