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FINANCIAL MANAGEMENT IN A MILITARY DEPARTMENT

6 November 1958

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Honorable J. Sinclair Armstrong, Assistant Secretary of the Navy for Financial Management, was born in New York City on 15 October 1915. He received an A.B. degree from Harvard College in 1938, and an LL.B degree from the Harvard Law School in 1941. From 1941 until 1945 he was associated with the law firm of Isham, Lincoln and Beale. From 1945 to 1946 he was on active duty with the U. S. Navy Department assigned to the Office of the General Counsel. In 1946 he returned to his law firm and was appointed a partner in 1950. On 16 July 1953, he took office as a member of the Securities and Exchange Commission and on 25 May 1955, he was designated Chairman of the Commission. On 27 May 1957, he resigned from the Commission and the next day assumed his present office. He is a member of the bars of the States of New York and Illinois. This is his first lecture at the Industrial College.

FINANCIAL MANAGEMENT IN A MILITARY DEPARTMENT

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ADMIRAL CLARK: You will recall that yesterday when Mr. Lawrence Powers of the General Accounting Office spoke on the subject, "Improvements in Financial Management," he dealt with the Department of Defense generally. This morning we are going to turn our attention to financial management in one of the military services--the Navy.

Our speaker has the responsibility for the development of policies and for supervising the procedures and practices in the financial management of the Navy. You have read in his biography that he has had a distinguished career in law, as Chairman of the Securities and Exchange Commission and in the Navy.

It gives me a great deal of pleasure and it is an honor to introduce the Assistant Secretary of the Navy for Financial Management, the Honorable J. Sinclair Armstrong. Mr. Armstrong.

MR. ARMSTRONG: Admiral Clark, Gentlemen: I have a prepared talk. I don't like to give prepared talks, but there are a number of subjects that I thought would be interesting to you about the financial management of the Navy and some of the problems that we are presently looking toward and facing. Therefore I prepared this, and with your indulgence I will read it. I understand that afterwards we can have a question and answer period, and that will perhaps be given additional stimulation by what I am about to read from this paper.

I am very pleased to be with you this morning to discuss financial management in the Navy. I think this is a subject which is becoming increasingly important. The amount of funds available to the Navy is limited, and, as a result, it is essential that we use our funds wisely and use them only for essential purposes.

Money is the limiting factor in virtually all our programs at the present time. We can't condone waste and extravagance and we can't afford the luxury of placing funds in programs of limited usefulness. Better management in the spending of our financial resources is a compelling necessity.

The Navy has just finished preparation of its budget for fiscal year 1960. This budget is now being considered by the Office of the Secretary of Defense and the Bureau of the Budget. Having just gone through weeks of intensive budget reviews, I am deeply concerned by the fact--as I will discuss in more detail in a few minutes--that the Navy has so many requirements of high priority which cannot be met under the stringent financial situation which confronts the Department of Defense.

Before considering the budget in more detail, I would first like to discuss the broad subject of comptrollership in the Navy.

We are in the midst of an era of financial reform in Government. The reform movement, which has been largely concerned with placing financial management in its proper place in the management process, has been under way for about 12 years. It had its beginning as an outgrowth of World War II when many people, both in and out of the military, felt that the military departments were not as efficient as they should be in carrying out business operations.

In 1949, this movement resulted in enactment into law of Title IV as an amendment to the National Security Act of 1947. Title IV, in addition to requiring the adoption of performance budgeting, property accounting, cost accounting, industrial and stock funds, and other new financial systems, provided for establishment of the Office of the Comptroller of the Navy and similar organizations in the bureaus and field activities.

I have been told that many segments of the Navy did not receive the advent of comptrollership very warmly. I think this is understandable, because the concept of comptrollership, which was taken largely from private industry, was not generally understood. I think the Navy acted wisely, and decided at the outset that comptrollership should not be forced by edict upon bureaus and field activities. It was determined, rather, that such organizations should come about largely by evolution. As in the case of private industry, the merits of comptrollership have had to be "sold" to management. This has been primarily an educational effort.

At the present time, nine years after the enactment of Title IV, I think comptrollership is widely accepted in the Navy. Comptrollership organizations exist in all bureaus and offices and in virtually all major field activities.

Now, what has the comptrollership concept accomplished? Looking back, I think it is safe to say that the Navy has come a long way in developing an effective financial management system. In each of the three basic areas of comptrollership--budgeting, accounting, and auditing--substantial improvements have been made.

In budgeting, a new performance budget structure was adopted in fiscal year 1951 which aligned fiscal responsibility with management responsibility and reduced the number of appropriations from 48 to approximately 20 we have today. In addition, the Navy planning system has been greatly strengthened. One of the products of this system--the Navy's program objectives--is providing a much sounder document on which to base the budget. Of particular significance is the fact that there has been a sharp increase throughout Navy in the time and attention which management personnel devote to budget considerations.

