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Financial And Program Controls Of Selected Community Action Agencies

B-130515

Office of Economic Opportunity

**UNITED STATES
GENERAL ACCOUNTING OFFICE**

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AUG. 23, 1973



UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

MANPOWER AND WELFARE
DIVISION

Handwritten initials

B-130515

Mr. Randal C. Teague
Acting Assistant Director
for Operational Activities
Office of Economic Opportunity 157

Dear Mr. Teague:

This is our report on the internal financial and program controls of selected community action agencies (CAAs) funded by the Office of Economic Opportunity (OEO) under title II of the Economic Opportunity Act of 1964, as amended. The report summarizes the results of (1) audits of OEO grantees by certified public accountants, the OEO Audit Division, and other independent auditors, (2) our 21 reviews of grantees' financial activities made pursuant to congressional requests, and (3) our review in calendar year 1972 of the financial controls of 12 CAAs and the program controls of 42 CAAs. 957

Weaknesses in financial controls were found by OEO auditors, independent auditors, and our reviews made pursuant to congressional requests. Our review in calendar year 1972 at 42 selected CAAs found weaknesses in financial and/or program controls which detracted from overall operations.

Grantees were selected for various reasons. Some were selected on the basis of their (1) indicated problems, (2) geographical area, (3) size perspective (large, medium, and small), and (4) proximity to other grantees previously selected to aid our field reviews. Because our selections were not randomly made, the results of our reviews are not representative of all grantees but indicate clearly a continuing need for improved financial and program controls.

A number of programs authorized by the Economic Opportunity Act, as amended, and delegated to the Departments of Labor and Health, Education, and Welfare (HEW) and other agencies, such as the Neighborhood Youth Corps and Head Start, are funded through the CAAs.

An official of the Manpower Administration, Department of Labor, said our observations on CAA financial and program controls would assist Department of Labor officials in their future dealings with CAAs.

Officials of the Office of Child Development said that they plan to evaluate operations of all Head Start programs currently

funded through CAAs and that our observations on financial and program controls would assist them in deciding whether the CAAs should continue to fund Head Start programs.

Accordingly, we are sending copies of this report to HEW and Labor officials.

FINANCIAL CONTROLS

The effectiveness of antipoverty programs depends considerably on the manner in which grantees administer individual projects. Accordingly, Federal agencies responsible for operating such programs should require grantees to exercise adequate controls to insure that funds, property, and services are effectively used and properly accounted for.

Weaknesses in financial controls were found principally in the areas of payroll, travel, procurement, property management, and maintenance of basic accounting records. The nature and intensity of these weaknesses varied from grantee to grantee.

ANNUAL INDEPENDENT AUDITS OF GRANTEEES

OEO's External Audit Division maintains a system for follow up on corrective action on audit findings. This system includes classifying grantee accounting systems and/or internal controls as adequate, weak, or inadequate, based on independent audit reports.

About 3,500 audit reports were prepared on grantees by certified public accountants, other licensed public accountants, and independent agencies from July 1, 1970, to December 31, 1972. The Audit Division classified more than 40 percent of the audit reports as showing that the grantees had inadequate or weak accounting systems and/or systems of internal controls.

The following table shows the number of audit reports received during fiscal years 1971 and 1972 and the first 6 months of fiscal year 1973 and the Audit Division's opinions of accounting and/or internal control systems discussed in the reports.

	Total reports received	Systems considered inadequate		Systems considered weak		Systems considered adequate (note a)	
		Number	Percent	Number	Percent	Number	Percent
Fiscal year 1971	1,454	111	8	539	37	804	55
Fiscal year 1972	1,472	86	6	552	38	834	56
First 6 months of fiscal year 1973	^b 621	39	6	222	36	360	58

^aNumber of adequate systems may be overstated. About 60 percent of over 1,000 audit reports on grantee operations issued in fiscal year 1970 reported no major accounting system and/or internal control deficiencies. We reviewed 27 from this group and found that 17 failed to disclose significant deficiencies in grantees' financial operations. See our report to the Congress entitled "Need for More Effective Audit Activities," Office of Economic Opportunity (B-130515, Apr. 4, 1973).

^bTwenty additional audit reports were received which did not contain an evaluation of the accounting system and/or system of internal controls.

