Exhibit 2

COMPOSITION OF TOTAL INVENTORY CARRYING COSTS AS A PERCENT OF INVENTORY VALUE

Carrying Cost Item	Percent of Inventory Value		
	Alford & Bangs Production Handbook	Remington Rand Inventory Control for Wholesalers	NAW Profit Planning Seminar 17 Participants
Obsolescence	10.00%	7.00%	4.00%
Interest on Capital Invested	6.00	5.00	7.00
Deterioration or Its Prevention	5.00	4.00	4.00
Handling and Distribution	2.50	2.00	3.00
Transportation	.50	.50	1.00
Taxes	.50	.50	.50
Insurance	.25	.25	.25
Storage Facilities	.25	.75	.25
TOTAL	25.00%	20.00%	20.00%

See source note: Page 9

COMPUTING INVENTORY CARRYING COSTS

This computation would be made by adding all the costs connected with the *"owning"* or *"holding"* of inventory for a given period of time and dividing the total of these costs by the dollar amount of the average value of the inventory held during this period. Since each of the costs of possession cannot be found directly in accounting records, it might be helpful to enumerate the various cost elements which comprise the typical wholesale-distributor's **TOTAL COST OF CARRYING INVENTORY.** These would include the following:

STORAGE SPACE COSTS
(Proportionate share of each)

1. Taxes on land and building
2. Insurance on building
3. Depreciation on building (if owned)
4. Depreciation on warehouse installations
5. Maintenance and repairs of building
6. Utility costs, including heat, light and water
7. Janitor, watchman and maintenance salaries
8. Rent (if paid)

HANDLING EQUIPMENT COSTS

9. Depreciation on equipment
10. Fuel for equipment
11. Maintenance and repair of equipment
12. Insurance and taxes on equipment

INVENTORY RISK COSTS

13. Insurance on inventory
14. Obsolescence of inventory
15. Physical deterioration of inventory
16. Pilferage
17. Losses resulting from inventory price declines

INVENTORY SERVICE COSTS

18. Taxes on inventory
19. Labor costs of handling and maintaining stocks
20. Clerical costs of keeping records
21. Employer contribution to social security for all "space," "handling" and inventory "service" personnel
22. Unemployment compensation insurance for all "space," "handling" and inventory "service" personnel
23. Employer contributions to pension plans, group life, health and accident insurance programs for all "space," "handling" and inventory "service" personnel
24. A proportionate share of general administrative overhead, including all taxes, social security, pension and employer contributions to insurance programs for administrative personnel

CAPITAL COSTS

25. Interest on money invested in inventory
26. Interest on money invested in inventory handling and control equipment
27. Interest on money invested in land and building to store inventory (if owned)

The above costs are **REAL.** It may take some time to calculate them for your firm **BUT, can you afford NOT to know what YOUR INVENTORY CARRYING COSTS ARE?**

ANALYZING INVENTORY CARRYING COST ELEMENTS

While the total costs of carrying inventory are found by adding up the cost elements in the above list, some of these elements may not vary with the amount of inventory carried. That is, some costs will remain relatively "fixed" in the short run, regardless of variations in levels of inventory stock. To the extent that storage space is available and cannot be used for other productive purposes, for example, the costs related to the space occupied will not fluctuate much with changes in inventory levels. If any inventory space is rented *(item 8)*; or, if the space could be used for other profitable purposes; or, if additional storage facilities are needed, then space costs *(items 1 through 8)*, may be directly affected by the amount of inventory on hand.

Depreciation on (handling) equipment *(item 9)* continues whether the equipment is used or not. But the amount of the expense may depend on the magnitude of inventory held. Items 10 through 24 differ from one firm to another, but for the most part, these costs vary with the quantity of inventory on hand. It should also be noted that an increase in inventory on hand may cause a proportionally **greater increase** in some of these costs due to duplication of handling as a result of **inefficient placement** and **crowding.**

Some wholesale-distributors might make the mistake of thinking that cash tied up in inventories *(item 25)* **costs nothing,** especially if the funds used to finance the inventory are generated internally, through retained earnings or depreciation. The inference is that if cash were not invested in inventory, it would sit idle and earn nothing for the company. But, in any well-run business, **surplus cash should be invested** in other income-producing assets.

The rate of interest expense or cost on a dollar of cash invested in inventory depends on the financial policy of the particular wholesale-distributor firm. It may be based upon the rate that the company is currently paying for external sources of funds, such as bank loans or mortgage loans. In some cases, however, the rate a company would have to pay for additional money to acquire inventory may be different from what it currently is paying for capital for other purposes. In these instances, the rate of interest costs on cash invested in inventory should be based on the cost the firm would **have to pay for more money.** Inventory not only comprises a large part of the total assets of the average wholesale-distributor firm but it is also the least liquid of the current assets. In general, to compensate for the risks involved, it is reasonable to assume that a wholesale-distributor firm's interest rate or cost assigned to money invested in inventory normally should be slightly higher than its usual interest costs. This may explain why the concensus opinion of the wholesale-distributors in Exhibit #2, third column, was 7%.

The most dangerous thing about inventory carrying costs in wholesale-distribution is that **these costs are never itemized** on a profit and loss statement. They are too seldom calculated and watched. Thus, their effect on profits, although often great and direct, is seldom realized.

INVENTORY TURNOVER AND CARRYING COSTS

The potential magnitude of the costs of carrying inventory in a wholesale-distributor firm provides management with a strong incentive to improve inventory turnover by reducing *"stock"* in relation to sales. Indeed, one of the most important **benefits** of a relatively **high inventory turnover rate** is that **expense items** that have to do with owning a stock of goods **are decreased.**

This may be made clearer perhaps, by examination of the purely hypothetical example in Figure #1, which is designed merely to illustrate the effect of turnover on inventory carying costs and not to suggest what the turnover rate of any wholesale-distributor firm is, or should be. As illustrated here, if only one turnover is secured on an annual sale of goods costing $1,000,000, the total cost of carrying inventory amounts to $200,000 per year (using the earlier-determined 20% carrying cost). When the turnover rate is increased to two turns a year, an annual savings of $100,000 is effected in carrying costs as only 50% as much inventory must be carried. Each successive increase in the turnover rate further reduces these costs when the carrying-cost rate is assumed to remain static.

BALANCING ACQUISITION COSTS WITH CARRYING COSTS

While a high rate of stock turnover decreases the expenses that are directly associated with owning or carrying inventory, a **too high turnover rate** often has an **adverse effect** upon the cost **of acquiring stock.** When skeleton stocks are carried and small quantities are ordered more frequently, more expense and time is spent in performing the buying function. Thus, a very slow turnover tends to increase the carrying cost and a very rapid turnover increases the acquisition cost. This is clearly illustrated by the hypothetical example in

Figure #2, where the relationship between the cost of carrying, or possession, and the cost of acquisition at various turnover rates is indicated.

It is evident that as the rate of stock turnover is increased, total costs decline and profits increase—**BUT ONLY TO A CERTAIN POINT.** Eventually, a point will be reached at which the lower possession costs that are associated with the rapid turnover rates will be **MORE THAN OFFSET** by the higher acquisition costs attributable to stocks that are unduly low in relation to sales volume.

The most profitable turnover rate is the one that produces the **lowest overall cost.** It is obtained when the **cost of possession** and the **cost of acquisition** are **reasonably balanced to maximize profits.**

To maximize profits, then, wholesale-distributors must carefully establish inventory management policies that take into account both inventory acquisition costs and inventory possession or carrying costs. Such cost analysis, to truly maximize profits, should be made by product lines as well as for the total inventory stock. Wholesale-distributors should carry only such slow-moving, *"slow-turn"* inventory as is **necessary to meet the firm's customer service policies.**

Figure 1

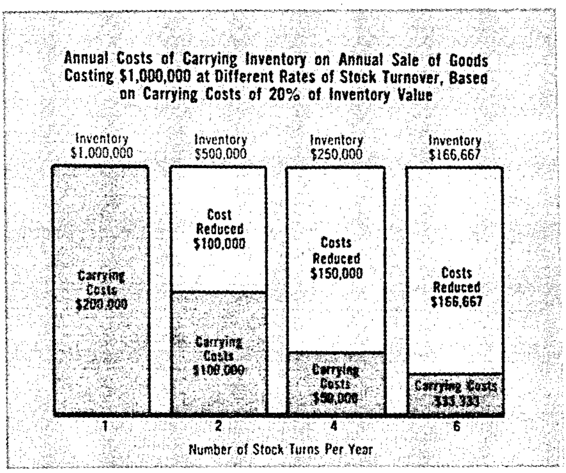
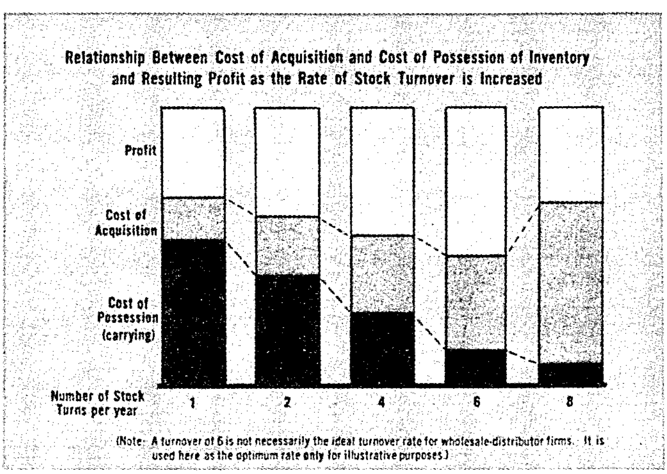


Figure 2



INVENTORY CLASSIFICATION FOR WHOLESALE-DISTRIBUTORS

Many wholesale-distributor firms obtain up to 75 to 80 percent of their gross sales from as little as 15 to 20 percent of the number of inventory items or lines in stock. Value analysis of your inventory by item and by product line, with classification of items and lines by "A", fast-moving, high volume items and lines; "B", slow-moving, lower-volume items and lines; and, "C", very slow-moving (should they be carried?) very low-volume items and lines, is a very necessary first step toward good inventory management for maximum profit.

The "A" class items must be carefully controlled, so that they are **seldom, if ever, "out of stock."** These items are excellent candidates for perpetual inventory.* They may number only 15 to 20 percent of the items or lines and may very possibly account for up to 75 to 80 percent of total gross sales. The rate of turnover on this class of stock is so high that **carrying costs are usually minimized.**

The "B" class items need less careful control from the standpoint of *"out of stock"* sales losses. This class of item may even be excluded from the perpetual inventory system, if one is used. They may comprise between 25 and 35 percent of the number of items in stock and only account for between 10 and 15 percent of total gross sales. In this class of slower-moving stock items, turnover is lower and **carrying costs begin to increase**—thus bear watching.

The "C" items and lines, often 50 percent or more of the number of items in stock, need **NOT** be watched closely for *"out-of-stock"* reasons and very probably should **NOT** be in the perpetual inventory system, if one is used. They probably represent only 5 to 10 percent of total gross sales. These "C" items may often be adequately controlled as to reorder time by a *"tag system"* or *"bin-divider"* system. In this way, the higher carrying costs associated with Class "C" items will tend to be minimized. "C" items should be periodically checked for **possible elimination from inventory altogether** as customer service demands for them decrease.

Wholesale-distributors who concentrate their purchasing and control attention on the fastest-moving "A" items, and devise automatic *"minimum clerical work"* systems to adequately control slower-moving "B" and "C" items, periodically reviewing and eliminating stagnant *"stiff stock"* from inventory, will **increase sales, reduce inventory carrying costs, maximize profits and increase their return on invested capital**—a wholesale-distributor industry goal!

* It should be noted that mechanized inventory control systems (EDP) are usually designed to provide perpetual inventory on **all** items in stock. Even here, however, classification for report purposes may prove beneficial and worthwhile.

INVENTORY MANAGEMENT— KEY TO YOUR FUTURE

YOU are a *"distribution specialist"*— there is no other economic justification for your continued existence.

Marketing analysts and writers for business magazines and trade journals predict that in the near future wholesale-distributors will be confronted with dealing with larger and larger suppliers and customers, as manufacturers, retailers, business users and service establishments continue to increase in size and thus in economic power. To insure their continued use of wholesale-distribution channels, YOU, the *"distribution specialist,"* must attain optimum efficiency in the handling of inventory. This means you must increase the *"rapidity of flow of goods"* through your warehouse—maximizing inventory turnover rates and minimizing inventory carrying costs.

In the last analysis, the principal economic justification for the continued existence of the wholesale-distributor lies in his **ability to carry and move inventory** near the point of demand **at the least cost**—a lower net cost than others can carry it for themselves.

Therefore, **know YOUR cost of carrying inventory; know YOUR cost of acquisition;** and, above all, achieve that balance between those costs which will return the maximum profit to YOU!

Those wholesale-distributors who do so will have a better chance of being in business in the 1970's. WILL YOU?

Source: Exhibit 2

L. P. Alford and John R. Bangs (Editors), **Production Handbook** (New York: The Ronald Press Company, 1955); p. 397; Remington Rand, **Inventory Control for Wholesalers** (New York: Remington Rand), p. 2; and the National Association of Wholesalers, Washington, D. C.

NOTE: For further discussion, see Theodore N. Beckman, Nathanael H. Engle and Robert D. Buzzell, *Wholesaling* (New York: The Ronald Press Company 1959) pp. 371-372 and William R. Davidson and Paul L. Brown, *Retailing Management* (New York: The Ronald Press Company, 1960), pp. 272-274.