In accounting, radical changes have been or are being made to place greater emphasis on cost accounting and the development of data which management can use as the basis for operating decisions. Industrial funds, which operate in a manner similar to business corporations, have been or are currently being established at all industrial activities, such as shipyards, ordnance plants, laboratories, and overhaul and repair shops. Double-entry, accrual accounting is also being installed throughout the Navy in line with modern business practice.

Many of these accounting changes have been dictated by laws passed by the Congress subsequent to Title IV. The Congress has acted largely on the basis of conclusions reached by the Hoover Commission as well as on the recommendations of the Bureau of the Budget, the Treasury Department, and the General Accounting Office to the effect that the Department of Defense should adopt accounting systems similar to those in private industry. Now, I think I should say candidly that we have implemented some accounting changes which were not entirely in accordance with our own desires or wishes, in the Navy. But I think that for the most part what has been done has been sound.

In internal auditing--a subject largely unknown in the Navy until 1950--substantial progress has been made in reviewing the financial aspects of work being done in bureaus and field activities. In many instances, as many of you probably know from first-hand experience, audits have resulted in more economical operations as well as improved financial controls and record keeping. Fund limitations, as well as difficulty in recruiting capable personnel, however, have held the development of internal auditing below what is adequate in scope and frequency of audits. This is a program which we are attempting to step up.

Now, what about the future of financial management? In spite of these accomplishments that I have mentioned, I think much remains to be done, particularly in installing new management tools and in eliminating inadequate and outmoded systems and practices. I think we all know that custom and tradition die hard in any organization and that new and untried ideas are not always eagerly accepted.

The stature of financial management in the Navy will undoubtedly increase in the years ahead. We are likely to see many new innovations and much progress in the better utilization of the product of our financial management system.

The major weakness in our financial management system today, I think, is the fact that management personnel, possibly because of their concentration on operational matters, very often do not use the financial and other information placed at their disposal.

Comptrollers have a major responsibility in this connection. Many times, management personnel simply do not know how to use the financial information that is available, and the comptroller's job is to assist management in this connection. The lack of well trained, effective comptrollers, able to work closely with management personnel, has undoubtedly been a factor in the slow advance in getting management to make better use of the financial resources.

A good comptroller really has a lot more to do than just being a good accountant. I think accounting may be a detriment to a comptroller if it blinds him--and sometimes it does--to the more fundamental requirements of his position.

I'd like to describe the qualifications that I think a good comptroller should have. He's got to be effective in dealing with people. He's got to be an individual with initiative. He's got to be alert, and he's got to be able to think up, devise, and suggest improvements in policies and procedures which will facilitate management processes, because, essentially, a comptroller's primary responsibility is to aid management in arriving at decisions. The nature of this assistance extends far beyond pure fact-finding. It encompasses analyzing and evaluating data and presenting such evaluations effectively in written or oral form.

Many of you have known people who gained reputations as excellent comptrollers. If you will analyze their qualities, I am sure you will arrive at similar conclusions as to what made them effective.

I would like to speak now for a few minutes about some current problems in the financial management field. I obviously don't have time to discuss many of the financial problems with which the Navy is confronted, but I would like to mention a few.

First--the reorganization which is under way in the Department of Defense. The reorganization of the Department of Defense is a subject which obviously will take a considerable amount of time to resolve, and few final decisions have been made at this time. The proper organization of the Department of Defense is a tremendously complicated subject, and views as to how the law should be implemented naturally vary.

As you know, the budget is largely a control device. It is through the budget and planning process, therefore, that the effects of the reorganization will become apparent and will be felt.

I would like to discuss the possible effects of the reorganization act on the financial management process in the Navy by centering my comments on two examples. I do this primarily so that you will gain a better understanding as to what is at stake so far as the Navy is concerned--not because any final decisions have been made. They haven't.

First, let us consider the unified commands which have been or are in the process of being established. The question arises as to whether such commands, which are directly under the supervision of the Secretary of Defense, and which are composed of elements of the three services, should be made responsible for establishing their own requirements and for doing their own budgeting. If this were done, these unified commands would presumably determine how many ships, aircraft, missiles, weapons, troops, and so forth were needed to carry out their missions, and their program and dollar requirements would then be submitted directly to the Office of the Secretary of Defense for review and approval. This might even be done through some reviewing procedures of the newly enlarged Joint Staff.

Any process of this sort, which bypassed the Navy Department, would obviously seriously affect the responsibility and authority of the Secretary of the Navy. It would place preparation of the Navy's budget, as well as those of the other services, primarily in the hands of the Department of Defense. It would weaken our vital constitutional concept of civilian control of the military.

This, that I have just described, is, of course, an extreme view as to the manner in which the financing of unified commands could be handled. But it could happen.

