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REPORT TO THE COMMITTEE ON APPROPRIATIONS HOUSE OF REPRESENTATIVES

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Weaknesses In Management Of Clubs And Other Recreational Activities

B-148581

Department of Defense

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**BY THE COMPTROLLER GENERAL
OF THE UNITED STATES**

B-148581

MAY 7, 1971

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

B-148581

Dear Mr. Chairman:

In your letter of January 26, 1970, you requested a comprehensive review and evaluation of the operation and management of nonappropriated fund activities in the Department of Defense. In response we have issued several reports to you on clubs and other recreational activities at selected installations of the Army, Navy, Marine Corps, and Air Force around the world and at departmental headquarters. This report summarizes our work at these installations and headquarters offices, except for work relative to the exchanges and theaters which we reported to you earlier.

Although the results of our work were discussed with responsible local officials, they were not discussed with higher officials nor did we request their formal comments. Because the report contains suggested actions which should be taken by the Department of Defense to improve its management of clubs and recreational activities, you may wish to review these matters with Department of Defense officials.

We plan no further distribution of this report unless copies are specifically requested, and then we shall distribute them only after your agreement has been obtained.

Sincerely yours,



Comptroller General
of the United States

The Honorable George H. Mahon
Chairman, Committee on Appropriations
House of Representatives

D I G E S T

WHY THE REVIEW WAS MADE

At the request of the Chairman, House Committee on Appropriations, the General Accounting Office (GAO) has reviewed the management of clubs and other recreational activities of the Armed Forces.

This report is one of a number made on Department of Defense (DOD) non-appropriated fund activities at the request of the Chairman. Previously GAO reported on the management of military exchanges and theaters and on various individual recreational activities.

FINDINGS AND CONCLUSIONS

Appropriated fund support of recreational activities is loosely controlled.

- DOD's data on the amount of appropriated fund support for recreational activities are inadequate. (See p. 7.)
- Regulations provide that the Government be reimbursed for certain services and supplies furnished to a recreational activity by a military organization. Billing procedures for such reimbursement are inadequate. (See p. 8.)

Many recreational activities could not operate in their present manner without substantial support from appropriated funds. (See p. 9.)

Policies on distribution of nonappropriated funds and other resources are inequitable.

- Each military department uses a different distribution system. Some activities receive a disproportionate share because the activities' needs are not considered. (See p. 10.)
- Assessments made by commands on the earnings of activities have not been levied equitably. (See pp. 15 and 16.)
- Large sums have been allocated to activities without a demonstrated need. (See p. 17.)

When nonappropriated funds were obtained at some installations, questionable construction projects were undertaken, with and without required approvals. (See p. 25.)

Although purchasing controls prescribed appear adequate, widespread violations have occurred.

- Required approvals have not been obtained; purchasing limitations have been circumvented. (See p. 18.)
- Procurements have been made without competition. (See p. 18.)
- Purchases of consumable supplies have been imprudent; money spent for entertainment has exceeded limits set by regulations. (See pp. 19 and 20.)
- Establishment of central purchasing agencies for clubs in some geographic areas has not eliminated all major violations. (See p. 21.)

Controls over cash and other resources were ineffectively implemented at most sites reviewed by GAO.

- Responsibilities for custody and recording of assets were not divided and assigned properly. (See p. 24.)
- Concessions operating in overseas clubs and other activities were poorly controlled by host installations and commands. (See p. 25.)

Controls over inventories were unsatisfactory. (See p. 25.)

The personnel policies of nonappropriated fund activities need to be improved.

- Military personnel often have inadequate training in managing recreation activities. (See p. 27.)
- Despite international agreement, reserves were not established in some overseas clubs and messes for severance and retirement pay of employees who were citizens of the host country. (See p. 28.)
- Controls over personnel and payroll were inadequate at many activities. (See p. 29.)

The reporting of financial results of the operation of the activities has been ineffective.

- Inadequate financial statements were prepared by the activities and were accepted by major commands. (See p. 30.)
- Little or no corrective action resulted from reports of unsatisfactory conditions. (See p. 31.)

Controls were loose on slot machine operations at overseas clubs.

- Guidelines for control of cash income were inadequate. (See p. 33.)
- Cash revenue to the sponsoring clubs was not protected by the use of coin meters and other safeguards. (See p. 34.)
- In many countries U.S. clubs operated slot machines despite local laws prohibiting them. (See p. 33.)

Improved auditing procedures were needed.

- Audits made have not provided the evaluations needed by the activities or by management responsible for overseeing them. (See p. 42.)

RECOMMENDATIONS OR SUGGESTIONS

GAO has made a number of suggestions for improvements in DOD's management of military clubs and other recreational activities. (See pp. 9, 13, 14, 22, 26, 36, and 42.)

MATTERS FOR CONSIDERATION BY THE COMMITTEE

Since DOD has not had an opportunity to prepare formal comments on this report, the Chairman may wish to review it with DOD officials.

The Committee may wish to consider directing the military departments to establish

- systems for identifying the costs of appropriated fund support given to nonappropriated fund activities;
- centralized purchasing agencies where appropriate; and
- a separate centralized audit office, directly under the Secretary of each department, financed by nonappropriated funds, to audit clubs and other welfare and recreational activities and to provide them with any audit services they need.

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ABBREVIATIONS

CONUS Continental United States

DOD Department of Defense

FICA Federal Insurance Contribution Act

GAO General Accounting Office

USAFE U.S. Air Forces in Europe

D I G E S T

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The Committee may wish to consider directing the military departments to establish

- systems for identifying the costs of appropriated fund support given to nonappropriated fund activities;
- centralized purchasing agencies where appropriate; and
- a separate centralized audit office, directly under the Secretary of each department, financed by nonappropriated funds, to audit clubs and other welfare and recreational activities and to provide them with any audit services they need.

CHAPTER 1

CERTAIN ACTIVITIES ARE SUPPORTED BY APPROPRIATED AND NONAPPROPRIATED RESOURCES

DOD's policy is to provide a well-rounded morale, welfare, and recreational program for ensuring the mental and physical well-being of its personnel; to acquire, operate, and maintain adequate free-time facilities with appropriated funds; and to supplement these efforts with nonappropriated funds.

Welfare and recreation activities (such as bowling centers, hobby shops, community service activities, libraries, and youth activities) rely heavily upon appropriated fund support in providing recreation and sports opportunities to eligible personnel. This support is supplemented mostly by nonappropriated funds produced by the military exchange and, to a lesser extent, by income from the activities.

We observed that stateside welfare and recreational facilities were used to a much lesser extent than those overseas. For example, an average of 6.4 percent of the base population at Newport Naval Base used special services facilities daily in contrast to the greater use of such facilities overseas by a majority of those eligible.

Questionable criteria are applied in granting use of some recreational facilities. For instance, the golf course, slot machines, and bingo games at John Hay Consolidated Open Mess were being used primarily by Philippine Nationals, although they could not use similar facilities at Clark Air Base. The pools and beach houses at Camp Lejeune were inequitably divided between officers and enlisted personnel. The recreation fund operated 18 beach houses and three swimming pools for 2,500 officers and 40,000 enlisted personnel. All the pools were open to officers but only two were available to enlisted personnel, and eight of the beach houses were reserved for officers.

Officers', noncommissioned officers', and enlisted men's clubs and open messes are established, under the authority of the Secretary of Defense, to serve food and liquor and

entertain a limited, voluntary membership of military personnel, their dependents, and/or civilian personnel. Although these activities receive some appropriated fund support, they rely primarily on self-generated revenue.

Service clubs, operated with appropriated and nonappropriated welfare funds, have an open membership and sponsor social activities but do not serve liquor.