Of the 360 systems considered adequate during the first 6 months of fiscal year 1973, OEO's summary showed that 118 contained no deficiencies or questioned costs; OEO did not consider the deficiencies cited in the remaining 242 reports significant enough to require that the grantee be classified as having an inadequate or weak accounting system and/or system of internal controls. Such deficiencies included

- questionable expenditures,
- lack of required personnel or property records,
- excess costs incurred for property and services,
- organizational weaknesses,
- lack of controls over contracting,
- financial statements not prepared and/or used by management,
and
- inadequate non-Federal share for grants.

By letter dated May 31, 1973, OEO stated it is mainly concerned with correcting weaknesses disclosed in a given report, rather than the percentage of audits classified under the broad category of weak accounting system. Our April 4, 1973, report indicated that OEO was lenient in disposing of auditors' monetary and

nonmonetary exceptions and, as a result, grantees' deficiencies were perpetuated in many cases.

SUMMARY OF OUR AUDITS OF 21 GRANTEES

During fiscal years 1971, 1972, and 1973, as a result of financial audits of 21 CAAs made at the request of Members of Congress, we reported that:

- Financial controls of three grantees were generally inadequate.
- Financial controls of six of the grantees were generally adequate although various weaknesses were noted.
- Financial controls of the other 12 grantees were weak.

These audits covered various program years between 1965 and 1972, and our tests were limited, sometimes to 1- or 2-month transactions. Although our findings may not be typical of all grantees--since many of the requests stemmed from complaints about grantees' operations--we believe the findings indicate a need for improved financial controls over grantees' operations.

Payroll and personnel records

Seventeen of the 21 grantees did not properly maintain payroll and personnel records.

At five grantees, time and attendance (T&A) records were not maintained or were not kept current for all employees. At seven grantees, T&A records either lacked employees' signatures, their supervisors' signatures, or both. Also, at one grantee, supervisors approved their own T&A records.

At 6 of the 21 grantees, leave records were not maintained for all employees, or they were not kept current. At seven grantees, including one of the preceding, grantees made errors in computing employees' leave and in recording it. OEO instructions required that starting salaries exceeding \$5,000 be limited to an amount which does not exceed, by more than 20 percent or \$2,500, whichever is less, the person's salary at his last employment unless approved by OEO. Personnel files at 12 grantees did not always contain information on employees' salaries at their prior employment. Employees at six grantees were started at salaries exceeding these limitations without OEO approval.

Six grantees had granted employees salary increases above the OEO prescribed limitations without OEO's approval. At one grantee, OEO approved salary increases above prescribed limitations for five employees, but the information the grantee submitted was incorrect.

Other weaknesses follow in internal controls over payroll functions.

- Two grantees did not adequately segregate various payroll functions.
- One grantee allowed six employees to accumulate a total of 894 hours of compensatory time without requiring them to obtain prior OEO approval for the additional time and for insuring that the time was necessary.
- Two grantees had inadequate controls over employee loans and advances; one had made loans to 74 employees, or 31 percent of its staff members.
- Two grantees paid severance pay, totaling about \$7,200, to 15 unauthorized individuals.
- Two grantees prepared payrolls before completing and submitting supporting T&A records.
- Two grantees did not pay for payroll tax liability when due to the Internal Revenue Service.

Travel

Weaknesses existed in internal controls over travel expenditures at 16 of the 21 grantees.

At each of the 16 grantees, adequate documentation was not available to support the reasonableness of all travel costs claimed, including 5 grantees at which travel vouchers were not always submitted. Employees at seven grantees did not always obtain written authorizations before traveling. At one of the grantees, travel had not been authorized in advance for 20 of 33 travel claims paid during a particular month for travel outside the grantee's normal operating area.

Two of the more significant examples of weak controls involved support for the travel costs incurred.

1. A review at one grantee of \$11,756 of \$57,389 reported as travel expenditures during program year 1971-72 showed that expenditures of \$1,960 were not adequately supported.
 - Per diem claims totaling \$1,215 did not show the period of travel, including times of departure and return, which were the basis for computing per diem.

--Travel vouchers for out-of-town travel totaling \$500 had no supporting travel authorizations.

--Mileage claims of \$245 were not properly supported by odometer readings.

2. A review of \$933 of travel costs incurred during a 2-month period at another grantee showed that \$452, or 48 percent, had not been adequately supported by the travel vouchers or other documentation, as required under the Standardized Government Travel Regulations.