PROGRESS IN ITEM REDUCTION

Representative CURTIS. I want to thank you for opening up this area again as forcefully as you have. This committee has considered this over a period of time, and it is really restating a truth, somewhat like Mr. Gainsbrugh said in his suggestions, that once the Bureau of the Budget establishes certain criteria, it then becomes a question of how do you enforce it.

These principles that you have enunciated here have been established, but believe me I am beginning to wonder how you ever bring about enforcement. It would look like there is some improvement just on the bare figures that we have seen here of the reduction of 5 million items as set forth in that study of 1953, to where, if it is accurate, we have 3.9 million today.

Mr. MARSHALL. That is good.

Representative CURTIS. Particularly since during this period, too, we have undoubtedly increased the number of end items that we use. So maybe there is some progress, but hardly enough progress, and this is what I guess you are really saying.

Mr. MARSHALL. Yes, sir.

Representative CURTIS. Let me restate again in my own words what I think you are saying. I think the important thing here, and it ties in with what Mr. Gainsbrugh was pointing out, is that there is no sense in our duplicating the great distribution system that exists in our society with a military distribution system.

Mr. MARSHALL. Right alongside.

DUPLICATION IN DISTRIBUTION SYSTEMS

Representative CURTIS. I mean there are reasons for setting up a military distribution system where the civilian distribution system cannot function, and these are the areas that we have mentioned here. But so much of what the military uses, whether it is human skills or something else, there has been no coordination, no study, when so much of this has its counterpart in the private sector.

I argued that you may think you are saving by buying, say, 1 million hammers at $1 at the factory, instead of buying it at $2.50 in the retail outlet, but if you ever took into effect the cost of warehousing and distribution, then you would realize that you are probably, under that system, paying $5 a hammer. This is another aspect of what you are saying here, as I see it.

I want to put on the record again what the then General Eisenhower told the Bonner subcommittee when we visited him in Paris before he became President. We were looking into, among other things, the fact that the Air Force was setting up its own supply system for common-use items instead of relying on the Army, which they were supposed to do over in the United States. They said they weren't going to duplicate, but when we got over into Europe, we found that they were. General Eisenhower said:

> You know that "responsiveness to command" is the shibboleth that is constantly used by military leaders to avoid these kind of efficiencies.

I only say that, Mr. Chairman, because this is what the military has given us for years. Whenever we try to dig into these things, they say, "Well, when we have to have things, we have to have them." Of course, that is true. But, having said that and agreed to them, then let's get down to the details.

I recall well this was the time right after the Berlin airlift, and a colonel of the Air Force was testifying as to why it was necessary for the Air Force to set up this supply system. He said:

"As a matter of fact, do you know that if we had to rely on the Army to give us handtools to repair aircraft, we would have just been in the soup."

I said, "Well, what happened? I thought the airlift was a great success. Where did you get these handtools?"

He said, "Why, we had to go in and buy them in the hardware stores in Germany."

I said, "You did, didn't you?"

He said, "Yes, we had to buy them there."

So what is wrong? Really, it is so true. Sure, we have to give the military a priority, possibly on some of these things.

Mr. MARSHALL. Yes.

Representative CURTIS. If, for instance, wrenches or something became in short supply for some unanticipated reason. We did this all the time. We did in the textile industry where we gave priority under our laws to the military procurement of certain textile products that we needed for the immediate war in Vietnam.

Well, I am really just underscoring what your testimony gives to us. I hope that we, our subcommittee, will look into this from the standpoint of a progress report. Evidently some movement has gone forward here, if these broad figures are reasonable, from 5 million to 3 million. I think we need to constantly watch it. I am satisfied we have gone nowhere near as far as we can in this area.

Mr. MARSHALL. Well, it might be a little better than you think, sir. I misspoke. This is 1963 instead of 1953. I said 1953 at first, but it is 1963.

Representative CURTIS. 1963?

Mr. MARSHALL. Yes, sir.

Representative CURTIS. That is much better.

Mr. MARSHALL. So that we have made a 1 million and some decrease in some 2 or 3 years.

Representative CURTIS. We have on that.

Mr. MARSHALL. Yes.

Representative CURTIS. On the other hand, I am going to say again for the record, because I am still in a state of shock from that testimony yesterday from the Defense Department, why it wasn't worth the paper it was written on. I have been relying in the past—I do not intend to get you involved in this—in testing whether or not we were making progress, of how much we were getting into competitive bidding, only to find out, for the indications are very strong, that they have been playing with the definition of "competitive bidding." So that I now can't rely on it. So I don't know whether I can rely on these figures.

NEED TO LOOK BENEATH DEFINITIONS

I am very serious. I am just shocked at this kind of thing. If the Defense Department thinks that as far as I am concerned they can play around with figures in this fashion and nomenclature, they have got another think coming.

On the other hand, I should hold my temper a bit and give them an opportunity to reply to the reports that we have before us from the General Accounting Office. I know they have had these reports, and what is in them sufficiently ahead of time, so that they could have responded a lot better than they did yesterday.

But I think we must look beneath these definitions, when they say they have reduced them from 5 million to 3.9 million, I regret to say I have to see their working papers now.

Mr. MARSHALL. Yes, sir.

Representative CURTIS. Thank you very much.

Chairman PROXMIRE. Thank you, and I hesitate to stop now, but we are past the zero hour. At 12:15 we were supposed to be out of here because another group is coming in at 12:30.

I would just like to say before we conclude I have had a chance to look at Mr. Gainsbrugh's splendid statement, and I am most impressed by it. I am very disappointed I was not here when you delivered it, Mr. Gainsbrugh, and I understand you may have a suggestion that we might possibly through legislation provide for a commission to make this kind of a study, and I would be extremely interested, and I am sure Congressman Curtis would, too, and we would like to have you give us a memorandum on this so we can work on it.

The committee will reconvene Tuesday, May 16, in room S-407, the Capitol, to hear Lawson Knott of the GSA, and Director Charles Schultze of the Bureau of the Budget.

(Thereupon, at 12:20 p.m., the subcommittee adjourned, to reconvene Tuesday, May 16, 1967, at 10 a.m.)

ECONOMY IN GOVERNMENT

TUESDAY, MAY 16, 1967

CONGRESS OF THE UNITED STATES,
SUBCOMMITTEE ON ECONOMY IN GOVERNMENT,
Washington, D.C.

The subcommittee met, pursuant to recess, at 10:03 a.m., in room S407, the Capitol, Hon. William Proxmire (chairman of the subcommittee) presiding.

Present: Senators Proxmire and Percy; and Representatives Griffiths and Moorhead.

Also present: John R. Stark, executive director, and Ray Ward, economic consultant.

Chairman PROXMIRE. The subcommittee will be in order.

We are pleased to have with us this morning the junior Senator from Montana, the Honorable Lee Metcalf, who has a short statement he wishes to make on economy in Government. I have read your statement, Senator, and note your concern over noncompetitive procurement of drugs and the possible overuse of the Buy American Act, and your concern that the GSA may not be doing all it should under its authority in appearing before Federal and State regulatory bodies, representing the Government as a user of utilities to obtain fair and reasonable rates. Your work on "Overcharge" makes you an expert in this area.

You perhaps are aware of the fact that the junior Senator from Wisconsin started hearings yesterday on the high cost of drugs, in the Senate Small Business Committee, and we will not, of course, duplicate that effort in any way. We have been concerned in our hearings of May 8, 9, and 10 about the general competitive bid procedure and today we will discuss with GSA and BOB witnesses the use of the Buy American Act which, of course, relates to competitive procurement.

Senator METCALF. I am going to have to depart shortly for hearings at the Agriculture Committee but I will come right back. I have my dairy import bill up today and I know you understand the importance of it.

Senator METCALF. That is of very great importance to both of us and if it is an executive markup I hope you will go over and protect our mutual interests.

STATEMENT OF HON. LEE METCALF, A U.S. SENATOR FROM THE STATE OF MONTANA

Senator METCALF. Each year the U.S. Government spends hundreds of millions of dollars on drugs and medicines. Procurement of drugs accounts for substantial expenditures by the Armed Forces. Veterans' Administration, the Public Health Service, and under medicare and State welfare programs.

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Unless the procurement of drugs is handled more efficiently and economically, the bills will be so high as to constitute a heavy burden upon the entire population.

The only way to insure that Government agencies will secure the best product at the best price is to foster free and open competition in procurement. Purchases by generic name is the only method by which such competition can be achieved.

For some years the Defense Supply Agency, which procures drugs for the Department of Defense, and the Veterans' Administration have been buying drugs on a generic basis by competitive bidding, when drugs involved were not limited by a patent or exclusive license to one firm. Inclusion of foreign bidders since 1959 for procurement of *tetracycline*, one of the broad-spectrum antibiotics, and other drugs has drastically reduced bids of both domestic and foreign suppliers.

For example, in December 1959, the Military Medical Supply Agency bought 57,600 units of *tetracycline* from an Italian firm at $8.15 net a unit. The lowest domestic price offer was $16.75, more than twice the cost. By June 1961, the low foreign bidder had come down to $4.77. Pfizer, the low domestic offerer, came down to $6.07. By May 1962, an Italian firm quoted a price of $2.82. Awards were made later in the year at even less. Consequently the Department of Defense saved more than $1¼ million on this one drug.

The Veterans' Administration had similar experience. Foreign drug prices represented 80 percent savings on *meprobamate*, better known as Miltown, the tranquilizer, and 73-percent savings on *tetracycline*.

Although the Veterans' Administration continues to procure many drugs abroad, I regret to say that the Department of Defense has curtailed its foreign drug purchases. I hope this subcommittee can restore competition and consequent benefits to the taxpayer in this field.

In 1966, State welfare programs accounted for $140 million in purchases, of which the Federal Government paid $81 million. The Comptroller General recommended to the Congress in February 1966, and again last month that a generic program to provide drugs to welfare patients would result in great savings to the taxpayers. A study in Pennsylvania last year showed that use of generic names would have reduced the welfare drug bill by more than one-half.

Mr. Chairman, for several years I have been going out to Walter Reed Hospital for treatment for a high blood pressure condition and I am given *reserpine* that is brought by Walter Reed Hospital at about 50 to 60 cents a thousand. Now I am told if that were purchased on the open market it would cost about $39 a thousand. Of course, while this is presently more in Senator Nelson's jurisdiction than in mine, I want to point out that we Senators, the President of the United States, and the high-ranking military officers are permitted to go out to Walter Reed and take advantage of this kind of a purchase, yet the average welfare recipient or the man who has to have medicare goes trotting down to the corner drugstore and pays 70 or 80 times as much for the same drug as I have here in my hand that I get prescribed for me by Walter Reed.

I want to touch on another point.

GSA RATE CASE ACTIVITIES

I am pleased that representatives of the General Services Administration are before your subcommittee today, Mr. Chairman, because my final suggestion has to do with that agency.

GSA is responsible for protection of the Government's interest in obtaining economical utility rates. Uncle Sam is the biggest consumer of utility services in the country, by far. The Federal Government's annual utility bill amounts to about $4 billion. That includes communications, electricity, gas, sewage, and steam.

GSA's Utilities Division and Rates and Tariffs Division have eight professional staff members who devote approximately one-third of their time to rate case matters. Some other officials in GSA occasionally lend a hand. The sum total of the Government's force is smaller than the battery of accountants, lawyers, consultants, engineers, professors, statisticians, and financial vice presidents which one utility will produce in a rate case.

I am not as disturbed about the corporal's guard, however, as I am about the Administrator's attitude, as expressed to me in a letter this month. I quote his final paragraph. I am going to ask that the whole letter be put in the record.

Chairman PROXMIRE. Without objection that will be done.

(The letter referred to follows:)

GENERAL SERVICES ADMINISTRATION,
Washington, D.C., May 1, 1967.

Hon. LEE METCALF,
U.S. Senate,
Washington, D.C.

DEAR SENATOR METCALF: Thank you for your request of April 12, 1967, for information with respect to our staff capability in the utility regulatory representation area.

We do not have a separate staff assigned exclusively to regulatory case work. Rather, we utilize for rate case work, those engineers, economists, accountants and other professional employees of our Transportation and Communications Service whose duties also include management of utility services and rate and service negotiation. Our Utilities Division and our Rates and Tariffs Division, for example, have eight professional staff members who devote approximately one third of their time to rate case matters. In our Engineering and Operations Divisions we also have professional staff members who, although generally occupied almost full time on planning, managerial and negotiation matters, are available when needed for rate case work and have participated in several cases in recent years. Six attorneys in our Office of General Counsel who also assist in the management and negotiation function, handle, with the assistance of the TCS staff, regulatory proceedings which we initiate or in which we intervene. When appropriate, we use our regional counsel located in the geographic area where the regulatory proceedings are being conducted to assist in our participation.

In addition, as we have previously advised you, we exercise selective judgment in determining those regulatory proceedings in which we take active part. While these selections, of course, are influenced to some extent by staff limitations, they are made primarily on the basis of the potential cost to the Government of the proposal which is the subject of the proceedings, precedent value, and the merit of the case itself. We also endeavor to avoid duplication of regulatory commission staff or other customer intervenors' effort. For example, where commissison staff witnesses and counsel capably handle a particular issue, we will support that effort on brief or argument and refrain from introducing separate testimony.

In addition to our staff we are authorized to utilize the services of personnel in other agencies, to delegate responsibility for handling a particular case to another agency where it is in the interest of the Government to do so, or handle cases jointly with other Government agencies.