The Army Nonappropriated Funds Division, under the Deputy Chief of Staff, Personnel, is responsible for the administration and financial management of the welfare and recreational activities of the Army. Resources flow from the Army's share of dividends declared and paid by the Army and Air Force Exchange Service. These dividends are allocated quarterly by the Army Central Welfare Fund on a per capita basis to major commands, installations, and units.

The Army Central Mess Fund was established to lend financial support to individual clubs and messes in the continental United States (CONUS) and overseas and is financed by the sale of alcoholic-beverage-control decals to clubs and messes.

On October 26, 1970, the Army contracted with a private concern to study the Army nonappropriated fund system, to devise a management information and decision system for mission responsibilities and command controls, and to report the results by May 10, 1971.

The Special Services Division of the Bureau of Naval Personnel is responsible for the administration and operation of Navy nonappropriated fund activities. The Division's Central Recreation Fund receives its revenues from a percentage of profits from the Navy exchange and a percentage of slot machine income and gross sales from open messes and clubs.

The Air Force Welfare Board, under the Deputy Chief of Staff, Personnel, establishes overall policies and procedures for managing nonappropriated fund activities. Major commands are responsible for the operations of these activities. The Central Welfare Fund, like the Army's, receives a share of dividends declared by the exchange service, allocates them

quarterly on the basis of personnel strength, and distributes them to commands when requested. Activities of the Central Mess Fund (loans, grants, and insurance) are financed by assessing clubs and messes on the basis of a percentage of sales.

The Special Services Branch, under the Marine Corps Director of Personnel, maintains two central funds for administering nonappropriated funds--the Marine Corps Mess Fund for clubs and messes and the Central Recreation Fund for all other special services.

Special services programs for Marines and their dependents are the responsibility of the base commanding officer and are funded with profits of the base exchange and with self-generated revenues.

Clubs and messes are established upon approval of the Commandant of the Marine Corps and are assessed a percentage of slot machine income and gross income on sales of alcoholic beverages. Although Marine Corps personnel on Navy installations generally use Navy clubs and messes, in some cases they have established their own activities, such as those at the Newport Naval Base.

CHAPTER 2

APPROPRIATED FUND SUPPORT

Congressional appropriations for organizations supporting recreational activities are poorly controlled by DOD because the military departments do not maintain accounting systems that identify the amount of such support. As a result, a proper accounting for resources and operations is not made in the financial statements of the free-time activities because revenues are shown to be generated without reflecting the resources applied. In addition, the military commands' statements of appropriated funds do not sufficiently disclose the use of these resources.

At selected sites we obtained the following estimates of some of the appropriated fund support provided annually to these activities, which generated a combined gross non-appropriated fund revenue of \$47.1 million.

	Amount (<u>millions</u>)
Civilian and military pay	\$ 1.5
Maintenance activities and other unbilled support	<u>13.8</u>
	<u>\$15.3</u>

The appropriated fund support shown above is significantly understated in that it excludes real estate and a broad range of such services as management planning, inspecting, auditing, and engineering which were performed for the recreational activities by Government organizations.

The Congress has permitted the regulations of the defense components to have the force of law in the area of nonappropriated fund activities operated within DOD. The defense components have established through various regulations that the nonappropriated fund activities may receive almost any type of appropriated fund support considered necessary within local discretion to provide recreational facilities to the serviceman.

The regulations state that the Government will be reimbursed when certain services and supplies are furnished by a military organization to a recreational activity. We noted many instances in which the required reimbursements had not been made for transportation, food, and other supplies, primarily because the providing military organizations had rendered no bill to the recreational activity. For example, in accordance with our suggestion, the billing procedures at Headquarters, U.S. Army, Vietnam, were reviewed by the responsible officials, and the Noncommissioned Officers'/Enlisted Men's Open Mess System and the Saigon Enlisted Open Mess were billed \$1.2 million for previously unbilled commissary supplies.

Many recreational activities annually receive a far greater amount of appropriated fund support than the net profit earned from sales or allocations received from grants or exchange dividends. Our review covered activities with a combined appropriated fund support of at least \$15.3 million as contrasted to a combined net profit of \$11.4 million from gross revenues of \$47.1 million. Thus many recreational activities would be unable to exist without significant changes in operations if required to reimburse the Government in full for appropriation support.

A few ideally situated and well-managed messes, hobby clubs, and other recreational activities appear to report sufficient earnings to pay their way if required. The remainder would, in our opinion, be required to raise prices, possibly reduce the scope of service, and make many changes in management controls to make full reimbursement for Government resources used.

BILLETING FACILITIES

Savings to the Government were achieved at a few locations through reductions in per diem for persons traveling on official business and occupying nonappropriated fund billeting facilities. For example, during calendar year 1969 the Chao Phya nonappropriated fund billeting facility in Bangkok, Thailand, was used for about 94,000 occupancy days by persons traveling on official business. The savings to the Government through reduced per diem--even after allowing for appropriated fund support of the Chao Phya--were about

\$472,000 less than the costs that would have been incurred had these individuals used commercial hotels and received higher per diem allowances.

CONCLUSION

Many clubs and other recreational activities could not operate in the present manner without the substantial amount of appropriated fund support presently being provided. The military departments do not maintain adequate systems to identify the full amount of appropriated fund support received by recreational activities or to ensure the reimbursement for supplies and services cited in regulations.

The problems in identifying appropriated fund support as discussed in this report emphasize the need for new procedures in this area. The military departments should establish systems for identifying the costs of appropriated fund support provided to nonappropriated fund activities.

Once such appropriated fund support costs have been identified, the military departments should evaluate management effectiveness, usage, benefits provided, and the need to provide many of the recreational, morale, and billeting activities with substantial appropriated fund support.

MATTERS FOR CONSIDERATION BY THE COMMITTEE

As suggested in our earlier reports on nonappropriated fund activities, the Committee may wish to consider directing the military departments to establish systems for identifying the costs of all types of appropriated fund support given to military nonappropriated fund activities.

CHAPTER 3

ALLOCATION OF REVENUE

The nonappropriated fund activities operated by the defense components are supported, in part, by dividends from the exchange and motion picture services and by grants and loans from either the departmental headquarters or major command mess and welfare funds. The allocation of these dividends, the principal source of revenue for some activities, is discussed in this chapter. Grants and loans are discussed in chapter 4.

Each of the military departments uses a different system for allocating exchange dividends to benefiting welfare and recreational activities. Although the activities having the greatest needs do not always receive the most resources and others enjoy a disproportionate benefit, retaining a portion of the resources in central funds and distributing them as grants and loans helps to offset the inequitable basic allocation. The central funds have retained some of the income and have accumulated large reserves, much of which is invested.

The amounts of funds provided for welfare and recreational activities by exchange dividends during their most recent fiscal years follow.

<u>Department</u>	<u>Exchange dividends (millions)</u>
Air Force	\$ 32
Army	53
Navy	39
Marine Corps	<u>6</u>
	<u>\$130</u>

The Board of Directors of the Army and Air Force Exchange and Motion Picture Services annually declares a dividend which is paid quarterly from the profits of the two activities to the Army and Air Force central welfare funds on the basis of the respective military personnel strengths.

The amount of the dividend is determined by the Board on the basis of current operating needs of the two activities. The Army and Air Force Motion Picture Service has begun an extensive theater-rebuilding program and has declared a 5-year moratorium on payment of dividends to the two central welfare funds.

Of the \$39 million provided by the Navy exchange, \$30 million was transferred by individual exchanges to welfare and recreational activities on the installations and \$9 million was paid to the Bureau of Naval Personnel by the exchange headquarters.

The decentralized Marine Corps exchange paid dividends of \$6 million directly to recreation funds at Marine Corps installations.