Logic would dictate, however, that central, overall planning as to what is required in the way of ships, aircraft, missiles, and so on, for the proper implementation of the roles and missions of the Navy in the defense of the country should continue to be a function of the Navy Department and reside basically in the Secretary of the Navy, the Chief of Naval Operations, and the Commandant of the Marine Corps. I cannot visualize, myself, how it could work effectively in any other way.

It seems to me that the soundest method of handling the program and budget requirements of the unified commands is to continue, as we are at the present, with the commands budgeting for their headquarters costs only. This leaves all other requirements to be budgeted for within the framework of the three military departments.

Another question raised by the Defense Department Reorganization Act relates to the extent of the review of both program and budget requirements of the services by the Joint Chiefs of Staff. To what extent, for example, should the Joint Chiefs, with their expanded staff, review and have authority over the detailed programs of the three military departments?

Heretofore, the Joint Chiefs have made broad military and strategic policy decisions. The development of the detailed program and dollar requirements to implement those decisions has been largely a responsibility of the individual military departments. Their budgets have in turn been reviewed by the Comptroller of the Department of Defense and the Secretary of Defense before being forwarded, through the Bureau of the Budget and the National Security Council, to the President. This has been primarily a civilian, rather than a military review of the amount of dollars required to carry out the various defense programs.

This is an effective method of handling detailed program and budget requirements. It places emphasis on civilian control of the purse strings, and I hope no fundamental change will be made in these procedures and relationships.

Implementation of the reorganization act in the financial field is likely to come about slowly. Any substantial changes in the existing process will have to be worked out with the Appropriation Committees

of the House and the Senate. This is going to take time and we will all have to exercise patience as the pattern of the future unfolds.

Now I would like to speak about the appropriation structure for a moment, and the possible impact of reorganization on the Navy Department, the Department of the Navy, itself.

Turning to a matter involving the framework of the budget--the appropriation structure--for a number of years the Navy has prided itself on having a performance budget structure developed in accordance with the concepts of the first Hoover Commission report on budgeting and accounting in 1949. This structure is basically attuned to the bureau structure of organization, since it has long been a fundamental principle of budgeting that fund responsibility and organization responsibility should be aligned.

In the last few years, growing pressure has been exerted on the Navy to revise its appropriation structure once again, to place it on what is commonly referred to as a "category basis." A budget structure of this type would be confined to about six appropriations, one each for military personnel, maintenance and operation, major procurement, research and development, public works, and reserve forces. The Army and the Air Force now have appropriation structures along these lines. They fit in with their types of organization under a Chief of Staff, and they apparently work very satisfactorily.

In the Navy, however, because of the bureau pattern of organization, such an appropriation structure would create numerous difficulties, not only in preparation and execution of the budget but also in justifying it before the various review levels, particularly the Congress. For example, the one "maintenance and operation" appropriation would include funds for every bureau, covering all field installations, headquarters, and the maintenance, operation, and overhaul of ships, aircraft, and all other types of weapons and equipment.

In spite of the difficulties which we foresee, however, it appears that a new structure will be required of us, primarily on the ground that it will provide added flexibility in the use of funds. It is argued that, by having one large "pot" of money for maintenance and operation, the Secretary would be able to shift funds between programs so as to get maximum utilization out of the amounts provided and appropriated.

It is my feeling that the extent to which funds may be shifted is limited, for various reasons. First, the Appropriations Committees in the House and the Senate naturally look askance at any sizable transfer of funds once an appropriation act has been passed. Second, we have the practicalities of our internal organization structure in the Navy to contend with. The prospective change in the appropriation structure, as well as the implications of the Department of Defense Reorganization Act, have raised basic questions about Navy organization. For example: Is the bureau structure archaic? Has the time arrived to transfer functions between bureaus? Are certain bureaus needed today? What about the functions and responsibilities of the Office of the Chief of Naval Operations? The civilian Secretariat? The various offices of the Department? These questions and many others have been on the minds of top personnel for a long while.

Recent events have made it clear that a new look should be taken at Navy organization. The Secretary has accordingly recently appointed a committee, composed of top military and civilian personnel, and headed by the Under Secretary, to make a complete study of this subject. This committee is now at work and its recommendations, which should be forthcoming toward the end of the calendar year, may propose significant changes in the Navy as we know it today.

Now a little bit about the Navy budget. As I am sure you have gathered from what I have said up to now, most of our problems in comptrollership stem from the budget process.

Our primary budget problem is simply that the amount of funds available to the Navy is limited. As a result, there is never a sufficient amount to accomplish what is considered desirable from a purely military viewpoint.

The rapid developments in weapons, missiles, nuclear power, and other techniques have given rise to many internal problems of great complexity. The Navy is undergoing a period of transition. It is attempting to convert from the old to the new in the brief span of a few years--something which in more peaceful times would have taken decades.

With the approximately $11 billion available to the Navy today, it must sound as though we should have enough funds to finance virtually all of our requirements. But that is not the case. Modern weapons cost enormous amounts of money and our dollars do not go nearly as far as we would like them to go.