In view of the fact that there have been few major utility rate cases in recent years due to the generally excellent financial status of the utility industry, we believe that the total staff available to us as outlined above is, at the present time at least, adequate to assure effective representation of the Government's interest.

We are most appreciative of your interest in this function and your continued support.

Sincerely yours,

LAWSON B. KNOTT, Jr.,
Administrator.

Senator METCALF (reading):

In view of the fact that there have been few major utility rate cases in recent years due to the generally excellent financial status of the utility industry, we believe that the total staff available to us as outlined above is, at the present time at least, adequate to assure effective representation of the Government's interest.

I have spent a good deal of time studying the overcharges of the electric industry, and I shall not burden the subcommittee with the details. If any member of the subcommittee is interested, the name of the book is "Overcharge," published by McKay and written by my assistant, Vic Reinemer and myself.

Chairman PROXMIRE. We do not usually allow commercials, but that is a very effective commercial.

Senator METCALF. However, the fact that there have been few rate cases in no way follows from the fact that the utility industry enjoys excellent, even marvelous, financial status. The reason for the lack of rate cases stems from the fact that agencies that are responsible are not pressing for rate cases and reductions.

The State agencies for the most part are responsible for rate regulation, but GSA could certainly help. Most of the State commissions are not equipped to regulate the giant electric utilities, along with their many other responsibilities. Chairman Lee White of the Federal Power Commission has just provided me, in response to my request, a tabulation of the average return on common equity of the class A and B electric utilities, from 1937 through 1965. In the late 1930's and early 1940's it was around 7 percent. In 1965, for the first time, it exceeded 12 percent.

With your permission, Mr. Chairman, I shall include the FPC tabulation at this point in my testimony.

(The tabulation referred to follows:)

Classes A and B electric utility companies return on combined common equity, 1937–65

[Dollar amounts in thousands]

Year	Common equity [1]	Earnings available for common equity [2]		Year	Common equity [1]	Earnings available for common equity [2]	
		Amount	Percent of common equity			Amount	Percent of common equity
1965	$19,302,943	$2,366,543	12.3	1950	$6,981,299	$710,823	10.2
1964	18,353,368	2,184,618	11.9	1949	6,360,225	653,775	10.3
1963	17,190,109	1,970,897	11.5	1948	5,766,490	558,511	9.7
1962	16,297,809	1,848,360	11.3	1947	5,324,778	546,486	10.3
1961	15,366,196	1,673,963	10.9	1946	5,107,458	532,465	10.4
1960	14,525,003	1,590,791	11.0	1945	4,927,102	422,392	8.6
1959	13,605,142	1,469,747	10.8	1944	5,269,922	390,062	7.4
1958	12,575,990	1,340,622	10.7	1943	5,361,879	377,211	7.0
1957	11,700,764	1,244,703	10.6	1942	5,430,266	361,561	6.7
1956	10,855,088	1,171,769	10.8	1941	5,539,074	399,573	7.2
1955	10,216,604	1,093,476	10.7	1940	5,507,824	424,236	7.7
1954	9,660,995	990,277	10.3	1939	5,354,381	410,937	7.7
1953	8,961,574	892,423	10.0	1938	5,295,649	364,533	6.9
1952	8,434,061	818,154	9.7	1937	5,323,183	383,479	7.2
1951	7,515,926	695,363	9.3				

[1] Proprietary capital less preferred stock, yearend.
[2] Net income less preferred dividends requirements.

Senator METCALF. Most electric utilities are now considered growth stock. Return to investors are caviar compared to the crumbs occasionally given to the ratepayers. The overcharge of some of the utilities in areas where the Government is a major customer borders on the fantastic.

In 1965 Houston Lighting & Power had a rate of return—not return on equity, but a rate of return—of 11.32 percent. Its revenues amounted to more than $48 million. If its rate of return had been 6 percent—and that would have permitted a return on equity above that, because of lower costs on debt service—the operating income would have been but $25.5 million. So the overcharge by this one utility amounted to more than $22 million. And some of the situations in Florida and other States, where Defense, NASA, and other branches of the Government have big loads, are almost as bad.

OPPORTUNITY FOR ECONOMY IN GOVERNMENT

There is a real opportunity for economy in Government through reduction of utility overcharges. I think we should counsel with the GSA Administrator on that, Mr. Chairman. If for some reason that agency can't do the job then I think the responsibilities should be transferred somewhere else, perhaps to a consumers counsel.

Thank you.

Chairman PROXMIRE. Thank you for your comments, and for an excellent job and a very provocative and thoughtful presentation.

We have been informed in the press in recent days, thanks to the excellent advice by my colleague, Senator Nelson, of the differences between the generic and the trade methods of selling drugs. But your example here is more startling, I think, than any I have seen in the papers. I notice in the New York Times this morning there was a difference of 4,000 percent, 40 times. Yours is greater than that.

Senator METCALF. Yes, it is.

Chairman PROXMIRE. Apparently this is common.

Senator METCALF. Take reserpine and Serpesil, the same thing—Serpesil is the trade name and reserpine is the generic and is a very common drug for people who have hypertension and high blood pressure conditions.

Chairman PROXMIRE. Is it not true that this cuts across all committee jurisdictions? As I recall Senator Kefauver led a fight on this and at that time it was in the Judiciary Committee. Now I understand the Labor and Public Welfare Committee might possibly take jurisdiction or Senator Long might introduce an amendment to a social security bill which would require the procurement of drugs for medicare by generic name, and the argument I have heard is that it can save $50 million a year or more to the fund by using the generic system.

Senator METCALF. As I pointed out and as other witnesses have pointed out, the Veterans' Administration sometimes purchases these drugs abroad. There are terrific savings. It affects the health of almost every citizen and it comes across the jurisdiction of every single committee in the Congress.

ELECTRIC UTILITY RETURNS

Chairman PROXMIRE. Frankly, I am most startled by your presentation here showing in your table on electric utility companies, showing the enormous increase in return. It was my understanding that the State which allowed the largest return in recent years at least, was Ohio. I think as a matter of policy they allowed something like 9 percent. Most States permit 6 and 7 percent. We of Wisconsin have been very proud of our public service commission. We have always had distinguished and able members on it.

I am shocked, if I do not misunderstand you, that the average return of class A and B utilities throughout the country was a return of 12.3 percent for common equity in 1965.

Senator METCALF. That is correct.

Chairman PROXMIRE. Am I misunderstanding this?

Senator METCALF. No. That figure is correct. I want to concur that Wisconsin has one of the finest, most efficient operating public service commissions, or whatever you call them—a regulatory commission—in the United States.

California has also a fine one, until the other day when Governor Reagan came out and failed to reappoint a couple of men who had refused a rate increase to one of the large utilities down there and I feel that California's commission now will not measure up to the fine standard of your own Wisconsin commission.

STATE COMMISSION UNDERSTAFFED

But most commissions in the country do not have the personnel, the counsel, accountants, that can wrestle with even a small power company. In this matter, the statement of the General Services Administration that rates have gone along about the same is a statement that begs the question. As the chairman knows, we have had tremendous improvements in the development of power in both thermal and hydroelectric power, and in nuclear power. We are learning to transmit it over direct-current lines, high-tension lines. We are learning to produce it at much less cost.

Chairman PROXMIRE. It is also true that volume has increased enormously.

Senator METCALF. Tremendously.

Chairman PROXMIRE. As long as your fixed costs, your overhead remains fairly stable this enables you to get a far greater return, especially with the leverage factor when you borrow.

COSTS HAVE DECREASED

Senator METCALF. But the overhead has gone down and the fixed costs have gone down. And the efficiency of the modern plants has increased. The cost of producing a kilowatt of power has constantly decreased in modern times and yet the rate charged the consumer has remained about the same. And so when the General Services Administration comes in and says, "Well, the rate is about the same as it was before," or when you read the newspaper that inflation has hit new heights, everything else, but power rates have remained the same, they are begging the question because their costs have gone down to about half. And their returns have doubled.

GSA NOT A JUDICIAL BODY

Chairman Proxmire. The staff tells me that GSA represents the Government as a user and not as a judicial body.

Senator Metcalf. Well, that is correct. But the GSA is a user of about $4 billion worth of utility services and should have some people out here representing the Government in these various rate cases and helping these commissions prepare the rate cases. The commissions, responsible for regulation of utilities, gas companies, trucks and business licenses, and many other things, have not either the facilities to prepare a case nor the ability to present it.

Chairman Proxmire. Is there any precedent for that?

Senator Metcalf. Yes, the General Services Administration has gone in at times and presented experts and helped to prepare cases, but they not only have not nearly enough people involved in this, but they seem not to care at all about presenting the case of a user, even if there is a rate case.

SAVINGS ON SAGE

Chairman Proxmire. Is it not true that the GSA did save $100 million in one case—the SAGE?

Senator Metcalf. Just think of the savings that are possible in these huge consumptions of power for our Minuteman missile programs, and a facility out here that we are going to build in Chicago where we are going to use millions of kilowatts of electricity, the accelerator. The biggest consumer of power in America should be interested in rates.

Chairman Proxmire. I see that I have to run, although I will be back as soon as I can. I am going to ask Congresswoman Griffiths to take over the chair.

Representative Griffiths (presiding). Thank you.

Senator Metcalf. I am very grateful to the Chair for waiting and listening and interrogating me on this.

Chairman Proxmire. It is most informative to this subcommittee.

Representative Griffiths. I read your statement last night, Senator. That is why I am here. You did an excellent job. I am very impressed, and I hope the GSA is here.

$4 BILLION UTILITY BILL

Senator Metcalf. I hope the committee will direct some inquiries as to what can be done by the GSA because as the consumer of $4 billion worth of utility services, where it may be 25 or 30 percent of overcharge at least means that there alone can be savings of over a billion dollars a year—not only to the Government but they will also be instrumental in making a saving to consumers of much more than that.

BALANCE OF PAYMENTS AND LACK OF BIDDING ON DRUGS

Representative Griffiths. I wonder if the lack of bidding on the drugs, however, by the Defense Department was because of the balance-of-payments problem. I assume that must be it.

Senator METCALF. That certainly could be influential and have an effect upon some of the decisions that were made. As we both know—you as a member of the Ways and Means Committee and I as a member of the Finance Committee—there seems to be an undue concern about balance of payments among some people down at the Treasury at the cost of many of the programs in which we are both interested.

Representative GRIFFITHS. Congressman Moorhead, would you care to ask any questions?

Representative MOORHEAD. Yes, thank you, Madam Chairman.

First, let me commend you, Senator, on an excellent statement. This prompts me to remark how much we miss you on our side of the Capitol.

Senator METCALF. I feel that I come home when I come home to your side.

SAVINGS POTENTIAL IN PROCUREMENT OF DRUGS AND UTILITIES

Representative MOORHEAD. As I understand your proposal, it is that Government agencies as consumers, large consumers, particularly in the field of drugs and public utilities can, by a change of policies, save the people of America first as taxpayers and second as consumers large sums of money. This is the essence of it?

EXPERTS NEEDED TO HELP CONSUMERS

Senator METCALF. Tremendous sums of money. By virtue of the very fact that they are the largest consumers in these areas there should be some trained people to assist consumer organizations who have not had the opportunity to get the benefit of this kind of advice. Where do you learn to be a counsel or a statistician for a utility company? You cannot learn it at any college. You have to learn it just by trial and error or working for a utility. And you go into a rate case, even in a State such as Montana where we have a relatively small but very important and influential power company, the Montana Power Co., and you have a battery of lawyers and a battery of accountants, and a battery of statisticians and all sorts of experts and a couple of people representing the Montana Public Service Commission who spend most of their time checking truck licenses or going out and looking and seeing whether the oil wells are capped, and know nothing about that. The very few times that we have been successful in rate cases have been the times when GSA sent a rate expert out there to testify to a fair rate that was needed. And they met some of the issues presented by the vast battery of accountants, statisticians, engineers, vice presidents and public relations people and politicians and all present on one side of the case, with a couple of truck inspectors on the other.

Representative MOORHEAD. And few customers have enough at stake to get into this, but the Federal Government does.

Senator METCALF. The only other customer in Montana who has enough at stake is the Anaconda Co., which is a user of a considerable amount of electricity. You have to have a consumer's organization and they have to hire a lawyer who has experience in the presentation of that. It is our responsibility, it would seem to me, as the biggest consumer in America, to protect our taxpayers' interests as well as to protect the consumers' interests.

Representative MOORHEAD. Thank you, Senator. Thank you, Mrs. Griffiths.

Representative GRIFFITHS. Thank you very much. Senator Metcalf, I, too, am very pleased to have had an opportunity to see you again on our side.

Senator METCALF. I am delighted to appear before two of my former colleagues.

Representative GRIFFITHS. Thank you. We are pleased to have with us this morning Mr. Lawson B. Knott, Administrator of General Services.

Mr. Knott has had a long and varied background in the Federal Government and as a career employee has reached the top rung in a large and very important independent agency of the Government.

Chairman Proxmire's letter of April 26, 1967, to you outlined the subjects we desired you to cover today. Since these subjects are of a continuing nature and broad in scope, we have asked that you give us a 10-minute summary of the testimony which will be placed in full in the hearings. Chairman Proxmire's letter will be included in the record at this point.

(Letter referred to follows:)

APRIL 26, 1967.

Mr. LAWSON B. KNOTT, Jr.,
Administrator,
General Services Administration,
Washington, D.C.

DEAR MR. KNOTT: This letter confirms conversations between you and your staff and the Staff Director of the Subcommitee on Economy in Government of the Joint Economic Committee concerning the Subcommittee's schedule hearings on May 8, 9, 10, and 16. You and your staff are to testify at 10 a.m., May 16 (room to be announced later).

