

GAO

Report to the Chairman, Legislation and
National Security Subcommittee,
Committee on Government Operations,
House of Representatives

June 1986

INTERNAL CONTROLS

Defense's Use of Emergency and Extraordinary Funds



130467

RESTRICTED—Not to be released outside the General
Accounting Office except on the basis of specific
approval by the Office of Congressional Relations.

RELEASED

**Accounting and Financial
Management Division
B-221257**

June 4, 1986

The Honorable Jack Brooks
Chairman, Legislation and National Security
Subcommittee
Committee on Government Operations
House of Representatives

Dear Mr. Chairman:

This report responds to your inquiry about the Department of Defense's accountability over funds authorized by Defense's annual operation and maintenance appropriations for emergency and extraordinary (E&E) expenses. These funds are used for official representation expenses, such as entertaining the guests of Defense, and for confidential expenses, such as those related to intelligence activities. In fiscal year 1985, Defense spent approximately \$25 million for E&E expenses. You asked that we determine if Defense has established procedures to control the use of these funds and whether the procedures are adequate and are being followed.

We identified weaknesses in controls that should be addressed by Defense to ensure that the funds are adequately controlled.

- The Office of the Secretary of Defense (OSD) lacks a vital control over E&E funds used for confidential expenditures: It has not issued a departmentwide regulation setting forth criteria for how the funds may be used. As a result, regulations issued by Defense components governing the use of the confidential funds are inconsistent on whether the funds can be spent in violation of any law. Given the broad authority in 10 U.S.C. 140 for spending the funds for any purpose deemed proper, OSD should set criteria for how Defense components may use the funds. Another important control feature over checking accounts for confidential funds was lacking in the Army Intelligence and Security Command and the Air Force Office of Special Investigations. Units under these organizations were not separating critical duties to control checking accounts.
- While OSD has issued a departmentwide regulation establishing criteria on how E&E funds for official representation may be used, the regulation was not always followed. Contrary to the regulation, there were instances in which E&E funds were spent on the entertainment of Defense personnel. In addition, Defense components repeatedly used the funds for expenditures that we believe were not of an emergency and

extraordinary nature. Expenditures for the entertainment of Defense personnel and expenditures that were not of an emergency and extraordinary nature accounted for about \$112,228, or 19 percent, of the \$601,465 in official representation expenses we examined.

A discussion of E&E funds and the details of our work follow

Background

Under the provisions of 10 U.S.C. 140, Defense's annual appropriation acts contain authority for Defense components to spend funds from their operations and maintenance appropriations for emergency and extraordinary expenses. Within Defense, the funds are generally grouped into two categories: official representation and confidential military purposes. Official representation funds are authorized for maintaining the standing and prestige of the United States by extending official courtesies to guests of Defense. The funds for confidential military purposes are generally authorized for Defense investigative and intelligence activities when the use of the normal funding channels would compromise the security of operations, jeopardize the safety of personnel and sources involved, or result in losing an investigative or intelligence opportunity.

Defense expenditures for E&E expenses in fiscal years 1984 and 1985 were about \$24 million and \$25 million respectively. In both fiscal years, approximately 86 percent of the E&E expenses were for confidential purposes.

The law provides that E&E funds may be spent on the approval or authority of the Secretary of Defense or the service Secretary concerned for any purpose determined to be proper. While this authority is broad, Defense components must comply with governing Defense regulations when spending the funds. For example, OSD's regulation governing official representation funds prohibits expenditures for personal items, such as clothing and toilet articles, and requires that certain ratios of Defense personnel to authorized guests be maintained when spending the funds on social or entertainment activities for Defense guests.

Objectives, Scope, and Methodology

The primary objectives of our review were to determine whether adequate procedures were in place to control the use of the funds allotted to E&E expenses and to determine whether the procedures were being followed. We conducted our review at 18 of 175 organizations in the Army,

Navy, Air Force, and Defense Intelligence Agency that incur E&E expenses.

The organizations reviewed were selected based on the dollar amount of their E&E expenses for fiscal year 1984, the type of expenditures made (official representation or confidential), and the organizations' locations. Together, the expenditures made by the 18 organizations accounted for approximately 37 percent of Defense's E&E expenses in that fiscal year. To avoid duplicating prior audit work, we also considered Defense's audit coverage of E&E funds in making our selections.

We reviewed appropriate regulations, procedures, and accounting and related records, and interviewed Defense officials. To test the control procedures and determine compliance, we selected and reviewed at the locations we visited \$4.1 million out of \$14.9 million in available expenditure transactions from fiscal years 1984 and 1985.