The limitation of funds means that, each year, the Navy must face up to some difficult decisions, particularly in the relationship between current readiness and modernization. In essence, the basic budget problem is this: how far can the Navy afford to risk current readiness by reducing the size of the Navy in being--its military personnel, its ships, its aircraft, and its shore establishment--in order to build a more powerful Navy of the future, through modernization.

In the light of the grave conditions that exist in the world today, this is a very difficult problem to decide.

At the present time, about 53 percent of the Navy's funds, $5.8 billion, is going into current readiness--that is, personnel and operations--and the remaining 47 percent, about $5.3 billion, is going into the Navy of the future, through new procurement, construction, and research and development. This fiscal year, the Navy will spend approximately $1.8 billion for new aircraft, $1.3 billion for new ships, and about $500 million for missiles of various types. While these expenditures sound large, they are not nearly enough to bring about the rapid modernization of the fleet which is essential.

Now a little bit about how we prepared the budget--budget preparation. One of the major improvements in financial management which has come about in recent years stems from the better liaison between the Office of the Comptroller of the Navy and the Office of the Chief of Naval Operations. This has resulted in better program planning and in better decisions with regard to the utilization of funds.

A sound, well prepared budget invariably reflects "team" action within an organization. It takes the joint action of the planner, the programer, and the budget analyst, and the wisdom and foresight of those in command, to come up with a budget which can be defended properly before higher review levels.

The necessity of a "team" approach to the budget has not always been recognized in the Navy nor in other agencies, for that matter. The planner is sometimes inclined to develop plans in a vacuum, without regard to financial implications; the program manager is often inclined to look narrowly at his own program, inflating its importance and dollar requirements to the detriment of the Navy's overall objectives.

At the moment, this problem has largely been solved in the Navy. Personnel in the Office of the Comptroller and in the Office of the Chief of Naval Operations have worked out a system of coordination through the General Planning Group (which is known as Op 90) by which top

officers in the Office of the Chief of Naval Operations are kept fully apprised of budget developments as well as of the implications of fund availability on military requirements.

In turn, the Office of the Chief of Naval Operations keeps the Comptroller's office informed of changes in program requirements and of the priority which it attaches to programs which are competing for the available dollars.

Out of the trials of many years of experience, the Navy is emerging with a very fine budget system, one which has proven its worth and one for which the Navy has been highly commended by high-ranking officials both in the executive branch and in Congress.

Now I would like to mention briefly our Accounting Study Committee. This should be of immediate interest to you.

With the approval of the Secretary, I have recently appointed a committee of key personnel in my office to study the accounting system. During the months I have served in my present capacity, I have had discussions regarding the accounting system with many Navy personnel, both Supply Corps officers and officers of other codes serving in various capacities. Many of these people have informed me that they were of the opinion that the accounting system is not only unduly burdensome and complex but that it does not serve management adequately by providing timely and necessary information.

This has disturbed me, because the primary task of the accounting system is to provide management with the data it needs for making decisions. If this is not being done, it is essential that we determine why it isn't and take whatever corrective action is necessary. Accounting obviously should not be performed just for accounting's sake.

As a basis for the committee's work, I have written a letter to all bureaus and offices, to 65 field installations, and to 11 fleet activities requesting that they provide our Accounting Study Committee with their views and recommendations on this subject. Perhaps some of you have seen this letter. The committee needs the viewpoints and the experience of personnel, such as yourselves, and I know the committee will welcome any remarks that you have or suggested changes. We have received a wonderful response from this letter and many scholarly answers are now being analyzed by the committee.

An outside consultant, whom we have employed to serve on the committee, and various members of the committee are also discussing accounting matters with field installations, which they visit, and are becoming familiar with problems posed by field personnel.

This committee, which will submit a preliminary report by 15 December, has a formidable job on its hands when you consider the various requirements of law, the continuous pressure from the outside to establish more accounting along commercial lines, and the internal requirements of the Navy to provide an effective accounting system at the least possible cost.

Before closing, I would like to say a word about the Navy Regional Accounting Offices.

As many of you know, Title IV required the establishment of the Office of the Comptroller of the Navy. It is a statutory office, and the law prescribes the functions of the Office of the Comptroller.

I have heard some Supply Corps officers express the feeling that the law went too far and that accounting responsibility, other than the establishment of basic policy, should have been left with the Bureau of Supplies and Accounts. The law itself, however, as well as the intent of the law, as expressed in the hearings and the committee reports, made it clear what the Congress expected the Department to establish and to accomplish.

Accordingly, beginning in 1950, various accounting and audit functions carried on by the Bureau of Supplies and Accounts have been transferred to the Office of the Comptroller. The Cost Inspection Service, now known as the Contract Audit Division of the Comptroller's Office, was the last sizable function to be transferred.