We found only check stubs and canceled checks to support \$365 of these costs. The supporting vouchers or other documentation for the remaining \$87 did not show odometer readings or, where odometer readings were shown, mileage computations did not agree with the readings.

At five grantees, travel advances were not recorded in the agencies' books as advances but were charged directly to expense accounts. This lessened the agencies' controls over the funds and increased the possibility of overstating expenses because advances might not be liquidated based on actual expenses incurred.

For example, travel advances of \$1,444 at a grantee had been charged to travel expense accounts instead of to employee receivable accounts pending subsequent offset against travel expense vouchers.

Procurement

We noted weaknesses in the internal controls over grantees' procurement processes in 10 of the 21 grantees audited.

Nine grantees lacked adequate receiving reports or other evidence that certain goods or services paid for had actually been received. Also, at seven grantees, purchase orders generally were not prepared or were prepared after the purchase was effected.

Other procurement deficiencies noted included such things as duplicate payments of invoices, competitive prices not obtained from potential suppliers, and overpayments resulting from a failure to audit billings before payment.

Examples of weaknesses in internal controls over procurement at various grantees follow.

1. For each of the 364 procurement transactions totaling about \$100,000 that we examined at 1 grantee, 1 or more of the following discrepancies existed.

- Large purchases were made without approved purchase orders or evidence of approval by responsible agency officials.
 - Purchase orders supporting recorded expenditures were not on file, and these few on file were frequently incomplete.
 - Vendors' invoices were not on file.
 - Payments were made without evidence that goods and/or services were received or authorized.
 - Preaudits of billings were not made--we identified four overpayments totaling about \$312 resulting from duplicate payments and mathematical errors.
 - State taxes were paid even though the grantee was tax exempt.
2. We reviewed 161 payments made during a 2-month period at another grantee for supplies, services, equipment, and miscellaneous items totaling \$25,228. The grantee had not fully complied with its procedures or OEO guidelines, which provide that purchases be initiated by purchase orders or requisitions and that the receipt of goods and services be adequately documented. Also, the grantee did not have an effective procedure for auditing billings before payment and for examining records to prevent duplicate payments. Of the 161 payments reviewed, 155 totaling \$23,994 were not supported by purchase orders or requisitions. Further, 62 of these payments totaling about \$6,600 were not supported by signed receiving reports showing what was actually purchased and delivered.
 3. Of a grantee's expenditures of \$23,311 in August 1970 for supplies, equipment, contractual services, and space rentals, \$7,210 was questionable for the following reasons.

<u>Cost category</u>	<u>Amount expended</u>	<u>Amount questioned</u>	<u>Basis for questioning</u>
Consultant and contract services	\$ 3,858	\$2,220	Amounts not provided for in budget as required by OEO guidelines
Space rentals	14,998	3,375	Rentals for time periods for which no lease agreement existed
Consumable supplies	2,102	797	No purchase authorization or evidence of receipt
Equipment	2,353	38	Duplicate payment
		<u>780</u>	No purchase authorization
Total	<u>\$23,311</u>	<u>\$7,210</u>	

Nonexpendable property

Controls over nonexpendable property were weak or inadequate at 9 of the 21 grantees audited. Seven grantees either did not always prepare property control cards and those prepared were incomplete, inaccurate, or not current.

At four grantees, documentation was not available showing that annual inventories were taken as OEO required. Three grantees submitted inaccurate or out-of-date inventory reports.

At five grantees, tests of inventory records showed them to be inaccurate. One of the most significant examples follows.

In a test of 88 nonexpendable items valued at \$8,600 on the grantee's inventory listing, 17 valued at \$2,900 were located. Of the remaining 71 items

--61 valued at about \$4,300 could not be positively identified because they did not have any identification numbers matching those on the inventory listing, although items meeting their general description were on hand, and

--10 valued at about \$1,400 could not be located; the acting executive director was unable to furnish us with the locations of these items.

In addition, four items--two fluid duplicators, a copying machine and a recorder--marked as property of the grantee were not recorded on the inventory listing. Also, two stoves and three filing cabinets were on hand, but no information was available as to whether the grantee owned them.

Cash controls

Seven of the 21 grantees had weaknesses in their internal controls over cash.