In general, we will pursue the topics previously under review by the Subcommittee on Procurement and Regulation with emphasis on accomplishment in attaining economy and efficiency during the past year. We are particularly interested in the national programs in the supply and services areas.

The specific recommendations of the May 1966 report affecting GSA should, of course, be covered in your testimony.

We have been receiving numerous inquiries about inconsistencies in application of differentials under the Buy American Act when contracts are awarded by the Department of Defense and the General Services Administration. While we have discussed this topic before, it would seem that no corrective action has been taken to date and we want full information from you as to the volume, trends and operating problems encountered. Your recommendations will also be welcomed.

Please give us complete information about the program in being or planned for the better management of short shelf life items including the medical stockpile items. Full statistics on inventory losses disclosed in the management of medical stocks, paint, handtools, and other items will be helpful.

Your statement should cover plans or programs for screening the Government's real property holdings under the revised Budget Bureau instructions in Circular A-2.

Will you also send one of the medical laboratory Chests recently declared surplus by the Public Health Service to Room G-133, NSOB before May 8.

Please forward 100 copies of prepared statements to Room G-133, NSOB at least one day before your appearance and refer any questions you may have for information to Mr. Ray Ward, Staff Director of the Subcommittee, phone 173/8169.

Sincerely,

WILLIAM PROXMIRE,
Chairman.

STATEMENT OF HON. LAWSON B. KNOTT, JR., ADMINISTRATOR, GENERAL SERVICES ADMINISTRATION; ACCOMPANIED BY H. A. ABERSFELLER, COMMISSIONER, FEDERAL SUPPLY SERVICE; AND JOHN G. HARLAN, JR., COMMISSIONER, DEFENSE MATERIALS SERVICE

Mr. KNOTT. Thank you, Madam Chairman.

I brought to the table with me Mr. John Harlan, who is the Commissioner of our Defense Materials Service and Commissioner Abersfeller, who is the Commissioner of our Federal Supply Service. These are the two areas that seem more importantly involved in the subcommittee's areas of interest.

Representative GRIFFITHS. Since your statement is quite short, would you please read it? I think that probably would be best. I personally discovered that it takes longer to summarize these things.

Mr. KNOTT. I appreciate the opportunity to appear today before your Subcommittee on Economy in Government, to discuss the programs and activities of the General Services Administration concerned with procurement, supply, and property management for the Federal Government and to tell you about some of the things we have done, as well as other actions we plan to take to reduce the costs and improve the efficiency of these operations.

ANNUAL REVIEW BY COMMITTEE

Before discussing these programs, I wish to reiterate the statement I made during my testimony at the hearing in March 1966, to the effect that the stimulus provided by the annual review of the Joint Economic Committee of the Congress of GSA's role in the field of Federal procurement, supply, and property management had led to many improvements.

GAO REPORTS

Also, during the past year the General Accounting Office has examined several GSA operations. In each instance, the approach was fair and reasonable and we were afforded an opportunity to comment upon proposed findings and recommendations prior to publication of the final GAO report. Although we do not always agree with the GAO findings and recommendations, we do agree with the majority of them and our views and statements of corrective action taken are included in GAO's final report to Congress. The GAO recommendations are constructive and helpful to our management of the affairs of GSA and the GAO examinations supplement our own self-evaluation capabilities which we are taking steps to strengthen.

In my testimony today I will, as requested, give an account of the actions taken concerning the recommendations contained in the May 1966 report of your predecessor Subcommittee on Federal Procurement and Regulation which involve GSA and I will discuss, also, other matters mentioned in your letter to me of April 26, 1967.

Mr. Chairman, we work continuously toward elimination of avoidable duplication and overlap between the supply systems within the executive branch. We believe this the key to the further success in this area.

NATIONAL SUPPLY SYSTEM

Accomplishments toward integrating into the national supply system the wholesale supply systems maintained by other civilian agencies during the past year may be summarized as follows:

GSA has assumed direct wholesale level supply support for common use items of larger postal installations. This is some 220 items involving $4.2 million annually and this involves 2,000 first-class post offices who have revenues of over $200,000 a year.

Agreement has been reached with the Veterans' Administration for transfer to GSA of all common-use items in the VA wholesale supply system except for nonperishable subsistence, medical supplies, and certain clothing and textile items. This transfer will be completed by July 1, 1967. This involves about 1,200 items with an annual volume of $8.4 million.

DOD/GSA RELATIONSHIP

I am pleased to report that the cooperative relationships between the Department of Defense and GSA with respect to the national supply system have continued at a high level during the past year. At the hearing last year we reported that DSA/FSS Material Management Review Committee had completed review of 152 Federal supply classes managed by DSA. Since that time the following progress has been made:

Fifty-two classes consisting of about 17,000 items will be transferred to GSA on July 1, 1967, with one additional class, paper and paperboard, to be transferred later. The remaining 99 items stay with DSA.

Forty-seven additional classes designated for integrated management within DOD will shortly be scheduled for review.

The Department of Defense has agreed to assume Government-wide supply support for fuel and electronics and has agreed to assume supply support to selected agencies for certain common-use items of clothing and textiles, medical, and subsistence.

Concurrent with the extension of DSA perishable subsistence support to civilian agencies, a joint task group of military and civil hospital personnel has reviewed perishable subsistence requirements of military and civilian agency hospitals and agreed upon uniform specifications for more than 300 hospital feeding items. This standardization will significantly increase the range of items available from DSA for use by both military and civilian hospitals.

CROSS-UTILIZATION OF LONG SUPPLY

A formal agreement which will provide for cross-utilization of long-supply items stocked in both GSA and DOD systems is in final stages of coordination. Meanwhile, GSA and DSA have established interim arrangements to interchange information on dual stocked items in long supply. We have effected cross-servicing on nine items so far.

A GSA regulation (FPMR No. E-3) was issued on September 28, 1966, establishing a policy for utilization of long-supply items by civilian agencies. We are working with the agencies to develop detailed procedures assuring implementation of the policy.

SHORT SHELF LIFE ITEMS

Together with DOD we are developing a standard system for the identification of material inherently subject to accelerated deterioration—commonly called short shelf life items—and prescribing the frequency of inspection to determine the remaining useful life of the items. I believe Senator Douglas last year called them perishable items.

Shelf life item codes for all items in the GSA stores stock program were updated in May 1966, and a GSA regulation requiring other civilian executive agencies to use this coding system to manage short shelf life items will be fully implemented by the end of fiscal year 1968.

PLAN TO USE MEDICAL STOCKPILE

With respect to the specific problem of short shelf life items in the civil defense medical stockpile, an interagency committee composed of representatives of GSA, DOD, PHS, and VA, has developed a plan to assure utilization of stockpile materials prior to expiration of their shelf life. The plan under consideration contemplates continual rotation of short shelf life items through the use of medical stockpile materials to meet current Federal needs, and replenishment of the stockpile with newly acquired materials. This plan is in the process of final clearance within the agencies represented on the committee. Pending adoption, short shelf life medical items are being utilized under interim arrangements between DOD, VA, and PHS.

Under the present civil defense medical stockpile program, 750 items of material valued at about $176 million were in inventory as of February 1967, at 2,256 prepositioned hospitals (approximately $64 million); 11 manufacturers' sites (approximately $4 million); and 13 PHS/GSA emergency depots (approximately $108 million).

Retention of inventories at the 11 manufacturers' sites has been discontinued and the materials declared excess during April of this year are available for use by DSA and VA.

PHS has reported, with respect to the $176 million inventory, that materials valued at approximately $9 million were utilized by VA and DOD from July 1 to December 31, 1966; materials valued at $24.6 million were destroyed between June 1964, and April 1967, due to expiration of the shelf life or obsolescence; and 186 items valued at $42.5 million will be subject to rotation by December 1968. A word about the $24 million destroyed, $11.9 million of that amount was intravenous solutions, $3.3 million consisted of barbiturates and antibiotics accounted for another $3.2 million.

INTERAGENCY COMMITTEE

The interagency committee mentioned earlier also is working toward standardization of new items entering the stockpile programs so that, to the maximum extent possible, new procurements by PHS will utilize purchase descriptions based on military specifications so as to increase utilization by DOD, the largest user of medical items.

To reduce stockpile losses due to expiration of shelf life and obsolescence, the task force on emergency health preparedness, under the auspices of the Office of Emergency Planning, has developed a plan whereunder a 30-day inventory of certain medical items will be located at and rotated by community hospitals.

INVENTORY LOSSES

The problem of inventory losses is of special concern to GSA, and one to which we give special and continuing attention. Inventory losses from all causes for the period July 1, 1966, through March 31, 1967, amounted to less than 1 percent of the inventory, and we look for improvement in the year ahead.

Turning now to the matter of advertised versus negotiated procurements, in fiscal year 1966, procurement dollars expended by GSA totaled $724.7 million, excluding $64 million procured from mandatory Government sources.

83 PERCENT ADVERTISED BIDDING

Eighty-three percent or $602 million of the total, including total small business set-asides, was expended on a publicly advertised competitive bid basis.

Seventeen percent or $122.7 million of the total expended on a negotiated basis includes $25.3 million procured under multiple-award schedule contracts and $97.4 million in other negotiated procurements including:

Fifty-one million four hundred thousand dollars in purchases under $2,500.

SMALL BUSINESS

Forty-six million dollars in purchases partially set aside for small business and surplus labor areas, purchases under authority of AID not requiring or permitting advertising, and purchases under our own authority to negotiate where the public exigency would not permit of the delay incident to formal advertising.

While this $97.4 million in procurements by GSA are properly reportable as negotiated, I wish to emphasize to the subcommittee that the methods and procedures under which these procurements are made require the maximum publicity and competition consistent with the particular circumstances of each transaction.

FEDERAL SUPPLY SCHEDULES

In addition, GSA enters into Federal supply schedule contracts on both a negotiated and publicly advertised basis for use by all Government agencies. The contractors reported that orders received under these contracts during fiscal year 1966 totaled $1.02 billion, of which $200 million were under publicly advertised schedule contracts and $820 million were under negotiated multiple-award schedule contracts. It is interesting to note that that $820 million is made up this way, that $358 million is for ADP equipment and $80 million for office machines $111 million for automotive parts, $75 million for printing equipment and $58 million for photographic copying equipment and supplies.

BUY AMERICAN ACT: LACK OF UNIFORMITY BETWEEN DOD AND GSA
A PARADOX

The problems resulting from lack of uniformity between DOD and GSA in applying the differentials under the Buy America Act continue to present a paradox in Government procurement practices.

The trend of procurement of foreign tools such as wrenches, screwdrivers, precision measuring tools, twist drills, taps and dies, and portable power tools is on the increase.

During fiscal year 1966 contracts awarded for foreign tools totaled $1.9 million or 2.07 percent of the total of $91.6 million expended by GSA for tools. During the first 9 months of fiscal year 1967 awards for foreign tools amounted to 2.31 percent of the total tool expenditure. We have a number of pending procurements that involve foreign procurement and the dollar volume is on the increase.

BOB STUDYING PROBLEM

On the basis of our recommendations that uniform percentage differentials under the Buy American Act be applied by both DOD and GSA, the matter is under the active study by BOB.

Although we regard the prevailing inconsistency between DOD and GSA in applying the Buy American Act differentials as a major problem because of its impact on specific industries, it should be recognized that GSA procurements from foreign sources in fiscal year 1966 totaled $3.3 million or less than one-half of 1 percent of total GSA procurements during the year.

DATA PROCESSING PROGRAM

Summarizing our accomplishments in the Government-wide automatic data processing program, we have done the following:

Negotiated with equipment manufacturers improved Federal supply schedule contractual terms and prices.

Encouraged and/or arranged for the leasing of equipment from third party lessors on terms more favorable than available from the original equipment manufacturers. There is a saving here of about $450,000 annually so far.

Studied the management of Government-owned computer magnetic tape. Over 10 million reels are either in use or in storage representing an investment of $250 million. It now appears that specifications, testing, quality control, and storage of magnetic tape can be considerably improved.

Expanded and reemphasized the ADP sharing program which now consists of the operation of 18 sharing exchanges located in cities having major Government programs. GSA doesn't operate all of these. We delegate this responsibility to the predominant, interest agency. For example, in Huntsville, Ala., and Houston, Tex., the exchanges are operated by NASA; in Norfolk, by Navy, in Philadelphia, the VA. It depends on the predominant interest and availability of manpower, talent, human resources to operate the program.

Working with the Bureau of the Budget, developed a system of reporting current ADP data, including age, condition, configurations, utilization, and future use plans.

Our goals for the future include:

Development, in coordination with the National Bureau of Standards, of measurement techniques relating equipment cost and capability which will enable agencies to purchase or lease the most economical and efficient equipment suitable to their needs.

Continued improvement of procurement practices emphasizing full implementation of the single purchaser concept.

Determination of the most efficient, effective and economical ADP maintenance system for Government use.

Reexamination of procedures for reutilization of excess ADP equipment and utilization of available machine time now unused to assure maximizing use of available assets.

Determination, well in advance of planned termination of use of equipment by one agency, whether there is need for its continued use by other Government agencies.

Working with the National Bureau of Standards, in the development of uniform programing languages, standards, machine applications, and a library of common use machine programs.

Development and acquisition of a system for storing archival and similar data on other than magnetic tape, thereby releasing for reuse several thousand reels of tape.