In selecting the transactions for review, we determined the major categories of expenditures at each location visited and judgmentally selected transactions from each category to ensure that we examined the various types of expenses for which the funds were used. Our review was conducted from May 1, 1985, to January 31, 1986. Our work was performed in accordance with generally accepted government auditing standards, with one exception. As you requested, we did not obtain formal comments from Defense officials.

Controls Over Confidential Funds Can Be Strengthened

Defense lacks an important ingredient in its management control of E&E funds used for confidential purposes because OSD has not issued a regulation establishing criteria as to how such funds may be used. As a result, Defense components' regulations¹ for the confidential funds related to intelligence activities do not consistently spell out restrictions as to how the funds may be used. While one component's regulation clearly states that the funds are not to be used in violation of law, the others provide for exceptions. Also, the views of various Defense officials differ on whether the confidential funds may be used in violation of law.

We also found that the regulations of the Army Intelligence and Security Command and of the Air Force Office of Special Investigations do not

¹Defense component regulations implement OSD regulations

require adequate separation of duties related to checking account responsibilities for confidential funds.

Components' Regulations and Defense Officials' Views on Use of Confidential Funds Are Inconsistent

Lack of an OSD regulation setting criteria on what confidential funds may be used for has resulted in inconsistencies in components' regulations. The Defense Intelligence Agency's regulation prohibits the use of confidential funds for purposes that would violate law. The Defense Intelligence Agency's regulation states that the funds "will not be used for purposes expressly forbidden by statute" and does not provide for any exceptions. While the Army, Navy, and Air Force regulations cite certain restrictions, their expenditure review and approval processes allow for exceptions. The regulations for these three services do not contain language which, as in the case of the Defense Intelligence Agency, clearly forbids expenditures that would be in contravention of any law without exception.

OSD intelligence officials acknowledged that components' regulations are inconsistent about whether the funds can be used in violation of law. They advised, however, that all intelligence activities, regardless of what funds are used, are to be conducted in accordance with Executive Order 12333, United States Intelligence Activity. This order states that the collection of intelligence information will be pursued in a responsible manner that is consistent with the Constitution and applicable law; the order specifically prohibits activities such as assassinations and unauthorized electronic surveillance.

We asked Defense officials whether E&E funds could be used in violation of law and found that their views varied. An OSD general counsel official would not say whether the funds could be used illegally, but told us that the purpose of the emergency and extraordinary authority was to make funds available for uses which would otherwise be unauthorized. An Army general counsel official advised us that he interpreted the OSD view to be that the funds could be used for any purpose unless specifically prohibited by statute. The official explained that if a statute does not specifically state that E&E funds cannot be used, then these funds could be used in contravention of that statute.

A Navy intelligence official told us that since E&E funds can be spent for any purpose determined to be proper, the intelligence command can spend the funds on anything so long as the appropriate department head's approval is obtained. Finally, Defense Intelligence Agency and

Air Force intelligence officials believe that the funds are not to be used in violation of any law.

When asked why a departmentwide regulation has not been issued for the confidential funds, an OSD official responded that there is no such regulation because 10 U.S.C. 140 allows the confidential funds to be used at the discretion of the heads of the Defense components concerned. However, we noted that this view is not consistent with the fact that OSD has issued a departmentwide regulation for the official representation funds, which are also governed by 10 U.S.C. 140.

The departmentwide regulation for official representation was issued because OSD wanted assurance that the Defense components were using representation funds for appropriate purposes. Similarly, issuing an OSD regulation would establish uniform requirements on what OSD considers to be appropriate uses of confidential funds.

Controls Over Checking Accounts Need Improvement

At five Army Intelligence and Security Command locations and one Air Force Office of Special Investigations location we visited, the same individuals who controlled the checking accounts for confidential funds also reconciled the checking accounts' balances to the monthly bank statements. Such a procedure can result in a manipulation of an account's records to cover errors or wrongful acts. Although we did not identify any improprieties, the reconciliation of the checking account records to the monthly bank statements should be performed by an independent person to reduce the risk of potential improprieties.

Both the Security Command and the Special Investigations Office regulations allow the same individual responsible for controlling checking accounts to also perform the monthly check reconciliations. This is a serious internal control weakness. The procedures should provide for adequate separation of duties.

Official Representation Funds Improperly Used

Our review of selected fiscal year 1984 and 1985 transactions disclosed that certain expenditures for official representation were either prohibited by regulations or were not of an emergency and extraordinary nature. These expenditures accounted for approximately \$112,228, or 19 percent, of the total \$601,465 in official representation expenditures we reviewed.