Control over the signing of checks was inadequate at two grantees--at one, several individuals had access to both required signature stamps and at the other, where two individuals were also required to sign checks, individuals would occasionally sign blank checks if they planned to be away from the main office at a time when a number of invoices were expected to be paid.

At another grantee, 151 checks totaling \$3,380 were made payable to cash from April 1971 through April 1972 and were reportedly cashed by employees of the grantee for purchasing food stamps for needy persons. Because controls were inadequate over these expenditures we could not determine whether the funds were used to acquire food stamps. In addition, 79 of the 151 checks were written in amounts exceeding the \$15 limitation printed on the checks. The amounts on the 79 checks ranged from \$16 to \$129.

We also found that one grantee did not promptly deposit its cash receipts and that another grantee did not promptly reconcile its bank statements, in some cases several months late.

Three grantees were maintaining cash balances exceeding program needs without placing the funds in interest-bearing accounts. An example follows.

The grantee received OEO's check for \$164,000 in July 1970 and held it until September 30, 1970, when it was placed in a non-interest-bearing checking account. No project expenditures were made until October 1970. A large part of these funds remained in the checking account until March 1971, when some funds were transferred to interest-bearing accounts. From October 1970 through March 1971 the grantee had ending monthly cash balances averaging \$124,147, but its monthly program expenditures averaged only \$12,196. An estimated \$3,600 of interest income was lost from July 1970 to March 1971.

RESULTS OF OUR REVIEWS OF FINANCIAL CONTROLS

We made a limited review in calendar year 1972 at the first 12 of 42 grantees selected for our review to determine if they had weaknesses in financial controls, similar to those found by independent audits and those made by us pursuant to congressional requests. Each grantee had weak controls in maintaining basic accounting records and in the areas of payroll, travel, procurement, and property management. The 12 grantees had received about \$14 million from OEO, individual grantees received funds ranging from about \$240,000 to about \$5.8 million. In view of our results at these 12 grantees, we did not pursue this

issue further at the remaining grantees we reviewed. However, our cursory observations at these other grantees showed that several may have had similar weaknesses in financial controls.

Accounting systems not fully implemented

Seven CAAs did not have the basic accounting manual necessary for guiding officials and employees responsible for operating the system.

Five CAAs had not implemented or were not maintaining the necessary accounting records to adequately record their financial activities. For example, yearend adjusting entries were not posted to the general ledger, postings to the general ledger were not current or complete, books were closed without including all expenditures incurred, and cash transfers to delegate agencies were not established as receivables on the grantees accounting records or as payables on the delegate agencies' accounting records. As a result, the financial reports submitted by the five CAAs to OEO did not agree with accounting records.

Below are specific examples of discrepancies between financial reports and grantee accounting records resulting, at least in part, from incomplete accounting systems.

1. Financial reports submitted by one grantee were not supported by the books of account which consisted of only a cash journal, a general ledger, and a general journal, all of which were incomplete. No recordings had been made in the general journal between June 1971 and July 1972. Also, instead of recording and reporting actual non-Federal funds expended, each month the grantee reported an amortized amount of the total non-Federal funds required by the grant. Accordingly, OEO had no basis for knowing whether the grantee met the requirement of non-Federal funds in operating its programs.
2. On receiving initial funding, one grantee hired a local certified public accounting firm to design an accounting system that would meet OEO requirements. The certified public accountant designed an accounting system that included a general journal, general ledger, cash receipts and disbursements journal, and subsidiary ledgers for accumulated leave, employee earnings, and property. The grantee was not maintaining the general journal and general ledger during the program year and did not complete these records until 1 month after the close of the program year. As a result, we were unable to reconcile amounts reported to OEO with those of the accounting records. The grantee's bookkeeper could not explain the differences in the accounting records and the financial reports to OEO.

3. Some CAAs were reporting to OEO, as expenditures, funds advanced to delegate agencies or other contractors. In one instance, about \$70,000 granted to about 35 communities for various projects was not shown as assets on the CAA's accounting records as provided by OEO guidances, and accountability for these funds was lost.

Payroll and personnel matters

Our review showed weaknesses in the internal controls over payroll and/or personnel records in 9 of the 12 grantees. At eight of the grantees, the responsibilities for performing various payroll functions were not adequately separated to insure that no one person controlled a transaction from beginning to end. Separating duties provides a check on the accuracy of the work and substantially reduces the opportunity to commit fraudulent or other irregular acts.