Our study of the management of magentic tape affords a basis to conclude that centralization of the function of cleaning tape for reuse could save several million dollars annually. We hope to be able to do something about this as soon as the revolving fund requested in GSA's fiscal year 1968 budget is available. I am pleased to report that the House committee has approved and included in our appropriations request this year the $10 million we asked for.

Determining the feasibility of establishing human resource pools such as key punch operators and programers.

UTILIZATION OF EXCESS PROPERTY

With respect to GSA's program to promote the utilization of all types of excess personal property, we strive continually to improve techniques for increasing such utilization throughout the Government in lieu of new procurement and we consistently stress to Federal agencies, in keeping with the President's cost reduction program, the cost avoidance benefits of using available excess property.

Excess personal property costing $95 million was transferred by GSA to other Federal agencies for further use in 1956. By 1965, 577,524 line items costing $677 million were so transferred. While the quantity of excess property available decreased significantly in 1966 due to the military buildup in Southeast Asia, the quantity of such property transferred for further Federal use remained high at 585,497 line items costing $617.1 million. A further reduction in available excess properties is being experienced in fiscal year 1967 with property costing only $1.5 billion becoming available during the first 8 months, $409.5 million of which has been reassigned for continued Federal use.

Excess property currently being generated continues to include increasingly larger proportions of property with limited potential for further Federal use, such as aircraft, electronic communications equipment, instruments and laboratory equipment, missile support equipment, and similar items related to weapons systems.

USE OF CONTRACTOR INVENTORY

Over the past several years we have made special efforts to increase the utilization of excess inventory in the hands of contractors. Last year we reported that the quantity of contractor inventories transferred for further Federal use increased annually from 1962 by $105.6 million to an annual level of $140.4 million in 1965. In 1966 the quantity so transferred declined to property costing $117.5 million due to the lower volume of property available for transfer. Contractor inventory costing $74.7 million has been transferred in the first 8 months of fiscal year 1967. Defense contractors are the largest source of excess contractor inventory and a large portion of further Federal utilization achieved is represented by transfers to other defense activities including defense contractors.

$429.2 MILLION DONATIONS TO SCHOOLS, ETC.

Surplus personal property costing $429.2 million was donated by GSA for educational, public health, civil defense, and public airport purposes in fiscal year 1966, an increase of $21.4 million over fiscal year 1965. During the first 8 months of fiscal year 1967, donations have fallen off sharply to $192.8 million, reflecting the overall drop in the volume available coupled with the high rate of excess property reuse by Federal agencies. During the last 5 years, surplus personal property costing more than $1.9 billion has been donated for public purposes, primarily for educational use.

SALES OF SURPLUS PROPERTY

Excess personal property which is not transferred for further Federal utilization or donated for public purposes, is sold as surplus. Usable property costing $17 million was sold by GSA in 1960 and the volume increased to $72 million in 1966, an all-time record. During the first 8 months of fiscal year 1967, property costing $34.3 million has been sold. The return on surplus personal property sales by GSA during the past 7 years has averaged 15.3 percent of original acquisition cost.

DISPOSAL OF EXCESS STOCKPILES

With regard to the disposal of excess strategic and critical materials in the Government stockpiles, I am pleased to report continuing substantial headway. Out of the 48 million tons of such materials now in inventory, more than 20 million tons are excess to emergency requirements determined by the Office of Emergency Planning. These substantial excesses represent a Federal investment of more than $3.3 billion and are costly to maintain. They also present a potential economic threat and market burden to producers and consumers who otherwise would be concerned only with the usual competitive forces of supply and demand.

In fiscal year 1966, our level of sales reached an unprecedented volume of $1.028 billion, approximating the cumulative sales of excess materials from the beginning of the disposal program in 1958. Thus far this year sales are approaching the half billion dollar level. Disposal of these basic raw materials at the foregoing levels has been accomplished without adversely impacting normal commercial markets.

The unparalleled expansion of our economy and resulting demand growth for industrial raw materials is providing an unprecedented opportunity to dispose of stockpile excesses at a time when normal supply sources for many of the materials are not able to keep pace with the demand. Availability of the excess stockpile materials in quantities commensurate with industrial needs exceeding normal supplies has had the incidental, but highly beneficial effect of stabilizing prices which otherwise would fluctuate widely during these periods of rapidly changing supply and demand conditions.

In addition to the benefits accruing to the private sector of the general economy from these substantial disposals of stockpile excesses, the direct benefits accruing to the Government include substantial recovery of its investment in unneeded inventories, reduction of storage, interest, and other costs associated with inventory maintenance, and improvement of the Government's balance of payments position.

The out movement of large quantities of stockpile materials through the disposal program has made possible substantial savings in recurring storage costs. To date, we have been able to deactivate five GSA storage facilities at an annual cost reduction in excess of $700,000, and to reduce our annual storage costs at military facilities by close to $150,000. Annual costs of storage at commercial facilities which amounted to $1.3 million in 1963 have been reduced to $345,000 for the current fiscal year.

MANAGEMENT AND SCREENING OF REAL PROPERTIES

In my testimony during the 1966 hearings of your Subcommittee on Federal Procurement and Regulation, I reported that we had been working closely with the Bureau of the Budget to increase reports of excess of real property holdings by the holding agencies to General Services Administration and to accelerate the disposal of surplus real property. The subcommitte's report of May 1966 points up the continuing need to screen the Government's real property holdings to determine whether they are being put to the highest and best use.

BUDGET CIRCULAR A–2, APRIL 5, 1967

As you know, the Bureau of the Budget issued, under date of April 5, 1967, Revised Circular A–2 on utilization, retention, and acquisition of Federal real property. This was not revised since 1956. This circular stresses the importance of systematic and thorough reviews of real property holdings to identify unneeded and uneconomically used properties. It also requires agencies to notify GSA and the Bureau of Land Management, as appropriate, of additional real property requirements before proceeding with acquisition. These are new requirements.

Additionally, Revised Circular A–2 requires that agencies annually report to GSA and the Bureau of the Budget the results of its real property reviews. These steps should give added impetus to the identification and reporting as excess of real property not required to meet program needs.

TRANSFERS OF EXCESS REAL PROPERTIES

Thirty-five excess real properties with an acquisition cost of $40 million were transferred to other Federal agencies during the first 6 months of this fiscal year for continued use, 10 more properties than were so transferred in the first half of fiscal year 1966. The increase is attributable in part to emphasizing the practice of disposing of excess real properties by exchange for privately owned properties needed to fulfill current Federal requirements, thus substantially reducing the amount of funds needed to be appropriated for new acquisitions.

SALE OF SURPLUS PROPERTY STRESSED

We stress disposal of surplus property by sale to (1) return its full cash value to the Treasury, (2) reduce maintenance costs, and (3) return property to the local tax rolls and to the civilian economy as a source of jobs and payrolls in local communities. During the first 5 months of fiscal year 1966 six properties were sold to user-buyers returning $14.6 million to the Treasury and providing job opportunities for 3,450 employees, bringing to the affected communities payrolls estimated to total $21.5 million annually. An excellent illustration of sales to user-buyers which accomplishes such objectives was the sale of the Connecticut Advanced Nuclear Engineering Laboratory at Middletown, Conn., to the United Aircraft Corp. for $14.6 million in August of 1966.

During fiscal year 1966 GSA sold a total of 365 surplus real properties valued at $125 million, an alltime record high. Cash receipts during the year from surplus real property totaled $79.3 million.

COST OF MIDDLETOWN, CONN., NUCLEAR LAB

Representative GRIFFITHS. Could you put at this point in the record the original cost of this nuclear engineering laboratory at Middletown, Conn.?

Mr. KNOTT. Yes.

(The information referred to follows:)

The initial cost to the Government for land, improvements and equipment of the Connecticut Advanced Nuclear Engineering Laboratory, Middletown, Connecticut, as reported to GSA by the owning agency, AEC, was $43,329,771.

REAL PROPERTY DISPOSALS OTHER THAN SALES

Mr. KNOTT. Although, as stated, we stress disposal of surplus real property by sale, we give due recognition to disposals for non-Federal public uses which qualify under existing law for conveyance at discounts up to 100 percent, with restrictions as to use. Such disposal during fiscal year 1966 includes:

135 properties for health and education uses.
26 properties for park and recreation uses.

15 properties for Federal highway uses.
11 properties for airport uses.
1 property for wildlife conservation uses.
1 property for historic monument.

During the first 6 months of fiscal year 1967, 94 surplus real properties have been conveyed for public uses.

A change in emphasis on surplus real property disposal from a preference for public use conveyances at price discounts to a preference for disposal by sale, with only residual properties being made available for conveyance at price discounts for public uses, could increase return of cash proceeds from sales by about $30 million annually.

LAND AND WATER CONSERVATION FUND ACT OF 1965

As you know, with the enactment of the Land and Water Conservation Fund Act of 1965 (78 Stat. 897) the net proceeds from the sale of surplus real property is covered into the fund and is available for appropriation for the purposes of the act, including the purchase of lands. On the other hand, public use conveyances at price discounts not only deprive the Treasury of the full value of the property but sometimes result in uses of property not wholly consistent with its highest and best use simply because it can be obtained without cost or at substantial discounts by the using public body. In addition, to the extent that surplus property is donated for use in federally assisted public health and education programs under recently enacted legislation, the amount of Federal assistance is significantly augmented by the value of the property so conveyed.

RECORDS MANAGEMENT

Among GSA's varied responsibilities is the improvement of current records management and paperwork practices in Federal agencies. Further, it is charged with selecting, preserving, and making available, both to the Government and to the public, the permanently valuable noncurrent records of the Federal Government and with expediting the disposal of unneeded records. In fiscal year 1966 GSA's total records centers program, by accessioning Agency records, cleared for reuse 331,000 square feet of office space and 89,000 square feet of storage space. To have leased an amount of space equivalent to that cleared would have cost the Government $1.1 million. These records transfers also emptied 65,300 filing cabinets, 5,700 transfer cases, and 398,500 linear feet of shelving. Federal agencies were thus enabled to avoid the purchase of new filing equipment valued at $3.7 million. The storage of records in GSA records centers rather than in agency space avoided additional expenditures of $6.2 million.

COST REDUCTION PROGRAM

Dealing specifically with the cost reduction program directed by President Johnson last September 16 calling for an intensified effort to reduce costs in the areas of procurement, supply, and property management, we have taken affirmative actions to effect savings and avoid costs in accordance with his directive.

For instance, a week after receiving the President's memorandum, I established an ad hoc committee of representatives of 13 agencies responsible for 96 percent of Federal civilian employment. This committee, represented at the Assistant Secretary level, approved specific policies and actions to cut Government costs. As a result of this combined effort, we have:

Saved or avoided costs of $176 million.

Eliminated several hundred items from supply systems.

Revised equipment use and replacement standards.

Conducted a "walk through" of Government buildings to identify and reassign unneeded supplies and thus avoid new procurement.

Initiated publication of a periodic flyer for the exchange among agencies of cost-cutting ideas.

RESTRICTIONS ON PURCHASES OF FILE CABINETS

Furthermore, GSA has continued to enforce Government-wide restrictions on the purchase of filing cabinets, office machines, and furniture. During fiscal year 1966 and the first 8 months of the current fiscal year, a total of 12,927 excess file cabinets were transferred for further Federal use, many of them after rehabilitation. Since January of 1965, when the restriction on the purchase of new file cabinets was imposed, the Government's purchase of filing cabinets has been reduced by 62 percent. Federal purchases during calendar years 1965 and 1966 totaled 34,467 and 46,383, respectively, in contrast to 106,678 purchased in calendar year 1964.

During 1966 and the first 8 months of fiscal year 1967, office furniture and office machines rehabilitated for further Federal use amounted to 826,720 units with a total acquisition cost of $93.5 million. The rehabilitation cost approximated $13.4 million, or about 14 percent of the cost of new procurement. Small businesses skilled in repairs, maintenance, and reconditioning benefited from the work while, at the same time, the Government avoided larger expenditures for new procurements. GSA is now providing repair and rehabilitation services for 37 different classes of property.

This completes my statement, Mr. Chairman. I have with me several members of my staff to assist in answering any questions you may have.

We think we have covered the points you asked us specifically about. We are prepared to discuss these.

UTILITY RATE CASES

Representative GRIFFITHS. Suppose you begin by answering Senator Metcalf's question. Where the Government has allowed you the power why does not the GSA participate in ratemaking cases?

Mr. KNOTT. If I may, I would like to point out that we furnished him with the $4 billion figure in early correspondence to which he did not specifically refer. He asked us for an estimate of the Government's total annual utility bill and we told him that we would have to get that estimate from other agencies because, you understand, that we are not the procurers. The Department of Defense, when it established the Glasgow Air Force Station in Montana about which he was specifically concerned, did its own procuring. With respect to the $4 billion annual cost estimate, we broke it down as follows; $3 billion in communications costs—three-fourths is in communications costs and not in power costs. Approximately $500 million is in electric costs, and $500 million in gas, sewage, and steam costs.

Now, he later asked us for, and we gave him an explanation of our general procedures for attempting to negotiate satisfactory rates rather than litigating for such rates in regulatory proceedings, although we do intervene when negotiations do not produce satisfactory results and we are in several cases right now. But we attempt to negotiate first and see if we can handle it that way.

STAFF ON RATE CASE WORK

More than that—he asked us how much staff GSA had dedicated to this. We pointed out the number of people we had but also pointed out that, working with the Department of Defense, Atomic Energy Commission and other major procurers, we frequently will decide which agency has the major interest in a particular case and will delegate authority to that agency to represent the Government as a whole. So that in relating the eight people to $4 billion worth of procurement, it does look as though we are understaffed. But when we said we thought we were adequately staffed, we meant simply that we believe that by and large, with the total available staff, we were meeting the needs under the procedures we were using. That is, by using the staff resources of GSA and other agencies, we were meeting adequately the needs of the Government.