Components Made Prohibited Expenditures

OSD's regulation governing representation funds provides that expenses can be incurred to maintain the standing and prestige of the United States by extending official courtesies to guests of the Department of Defense. The regulation defines authorized guests to be (1) distinguished and prominent United States citizens who have made a substantial contribution to the nation or the Department of Defense, including individuals who are recognized leaders in their fields, (2) dignitaries and officials of local, county, state, and federal governments, and (3) dignitaries and officials from foreign governments.

OSD's regulation allows the funds to be used for entertainment expenses of Defense personnel when they are involved with extending official courtesies to authorized guests. However, use of the funds for entertaining Defense personnel is prohibited. Defense components' regulations contain similar provisions.

In certain headquarters offices in the Army and Navy, we found that the regulations regarding expenses for authorized guests were not being followed since representation funds were used for expenses that were primarily for the benefit of Defense personnel. Examples illustrating these exceptions follow:

- An Army general spent \$530.80 of fiscal year 1985 E&E funds to host a "stag" dinner for members of the Brigadier General Selection Board. The guest list shows that all of the attendees were Defense personnel.
- The Chief of Naval Operations hosted a hospitality tent at the Army-Navy football game on November 25, 1983. In a memorandum to the Navy Assistant for Administration, a Navy reviewing official hesitated to request payment, citing the "personal nature" of this event. The expense voucher was subsequently approved, and the E&E expense account was charged \$2,408.46.

While the authority to incur E&E expenses is broad, we were told by an OSD official that Defense components are not allowed to make exceptions that are contrary to the provisions of OSD regulations. Therefore, OSD should take appropriate action to obtain reimbursement for E&E expenses that were primarily for the benefit of Defense personnel.

Appendix I lists other examples of expenditures that were contrary to regulations.

Funds Used for Expenditures That Were Not of an Emergency and Extraordinary Nature

While Defense's annual appropriation acts authorize the use of funds for E&E expenses, our review identified expenditures that were not of an emergency and extraordinary nature as they recur on a regular basis and clearly could have been anticipated. OSD's regulation does not address the use of E&E funds to pay for events that recur regularly. Therefore, in determining whether an expenditure was for an emergency and extraordinary purpose, we applied the ordinary meanings of the words emergency and extraordinary. That is, in order for an expenditure to be considered an E&E expense, it should be related to an urgent or unforeseen situation of an unusual nature.²

Although E&E funds may be spent for any purpose determined to be proper, we are questioning the propriety of using the funds for recurring events. Examples of these recurring events follow.

- As in past years, the Army, Navy, and Air Force jointly hosted a Christmas reception for congressional staff in December 1984. These services spent \$5,236.35 of E&E funds for the reception.
- A Navy admiral holds monthly executive panel meetings, which are attended by various Defense and non-Defense officials. According to Navy officials, these monthly meetings have been going on for at least the past 10 years. The E&E expense account is charged for breakfast, lunch, dinner, and reception expenses in connection with the meetings. For fiscal year 1985, we identified approximately \$3,533 for these expenditures that were charged to the E&E account.

Appendix II lists other examples of recurring expenditures charged to E&E expense accounts.

Conclusions

OSD should have a departmentwide regulation governing all E&E funds, not just those used for official representation. Such a regulation providing overall OSD policy regarding the use of these funds should eliminate the inconsistency we noted in the components' regulations. Also, the Army Intelligence and Security Command and the Air Force Office of Special Investigations need to amend their regulations to provide for better internal controls over checking accounts.

²In a prior GAO report, *Review of Unvouchered Expenditures at the Department of State* (AFMD 82-57, March 23, 1982), we questioned the propriety of certain expenditures made from State's emergency expense account since the expenditures were not related to unforeseen emergencies.

While Defense components have been given broad authority in the use of E&E funds, they should not make expenditures that are for the benefit of Defense personnel. Appropriate action should be taken to obtain reimbursement for expenditures that were made for the benefit of Defense personnel. In addition, Defense should not be using official representation funds to pay for recurring events because they can be anticipated and, therefore, are not of an emergency and extraordinary nature.

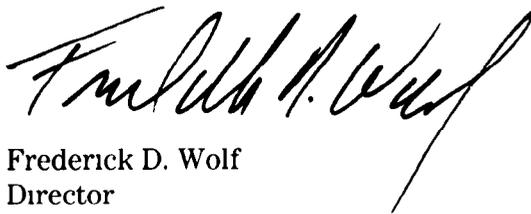
Recommendations

We recommend that the Secretary of Defense take the following actions:

- Issue a departmentwide regulation governing all uses of E&E funds, not just those for official representation. At a minimum, this regulation should establish criteria regarding the purposes for which confidential funds can or cannot be used.
- Direct the Secretary of the Army and the Secretary of the Air Force to require the Army Intelligence and Security Command and the Air Force Office of Special Investigations to revise their regulations to require an adequate separation of duties in controlling checking accounts used for E&E funds.
- Direct all Defense components authorized to use E&E funds for official representation to examine their records for at least the past 2 fiscal years and obtain reimbursement for E&E expenditures that were made primarily for the benefit of Defense personnel
- Require that all regulations governing representation funds prohibit using such funds in the future for recurring events.