Now another transfer of management responsibility is imminent and will soon be accomplished. For some time it has been apparent that management responsibility for the Navy Regional Accounting Offices should be lodged at the Secretarial level under the Office of the Comptroller.

The Navy Regional Accounting Offices provide, on an area basis, an accounting service for the various bureaus and other components of the Navy as well as the Office of the Comptroller. In doing this, they carry out the technical responsibility of the Office of the Comptroller.

I feel, as do the Secretary and the Under Secretary, that management control of the Navy Regional Accounting Offices can be improved by placing authority and direction over these offices under the Office of the Comptroller. In this way, the Navy-wide service of the Navy Regional Accounting Offices can be more closely tied in with the requirements of the other financial management functions, such as budgeting and progress reporting, which have made extensive use this past year of the service of the Navy Regional Accounting Offices, particularly in the area of expenditures.

Arrangements for the transfer of management responsibility of the Navy Regional Accounting Offices are presently being worked out between our office, the Comptroller's Office, and the Bureau of Supplies and Accounts, working under the guidance of the Under Secretary. There will also be transferred the Navy Accounts Disbursing Offices, the Navy Officers' Accounts Office, and the Navy Finance Center. This change in management responsibility is being effected quite apart from the considerations of the Committee on Navy Organization which I referred to a few minutes ago.

The transfer will in no way affect the careers or career opportunities of Supply Corps officers. This is something I want to stress very earnestly. While management responsibility will change, the internal management of these offices will continue to be carried out by Supply Corps officers, just as it is at present.

Supply Corps officers have made a substantial contribution to the development of comptrollership in the Navy. I hope that the Supply Corps will continue to take an active interest in comptrollership. Comptrollership billets provide an excellent stepping stone to higher positions, as is evidenced daily both in government and in private business.

In closing, let me say that the success of commanding officers in today's defense effort depends in no small part on their ability to be good business managers. I know of no better way to become familiar with the management process than by serving as the comptroller of a field activity. For, if any personnel outside of the commanding officer have a better chance to observe at first-hand the operations of the entire organization, or to get a feel for the overall management process, I don't know who they are.

So I hope that each and every one of you will consider the comptrollership function as an important one, careerwise and professionally, for yourselves, as well as an important one from the standpoint of carrying out our basic purpose of national defense.

Thank you all very much.

COLONEL LACKAS: Gentlemen, Mr. Armstrong is prepared to answer your questions.

MR. ARMSTRONG: If I can.

QUESTION: Mr. Secretary, as a Supply Corps officer I have a certain amount of interest in this. Would you care to elaborate on the management improvements that you envisage on transferring management control and technical control, that is, technical control of the auditing and accounting officers? Will you elaborate on the management improvements that you foresee, sir, and tell us whether you foresee a specialization in comptrollership as it affects the present Supply Corps officers?

MR. ARMSTRONG: Well, taking the second part of that question first, commander, I don't know what you mean by "specialization in comptrollership." I wouldn't look for Supply Corps officers limiting themselves to comptrollership any more than I would line officers or other specialty officers. I think the thing that we are trying to accomplish so far as the Supply Corps is concerned is to attain perhaps greater utilization of their talents in the comptrollership functions of the Navy. We expect, if we are lucky, to be able to have, for example, another flag billet, an additional flag billet for a supply officer in this accounting field, and certainly to maintain the present level of Supply Corps officers in these accounting offices, and our objective is to increase them.

But I want to get back to the position of line officers in the comptrollership business. I think the familiarity with comptrollership of line officers is also terribly important. I think that has been recognized, for example, in the top comptrollership assignments that have been made in the Navy. It is an interesting statistic that many of the rear admirals who have held the job of deputy comptroller of the Navy since the position was established have left as vice admirals, assigned to very important fleet commands. In CINCPAC Fleet, for example, Admiral Hopwood, at the present time, is a former Deputy Comptroller of the Navy. So it is extremely important to the line.

As to specific management improvements, I don't know that I can describe very satisfactorily what they would be other than to say there would be a more closely knit organization along functional lines, possibly somewhat greater efficiency in operation, and a continuing program along those lines. I am a little bit hesitant to predict specific management improvements, in part because I personally don't feel that the implication of existing management inadequacies, which might occur to someone from an allegation that there would be drastic improvements, is valid.

These offices are being well run at the present time, but we think we can do as well, and possibly better. Basically, the motivation, however, is compliance with the statute. We have to carry out the will of Congress, and we are trying to do it in the best possible way from the standpoint of management improvement, organizationally and personnelwise, particularly vis-a-vis the Supply Corps.

I think that what I have said would be in complete accord with the views of the Chief of the Bureau (Rear Admiral Boundy). As a matter of fact, he and I did something of a duet on this subject last night at the semi-annual meeting of the Supply Corps Association in New York, where we had a couple hundred or more Supply Corps officers at dinner at the New York Naval Shipyard. We were in full agreement on this thing. We have had wonderful relationships with Admiral Boundy in trying to work this transfer through.