ARMY

The Army's portion of the dividends from the exchange and motion picture services is sent to the Nonappropriated Funds Division at Army headquarters for the Army Central Welfare Fund. The Division establishes rates, on the basis of personnel strength and the amount of the expected dividends, for redistribution to major commands, central post funds, and unit funds. Commands and installations with greater strengths receive disproportionately lower per capita shares of the allocations. The current quarterly rates vary from \$1.45 a man for commands with less than 1,000 personnel to \$1 a man for those with 25,000 and over. Similarly central post fund allocations vary from \$1 to \$0.55 a man. Unit funds receive \$0.50 a man, regardless of personnel strength. Twice each month commands are allowed to draw funds from the central fund as needed within the limits of the allocations but are not to accumulate more than a month's needs. The commands furnish installations and units with necessary funds in accordance with the rates established by headquarters.

AIR FORCE

When the dividends from the exchange and motion picture services are received by the Air Force Welfare Board for the Central Welfare Fund, an allocation is made to all

major commands on the basis of their average daily personnel strengths at the rate of \$6 a man a quarter. This amount is then paid to the major commands during the quarter as needed. Unallocated funds are retained by the Board for contingencies and operating expenses.

The commands further distribute funds to installations as needed but at rates not less than \$1.50 a man a quarter and to isolated units at not less than \$2.25 a man a quarter.

For example, the Air Training Command received \$3,262,722 in calendar year 1969 and redistributed \$1,646,765. The balance was retained for loans and grants to subordinate activities, for fund administration, and for command recreation and other activities.

NAVY AND MARINE CORPS

Each installation receives a share of the profits earned by the local exchange to carry on welfare and recreation activities. The larger installations with the larger exchanges have more funds for welfare and recreation programs, whereas smaller installations may not generate sufficient revenue to support an adequate program.

The central recreation funds obtain revenue from the exchanges through assessments and dividends and attempt to support and equalize installation programs, primarily through grants and loans.

DUES SYSTEM

Dues are not normally charged by Navy clubs and messes and are permitted on an exception basis only in commissioned officers' messes. The majority of the clubs and messes we reviewed in other military departments relied on dues systems to provide income necessary for the operation of the clubs. Some clubs reported a profit without the use of dues, some did not show a profit until dues were included, and others showed a loss even after dues were included.

Examples of these variations are the Joint Services Officers' Open Mess in Tokyo which experienced a loss of

\$6,600 on operations even after collecting membership dues and admission charges of \$45,100, the Commissioned Officers' Open Mess at Camp Lejeune which reported a net profit of \$128,343 after collecting \$120,302 in membership dues, the Clark Air Base Airmen's Open Mess which collected dues of \$93,700 and reported a net profit of \$26,600, and the First and Second Class Petty Officers' Open Mess at Newport which reported a net profit of \$22,958 without benefit of dues.

In some instances dues may be the most expedient and practical method for a club to regain financial stability. The Subic Bay Commissioned Officers' Open Mess was having trouble repaying an expansion loan received from the Central Recreation Fund and had not fully funded existing liabilities for severance and retirement pay for local national employees. The mess was overstaffed but, because of lack of funds for severance pay, could not discharge the excess employees. We suggested that the commanding officer consider imposing a dues system as a short-time measure to assist the mess in solving its problems. He subsequently informed us that, as a result of our review, he had taken actions to establish certain controls and that, if these steps failed to stabilize operations, he would consider requesting authorization for imposing a dues system.

CONCLUSION

The Army and Air Force depend upon the commands down to the installation level to determine their needs for welfare and recreation funds. Funds from all the exchanges are commingled and distributed through the chain of command within the constraints of the allocations on the basis of personnel strength. The responsibility therefore is upon commands at each level to weigh and judge the needs of each lower activity.

This method of allocating exchange profits appears more closely related to welfare and recreation needs than the Navy and Marine Corps method. The Navy and Marine Corps should consider commingling the profits of the individual exchanges, distributing the profits that are not needed for exchange operations to the central recreation funds, and allowing the central funds to redistribute the profits to

the welfare and recreation activities at all levels according to their needs.

The clubs and messes should develop sound, long-range, financial plans on the basis of charges for goods and services to be provided and should employ capable managers to carry out those plans rather than rely on dues or grants to achieve or maintain financial stability.

CHAPTER 4

ASSESSMENTS, GRANTS, AND LOANS

The funds for grants and loans to clubs, messes, and other revenue-producing activities are obtained primarily by assessments. Commands and departmental headquarters have not levied assessments equitably in all cases and have permitted some central funds to accumulate large reserves.

The rates of assessments by departmental headquarters on the operations of clubs and messes vary from 0.5 to 3 percent of gross sales of food and liquor. Navy central funds also receive 50 percent of slot machine income and Marine Corps central funds receive 25 percent. On March 31, 1969, the assessment imposed by the Army Central Mess Fund was discontinued and replaced by increasing the cost of decals which all activities selling liquor must purchase. This action has resulted in a substantial increase of decal income to the central fund.

Assessments on clubs, messes, and restaurants imposed by departmental headquarters yielded the following amounts for the periods shown.

<u>Service</u>	<u>Amount</u>	<u>For year ended</u>
Army	\$ 148,500	Dec. 31, 1969
Navy	3,587,300	Dec. 15, 1969
Marine Corps	1,308,900	Nov. 30, 1969
Air Force	1,562,000	June 30, 1969
Army and Air Force Civilian Welfare Fund	<u>86,000</u>	June 30, 1969
Total	<u>\$6,692,700</u>	

Inequities have resulted from extraordinary assessments by lower commands. For instance, the U.S. Army, Vietnam, entered into an agreement whereby its Central Mess Fund, beginning July 1, 1969, would provide \$50,000 a month--\$40,000 from the noncommissioned officers'/enlisted men's account and \$10,000 from the officers' account--to the U.S. Army, Pacific headquarters, to finance the construction of

officers' and enlisted men's club facilities in a new rest and relaxation center at Fort DeRussy in Honolulu, Hawaii. (See p. 26.) This center was ostensibly for rest and recreation of all military members in Vietnam. The agreement was made with the understanding that, if there were substantial troop reductions in Vietnam during the 24-month period following the agreement, the agreement would be renegotiated. Although substantial troop reductions have occurred, the agreement has not been renegotiated.

GRANTS AND LOANS

The departmental headquarters and commands make grants (no repayment required) and loans, primarily for construction and renovation projects, to local clubs, messes, and recreation and welfare activities. In some cases grants are approved for special projects and educational assistance scholarships. The following table shows the amounts of grants and loans approved by the headquarters of the military departments during the periods shown.

<u>Department</u>	<u>Grants</u>	<u>Loans</u>	<u>For year ended</u>
Army	\$ 686,900	\$ 4,150,500	Dec. 31, 1969
Navy	4,465,500	6,366,400	Dec. 31, 1969
Marine Corps	618,000	827,500	Jan. 31, 1970
Air Force	<u>-</u>	<u>645,600</u>	June 30, 1969
Total	<u>\$5,770,400</u>	<u>\$11,990,000</u>	

The Army and Air Force Civilian Welfare Board approved \$349,300 for grants and loans during its fiscal year which ended June 30, 1969. We did not identify the amount for grants and the amount for loans because this determination is not made by the Board until the funds are distributed and such distribution had not been made at the time of our fieldwork.

Although the financial condition of the receiving activity may be considered, the approving activities did not have clear policies on the conditions governing approval of a grant in contrast to a loan. Large sums of money were distributed to clubs and other activities without a demonstrated basis for need.