REDUCTION IN UTILITY BILLS

We had also pointed out to him that in fiscal year 1966, as an example—through GSA representations, negotiations and rate reviews in fiscal 1966—we had secured a total reduction in utility bills of $1,349,306. This represents to us a return of over $11 for each $1 spent in this activity.

We don't have that calculated out on a Government-wide basis nor cumulative. I think it would be interesting and we would be glad to see if we can bring that together as a total.

Representative GRIFFITHS. Thank you. I think it would be interesting to the committee.

(The information referred to follows:)

The cumulative utility savings beginning with the fiscal year 1963 and extending through May 15, 1967, are $11.1 million composed of $1.4 million having a single year effect and $9.7 million which will accrue annually.

ROTATION OF MEDICAL STOCKS

Representative GRIFFITHS. You have referred to the Office of Emergency Planning and point out that you have developed a plan whereunder a 30-day inventory of certain medical items will be located at and rotated by community hospitals. The Office of Emergency Planning—is that the group from the executive offices that deals really with civil defense—which used to be considered as civil defense?

Mr. KNOTT. Right.

Representative GRIFFITHS. Do you mean that these medical items are only in community hospitals—and what is a community hospital?

Mr. KNOTT. This is in addition to these prepositioned hospitals which are packaged hospitals. This is a further step in which we are putting the hospitals in local communities and allowing them to use these materials and then to pay back out of new acquisitions.

Representative GRIFFITHS. Is that in all hospitals in any community?

Mr. KNOTT. It is in addition—this is in a substantial number. How much?

Mr. HARLAN. 2,300.

Representative GRIFFITHS. Are there not a lot more hospitals than that?

Mr. HARLAN. We have in addition to community hospitals, some 2,300 hospitals placed around in firehouses and places where they can be activated in the even of an emergency. They are all packaged and ready for activation.

Representative GRIFFITHS. Out of the firehouses are you sure that these shelf items are then made available to other hospitals or for purchase or some other way?

Mr. HARLAN. We inspect these hospitals each year. As the materials in the kits need to be replaced they are removed from the kits and taken back into our storage centers where an examination and analysis is made of them to determine whether they are fit for further utilization or processing or must be destroyed. One of the reasons why we are moving to the community hospitals sort of thing is to avoid so much of that destruction by asking the community hospitals to feed from the short shelf-life items in the kits and replace them from their new procurement so there would be a continuing turnover and rotation.

Representative GRIFFITHS. Unless you mean by "community hospital" any hospital in any community, I sincerely trust that you will change the definition because I do not see any reason why it should not be any hospital, private or otherwise.

Mr. HARLAN. I am not sure why they refer to it as a "community hospital."

Representative GRIFFITHS. You point out that the Office of Emergency Planning keeps out 20 million tons of such material. Who makes the determination of which material is necessary?

Mr. KNOTT. The Office of Emergency Planning.

Representative GRIFFITHS. Who in the Office of Emergency Planning, and how many employees do they have? Who determines it?

Mr. KNOTT. I don't know how many employees they have.

Mr. HARLAN. They are a very small staff.

Representative GRIFFITHS. They have practically nobody, do they not? So who really makes the determination?

Mr. HARLAN. This is made as a result of an interagency material advisory committee which consists of representatives of about 10 or 11 Government agencies, including the Department of Defense, Department of Commerce, Department of the Interior, GSA, Department of

Agriculture, Department of State, and so forth; anyone who has an interest in the stockpiling and in the mobilization question. Those agencies engage in extensive accumulation of data and information, through the appointment of task forces. Stockpiling decisions are made as a result of advice passed to the OEP by this interagency committee.

Representative GRIFFITHS. Do you review these decisions to determine whether this material is really sensibly saved or should be put on a surplus list?

Mr. HARLAN. This whole organization of which we are a part makes that review and makes recommendations to the Director of the Office of Emergency Planning; yes, ma'am.

Representative GRIFFITHS. I would like to say that I sat on the Holifield committee when we reviewed civil defense, and in my opinion we did not have any civil defense and we do not have it now. I went out to the Detroit office and one of the big shocks to me is that we still do not even have a way in this country of notifying the public in case of an attack, in spite of the fact that the early warning system has has cost us billions of dollars. Evidently all we really intend to save are a few ships at sea. Across the river in Canada the Federal Government pays for a system that notifies the people that they are under attack. I regret that I was not here when the Department of Defense was here because I intended to bring this up. I hope you suggest to them that they might spend a little money trying to save a few of the people in view of the fact that the taxpayers pay for the whole system.

I would think also that for the Office of Emergency Planning to save more than 50 percent of the inventory ought to be really looked at again because where is it? What are they doing? As far as I can see they are not doing anything. They could either sell it all or they ought to put in some more money and decide upon doing something.

Mr. KNOTT. You are talking about the stockpile?

Representative GRIFFITHS. Yes. What are they doing with it? Where is it? Where would it be available? They do not really have any plan. I have checked all over the country. I do not see any plan. I do not know why they should have anything else—it really is at some point available.

STOCKS AT MANUFACTURERS' PLANTS

Mr. KNOTT. Of course many of these materials are stocked at manufacturers' plants; in fact, more is stocked at plant sites than at Government installations. We have gradually taken them out of Government installations.

Representative GRIFFITHS. How much of it is just stocked to keep it from competing with commercial products today?

Mr. KNOTT. Substantial quantities have been turned over to us for disposal, and we have disposed of large quantities without disruption of the market. This is a mandate of the law, no matter what the excesses are, we can't feed them into the marketplace at a rate which would disrupt the market. It may take us as much as 50 to 75 years to dispose of some of it.

Representative GRIFFITHS. I would assume that since the investment credit was necessary that we could feed quite a lot of it into the marketplace right now.

Mr. KNOTT. Some of it is short, in really short supply. Others in long supply.

Representative GRIFFITHS. Thank you very much.

Mr. Moorhead?

ADPE PROGRAM

Representative MOORHEAD. Thank you, Madam Chairman.

Mr. Knott, I was pleased that you spent so much time in your testimony talking about automatic data processing. As you know, I have an interest in that.

$3 BILLION ANNUAL COST

What is your estimate as of the total annual expenditure by the Government for this type of equipment?

Mr. KNOTT. About $3 billion, I understand.

Representative MOORHEAD. In recent years has there been any trend toward increased purchasing as opposed to leasing of this equipment by Government agencies?

Mr. KNOTT. Within the last few years there has been a trend in that direction—there was a time when some of the companies wouldn't sell, as you know.

THIRD PARTY LESSORS

Representative MOORHEAD. I was interested, and I did not quite understand your testimony about the acquisition from third party lessors.

Mr. KNOTT. Yes, that is an interesting arrangement. We began to hear about this about a year ago. Proposals were made by third parties who would go in and buy equipment from, say IBM. They would buy IBM equipment and lease it to the Government at less than we could lease it from original equipment manufacturers because they would amortize it over a longer period of time than the equipment manufactured. Perhaps Mr. Abersfeller, who actually negotiated some of these—the Department of Agriculture, Department of Labor, Department of Justice, and Social Security have been the beneficiaries of some of these arrangements—can explain in further detail.

Mr. ABERSFELLER. I think you pretty well covered it. This is simply a question of pricing, Mr. Moorhead. The leasing companies—third party leasing companies—choose to amortize their equipment over a longer period than the original equipment manufacturers do. Therefore, we get reductions of approximately 25 percent in the leased price as compared to the original equipment manufacturers' leased price.

Representative MOORHEAD. That is interesting.

RECORDS OF AGENCY USE

How are your records on utilization of this type of equipment by the various agencies? Can you keep tabs on that?

Mr. KNOTT. We are getting a better hold on it. We have not had a really up to date inventory. I do not believe.

GETTING MORE COMPLETE INVENTORY

Mr. ABERSFELLER. Yes. We are getting a more complete inventory now. We developed a management information system. This will be fully effective in December of this year. We will for the first time get a most accurate record of our inventory and the type of equipment there is, the time the equipment is being used and this system will also tell us when agencies plan to dispose of the equipment and other things that we will find very helpful in the management of ADP.

800,000 HOURS OF UNUSED TIME

Actually, utilization of time on equipment is not as good as we would like to see it. We have about 800,000 hours of unused time currently, of which about half is usable for sharing. We are currently barely scratching the surface, Congressman Moorhead, on the utilization of equipment, notwithstanding the fact that we shared or used $26 million worth of that time among Government agencies. This year we are shooting for $30 million. We are very hopeful that the next few years we will be able to take a bigger bite of that unshared time.

$10 MILLION REVOLVING FUND

Mr. Knott. The $10 million, which will constitute the initial capitalization of the revolving fund and which our appropriations committee authorized a couple of days ago, will provide the means of saving $19 million over a period of 6 years.

GSA RATE CASE PARTICIPATION

Representative Moorhead. In connection with the testimony about participation either directly or by delegation in these rate cases I wonder if you could supply for the record the proceedings in which GSA directly intervened and those in which it delegated to another agency the duty of intervening.

Mr. Knott. Right. Over some particular period?

Representative Moorhead. The last year.

Mr. Knott. All right.

(The information which follows was subsequently supplied:)

During fiscal year 1966, GSA intervened in one utility (other than transportation and communications) regulatory proceeding (District of Columbia Public Service Commission No. 511, Potomac Electric Power Co.) and delegated one case to the Department of the Navy (California Public Utilities Commission No. 8209, Utilities Line Extension Rules). During fiscal year 1967 to date, no new utilities cases were entered or delegated by GSA, and one GSA case (PEPCO) and three delegated cases (Florida Public Utilities Commission 7764–EU, Tampa Electric Co.; Florida P.U.C. 7763–EU, Gulf Power Co. (both Air Force) and Federal Power Commission RP 65–1, United Gas Pipe Line Co. (Army) were closed.

As of May 15, 1967, there were pending two GSA cases: Florida P.U.C. 7759–EU, Florida Power & Light Co.; and FPC R–264, Accounting for Liberalized Depreciation, and five delegated cases: Arizona Corp. Com. U–1345, Arizona Pub. Serv. Co. (Army); FPC RP 64–9, Cities Service Gas Co. (Army); Kansas Corp. Com. 73,100, Certain Pipeline Companies (Army); Florida P.U.C. 7767–EU, Florida Power Corp. (Air Force); and California P.U.C. No. 8209, Utilities Line Extension Rules (Navy).

Representative Moorhead. Thank you, Mr. Chairman.

Chairman Proxmire (presiding). There was a very crucial meeting of the committee, the Agriculture Committee, and I had to testify on my dairy import bill. It is mighty important to Wisconsin.

I will not detain you long. I know that my colleagues, Mrs. Griffiths and Mr. Moorhead, have done a fine job in questioning you.

COMPETITIVE PROCUREMENT OF TIRES

Let me ask a couple of things. In the testimony we got from the Comptroller General, he said that there was an instance of automobile tires which are a classic example of what should be procured on a competitive basis. Here you had a fairly standard product and several competing companies. It was not until the Comptroller General pointed this out and emphasized it and highlighted it that the GSA proceeded to make these purchases on a competitive basis. I asked him whether or not he did not feel—whether this was not a helpful function by the Comptroller General, but that it should be the responsibility of the procuring agencies to analyze every procurement and determine whether or not it would fit into a competitive category and insist on competition.

I am wondering, first, why it took the prodding of the Comptroller General to secure this type of competitive procurement; and second, if there has been a comprehensive effort to analyze all procurement with this kind of criteria to determine whether we want to use competition more than we do.

Mr. KNOTT. That is, as he pointed out, a classic example. I don't think it is too typical. The Comptroller General, as pointed out in my statement, has been very helpful in many of these areas, including the tire procurement. We have discussed this matter with him and the decision we reached was that we would stock tires. We tried to avoid stockage as much as possible as distinguished from having items on schedule which agencies can buy directly from the schedule. But we decided that we would be ahead of the game in terms of cost and savings to stock them. This is a decision that we have reached on tires.

Looking back, I think we should have perhaps reached that decision earlier.

COMPETITIVE RENTAL OF AUTOMOBILES

Chairman PROXMIRE. I am not talking about stocking, I am talking about competitive procurement so it will be open to all suppliers to bid on and you could take the lowest bid. I think there is also a reference by the Comptroller General to the rental of automobiles and a finding that this was found to be most economical when done on a competitive basis.

Mr. KNOTT. I believe that was the Department of Defense.

Chairman PROXMIRE. I think maybe you are right.

Mr. KNOTT. Do you want to discuss this, Mr. Abersfeller?

Mr. ABERSFELLER. Mr. Chairman, prior to both Mr. Knott and me assuming our present positions there was a study conducted in General Services Administration by an expert in automobile tires. This study concluded that the way we had been buying tires at that time under the schedule was in fact the best way. It lay there then for a couple of years until we assumed our present positions and concurrently——

Chairman PROXMIRE. You mean that advice by the expert was not followed or was followed?

Mr. ABERSFELLER. It was followed and accepted. It was a continuation, if you will, of the existing policies.

Chairman PROXMIRE. That method was noncompetitive?

DEFINITION OF "COMPETITIVE BIDS"

Mr. ABERSFELLER. It tends to be competitive in this sense, in that we ask for bids on a negotiated basis and when we get a price that is low and acceptable we allow anyone else to come in on a negotiated basis who is willing to match the low price. That is how we were buying tires.