At 4 of the 10 grantees where T&A records were examined, the T&A system was weak. At one grantee, the T&A records were completed 4 to 6 days before the end of the bimonthly pay period so that the payroll could be prepared and checks distributed on the last day of the pay period. The bookkeeper at another grantee prepared the payroll before receiving the individual T&A records.

At a third grantee, we tested 19 T&A records and found that 11 were not current. The T&A records for some employees at a fourth grantee did not show employees' working hours but only their attendance and leavetaking. Also, not all T&A records were approved by the employee's supervisor.

In addition to the weaknesses in the T&A records, weaknesses existed in the systems for maintaining employees' leave records at three of the above grantees. At one grantee, employees absent for less than 4 hours charged their absence to administrative leave rather than to annual or sick leave as appropriate. At the second grantee, leave was not always authorized in advance. For example, advance authorization was not given for 319 hours of the 439 hours of leave taken by five employees over a 16-month period in 1971. Also, 24 part-time employees were paid for a holiday for which they were ineligible. At the third grantee, sick leave taken was not supported by requests for leave, and in 1971, employees were granted three additional holidays--the day after Thanksgiving and 2 days at Christmas--without the grantee board of directors' authorization.

Three grantees were paying employees in excess of OEO instructions on compensation without obtaining required waivers from OEO. At one grantee three employees received excess salaries of \$170, \$105, and \$5 per month.

The second grantee paid four regular employees excessive amounts, ranging from about \$40 to about \$300 per month. In addition, two doctors working part time for the grantee were paid at hourly rates of \$13.58 and \$17.03 although OEO instructions restrict hourly rates to \$7.21 unless a waiver is granted by OEO.

During the year ended March 31, 1972, at the third grantee, four employees received excessive pay increases totaling about \$900.

Travel

The following weaknesses existed in controls over travel expenditures at six grantees.

- Travel was not authorized in advance.
- Travel advances were charged to an expense account instead of accounts receivable.
- Travel vouchers were not submitted or when submitted did not show purpose and location of travel, odometer readings, time of arrival and departure, or proof that travel had been performed.
- Travel claims were paid based on itineraries rather than on a travel voucher.
- Per diem was not calculated in accordance with the Standardized Government Travel Regulations.

Travel transactions were improperly administered and, as a result, expenditures were made for travel that were not approved or were reimbursed in amounts over those allowed. Travel policies and procedures at three CAAs were inadequate, obsolete, or nonexistent.

Procurement

Weaknesses were noted in seven of the nine CAAs where we examined internal controls over the grantees' procurement functions. At six of the nine grantees, adequate supporting documentation, such as properly approved purchase requisitions or purchase orders, price quotations, or vendor invoices, was not always available to support procurement expenditures.

For example, at one grantee, adequate supporting documentation was not available for about \$1,500, or 23 percent of about \$6,500 in procurement transactions tested. OEO auditors found similar weaknesses at another grantee.

Nonexpendable property

Controls over nonexpendable property at all 12 grantees were, for the most part, inadequate. Each of the grantees reviewed had numerous weaknesses in its controls over property; for example:

- Property records were not always maintained and those maintained were incomplete or not current.
- Control accounts were not established.
- Property was not marked for identification purposes.
- Physical inventories were not taken annually or were taken by the same individuals who were responsible for maintaining property records.
- Adjustments were not made between the physical inventory amounts and the control account.
- Equipment was not used after it was acquired, and deteriorated because of inadequate storage.
- Equipment was used for personal use.
- Inventories were not furnished to the OEO regional offices.

We also noted poor property controls. At liquidation, one CAA reported that the inventory of property acquired with OEO funds at December 31, 1970, amounted to \$134,955. The successor grantee, however, did not accept the CAA's inventory but reinventoried the property and found inventory valued at only \$95,506, or \$39,449 less than the amount reported. The accuracy of the former CAA's physical inventory could not be determined because perpetual inventory records were not current.

PROGRAM CONTROLS

In August 1971 OEO became less directly involved in the program monitoring of grantees and took steps to insure that its grantees would adopt adequate planning procedures and accumulate needed program information regularly to assess the progress of programs toward achieving their goals.