For example, the officers' open mess at Ramstein Air Base had an outstanding interest-free loan from the U.S. Air Forces in Europe (USAFE) Mess and Sundry Loan Fund in the amount of \$37,000 on April 30, 1970. At the same time the mess had \$25,000 on deposit with the USAFE Mess and Sundry Loan Fund, and the advisory council had approved the deposit of an additional \$25,000. The mess, therefore, is receiving interest from the loan fund on money it had obtained interest free from the fund. USAFE officials contended that (1) the mess did not need the funds borrowed, (2) the interest could be considered as a grant to the mess, (3) grants of funds were authorized, and (4) the amount of the loan also could have been in the form of a grant. They further indicated that they did not intend to request that the loan be liquidated or repaid in advance of schedule.

CONCLUSION

Because assessments against operations of clubs, messes, and recreation activities often are based on the gross revenues or profits, some activities have had difficulties, even to the extent of suffering losses, in paying the assessments. The assessments should be levied on the bases of the needs of the levying fund and the ability of the activities to pay. The bases for the assessments should be reviewed, and consideration should be given to assessing net profits rather than gross sales or income or to converting to some other basis which would not create a financial hardship for the paying activity.

Large sums of money have been given to clubs and other activities without a demonstrated need, and clear policies have not been applied in approving grants and loans. More effective policies should be determined by the military components to aid in establishing guidelines to be used in approving grants or loans and in accumulating large central funds.

CHAPTER 5

PURCHASING PRACTICES

Purchasing is a key function of nonappropriated fund activities in DOD. The nonexchange activities obtain most of their goods and services in a decentralized fashion using local merchants and the installation's supply system but have made limited use of Government purchasing activities and supply sources. Many abuses have developed from this practice and have continued because of the lack of supervision.

ABSENCE OF REQUIRED APPROVALS

The failure to properly use purchase orders was a significant weakness in internal control in the activities we visited. Frequently, approved purchase orders for goods and services either were not obtained or were prepared and approved after receipt or payment.

In each of the military departments, limitations have been established on the size of purchases that may be made without (1) the approval of the installation commander or (2) the assistance of a purchasing and contracting officer. Some activities have ignored the limitations and others have attempted to circumvent them.

NONCOMPETITIVE PROCUREMENT

Although nonappropriated fund activities are instrumentalities of the Federal Government, they are not subject to the restrictions imposed upon appropriated fund activities by the Armed Services Procurement Regulation. Purchasing policies for these activities are outlined in regulations of the military departments which require fair and equal consideration of all responsive offers from potential suppliers. We found that competition was often discouraged or nonexistent in nonappropriated fund purchases.

Some of the activities we reviewed did not formally advertise for vendor proposals and, of those that did, some did not provide sufficient time and information for vendors

to adequately respond. At the Headquarters, 6th Army, for example, a contract for insurance for substantially all 6th Army nonappropriated fund activities was awarded after a period of 17 days was allowed for the 10 agents who were solicited to submit proposals. Under the circumstances, only the agency which had previously provided the insurance would have had the necessary information to make an adequate proposal.

Most activities solicited small groups of vendors and contended that these groups provided what the activities wanted at low prices, although other activities in the same area were obtaining similar items from other suppliers at lower prices. This practice (1) shows a disregard for regulations, (2) does not ensure that the activities concerned will receive the lowest prices, (3) stifles competition, and (4) provides an opportunity for rebates to fund custodians and employees.

EXCESSIVE PROCUREMENT OF SUPPLIES AND ENTERTAINMENT

Large amounts of supplies were purchased without regard for past experience or current needs. For instance, the July 25, 1970, inventory of the Saigon Enlisted Open Mess included 108 of 228 line items which, on the basis of the preceding 12 months' issues, exceeded 1 year's requirements. The value of these 108 items was \$54,000, or about 50 percent of the total value of the supplies inventory of \$109,000.

Generally activities are limited in the amount of money they can spend for entertainment to a percentage of gross sales or, for the Navy enlisted men's club, to a percentage of profits. At many activities the amounts expended for entertainment exceeded the limits imposed by regulations, as shown in the examples below.

	<u>Air Force</u>		
	<u>Officers' open mess</u>	<u>Noncommissioned officers' open mess</u>	<u>Airmen's open mess</u>
Clark Air Base actual in fiscal year 1969	9%	18%	19%
Pacific Air Forces standard	<u>15</u>	<u>15</u>	<u>15</u>
Deviation	<u>-6%</u>	<u>+3%</u>	<u>+4%</u>

	<u>Army</u>	
	<u>Officers' open mess</u>	<u>Noncommissioned officers' open mess</u>
Fort Lewis actual in fiscal year 1969	10.9%	9.3%
Continental Army Command standard	<u>10.0</u>	<u>8.0</u>
Deviation	<u>+0.9%</u>	<u>+1.3%</u>

	<u>Navy</u>			
	<u>Officers' open mess</u>	<u>Chief petty officers' open mess</u>	<u>First and second class petty officers' open mess</u>	<u>Enlisted men's club</u>
Rota actual in fiscal year 1969	8.7%	5.6%	8.0%	72.6%
Bureau of Naval Personnel standard	5.0	5.0	5.0	-
Navy Resale System standard	<u>-</u>	<u>-</u>	<u>-</u>	<u>70.0</u>
Deviation	<u>+3.7%</u>	<u>+0.6%</u>	<u>+3.0%</u>	<u>+2.6%</u>

CENTRAL PURCHASING AGENCIES

Although abuses in purchasing are difficult to eliminate, they can be significantly reduced by centralized purchasing. Of the club and recreation activities we reviewed, only two had access to a central purchasing agency. There were notable deficiencies in one such agency which was recently established.

Regulations of the U.S. Army Support Command in Thailand require that all open messes submit their purchase orders to the Central Procurement Agency for the purchase of essential equipment, supplies, food, and liquor; they prohibit the transaction of business between open messes and commercial vendors, unless specifically approved by agency officials. Nevertheless, the Bangkok Officers' Open Mess located in the Chao Phya Hotel frequently placed orders directly with commercial vendors and submitted purchase orders to the Central Procurement Agency for approval after the goods and services had been received.

As a result of the widely publicized irregularities in contracting and purchasing by the Vietnam open messes, a central purchasing agency recently was established by the U.S. Army, Vietnam. This agency is responsible for centralized purchasing, ordering, and requisitioning for all Military Assistance Command, Vietnam, and U.S. Army, Vietnam, nonappropriated fund activities. We identified several weaknesses in controls over purchasing at this agency; namely, inadequate negotiation and administration of contracts, a contract award to an ineligible firm, and permission for an ineligible contractor to continue performing.

In an earlier report on the nonappropriated fund activities at Lackland Air Force Base, we discussed several purchasing weaknesses and suggested that the Army and the Air Force establish a joint, consolidated purchasing office in the San Antonio, Texas, area. The activities should benefit from (1) broader competition because of consolidated requirements, (2) quantity discounts, (3) professional purchasing agents (not now available in the messes), and (4) better quality control over merchandise purchased.

CONCLUSION

Although prescribed purchasing controls for the clubs, messes, and recreation activities appear adequate, widespread violations have occurred, chiefly among the clubs and messes. The more significant of these are the absence of required prior approvals of purchases and the failure to seek competition among vendors. The establishment of centralized purchasing offices has not completely corrected these conditions. The difficulty lies in the failure of supervisors and overseers to ensure that regulations are followed.