QUESTION: Mr. Secretary, I was interested in your remarks that the new functionalized budget would not work too well under the Navy organizational bureaus. As you know, in the Army we have the technical services, which used to have budgets like that, and which now have had them merged into the functional-type budget.

I can't comment on how well it is working in the Army, but you indicated that it appeared to be working satisfactorily. But it isn't clear to me, the difference between the Navy bureau system and the Army tech-services system that would make it work in one case and not work in the other. I wonder if you would elaborate on that.

MR. ARMSTRONG: Yes, I think that's a good subject to try to elaborate on, and I won't be too articulate on a comparison between Navy and Army, but I think I can be quite articulate on the Navy problem as we see it.

There are two sides to this question: Should we have a single maintenance and operation appropriation? We have at the present time an appropriation, "Ships and Facilities, Navy," administered by the Bureau of Ships, for the maintenance, operation, and overhaul of the fleet. A similar appropriation is "Aircraft and Facilities, Navy," which the Bureau of Aeronautics administers. We have a similar appropriation for "Ordnance and Facilities, Navy." The Bureau of Ordnance administers it. They allot amounts out to various commands and types of commands, and so on. Also, the CNO organization has some responsibilities. Then we have some other appropriations which have somewhat divided management, for example, those from which certain administrative offices (Op Nav and EXOS) are funded. We also have an appropriation for the Bureau of Supplies and Accounts and so on.

On the question of flexibility: Is the Navy Comptroller about to be forced into the position of arbitrating every effort during a period of program execution by a bureau chief or a program sponsor to obtain more money out of the single "M and O" account to increase his program or to get him out of difficulties that have occurred? I certainly hope not. It would be a very difficult position. It would be a lot tougher than being the senior umpire in a World Series game and it would go on every business day of the year.

This is one of the dangers. Perhaps, if there were a simplification of bureau structure along lines which would be more attuned to the different types of activities that the Navy engages in, the problem I just mentioned of competition during execution of the budget could be limited or reduced in scope.

The other side of the flexibility argument--and this is one that appeals to me--is that from time to time you've got to do things in a hurry and you can't wait. If you have a Lebanon, as you had Suez, if you have specific operational requirements, these operational requirements are valid. That's what our defense forces are here for. You run into things that you have to do in a hurry that may not be properly budgeted for, and could not have been properly budgeted for in advance, because they cannot be anticipated, and if you do try to anticipate them, they are knocked out in the budget review under the rules laid down by the Bureau of the Budget.

Well, in passing, we proposed for inclusion in "Ships and Facilities, Navy," last year, $1.25 million, or some similarly modest amount of money, for damage resulting from storms and typhoons. The DOD

budget staff was knocking it out in the course of a hearing, and Admiral Cooper, who was Deputy Comptroller, made the remark sotto voce to me that some of the people on the DOD staff obviously weren't sailors, because they seemed to think that storms were never going to happen.

You can't budget in advance for extra expenses that are incident to deployments that may occur, such as the deployment in Suez and the one that went on in Lebanon this year.

Validly, programs may be out of control. For example, we had this year a program for dependents' medical care. A transfer in this case, a transfer which would have been possible between bureaus had there been a single "M and O" appropriation, would have been very sound. The freedom of choice of dependents as between civilian and military hospitals was something that Congress provided for. There were no statistics in advance when the program was first budgeted in December of 1956. We, the Navy, ran about $12 million over the single appropriation, "Medical care, Navy." Army and Air Force did the same thing, but, with a billion-dollar "M and O" appropriation, they simply transferred the funds. The Navy had to go back to Congress to get a deficiency appropriation, and Congress said, "No, you haven't interpreted the rules right. You shouldn't have given so much free choice." We said, "Yes, but the law says that the Secretary of Defense and the Secretary of HEW provide the regulation under which freedom of choice or lack of freedom of choice or limited freedom of choice is granted, and all we did was follow the regulations." We got into an awful "box" on that because we didn't have the flexibility. At the present time, the Army, which has a single manager, has paid the bill and may ultimately wind up with having paid a deficiency, if Congress doesn't give us the money.

I don't know that that answers your question. It is a little hard to answer it, because it's a dual question, involving simplification of the appropriation structure and simplification of bureau structure. You can sit down in the evening and revamp the bureaus any way you think might be good on paper, but ultimately their efficiency depends on the people who manage them. I have been told that some witnesses before the Under Secretary's committee said, "Well, we shouldn't change the bureau structure. We've won a number of wars with the bureaus the way they are." Well, that doesn't answer the question, either, and yet it's true.

