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Honorable John Tuber, Chairman Committee on Appropriations House of Representatives

Dear Mr. Chairman:

Further reference is made to your letter of Aubust 20, 1953, acknowledged September 2, relative to the difficulty confronting the Committee on Appropriations, on many occasions, to ascurtain the amount of actual obligations incurred against particular appropriated funds. You attribute this situation to the difference of opinion on the part of adminstrative officers as to what constitutes a proper obligation against appropriated funds and, therefore, suggest that the General Accounting Office undertake to set forth a clean-out definition of the word "obligation" and to state clearly to all agencies concerned what will be recognized as valid obligations under law.

As you know, this matter has been the subject of discussions between representatives of the General Accounting Office, of the staff of your Comittee, and of industry.

Neither the Congress nor the accounting officers of the Government have heretofore undertaken to define, for Federal fiscal purposes, a precise and all-inclusive definition of the term "obligation". In determining whether and to what extent obligations against appropriations or funds have been incurred, certain basic principles have been applied but the vast operations of the Government they many questions which have arisen have been considered on an individual basis.

Consistent with various decisions rendered by the accounting officers through the years, there is now in effect Budget-Treasury Regulation No. 1 issued jointly by the Director, Bureau of the Budget and the Secretary of the Treasury, with the concurrence of the Comptroller General. This regulation prescribes, in considerable detail, the basis for determining, recording and reporting obligations under varying situations. See the revision of September 1953. In my opinion a proper applicaton of the principles set forth therein, and in the decisions rendered by the accounting officers, would largely remove the problem you mention.

The term "obligation" when used in connection with appropriating language and in conjunction with provisions of the general and special statutes relating to the period of availability of Government funds expresses the action of an administrative officer in the employment of personnel, the placing of purchase

orders, the execution of contracts, the authorization of travel of persons and shipment of things, etc., to supply certain services and benefits in accordance with stated appropriation objectives and purposes.

In determining the appropriation properly chargeable in such cases, an obligation generally has been considered to be a definite commitment which creates a legal liability of the Government for the payment of appropriated funds for goods and services ordered or received.

The normal fixed price end-item procurements of Government agencies, and expenditures relating to personal services, travel and communication, etc., usually commenced and completed within the same fiscal year or shortly thereafter, generally present little, if any, real difficulty to the administrative agencies or to the appropriation committees of the Congress in respect of determining the amount of actual obligations incurred for any given period time.

On the other hand, it is recognized that the great diversity in the many types of goods and services purchased by the major spending agencies of the Government, the unusual circumstances surrounding the transactions, and the time lag between the order and the delivery of goods give rise to difference of opinion not so much as to what contributes a proper obligation but rather the precise time the obligation was created and the actual amount thereof and, therefore, the particular fiscal year appropriation properly chargeable therewith. It is often very difficult, under such conditions, to determine at what stage in a given transcation an obligation against an appropriation results in a legal liability for the payment of money as well as the actual amount thereof. Such determinations, of course, involve questions of both law and fact based upon the facts and circumstances in each particular case, and involve situations directly related in number and variety with the multitudinous procurement transactions in which the Government is concerned. For such reasons, no simple all-embracing definition of an obligation appears feasible.

As an example of a situation giving rise to the difficulty of determining when an obligation is incurred and the amount thereof, the following may be cited:

The Marine Corps places an order with the Ordnance Corps of the Army for a weapon. This order is consolidated along with other similar orders from within the Army, from other services and for military assistance. The Ordnance Corps then enters into contracts with private industry for certain components and will manufacture certain components in its own facilities after contracting with outsiders for materials and possibly minor components to become a part of its own manufacture. It may not be successful in immediatley obtaining contracts sufficient to fill total reqirements for all components, but may be successful for the major portion of them. Now suppliers must be developed for the remainder. The contracts with private industry any involved progress payments well before any deliveries are contemplated. Moreover, such contracts may include price redetermination clauses which will be settled by audit and negotation long after an initial supply of the components involved has been received.

Assume that after several progress payments are made a portion of the components are delivered to Ordnance and are credited against the progress payments, but the final price is yet undetermined. Ordnance employees a private contranctor using a Government-owened facility to assemble the various components, including

both Government and contractor furnished materials. At this point it is determined to make a slight modification in the engineering design of one of the components being produced by a private contractor, so at some point in the assembly process the modified component at higher or lower unit price will be introduced but some completed units will contain the original part. Assume further that this continuing process requires about eighteen months for the first completed items to be delivered. When the completed product is delivered it is allocated to the respective participants in the joint order by a military committee on the basis of necessity and with no relationship to the sequence in which orders were placed by the various customers.

It will be seen from the cited illustrations, which is representative, that the processes which give rise to a "valid obligation" are not accomplished at any one time or in any uniform manner. Thus, the purchase of certain components from private industry may be one step, purchase of materials for use in an Ordnance operated manufacturing plant is another step, use of labor in Ordnance is still another step, contracting with private industry to assemble the components in a Government plant is a further step, etc.

The problem is further complicated by present procurement practices. In many each cases the amount of the obligation can be determined only by an estimated basis subject to revision as the work progresses under the contracts, such as cost reinbursable or cost-plus-a-fixed-fee contracts; fixed price incentive contracts which are essentially redeterminable contracts consisting of four main elements: (1) target costs, (2) target profit, (3) a flexible profit formula depending upon the variation of the total cost from the target costs, and generally, (4) a ceiling price which may be for later determination; contracts containing price oscalation clauses; and other fixed price redetermination contracts which may contain any one of at least five standard revision clauses. The revision clauses may provide for upward or downard revisions or both, retroactive or prospective effect of revisions, various profit formulas, etc. In addition, many cotnracts contain estimated amounts for concurrent spare part, engineering charges, special tools and ground handling equipment, etc., which in most cases are based upon a percentage of the cost of the basic items, but the specific spare parts, charges or equipment to be determined later.

Because of such considerations, in the light of the present legal concept of an obligation--see 31 Comp. Gen. 83, 85, 86--this Office is convinced that it is impracticable, if at all possible, to phrase into words a clean-cut and all-inclusive definition for the term "obligation" which would serve for all purposes and under all circumstances.

The question as to the validity of reported obligations has been of concern to this Office for some time. At your request we examined obligations reported by the Department of Defense as of June 30, 1952, including the financial policies and practices relating to the obligation of funds under the Natural Security Program. A report was furnished to you under date of April 24, 1953. By letter of March 5, 1954, we furnished you a report of survey of obligations reported by the Department of Defense for aircrafts and related procurement as of June 30, 1953. This, also, was prepared at your request. These projects disclosed many deficiencies and improprieties in reported obligations but I have been assured that there has been improvement in this area and that the military departments hav placed a greater emphasis on the proper resolution of the problem involved. We anticipate and will insist upon further continuous improvement and will cooperate to that end.

Sincerely,

Frank H. Weitzel Acting Comptroller General of the United States