Requiring the use of, or establishing, centralized purchasing activities--combined with increased supervision including audit to ensure that regulations are followed--should do much to eliminate purchasing irregularities and to realize the benefits cited above. Relieving the activity managers of the purchasing burden would permit them to give greater attention to the operations of the activities. Entertainment procurement has been a continuing problem. In addition to having the problems highlighted in recent public disclosures alleging the acceptance of bribes and kickbacks by club and other officials, the clubs have difficulty in finding and hiring talented performers. We believe that the obtaining of entertainment should also be accomplished by a central agency. This would result in benefits to both the entertainers and the clubs through auditioning and scheduling and through reducing the number of contacts between club personnel and entertainers. Package deals also could be arranged to make well-known performers available to smaller activities.

Some centralized entertainment agencies have been established but have not been in operation long enough for us to give a fair evaluation. Air Force officials in Europe also are considering establishing a central entertainment booking agency.

MATTERS FOR CONSIDERATION BY THE COMMITTEE

In view of the irregularities encountered through independent purchasing by nonappropriated fund activities,

the Committee may wish to consider directing that the military services establish and use centralized local purchasing agencies when appropriate.

CHAPTER 6

CUSTODY AND CONTROL OVER ASSETS

Each of the military services has prescribed procedures in regulations and manuals which are generally adequate for control over the assets of nonappropriated fund activities. The prescribed procedures were essentially adhered to by headquarters activities but were violated by installation activities.

CASH

Cash control, particularly involving slot machines, was the weakest area of internal control at installation activities. Control over slot machine operations is discussed in chapter 9. Some cash procedures could be improved and others were not being followed. Responsibilities for custody and recording of assets were not adequately divided; cash registers and receipts were not always used; concessionaire income was not controlled; cash was not deposited on time; and inadequate procedures were used to estimate expected cash receipts from bar operations. At two Army clubs in Germany, the noon cashiers were not ringing up sales on the cash registers upon receipt but instead were waiting until business slowed and then were ringing up all receipts at one time.

Assignment of related duties to the same employee was a common problem. At the Lackland Noncommissioned Officers' Open Mess, for instance, the same employee was responsible for extending credit, receiving cash, posting accounts receivable, and performing other duties. At other activities, the responsibility for preparing payrolls and disbursing payroll checks was given to a single employee.

An important problem in bar operations is the determination of expected receipts as part of the control over cash and inventory. To achieve good control, inventories should be taken when bartenders are changed, or at least daily. Not all clubs took inventories within these time limits. Various inventory methods were used. Some methods were adequate, but others were inadequate because the inventories were commingled or because inventory teams did not independently verify and price the stock on hand.

Concessions operated in the overseas activities were poorly controlled by officials of the host installations and major commands. This lack of control was characterized by a failure to

- audit concessionaires' financial statements,
- review concessionaires' internal controls,
- review concessionaires' pricing structure, and
- validate commissions paid to clubs by concessionaires.

INVENTORY

Control over inventory at many activities was poor. This was evidenced by ineffective controls over the issuance of merchandise, unrestricted access to warehouses by activity employees, exposure of inventory to the weather, and poorly conducted periodic inventories.

Count techniques and conditions at many of the activities did not result in reliable inventory figures. For example, the accuracy of the counts of inventories in Vietnam was questionable because supervisors failed to check the counts made by local national employees and did not reconcile variances between recorded balances and the counts. The physical condition and location of one of the mess warehouses did not provide adequate flood protection after rains.

CONSTRUCTION

In some instances when nonappropriated fund resources became readily obtainable, questionable construction projects were undertaken, both with and without the approval required by regulations.

As an illustration, we question the propriety of the approved undertaking of two projects at the Newport Naval Base. A boathouse was repaired, by using nonappropriated funds, at a cost amounting to 77 percent of the replacement value established in 1966. Further, boats had to be transported overland to where they were to be used. In another project the chief petty officers' mess expects to construct a new, larger facility and has received the approval of the Bureau of Naval Personnel which was given on the basis of a population estimate that was overstated with the apparent

knowledge of the installation commander. Furthermore the military strength of the base is being reduced, thus the need for a facility as large as the one planned by the club is further diminished.

The Army has initiated a project to construct a 15-story high-rise facility for recreational purposes at Fort DeRussy, Hawaii, at a cost of about \$19 million in nonappropriated funds. The project was submitted in fiscal year 1969 for consideration under the military construction program, in accordance with a suggestion in the 1968 House Committee on Appropriations military construction report. The Secretary of Defense elected to defer it until fiscal year 1970 since the project had not been properly planned. In March 1969 the project was approved by the Deputy Assistant Secretary of Defense (Properties and Installations) with the stipulation that it be financed with nonappropriated funds. The project recently was temporarily suspended pending a revision of plans to incorporate changes recommended by the President's Property Review Board.

Many of the construction projects we examined were not properly approved. At Clark Air Base the patio area and a snack bar counter for the officers' open mess were constructed without proper supporting documentation and authorizations. A sports facility was constructed by the Rota Special Services Department upon the verbal request of the station commander; approval for the construction had not been obtained from the Bureau of Naval Personnel as required by regulations.

CONCLUSION

The deficiencies in controls over cash and other resources described in this chapter represent violations of procedures in existing manuals and regulations of the military departments. Special attention should be given by responsible officials at all levels to ensure that the prescribed procedures are followed in operating the nonappropriated fund activities.

CHAPTER 7

PAYMENT AND USE OF PERSONNEL

Military personnel with little training or experience in managing clubs have been assigned to manage, operate, and maintain command supervision over open messes and clubs. Payments to these personnel from nonappropriated funds for overtime work have been poorly controlled. Certain clubs and messes have not established adequate reserves for retirement and severance pay for local national employees.

INADEQUATELY TRAINED MILITARY PERSONNEL ASSIGNED

Many of the clubs and messes have assets valued in the millions of dollars and generate revenues of millions of dollars annually. Nevertheless, the inadequate training of other than Navy club and mess management personnel at the sites we reviewed is evident from the summary below.

<u>Service</u>	<u>Total number of management personnel</u>	<u>Specialized nonappropriated fund training</u>
Army	78	32%
Navy	13	92
Air Force	39	59
Marine Corps	<u>17</u>	<u>30</u>
Total	<u>147</u>	<u>45%</u>

A majority of managers of Army and Marine Corps clubs and other recreation activities we visited possessed little or no training for their positions. For example, at one overseas Army installation, the managers of the officers' open mess and the enlisted men's club had been trained primarily in weapons and combat engineering, respectively, and had worked exclusively in these areas prior to assignment as mess managers. The officer in charge of the officers' club annex at one of the Marine Corps activities we reviewed was trained only in auto maintenance and had no background relating to the management of nonappropriated funds.

The Army Audit Agency annual report for fiscal year 1970 points out the need to ensure that the responsibility of custodians and managers for monitoring operations of non-appropriated fund activities is assigned to those possessing the necessary experience and training.

RESERVES FOR SEVERANCE PAY
AND RETIREMENT BENEFITS

Under an agreement between the U.S. Armed Forces and a Philippine civilian association, severance pay and retirement benefits will be paid to all eligible employees whose employment is terminated involuntarily and, in the case of retirement benefits, voluntarily.

Open messes are required by regulations to fund the costs of all their nonappropriated fund payroll, including severance pay and retirement benefits. Nevertheless, the open messes on U.S. bases in the Philippines had not established adequate reserves to fund existing liabilities for these benefits for Philippine Nationals employed by the messes and, as a result, had substantially overstated past profits.

The amount of funds set aside in a given month had varied with the profitability of operations for that month. Such a system resulted in a distortion of reported profits and a correspondingly erroneous picture of operational efficiency and financial condition.

For instance, the open messes at Clark Air Base had estimated their liability for severance pay and related retirement benefits at about \$760,000 on July 1, 1970. By February 1970 only \$30,356 had been reserved for these benefits.

Had the necessary allocations been charged against operations in the past, management probably would have incurred an operating deficit and might have been faced with the need to adjust prices and operations. The need for establishing reserves for severance pay and retirement benefits has been recognized by command officials.