On January 1, 1972, OEO reemphasized to its grantees the importance of adequate program planning. A new work program format was designed which required that grantees logically state their proposed activities in terms of

- multiyear and annual goals, quantified to the extent possible;
- program priorities assigned by the grantee;
- activities required to achieve goals; and
- training and technical assistance needs.

OEO anticipated that this format would become the basis for subsequent program monitoring and self-evaluation.

To provide the information for making such assessments, the program control system should include (1) establishing realistic goals and milestones, quantified to the extent possible, (2) accumulating and reporting data on accomplishments in relation to goals, and (3) formally evaluating programs, including validating accomplishments.

RESULTS OF OUR REVIEWS OF PROGRAM CONTROLS

During calendar year 1972, we reviewed the program control systems at 42 OEO grantees to determine whether the systems provided them with information necessary to assess program quality and effectiveness and whether program funding should be continued at the same or modified levels.

Adequate information for making assessments of program operations was not available at 40 of the 42 grantees because their systems contained one or more of the following deficiencies:

- Program objectives were stated too generally.
- Program goals were not sufficiently quantified.
- Program accomplishments were not adequately reported.
- In-house evaluations of programs were not always made, were inadequate, or were not available for use.

Unclear statements of program goals

Program goals are standards against which results may be compared to judge an activity's relative success. The established goals at 31 grantees were not clear because they were stated only in general terms or had not been quantified to the extent possible.

For example, at one grantee, the work programs for its delegate agencies for the most part merely reflected general statements of planned activities, such as

- create and implement an economic development program;
- expand the agency's multiphasic health program for the elderly;
and
- establish and implement better methods and procedures for housing the elderly and all people in public and/or private housing.

The grantee's quantification of goals was generally limited to estimates of that segment of the target population which would be served by all programs of each delegate agency rather than to specific numbers of persons to be served by each program. At another grantee, the number of persons eligible for services rather than the number to be served was included in the work program.

Inadequate progress reporting

Of the 42 grantees covered by our review, 14 did not require all of their programs to submit progress reports, and 24 submitted progress reports containing data not related to program goals. In addition, 31 grantees did not verify program data submitted.

Even when the grantee required progress reports, our review disclosed the following deficiencies:

- Reports were not being submitted or were submitted late.
- Reported data was inaccurate, inconsistent, or misleading.
- Statistical information on persons served or services provided was not required.
- Operators of vocational training programs were not required to report the number of graduates or the number of graduates who were placed in jobs.

Lack of program evaluations

Most of the 42 grantees had not evaluated all of their in-house and delegated programs at the time of our review.

For example, one delegate agency had not been evaluated by the CAA even though the agency had been funded since 1965 and received \$640,000 in OEO funds for the year ended May 31, 1971. This same delegate agency was not submitting regular progress reports to the CAA.

We found other cases in which

- evaluations were performed but were not recorded,
- prior evaluation reports were lost,
- CAA board of directors' evaluation committees were not functioning entities, and
- evaluations were not being performed regularly.

Without adequate program information and evaluation, a grantee cannot assess program quality and effectiveness or decide whether one program needs funding over another.

In August 1972, while our review was still in process, OEO directed that each CAA establish a Program Progress Review system which would generate reports on the achievements of proposed goals, provide the basis for modifying activities and milestones for successive periods, and facilitate self-evaluation.

Under the new system, each grantee was required to review its programs at least twice yearly and prepare a report summarizing and analyzing accomplishments in relation to established program goals. In addition to preparing the basic report, each grantee was required to prepare an annual summary covering

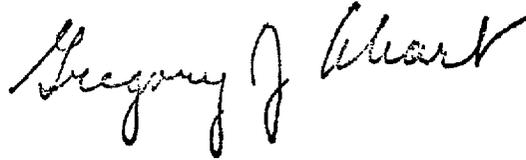
- the impact of program accomplishments,
- problems affecting program progress and corrective action taken,
- overall mission effectiveness,
- planned changes in goals and program management, and
- technical assistance needed.

The system was designed to assist the grantees' internal program management, and the reports furnished to the OEO regional office were designed to allow the office to monitor grantee progress and to identify grantees requiring technical assistance. The revised system had not been effectively implemented at the completion of our review.

B-130515

We shall be happy to meet with you or with members of your staff to discuss our findings.

Sincerely yours,

A handwritten signature in cursive script, appearing to read "Gregory J. Alant".

Director

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