Chairman PROXMIRE. What do you mean you were asking for bids on a negotiated basis?

Mr. ABERSFELLER. We asked them to submit bids for the price of the tire they were willing to vend. Once having established who is low among that entire group you then announce those prices and say, in effect, to all the losers "If any of you want to get in on this, God bless you, meet this price and you are in."

SYSTEM LACKS INCENTIVE

Chairman PROXMIRE. What incentive would anyone have to bid low?

Mr. ABERSFELLER. Precisely the point and this is why we faced up to this after the study I referred to earlier and after new people came in to our organization we reexamined this and couldn't agree with the conclusions of our experts. It was concurrently with that action that the General Accounting Office got involved in this matter and worked very closely with us. We then took the 87 volume items—there are well over a thousand items on schedule—analyzed them rather thoroughly and concluded we could save up to 35 percent. Under our Federal supply scheduling program we still have competition in tires—what we call a maximum order limitation. If a requirement occurs above that level we buy competitively. It was through those competing procurements we found we would save that percentage. This is what really started us on that course of action, finding that when we were getting competition we saved 35 and 40 percent. Obviously it is very clear, when you get competition you get better prices.

WILL STOCK 87 ITEMS

To make a long story short, we have decided to stock these 87 items, the GAO agrees with us, we estimate a saving of a million dollars.

DEFINITION OF "COMPETITIVE PROCUREMENT"

Chairman PROXMIRE. Is your definition of competitive procurement different than that of the Department of Defense? We are very troubled by their definition. Their definition includes all procurement of less than $2,500. It was pointed out by the Comptroller that their analysis chosen at random showed that 70 percent of these procurements of less than $2,500 were in fact not competitive and were specified as not competitive.

"FORMALLY ADVERTISED" IS TRULY COMPETITIVE

Mr. ABERSFELLER. We really don't draw that kind of distinction. We draw a distinction between formally advertised, which we consider to be truly competitive.

GSA REPORTS 83 PERCENT FORMALLY ADVERTISED

Chairman PROXMIRE. What portion are formally advertised?

Mr. ABERSFELLER. 83 percent.

Chairman PROXMIRE. You have the best record.

Mr. ABERSFELLER. We have one of the best records, if not the best record; yes, sir. The remaining 17 percent, of course, is what we call negotiated. That includes about $50 million of procurement under $2,500.

Chairman PROXMIRE. You call these negotiated?

Mr. ABERSFELLER. Yes.

Chairman PROXMIRE. So your definition is that a competitive bidding is formally advertised competitive bidding where all suppliers can come in who can meet the standards.

Mr. ABERSFELLER. Yes, sir.

Chairman PROXMIRE. And a lower price schedule.

Mr. ABERSFELLER. Yes, sir.

SHOULD HAVE UNIFORM DEFINITION

Chairman PROXMIRE. Any reason you know of why this cannot be universal in Government agencies?

Mr. ABERSFELLER. The definition? I think we ought to have a uniform approach.

TRUTH IN NEGOTIATIONS ACT

Chairman PROXMIRE. That is good to hear. Have you had any experience with the Truth in Negotiation Act, Public Law 87-653?

GSA INCORPORATES PROVISIONS OF PUBLIC LAW 87-653 IN REGULATIONS

Mr. ABERSFELLER. Yes, sir. As you know, the law itself is not applicable to General Services Administration and for that matter most civil agencies, but GSA did incorporate the provisions of the law in the Federal Procurement Regulations.

Chairman PROXMIRE. So you require when you negotiate that the contractor specify his prices are accurate, current, and complete. You have to meet the three criteria. You insist on that?

Mr. ABERSFELLER. Unless there are exemptions, Senator.

Chairman PROXMIRE. How common are these exemptions?

Mr. ABERSFELLER. In the kind of things we do they are quite prevalent.

Chairman PROXMIRE. Why?

COMMERCIALLY MARKETED ITEMS EXCLUDED

Mr. ABERSFELLER. The item is marketed commercially and that is an accepted exception.

Chairman PROXMIRE. I am not talking about competitive procurement. I am talking about negotiated procurement.

Mr. ABERSFELLER. We are talking about the same thing. The Truth in Negotiation provision has an exception where you don't need cost or don't need to get cost and pricing data, if in fact a substantial amount of the material that you are buying is sold commercially.

Chairman PROXMIRE. You match the commercial price.

Mr. ABERSFELLER. The market price determines that the price is reasonable.

Chairman PROXMIRE. When you say substantial, how substantial? How large a proportion?

Mr. ABERSFELLER. The word is no further defined than this in the law.

Chairman PROXMIRE. I am talking about the proportion of your negotiated procurement which does not meet the standards of the Truth in Negotiation Act.

Mr. ABERSFELLER. Does not meet?

Chairman PROXMIRE. You said some of it does not have to because it is commercially procured. What does that amount to, that 17 percent of your procurement which is not advertised?

FEDERAL SUPPLY SCHEDULE CONTRACTS NEGOTIATED

Mr. ABERSFELLER. It really does not apply at all in that particular area. It applies only in that area that we serve other agencies which is not included in this 83–17-percent break. That is the $1,020 million a year that we contract for under the Federal supply schedules. Of that $1,020 million, $820 million is negotiated under multiple award schedules. The largest single item is ADP equipment. Here we face the Truth in Negotiation problem immediately. If, as an example—and again to take the name of the three initialed companies—the equipment they have is sold in substantial quantities, we would accept that fact to exclude the need for any further cost and pricing data from them.

CONTRACT REFUSED TO COMPANY NOT WILLING TO COMPLY WITH REGULATIONS

However, in last year's negotiations it developed that they couldn't support this on two items. They refused to give us cost and price data and we refused to contract with them for it. We adhered very closely to the Truth in Negotiations law, have, in fact, by the example I have given you, refused to enter into a contract with a company who had refused to give us the information.

Chairman PROXMIRE. Do you find this uncommon that they refuse to give it to you?

Mr. ABERSFELLER. Yes; uncommon.

Chairman PROXMIRE. The Truth in Negotiations Act does not impose any difficulties as far as you are concerned?

Mr. ABERSFELLER. No, sir.

Chairman PROXMIRE. You insist—I take it from your last answer—in these cases that in your contracts they specify the accurate, complete, and current costs?

Mr. ABERSFELLER. Yes, sir.

Chairman PROXMIRE. So you get it this way? You can examine their records?

Mr. ABERSFELLER. Whenever that is required, Senator. Frankly, we have never had occasion that I can recall to examine any records. Most of the equipment we buy falls out, or the requirement for examination of records is excluded by the fact that they sell the items in substantial quantities commercially.

AUTHORITY OF GSA

Chairman PROXMIRE. What is your authority to use truth in negotiation procedures?

NO NEED TO AMEND BASIC ACT

Mr. ABERSFELLER. Federal procurement regulations.

Chairman PROXMIRE. Should your act be amended—should title 3 be amended?

Mr. ABERSFELLER. I don't think so. We don't plan to change or rescind our policy. There is, however, no legislative requirement for it.

Chairman PROXMIRE. You feel you do not need it.

Mr. ABERSFELLER. I do not think we need it. We are dedicated to the principle.

Mr. KNOTT. Certainly there would be no objection to it.

Chairman PROXMIRE. There is no point in doing an unnecessary act. It is hard enough to get a bill through Congress.

OBSOLETE ADP EQUIPMENT

Mr. Gainsbrugh, a very eminent economist, testified we have $1.5 to $2 billion in obsolete ADP equipment. Is that correct? What will become of it if we have this much, up to $2 billion of obsolete data-processing equipment?

Mr. KNOTT. I have no way of verifying that one way or the other.

Mr. ABERSFELLER. I think it is inaccurate. Frankly, we don't have our management information system in yet. I don't know where he got the information.

Chairman PROXMIRE. Let me read it to you: "I served on the President's Commission relating to automatic data equipment and there I think Mr. Staats referred to this in his testimony, too. The Government is the largest holder of computer equipment. It is serving perhaps a very constructive purpose in the area of research and development, but it holds nearly $1.5 billion or $2 billion of obsolete equipment. There is an open question now as to how you treat this in Government accounting. What do you do with obsolete inventories?"

Mr. KNOTT. That would suggest that it is owned by the Government and I wonder if he isn't including equipment that is leased.

Chairman PROXMIRE. He said "holds"—that is the verb. If it is leased it is not much of a problem. That is not in your inventory.

Mr. KNOTT. Right.

Chairman PROXMIRE. He indicates that it is a matter of inventory, at least obsolete inventory. So I take it in this context he is talking about equipment the Government owns.

Mr. KNOTT. I don't believe we own that much.

Chairman PROXMIRE. How much do we own, do you have any record of that?

Mr. ABERSFELLER. Not in detail; but we own more than 50 percent of the installed equipment.

Mr. KNOTT. It is only very recently that we have begun to buy it. I don't know. I would like to check that and give you a figure on it.

Chairman PROXMIRE. Will you do that?

Mr. KNOTT. Fine.

(The information referred to follows:)

GSA STATEMENT ON VALUE OF COMPUTER INVENTORY

The Government owns $73,600,000, at acquisition cost, of first generation vacuum-tube-type computers, according to GSA inventory records. These records exclude digital computers used in military tactical programs and for classified purposes which are generally later than first generation models. GSA is unable to support Mr. Gainsbrugh's statement that the Government has $1.5 to $2 billion in obsolete ADP equipment which is assumed to include only first generation computers.

The inventory of business-type (digital) computers, exclusive of those used in military tactical programs and for classified purposes which generally are not obsolete, amounts to only $1.3 billion including all generation models.

Representative GRIFFITHS. I would like to go back to this negotiation. Do you mean that where the seller of an item is a seller in large quantities, and has set a price on the item, you then accept that price for yourself? Or do you mean if the seller has established a commercial price for the item and you buy a thousand you are willing to pay the price for all 1,000 that he is asking for one?

Mr. ABERSFELLER. No.

Representative GRIFFITHS. What do you mean?

Mr. ABERSFELLER. He does not have to reveal cost-and-pricing data with regard to the procurement of the item. We would never just accept his price. In other words, there is a difference between requiring cost-and-pricing data as contrasted with the price that you finally settle on with the vendor for the product. We would use his commercial price in the quantities that he sells to the wholesalers or others as a benchmark from which to move. But we would not accept that as a price.

QUANTITY OF IDENTICAL BIDS

Representative GRIFFITHS. How often do the prices that you are offered between companies really show very little variance?

Mr. ABERSFELLER. Well——

Representative GRIFFITHS. I recall we once went over this and it is surprising how many competing firms have bid the same price exactly.

Mr. ABERSFELLER. Let me take typewriters. Typewriters are on our schedule—they vary from $120 for manuals to $190, on the schedule. We are able by competitive procurement—and we do make many here—to reduce the prices there again by 25 to 30 percent when we buy competitively. For instance——

Representative GRIFFITHS. In what quantities?

Mr. ABERSFELLER. For a thousand typewriters; and here we get back again to the chairman's point on competition. In this case, Remington's bid price on the thousand typewriters was $114.50 on the competitive formally advertised competition. Under the negotiated schedule which we had previously entered into with them it was $166. The Olivetti-Underwood price was $183 and we bought the typewriter for $104. R. C. Allen's price on schedule was $142.50 and competitively priced at $122.44. (See appendix VII, p. 401.)

Representative GRIFFITHS. Is Olivetti an Italian typewriter?

Mr. ABERSFELLER. That is now considered to be a domestic product. They have merged with a domestic corporation.

FOREIGN GOVERNMENT SUBSIDIZED PRODUCTS

Representative GRIFFITHS. I observed in Senator Metcalf's statement the great differential between American-made items and those abroad. Have you ever checked—is the Government subsidizing those items abroad? That is, would the French Government subsidize an item made in France?

Mr. ABERSFELLER. I don't know about France.

Representative GRIFFITHS. How about Italy?

Mr. ABERSFELLER. I understand there is some subsidy in Japan. But that is simply an understanding. I don't know that to be a fact.

Representative GRIFFITHS. From the testimony we have heard regarding drug prices—and maybe it is true, since they seem able to meet or exceed dropping prices every time—it would raise a real question as to whether the Government of the competing companies was or was not subsidizing the manufacturers of these items.

PATENT RIGHTS INVOLVED

Mr. ABERSFELLER. One thing Senator Metcalf did not say was that much of this price reduction—the price difference between foreign producers and domestic producers—was brought about by patent rights that domestic producers had which some of the foreign producers did not recognize and manufactured in violation—I should not say violation—manufactured notwithstanding the U.S. patent rights.

Now prices have been reduced. We have similar histories here on chlorotetracycline. We buy some drugs. Chlorotetracycline prices ran around $11. We bought it on a competitive procurement for AID for $3.80. But this was also from a domestic producer, too.

GSA SALARIES

Representative GRIFFITHS. What are the salaries and grades of your purchasers?

Mr. ABERSFELLER. The Assistant Commissioner for Procurements is a grade 17.

Representative GRIFFITHS. What is the average?

Mr. ABERSFELLER. About a grade 9.

Representative GRIFFITHS. What is the average grade in GSA?

Mr. ABERSFELLER. About a grade 7.

Representative GRIFFITHS. That is some improvement over what you have been doing. I think purchasers should be well paid. I am one of the few people who really do not believe that you are going to do a lot better on the competitive purchase. I think the way to do it is to train the purchasers. How many women do you have purchasing?

Mr. ABERSFELLER. Quite a few. One of our section chiefs is a woman.