PAYROLL AND PERSONNEL CONTROLS

The major weakness in internal controls was an inadequate division of timekeeping and payroll duties. Also, limitations on the amount of hours that assigned military personnel may work overtime and be paid for from nonappropriated funds were being exceeded.

The payrolls of some of the activities amounted to thousands of dollars monthly, yet one club official at each activity kept track of time, certified time cards, and paid salaries by cash or check. Under these conditions, activity funds easily could be misappropriated.

DOD directives state that officers and civilian personnel are not to be employed by U.S. Government instrumentalities during their off-duty hours but permit the hiring of enlisted personnel. In many instances the managers and custodians, usually enlisted military personnel assigned full time to the clubs and messes, work overtime and receive additional compensation from nonappropriated funds, whereas other enlisted personnel assigned to appropriated fund activities do not receive additional compensation when required to work overtime.

The Federal Insurance Contribution Act (FICA) (26 U.S.C. 3122) leaves the decision of what constitutes wages of Federal employees up to the department heads. Service secretaries have determined that, under proper delegation from the Secretary of Defense, the amount of remuneration received from nonappropriated fund activities by off-duty military personnel does not constitute wages for FICA purposes, although wages paid to full-time and part-time civilian employees are considered wages and FICA taxes are withheld from their pay.

CONCLUSION

The various military components should establish policies and procedures so that civilian personnel with the required training and expertise are assigned to responsible positions with nonappropriated fund activities.

The messes should recognize the existing and future liability for severance pay and retirement benefits by charges to operations on the basis of a percentage of wages paid.

CHAPTER 8

REPORTING FINANCIAL RESULTS TO

VARIOUS LEVELS OF COMMAND

Each of the military components requires that individuals in a custodial capacity provide a periodic accounting of their activities. In accordance with this policy, financial reports on nonappropriated fund operations are forwarded through the military commands to the headquarters of each of the departments. Although the frequency of reporting apparently is adequate, many of the reports contain inaccurate and misleading data. Headquarters officials make little use of financial statements and tend to leave the management review of them to the lower commands.

ADEQUACY OF FINANCIAL REPORTING

Except in the Marine Corps, inadequate financial statements on nonappropriated fund activities were prepared at the installation level and were accepted by major commands.

Army regulations state that financial statements will be prepared by the individual nonappropriated fund activities--monthly by open messes and quarterly by welfare activities--and transmitted to the appropriate major command. The major commands then submit interim summary statements and annual statements to Headquarters, U.S. Army. Some of the financial statements we reviewed contained significant inaccuracies that misrepresented the financial position of the activity. For example, the inaccurate accounting records of the Saigon Enlisted Open Mess negated any possible use of the balance sheet as a management tool for highlighting problems.

The Navy's open messes prepare and transmit monthly financial statements to the Chief of Naval Personnel. The appropriate major command and/or area coordinators receive an information copy and make comments regarding the overall operations to the installation commander and the Chief of Naval Personnel.

Reports on welfare and recreational activities are prepared monthly by the Bureau of Naval Personnel Nonappropriated Fund Accounting Unit, Brooklyn, New York, and are sent to the installation commander for review before being transmitted through channels to the Chief of Naval Personnel.

The Navy Resale System Office prepares monthly statements for enlisted men's clubs and sends them to the exchange officer and the installation commander, who are responsible for the club, and to the Commander of the Naval Supply Systems Command.

Monthly financial statements for Air Force activities are prepared by each installation's fiscal control office. Because of the Air Force policy of decentralization, the responsibilities for reviewing and consolidating these statements were delegated to the major commands. The commands send consolidated statements to Air Force headquarters.

In many cases the financial statements prepared by Navy activities and by Air Force fiscal control offices were significantly distorted by the lack of disclosure and by improper accounting. For example, open messes at Clark Air Base and at the Naval Station, Subic Bay, in the Philippines, failed to disclose in financial statements, and establish reserves for, contingent liabilities of \$760,000 and \$50,000, respectively.

COMMAND ACTION ON FINANCIAL REPORTS

The inaccurate reporting of results of operations, the failure of some commands to take the necessary corrective action when unsatisfactory conditions were disclosed, and a lack of follow-up to ensure that the corrective action was implemented resulted in an ineffective use of financial statements.

In the Army, Navy, and Air Force, financial reports are sent up the pyramid of command and each level reviews, comments, and, in some cases, consolidates the reports before sending them to the next echelon or headquarters. Recommendations for corrective action within the Army and Navy are made by major commands and follow-up action is taken

through inspections by inspectors general. In the Air Force corrective action is recommended by the resident auditors.

At the headquarters, with the exception of the Air Force headquarters, financial reports from both major commands and installation levels are reviewed and comments are made. Headquarters, U.S. Air Force, has delegated all responsibilities to the major commands for the review of non-appropriated fund activities.

CONCLUSION

The reporting of financial results of operations of many nonappropriated fund activities to the various levels of command has been deficient, and command reviews and follow-up have not always been effective. The data contained in financial statements must be reliable for the statements to be an effective tool in monitoring nonappropriated fund operations. They then can be effective if they are used to indicate trouble spots, if corrective action is recommended, and if follow-up action is taken.

CHAPTER 9

LOOSE CONTROLS OVER

SLOT MACHINE OPERATIONS

On the basis of their interpretation of Public Law 906, 81st Congress (15 U.S.C. 1171 through 1177), the military departments have prohibited the operation of slot machines on military installations in the United States and its territories. Conversely, we have learned during our review that slot machines are operated (1) on U.S. military bases in many foreign countries where their use by citizens is prohibited, (2) where special permission, not obtainable by citizens, had been obtained, and (3) in a few places where local laws permit.

Slot machines have been an important factor in the generation of income in overseas nonappropriated fund activities and in some cases have made the difference between a profit and a loss on overall operations. We obtained the following data on amusement machine income generated annually worldwide by the military services.

<u>Military service</u>	<u>Annual amount</u> <u>(millions)</u>
Army	\$27.1
Navy	4.3
Marine Corps	2.1
Air Force	26.0

INADEQUATE GUIDELINES FOR CONTROLLING INCOME

At the time of our review, the Navy and Marine Corps had issued detailed departmental guidelines on the acquisition, operation, and disposal of slot machines, but the Army and Air Force had delegated this responsibility to overseas commands. Substantial improvement could be made in the guidelines from the overseas command and the guidelines from departmental headquarters.

Chiefly lacking among the guidelines were established payout percentages, prescribed limitations on deviations from the percentages, and a reliable method for determining whether the actual amount paid out was reasonable when compared with an expected, computed payout.

Only Navy headquarters had set a minimum payout percentage; certain Army and Air Force local commands had prescribed target minimum and maximum payout percentages. Commanders or headquarters had not established payout percentages and prescribed acceptable deviations from the standard percentages. We have been advised by a manufacturer of slot machines that a maximum deviation of 2 percent from the established payout percentage is usually allowed by commercial gambling casinos in CONUS for fully broken-in and properly maintained slot machines.

INADEQUATE CONTROL OVER CASH

There were weaknesses in controls over cash income from slot machines at virtually every overseas installation we visited. Contributing to the weaknesses were the use of coin meters that could be reset without appropriate control, the failure to use coin meter readings in verifying cash collections, the lack of control over slot machine keys, and improper coin collection practices.