Every now and again you have to create an organization in one of the bureaus that is almost like a single manager for a project, as, for example, our Special Projects Office that administers the Polaris fleet ballistic missile program. It has funds from five different appropriations, principally shipbuilding, procurement of ordnance and ammunition, and research and development. This so-called Special Projects Office, which is headed by a rear admiral, is nominally a part of the Bureau of Ordnance, but in fact it's sort of a satellite floating around in space out there, and it works pretty well. It receives guidance and direction from a Navy Ballistics Missile Committee of which the Secretary is the executive member. The office just doesn't fit any organizational pattern, and yet it's doing one of the outstanding project management jobs in government at the present time in bringing along the Polaris program. We have gotten away from the difficulties inherent in the five appropriations by setting up a project under the Navy Management Fund, so that the funds are all placed under a special account number and then are contracted for under the management fund concept, without citation of the appropriations from which the moneys were generated by Congress.

There are lots of different ways of conducting our business to get away from the alleged difficulties of the multiple "M and O" appropriations.

I hope I have answered that question. There is a lot to it.

QUESTION: I have two questions. The first one is based on two statements you made. One was on the coordination that you found necessary between the Comptroller and the Chief of Naval Operations, and the other one was that you mentioned briefly three separate offices--the Assistant Secretary for Financial Management (yours), the Office of the Comptroller, and the Chief of Naval Operations. What is the relationship among these three separate organizations? The second question is: What is the philosophy used behind internal audit?

MR. ARMSTRONG: The first question is: What is the relationship between the Assistant Secretary for Financial Management, the Comptroller, and the CNO? The Comptroller holds a statutory office established by Title IV. The statute gives him responsibility for all accounting, auditing, budget, progress and statistical reporting in the Navy. That's statutory. It also provides that he may be a civilian or a military man. The law provides, however, that if the Comptroller is military, then the Deputy Comptroller must be a civilian. As you will note, it is

permissible under the law for both the Comptroller and Deputy Comptroller to be civilians. Then an Act of 1954 came along and established two additional assistant secretaryships, and the justification made to Congress was that financial management was broader than comptrollership as specified in the Act of 1949, August 1949, and that it involved a much broader coverage, and therefore it would be wise to have an assistant secretary to whom the Secretary would delegate responsibility for financial management in its broad implications and aspects.

In the Navy the decision was that the Comptroller should be the same individual as the Assistant Secretary, hence a civilian with secretarial and Presidential-appointee rank. In the Army and the Air Force it was done just the other way around, so to speak. The Assistant Secretary for Financial Management, my counterparts, Mr. Garlock and Mr. Roderick, are not the comptrollers. The comptrollers are three-star general officers.

I think that the way we have done this in the Navy works very well. My deputy is a rear admiral of the upper half. Generally, the deputy has been an unrestricted line officer. At the moment, however, my deputy, Rear Admiral Beardsley, is an AEDO (Aviation Engineering Duty Only), an aviator with broad experience both in the fleet and in the Bureau of Aeronautics. Through him is the contact with Op 90, who, in turn, also is a flag officer in charge of the general planning group. On a day-to-day basis, therefore, the deputy comptroller is dealing with Op 90, who, in turn, is funneling information up to the CNO and VCNO and is getting information back down. That means that I, as the Comptroller, don't have to be bothering Admiral Burke or Admiral Russell, calling them up on the squawk box all the time, nor do they have to be bothering me. But, in the daily course of business with the various Ops, these officers develop ideas, and they then come over to us primarily through Op 90.

Also, structurally, within the Navy, under General Order 5, there is provided additional assurance of direct contact between the Comptroller and the CNO, because this Order provides that the Comptroller is a technical assistant to the Chief of Naval Operations as well as to the Secretary of the Navy.

I think that explains the structure. Was there another part to that question that I have missed?

STUDENT: The philosophy of internal audit in the Navy.

MR. ARMSTRONG: Yes, but I think I have covered the relationship of those three offices. I haven't completed the comparison with Army and Air Force, but I don't think I will, because, having described the Navy, I think perhaps that's enough.

The philosophy of internal audit. I don't know what you mean by philosophy. Internal audit is intended to provide assurance that funds that are handled by activities are handled properly in accordance with the appropriations and the accounting regulations and are used for the purposes for which they are appropriated. And every now and again, in fact quite frequently, internal audit is able to point out to the activity commander ways in which economies can be effected or in which money can be used more advantageously.

STUDENT: The area I was interested in was: Do you restrict your audit to pure financial management, or do you go beyond financial management to limit the dollars that are spent? Do you go beyond the scope of financial management per se?

MR. ARMSTRONG: I don't understand that. Do you mean do we tell them what kind of ships they ought to buy?

STUDENT: Yes; that's right.

MR. ARMSTRONG: No.

STUDENT: How effective are the purchases? How effective are certain operations among the technical forces or the line?

MR. ARMSTRONG: For example, I am trying to visualize your question. Should the fleet steam at 12 knots in order to save fuel, or can it steam at 20? Is that the type of question?

STUDENT: That's a little too broad.