Unless you publicly announce its contents earlier, we will not distribute copies of this report until 30 days from its date. After 30 days, we will send copies to the Director of the Office of Management and Budget, the Secretaries of Defense, the Army, Navy, and Air Force, and the Director of the Defense Intelligence Agency as well as any other interested parties. Copies will also be made available to others on request

Sincerely yours,



Frederick D. Wolf
Director

Examples of Expenditures Primarily for the Benefit of Defense Personnel

| | | |
|---|---|------------|
| 1 | Army hosted reception in honor of command sergeant majors on September 8, 1985 | \$6,951 60 |
| 2 | Army hosted receptions in connection with the Reserve Component National Security Issues Seminar on November 26, 1984, and May 14, 1985 | \$4,200 20 |
| 3 | Navy admiral hosted a dinner in honor of the Secretary of Defense on December 14, 1984. Additional funds were approved for the purchase of a Christmas tree and other decorations for the dinner and other functions | \$741 91 |
| 4 | Navy hosted reception in honor of a U S military officer on August 8, 1984 | \$641 37 |
| 5 | Army picnic held for command sergeant majors and their wives on September 13, 1985 | \$442 36 |
| 6 | Dinner held on April 19, 1985, for members of a U S Army accident investigation team | \$170 93 |
| 7 | Army hosted reception following the Army Family Week ceremony on November 23, 1984 | \$137 50 |
| 8 | Navy commodore hosted luncheon for his deputy and several other Defense personnel on May 31, 1984. In a memorandum for the Secretary of the Navy concerning the expense, the General Counsel for the Navy stated, "each of the attendees should pay their own share" and recommended that the Secretary deny payment of the expense, the expenditure was approved | \$69 18 |
| 9 | Secretary of the Army purchased a bathrobe on October 5, 1984, which was given to the Secretary of the Navy (It has been a tradition that the losing Secretary of the Army-Navy football game buy the winning Secretary a bathrobe) | \$33 33 |

Examples of Expenditures Which Are Not of an Emergency and Extraordinary Nature

| | | |
|----|--|-------------|
| 1 | Air Force hosted dinner for foreign air attachés stationed in U S on May 17, 1985 (annual event) | \$15,317 08 |
| 2 | Air Force held outing (including golf and tennis tournament) for foreign air attachés stationed in U S on July 6, 1984 (annual event) | \$7,246.38 |
| 3 | Air Force hosted a conference from February 14-16, 1985. Related expenses were primarily incurred by guests of the Air Force. These expenses included recreational activities such as golf and deep-sea fishing (annual event) | \$4,337 95 |
| 4 | Commander-in-Chief of Eighth United States Army, Korea, hosted New Year's reception for various Defense, U S Embassy, and Korean military and civilian officials on January 4, 1985 (annual event) | \$5,392.05 |
| 5 | Military departments jointly hosted Christmas reception for Senate staff on December 14, 1983 (annual event) | \$2,198 45 |
| 6 | Air Force hosted holiday receptions for select group of entertainment industry officials, civic leaders, industrial executives, elected officials, and news media on December 4 and 13, 1984 (annual event) | \$2,666.24 |
| 7 | Air Force hosted tour for foreign air attachés stationed in U S , from September 23-29, 1984 (annual event) | \$2,417 35 |
| 8 | Navy department held birthday breakfast for Members of Congress and staff on October 3, 1984 (annual event) | \$1,800 00 |
| 9 | Secretary of Air Force hosted 21st annual golf tournament attended by Members of Congress and staff on May 6, 1985 (annual event) | \$1,650 96 |
| 10 | Marine Corps held birthday reception for Members of Congress and staff on November 9, 1984 (annual event) | \$238 40 |

Requests for copies of GAO reports should be sent to:

U.S. General Accounting Office
Post Office Box 6015
Gaithersburg, Maryland 20877

Telephone 202-275-6241

The first five copies of each report are free. Additional copies are \$2.00 each.

There is a 25% discount on orders for 100 or more copies mailed to a single address.

Orders must be prepaid by cash or by check or money order made out to the Superintendent of Documents.

United States
General Accounting Office
Washington, D.C. 20548

Official Business
Penalty for Private Use \$300

Address Correction Requested

First-Class Mail
Postage & Fees Paid
GAO
Permit No. G100