MILITARY POLICY ON THE CONTINUED USE OF SLOT MACHINES

The military services generally have supported the use of slot machines to provide a means of amusement and relaxation, to provide additional funds for improved facilities and social programs, to maintain the low prices for food and beverages in the clubs and messes, and to provide additional funds for welfare and recreation purposes. The military services have reaffirmed their positions within the past 1-1/2 years, although we understand that military components very recently were considering the removal of slot machines from nonappropriated fund activities. The major reason given by the military components for retaining slot machines is that, to make a profit if slot machines were removed, clubs and messes would have to either increase prices of food and beverages or reduce service and entertainment.

However, the financial management of many of the overseas messes, particularly those in Vietnam, has been less than satisfactory and has resulted in poor financial condition of the messes. Even if slot machines are removed from a mess, the financial condition of the mess can be maintained and perhaps improved through more intensive management.

For instance, during our fieldwork at the 1st Air Cavalry Division, Bien Hoa, Vietnam, we noted the absence of slot machines in the messes. Representatives of the base comptroller and mess officials informed us that the commanding general was dissatisfied with the handling of proceeds from the slot machines and took the position that proper monitoring of the machines would require too great an effort and therefore directed their removal.

Mess officials said that, without the income from the slot machines, they had to concentrate on improving the management of the messes. They worked at improving meals, bar service, and entertainment. By doing so, they hoped to increase patronage and improve the financial positions of the messes. Although we were not furnished supporting data, mess officials stated that the messes showed profits for the first time. They concluded that slot machines were not necessary to ensure a successful mess operation and the lack of slot machines encouraged them to run a better mess. They advised us that they would not recommend reinstallation of slot machines in their messes.

CONCLUSION

Control over slot machine operations at overseas installations was grossly inadequate chiefly because departmental guidelines were lacking and local guidelines needed substantial improvement. Further, we have learned that slot machines are operated in foreign countries where the laws of the host countries prohibit their use by citizens.

There was a lack of adequate criteria for evaluating slot machine operations, and the payout limitations we encountered during our review were too liberal to be of much value to management personnel for controlling income.

Since completion of our fieldwork, the military departments have issued new regulations and directives which, if strictly adhered to, should do much to strengthen controls over cash collections from machines and keys to the machines in which we found many weaknesses.

The Office of the Secretary of Defense should (1) undertake a study of slot machine and other amusement machine operations and their effect on nonappropriated fund activities and (2) determine whether, in the light of the problems identified and the benefits to the activities, the continued use of such machines to pay out money or prizes is in the best interest of the members or customers of the activities.

If the overseas installations are to be allowed to continue operating slot machines and other amusement machines which pay out cash prizes, the military departments should

- devise an objective method for computing expected collections from slot machines on the basis of the number of coins played and predicted payouts,
- prescribe restrictive limitations on the extent to which the actual collections may vary from computed collections, and
- require that slot machines be operated only in consonance with the laws of the respective foreign countries in which the military installations are located.

CHAPTER 10

INTERNAL AND EXTERNAL AUDITS

Nonappropriated fund activities at military installations are usually audited by Army internal review staffs, Navy audit boards, Air Force Auditor General resident auditors, and Marine Corps Field Audit Service staffs. Nonappropriated fund activities at departmental headquarters are audited by central audit agencies or certified public accountants. At all echelons these activities are subject to audit by central audit agencies, which devote comparatively little effort to this work, and to reviews and inspections by inspector general and other investigating staffs. This total audit effort has proven to be unsatisfactory because much of the work has not been broad enough or deep enough to evaluate systems of internal control.

CENTRAL AUDIT AGENCIES

The Air Force Auditor General periodically audits nonappropriated funds at the installation level. The Army and Navy central audit agencies perform such work on an exception basis, i.e. when requested or as need indicates. The central audit agencies, also, audit headquarters funds except for the Army Central Welfare Fund which is audited by a certified public accountant.

The Marine Corps, on the other hand, has established the Marine Corps Field Audit Service which audits only nonappropriated funds but excludes exchanges. The number of personnel assigned to the Marine Corps Field Audit Service for fiscal years 1967, 1968, and 1969 were 136, 132, and 145, respectively. The other central audit agencies spent very little effort in auditing nonappropriated funds as shown in the following table.

	<u>Man-years</u>		Percent
	<u>Total</u>	<u>Nonappro- priated funds</u>	on nonappro- priated <u>funds</u>
U.S. Air Force Auditor General:			
Fiscal year 1967	807.0	52.4	6.5
Fiscal year 1968	787.0	37.7	4.8
Fiscal year 1969	724.3	25.0	3.4
U.S. Army Audit Agency:			
Fiscal year 1967	571.5	5.9	1.0
Fiscal year 1968	583.7	3.9	.7
Fiscal year 1969	535.7	4.3	.8
U.S. Naval Audit Ser- vice (note a):			
Fiscal year 1967	-	-	1.3
Fiscal year 1968	-	-	.7
Fiscal year 1969	-	-	1.6

^aMan-year information not available. Percentages provided by U.S. Naval Audit Service.

The Army and Air Force jointly audit the Army and Air Force Civilian Welfare Board and its civilian restaurants. The governing joint regulation provides that the Army annually audit restaurants located on Army installations but the Air Force left the frequency of audits of Air Force restaurants to the resident auditor. As a result the Army was auditing its restaurants annually but the frequency of Air Force restaurants audits averaged 27.8 months.

AIR FORCE

The auditor general's policy is to concentrate audits on the bulk of Air Force resources although he recognizes the morale effect of well-managed nonappropriated funds. His resident auditors are assigned to most major Air Force installations and are responsible for allocating their own audit efforts.

Because of the auditor general's emphasis on auditing the application of greater resources (appropriated funds),

the headquarters audits, although performed annually, did not include sufficient tests of internal controls and most of the nonappropriated fund activities at Air Force installations we visited had not been audited in 2 years.

On April 29, 1970, the auditor general issued a report on a special audit of the management of open messes undertaken in November 1969 at the direction of the Air Force comptroller. The audit, covering 138 open messes at 116 installations, appears to have been competently performed. The deficiencies found in this audit are similar to those we found during our review. The emphasis in the 31 recommendations made to Air Force headquarters was on improvement of open mess directives and the quality of the mess management.

ARMY

At the request of the Secretary of the Army, the U.S. Army Audit Agency conducted, during the period October 1969 to March 1970, a worldwide survey of the various means of auditing Army clubs and messes. A substantial portion of this survey was devoted to the audit of 32 officers' and noncommissioned officers' open messes in order to evaluate the effectiveness and efficiency of their operations. The agency concluded that the irregularities they found were not the result of inadequate audit coverage in the past, but were the result of deficient open mess management coupled with inadequate command and staff supervision.

The agency normally audits nonappropriated funds only at installations in Europe, the Army Central Mess Fund, and the Army and Air Force Civilian Welfare Board. On the bases of the system of internal control, reports, and working papers we examined, the agency's reviews appeared appropriate and competently performed.

In response to a DOD instruction dated November 3, 1970, regarding audits of nonappropriated funds (see p. 42), the Army Audit Agency has undertaken the audit of 60 selected clubs and messes worldwide. The estimated completion date for this undertaking is June 30, 1971. This increased work load cannot be met effectively without an increase in staffing. The agency anticipates problems in obtaining sufficient

capable staff members, either U.S. citizens or local nationals, to satisfactorily carry out this assignment, particularly in Germany where many of the clubs are located. Whatever alternatives are applied, the agency believes that this undertaking will appreciably decrease audits of appropriated funds.

INTERNAL REVIEW

Air Force fiscal control offices at most installations daily monitor nonappropriated fund activities and conduct periodic reviews of their internal controls and operations. These reviews were not comprehensive and follow-up action was weak. At Lackland the fiscal control office did not spend sufficient time in reviewing activities and did not adequately document the nature or scope of its work.