MR. ARMSTRONG: The answer to that question is no, we wouldn't pay any attention to how a commander steams his fleet or how he flies his airplanes or fires his practice rounds. Of course not.

STUDENT: I can give an example of that. The DOD internal audit I believe states that it is restricted to financial management and matters

related thereto. In Army, the matters related thereto have been expanded to include anything which money is spent on.

MR. ARMSTRONG: I wish I could enlighten you on that. I don't know just how. If you could give me an example it would help.

STUDENT: I will bow out.

MR. ARMSTRONG: All right. Let me elaborate on this just for a minute, if you will, from the standpoint of the Comptroller of the Navy, from the standpoint of the Assistant Secretary for Financial Management, with the implications of both of those offices. In Navy budgeting, CNO establishes the program objectives. The bureaus then develop the detailed programs to support these objectives. The programs are submitted to us with price tags attached by the Chief of each Bureau, and we then analyze them in our office to determine their financial validity.

You can't determine financial validity without looking at what the programs do in relation to the requirements, and this is one of the reasons why the constant interchange of information between the comptroller's office, the general planning group, and the bureaus--a 3-way street--is very valid. Now, let's take the shipbuilding program. We wouldn't think, in our office, of telling the Chief of Naval Operations that his mix in next year's shipbuilding program is wrong, that he has too many DDG's and too few SSN's. That isn't our business. But we might suggest to him, based on our experience daily before the Appropriations Committee, that it is harder to justify some particular procurement program than it is another. That's a little bit different from just plain comptrollership. It is very valuable to the CNO to have us aware of implications which are much broader than just money on programs.

I don't know whether it would be too rash on my part to do this, but I think I will. The attack carrier task force is the basic instrument of the United States defense force for limited war, for tense situations less than war, and for antisubmarine warfare and control of the seas. The attack carrier task forces also have missions and roles in connection with all-out war. They would make a contribution should such an event ever occur.

There are some highly responsible people in Congress who do not favor the expenditure of funds to build large Forrestal class aircraft carriers, among them the Chairman of the Committee on Appropriations of the House of Representatives, in the 85th Congress, who, last year,

made a speech on the floor of the House, which I, from the gallery, heard, in which he adverted most unfavorably to the attack aircraft carrier. This anticarrier point of view of a responsible Member of Congress presents a very serious problem to the Defense Department and the Navy, because, if the United States is going to maintain this capability out into the decade of the midsixties and beyond, obsolescence of our present attack carriers makes necessary the periodic building of additional attack carriers.

I mention this from the budgeting aspect because, if we put in the Navy budget in any year a carrier, there is a chunk of $300 million, which is a big piece of a shipbuilding program, and it presents very serious problems of judgment and evaluation as to whether it should be this year, or should have been last year, or should be next year, in relation to the other ships in the program--the cruiser conversions, the frigates, the guided missile frigates, the guided missile destroyers, the attack submarines, the Polaris submarines, the escort vessels, the mine sweepers, the AG's, the LPH's, and so on. Those are all budgeting questions as we in the Navy Comptroller's Office analyze the budget. They are also financial management and broad policy questions as we who participate in presenting the budget to the Congress advise the Secretary, the CNO, the Secretary of Defense, and higher authority as to the feasibility of obtaining the things that from the military standpoint are deemed necessary and from the financial standpoint are feasible.

QUESTION: Sir, in your survey of the accounting, and in trying to improve it, you indicated that you are asking a lot of people in field installations for advice. Have you turned to the GAO, which has Government responsibility, for any advice on how you should make the improvement?

MR. ARMSTRONG: No, sir. We may do that but we have not done it yet, because we felt that we should generate this as an executive department rather than as a congressional inquiry. Nor have we turned to the Department of Defense itself, because we felt that we had some peculiar Navy problems. The kind of thing that we run into we think perhaps in some respects is different from what other people may run into--the difficulty that a supply officer on an aircraft carrier has in complying with all the different accounting rules on shipboard involving millions of dollars and hundreds of thousands of items that he carries. Are the regulations so complex that he simply can't follow them? It is that type of thing. It's a rather unique problem, I think.

One supply officer on an attack carrier told me that if he followed the accounting rules he would be working 26 hours a day and is now working 16. Well, there's always a little room for exaggeration, and one admires hard work. But he has a problem, and we are trying to find out what it is.

We think we can do that first ourselves before we bring DOD or GAO into it.

COLONEL LACKAS: Mr. Armstrong, I see our time has lapsed. While I realize that there are many questions still in the audience, I feel, knowing that you have to leave, that we should terminate now.

Before that, I would like to say that we certainly appreciate your coming down here and providing us with this clear statement of the problem of financial management in the Navy. We also appreciate your frank and understanding answers to our questions.

Thank you very much.

MR. ARMSTRONG: Thank you.

(8 Jan 1959--4,225) O/mas:bbn