Army nonappropriated fund activities are periodically reviewed primarily by internal review staffs. These internal review staffs devote inadequate attention to nonappropriated funds. For instance, the internal review staff at Fort Lewis had assigned only one man to audit such activities at the fort and its satellite installations. Consequently, the reviewer spent very little time at some activities and did not visit the satellites.

In Vietnam the internal review division auditors lacked qualified personnel and adequate time to perform reviews. Furthermore agencies failed to adequately respond to recommendations made in the division reports.

Navy nonappropriated fund activities are audited quarterly by boards appointed by the installation commander. Our review of the working papers and reports of these boards, and our discussion with board members indicated that the limited scope of these audits did not provide an adequate basis for reviewing the operations and resources of nonappropriated fund activities. The boards' efforts were unsatisfactory because board assignments were additional rather than primary duties, too few persons were assigned to some of the boards, and many of those assigned did not have accounting or auditing backgrounds. These deficiencies have resulted in the boards' consistent inability to effectively assist mess management.

EXTERNAL AUDITS

On October 17, 1969, a DOD memorandum was issued which required that, in general, all clubs and messes be audited annually by public accountants. No actions were taken in the field to comply with this memorandum.

On November 3, 1970, a DOD instruction was issued which requires that all clubs and messes be audited annually on either an individual or system basis and that at least 25 percent of the clubs and messes be audited by public accountants, the cost of which is to be borne by the audited activity. The remainder are to be audited by military components.

Of the nonappropriated fund activities we reviewed (excluding the exchange and motion picture services), only the Army Central Welfare Fund had been audited by a public accountant. We reviewed the accountant's working papers and found that the audit work was fairly comprehensive and that appropriate tests had been made. Nevertheless we believe that the agreements with fund management for work by a certified public accountant gave insufficient emphasis to internal controls. Although the fund receives a financial statement certification, it does not receive in-depth evaluation of management policies and controls. The brief letters commenting on internal controls, provided along with certified statements, generally included only a few sentences on the very broad and complex procedures used to implement management policies.

CONCLUSION

The audits performed by the internal review staffs, by the central audit agencies, and by the certified public accountant have not provided the evaluations needed by the nonappropriated fund activities and management responsible for overseeing them. We suggest that a separate office be established directly under the Secretary of each military department for the purpose of auditing the clubs and other recreational activities at headquarters and at field locations. These offices should be adequately staffed with competent auditors who meet professional standards and should be supported with nonappropriated funds contributed by the central funds. Thus, the individual activities would be relieved of the financial burden of localized audit effort, and central audit agencies which are supported with appropriated funds could concentrate on auditing activities using appropriated funds.

MATTERS FOR CONSIDERATION BY THE COMMITTEE

In order that the military departments may provide the audit services needed by officials responsible for nonappropriated fund activities, the Committee may wish to consider directing that they establish directly under each Secretary separate centralized audit offices financed by nonappropriated funds, that would conduct financial and management audits of the clubs, messes, and welfare and recreational activities of the military departments.

CHAPTER 11

SCOPE OF REVIEW

The purpose of our review was to evaluate systems of internal control and internal audit and identify management procedures for controlling appropriated fund support and nonappropriated fund support used by morale, welfare, and recreational activities of the Department of Defense. Although we reviewed the management of many recreational activities including those which produced revenues, we concentrated our efforts on military enlisted and officer clubs and open messes at the installation level.

During the period January 1970 to August 1970, we examined accounting and administrative records, analyzed financial reports, reviewed audit reports and applicable regulations and tested internal controls including cash and inventory tests at headquarters of the military components and various commands and at selected installations. (See app. II.) We also reviewed and evaluated the work of internal auditors located stateside and overseas.

APPENDIX

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Congress of the United States
House of Representatives
Committee on Appropriations
 Washington, D.C. 20515

January 26, 1970

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Honorable Filmer B. Staats
 Comptroller General of the United States
 General Accounting Office
 Washington, D. C. 20548

Dear Mr. Staats:

The Committee is concerned with the management and operation of non-appropriated fund activities operated by the Department of Defense. In reporting the Department of Defense and Military Construction Appropriation Bills for 1970, the Committee voiced its concern with the policies and practices of the military services for the reporting and use of non-appropriated funds. The Committee is also interested in the support furnished non-appropriated fund activities from appropriated funds and in whether these activities are being properly managed to insure that there is no waste or other inappropriate use of such funds.

Accordingly, the Committee requests that the General Accounting Office make a comprehensive review and evaluation of the operation and management of non-appropriated fund activities. The review should include an investigation of the services' operating practices, procedures and management controls.

The Committee would appreciate a complete report as soon as possible. However, in view of the various types of non-appropriated activities and the extensive operations of the larger ones, individual reports may be submitted as the work

on each type of activity selected is completed.

The review should include, but not necessarily be limited to:

1. The extent to which various types of non-appropriated fund activities rely on support from appropriated funds, including such areas as personnel, facilities, transportation, and supply. The information obtained should be used as the basis for further detailed studies into selected areas to determine whether such support is necessary and should be more closely delineated in budget requests.
2. The procedures, guidelines, and controls established by each of the military services and the Department of Defense to insure that the collection of funds from various non-appropriated fund activities and the reallocation of these funds are in the best interest of the military personnel involved.
3. The adequacy of procurement practices and policies for the acquisition of facilities, materials, goods, and services.
4. The custody and control of all assets including facilities.
5. The control of the sale, donation, award, or other distribution of materials, goods, services, assistance, or other property acquired with non-appropriated funds.
6. The reporting of financial results and operations of non-appropriated fund activities to various levels of command in each of the military departments.

Sincerely,


Chairman

LIST OF INSTALLATIONS AND ACTIVITIES VISITED

DEPARTMENT OF THE AIR FORCE:

Headquarters, Washington, D.C.

Headquarters, Air Training Command,
Randolph Air Force Base, Texas:
Lackland Air Force Base, Texas

Military Personnel Center,
Randolph Air Force Base, Texas

Headquarters, U.S. Air Forces in Europe,
Wiesbaden, Germany:
Ramstein Air Base, Germany
U.S. Air Forces in Europe Class VI Fund, Mainz-
Kastel, Germany, and selected activities

Headquarters, Pacific Air Forces, Hawaii:
Clark Air Base, Philippines
John Hay Air Base, Philippines

DEPARTMENT OF THE ARMY:

Headquarters, Washington, D.C.

Headquarters, 6th U.S. Army,
Presidio of San Francisco, California:
Fort Lewis, Washington

Headquarters, U.S. Army, Europe, Heidelberg, Germany:
U.S. Army, Europe Class VI Agency, Heidelberg,
Germany and selected activities
Selected subcommands and activities

U.S. Army Special Services Agency, Munich, Germany

Armed Forces Recreation Center, Garmisch, Germany

APPENDIX II

DEPARTMENT OF THE ARMY (continued):

Headquarters, U.S. Army, Pacific, Fort Shafter, Hawaii:
U.S. Army, Ryukyu Islands/Fort Buckner, Okinawa
Sanno Hotel, Tokyo, Japan
Chao Phya Hotel, Bangkok, Thailand
Headquarters, U.S. Army, Hawaii
Headquarters, U.S. Army, Vietnam, and selected activities

DEPARTMENT OF THE NAVY:

Headquarters, Washington, D.C.
Headquarters, U.S. Marine Corps, Washington, D.C.
U.S. Naval Station, Newport, Rhode Island
U.S. Naval Station, Rota, Spain
U.S. Naval Station, Subic Bay, Philippines
U.S. Marine Corps Base, Camp Lejeune, North Carolina

JOINT ACTIVITIES:

Army and Air Force Civilian Welfare Fund, Washington, D.C.
Stars and Stripes, Darmstadt, Germany