UNIFORM "BUY AMERICAN" POLICY

Representative GRIFFITHS. Would a uniform Buy-American policy facilitate your work?

Mr. ABERSFELLER. Yes.

Representative GRIFFITHS. Thank you, I am finished.

Chairman PROXMIRE. Congressman Moorhead?

Representative MOORHEAD. No further questions.

Chairman PROXMIRE. It is 11:40 and we have Mr. Hughes here from the Bureau of the Budget. But before you gentlemen leave I would like to ask you if you would supply answers for the record—since we do not want to detain Mr. Hughes further—I wonder if you would answer these questions:

First, let me say that we had an excellent presentation by Mr. R. Douglas Marshall, chairman of the board of trustees of the National Association of Wholesalers.

If you could review that statement by Mr. Marshall and then tell us when you do stock; when you open-end-buy; when you make open-end purchases; and your criteria for each of these. Also, if you could give us an idea of your rate of inventory turnover and whether or not you have classes that move less than once per year. Then there are some questions which Mr. Ward will submit to you, two or three questions on real property management; and finally, you submitted some very impressive savings here and we are delighted to see those, of course—savings of $1.4 billion in 1965, $1.6 billion in 1966. Would you object if we asked GAO to look at your backup material and report to us on those savings?

Mr. KNOTT. Not at all.

Chairman PROXMIRE. We trust you completely but we would like to get as much of this as we can. We think we can learn a lot from it if they can report to us.

(Answers to the questions set forth by Chairman Proxmire were subsequently received by the committee from GSA and are included herein:) (App. I, p. 271.)

Chairman PROXMIRE. Thank you very, very much. It has been most impressive, helpful, and enlightening testimony.

Our next witness is Mr. Hughes, Deputy Director of the Bureau of the Budget. At this point in the record we will include the letter sent to the Director of the Bureau of the Budget.

APRIL 25, 1967.

Hon. CHARLES L. SHULTZE,
Director, Bureau of the Budget,
Washington, D.C.

DEAR MR. SCHULTZE: This letter will confirm conversations between members of our respective staffs that the Subcommittee on Economy in Government will hold hearings on May 8, 9, 10, and 16, 1967 and in general will follow up on topics previously considered by the Subcommittee on Procurement of the Joint Economic Committee. Your agency is scheduled to testify after the other executive agencies on the 16th. (Hearing room to be announced later.)

We will appreciate your views on the recommendations in the Subcommittee report of May 1966, namely, progress in developing a National Supply System, utilization of personal property inventories, progress in implementing the President's "Government Procurement Guidelines" of March 3, 1966, procurement under the Buy American Act, management of the Government real property holdings, and progress made in the management of automatic data processing equipment.

Please forward 100 copies of prepared testimony to Room G–133, NSOB at least one day before your appearance and refer any questions you may have for information to Mr. Ray Ward, Staff Director of the Subcommittee, phone 173/8169.

Sincerely,

WILLIAM PROXMIRE,
Chairman.

Chairman PROXMIRE. Go right ahead, Mr. Hughes.

STATEMENT OF HON. PHILLIP S. HUGHES, DEPUTY DIRECTOR OF THE BUREAU OF THE BUDGET; ACCOMPANIED BY JOHN B. HOLDEN, ACTING CHIEF, PROPERTY AND SUPPLY MANAGEMENT BRANCH, BUREAU OF THE BUDGET

Mr. HUGHES. I have with me Mr. John Holden, Chief of our Property and Supply Management Branch.

Mr. Chairman and members of the subcommittee, we are pleased to be here to discuss five areas in which the Bureau of the Budget has an interest and in which this subcommittee has expressed a particular interest and concern. They are:

1. Bureau of the Budget Circular A–76, issued on March 3, 1966, covering "Policies for acquiring commercial or industrial products and services for Government use."
2. Policies and procedures concerning the utilization, retention, and acquisition of real property as enunciated by Bureau Circular A–2, revised, dated April 5, 1967.
3. Management and acquisition of automatic data processing equipment.
4. Application of the Buy American Act and policy thereunder incident to Government procurement.
5. Progress in developing a national supply system.

COMPETITION WITH BUSINESS—A–76

As the committee knows; there has for many years been a continuing and active interest in both the legislative and executive branches of our Government in the subject of Government competition with private enterprise. Numerous studies of various aspects of the problem have been made by congressional committees and, since 1955, the Bureau of the Budget has issued four bulletins and circulars on the subject. The most recent circular became effective on March 31, 1966.

That circular reaffirms the Government's longstanding basic policy of relying on the private enterprise system to supply its needs. It also recognizes, as did the earlier issuances, that it is necessary, or in the national interest in some instances, for the Government to provide products and services which it uses. The principal difference between the new circular and the earlier bulletin is that it provides more explicit guidelines to the Departments and Agencies, which should result in more effective and uniform implementation of the Government's procurement policies in respect to competition with private enterprise.

We are now following up with the executive agencies to review the actions which they have taken since the circular became effective about a year ago. We have not completed our reviews but, on the basis of preliminary findings, we think progress has been reasonably satisfactory. For example, organizational and staffing arrangements have been completed by the agencies for assuring that the policies and procedures in A–76 are being effectively applied. The inventorying of commercial and industrial type products and services required by section 7 of the circular is proceeding and the provisions of the circular with respect to "new starts" are being implemented. Also, the reviews of existing commercial and industrial type activities, required by the circular to be completed by June 30, 1968, have been started.

We also asked the agencies to describe the problems they have encountered in applying the guidelines in the circular, along with suggestions for changes that would eliminate or alleviate such problems. In response to this request, we found that, of the 26 agencies queried, less than half had problems or suggestions for improvement of the circular. Suggestions related almost entirely to the need for clarification or refinement of the provisions of the circular without changing any of its basic policies or requirements. We are working now on a revision of A–76 to reflect these changes.

Some suggestions for change, however, would have an impact upon the substantive provisions of the circular. One of these relates to inclusion in the comparative cost statements of State and local taxes, that is, the Government cost of supplying a commercial or industrial product or service would be increased to include these taxes. Present provisions of A–76 provide for including Federal taxes foregone, but not State and local taxes. The other suggestion that would have an impact on the substantive provisions of the circular would change the 10-percent differential for new starts. As it stands now, new starts by the Government of commercial or industrial activities involving a capital investment of $25,000 or more, or additional annual costs of production of $50,000 or more, ordinarily will not be approved unless the Government's costs will be at least 10 percent less than costs of obtaining the product or service from commercial sources. This provision was adopted originally in order to allow a margin, or leeway, for uncertainties such as early obsolescence, miscalculation of maintenance and production costs, State and local taxes, et cetera. The suggestion made is to raise the 10-percent margin to 15 percent, but apply it only to new starts involving additional capital investment.

In the case of both these suggestions, we feel we need more study and experience before reaching a conclusion. The new circular, the committee may recall, has been in effect now for only a little more than 1 year, and none of the agencies with significant commercial or industrial type activities has completed the work required of them by the circular. Our initial estimate of the situation is that while the suggestion relating to State and local taxes would not have a significant impact, the one concerning "new starts" might. We want to be certain we are moving in the right direction on both these important matters before changing the circular.

As the committee has recognized, a great deal of Agency work is required by the provisions of A–76, the results of which cannot be properly evaluated until after June 30, 1968, the target date for completion of the reviews for determining which of the existing commercial and industrial activities shall continue in-house and which shall be done by private enterprise.

We will continue, with the Federal agencies, our efforts to assure effective implementation of the procurement policies of the Government in this area.

Policies and Procedures Concerning the Utilization, Retention, and Acquisition of Real Property by the Government—Circular A–2

With respect to Federal holdings of real property, we have reaffirmed existing policies and enunciated certain new policies in a recent issuance to agencies. Also we are striving, with the cooperation of all Federal Agencies, to improve procedures in the management of real property to assure—

Effective and economical use in meeting program objectives.
Identification of unneeded property.
Unneeded property is reported excess.
Return of surplus real property where appropriate to local tax rolls, and
That acquisitions, from whatever source, are consistent with actual program requirements.

Last year we advised the Subcommittee on Federal Procurement and Regulation that we were reviewing the problem of how to improve management of real property to assure stronger, sustained progress to achieve these objectives. Our preliminary studies have been completed and the Bureau has recently issued guidelines to the heads of Federal Agencies in the form of a revision to Bureau of the Budget Circular No. A–2, which we believe establishes a solid base for improving the management of Federal real property. The revised circular sets forth the Government's policy on the utilization, retention, and acquisition of Federal real property. It replaces one issued in October 1955 which was limited to providing guidelines for the identification and reporting of excess real property.

(Circular A–2 is included in the record at this point.)

Executive Office of the President,
Bureau of the Budget,
Washington, D.C., April 5, 1967.

Circular No. A–2 Revised.
To: the heads of executive departments and establishments.
Subject: Utilization, retention, and acquisition of Federal real property.

1. *Purpose.*—This Circular rescinds and replaces Bureau of the Budget Circular No. A–2, dated October 18, 1955. This revision redefines the Circular's coverage; restates the Government's general policy with respect to utilization, retention, and acquistion of Federal real property; provides guidelines for identification of excess real property; and prescribes an annual report to be submitted by each agency on the results of implementation of this Circular.

2. *Coverage.*—The provisions of this Circular apply to all Federal real property located in the United States, the Commonwealth of Puerto Rico, the Virgin Islands, and Guam, except those categories of real property specifically excluded in paragraph 2b, below.

a. For purposes of this Circular, Federal real property will include:

(1) Land, buildings, structures, and facilties (including Government-owned buildings, structures, and facilities located on other than Government-

owned land) acquired by purchase, condemnation, donation, construction, lease, or other methods; and

(2) Public domain land withdrawn and assigned to Federal agencies for use within the Federal Government for such purposes as military installations, airfields, and research facilities.

b. For purposes of this Circular Federal real property will exclude the following:

(1) Unreserved public domain (except as indicated in paragraph 5b);

(2) Real property which is to be sold or otherwise disposed of and which was acquired through (a) foreclosure, confiscation, or seizure in settlement of a claim of the Federal Government, or (b) conveyance to the Federal Government in connection with an indemnity or loan insurance or guarantee program;

(3) Rights of way or easements granted to the Government;

(4) Real property held in trust by the Federal Government;

(5) Oregon and California revested lands (43 U.S.C. 1181a);

(6) Land administered by the National Park Service, other than administrative sites outside of the established boundaries of a national park;

(7) Land administered by the Forest Service, other than administrative sites outside of the established boundaries of a national forest;

(8) Land on Indian reservations within consolidation areas approved by the Secretary of the Interior; and

(9) Land within the National Wildlife Refuge System.

3. *Utilization and retention of real property.*—Federal agencies will develop criteria to achieve effective and economical use of their real property in meeting the needs of each of their programs. Agencies will review their real property holdings in accordance with the criteria established and limit such holdings to those required for the efficient and effective conduct of assigned programs and functions.

Such real property as falls within the term "property," as defined in Section 3(d) of the Federal Property and Administrative Services Act of 1949, as amended, which is not needed should be identified and reported as excess to General Services Administration without delay pursuant to the provisions of the cited Act.

Portions of withdrawn public domain which are no longer required for effective conduct of the program for which withdrawn will be reported initially to the Bureau of Land Management, Department of the Interior, for a determination by the Secretary of the Interior, with the concurrence of the Administrator of General Services, in accordance with Section 3(d) of the Federal Property and Administrative Services Act of 1949, as amended, whether such property is suitable for return to the public domain. Any such property found unsuitable for return to the public domain and thereafter determined to be excess will be reported to the General Services Administration for further use or disposal.

All other real property covered by this Circular, as described in paragraph 2, which is not needed will be identified, screened for use for other programs of the agency and made available for such other purposes or disposed of in accordance with applicable law.

4. *Guidelines for identification of excess.*—Real property (including any separable unit) generally will be identified as excess when:

a. It is not being used by the accountable agency for program purposes and there are no approved current plans for future use, or

b. Substantial net savings to the Government would result if properties used for essential purposes could be sold at their current market values and other suitable properties for substantially lower current values substituted for them (see paragraph 7), or

c. The costs of operation and maintenance are substantially higher than for other suitable properties of equal or less value which could be made available by transfer, permit, purchase, or lease (see paragraph 7).

5. *Acquisition policy:*

a. *Restriction.*—Real property and interests therein will be acquired, within applicable authorities, only as necessary for effective program operation. Agencies will not acquire by any method areas of real property larger than needed for approved programs.

b. *Economic use.*—Prior to the acquisition of real property by purchase, condemnation, construction, or lease, each agency will review its existing holdings to determine (1) that the best economic use is being made of the agency's property and (2) whether it can fulfill its current needs by use of any property under its jurisdiction. If the new requirement cannot be met by use of the agency's existing real property, efforts will be made to determine if other satisfactory existing Federal holdings are available.

c. *Notification of planned requirements.*—Each executive agency will notify either the General Services Administration or the Bureau of Land Management, Department of the Interior, or both, as may be appropriate, of its current and future planned requirements prior to the acquisition of real property by purchase, condemnation, construction, or lease. The notification may be formal or informal as appropriate. GSA and the Bureau of Land Management, as appropriate, will advise the agencies if excess, unreserved public domain, or surplus real property is or may be available which might meet the need.

In specific cases where the agency's proposed acquisition of real property is dictated by such factors as exact geographical location, topography, engineering, or similar characteristics which limit the possible use of other available property, the notification will not be required. For example, in the case of a dam site or reservoir area, the construction of a generating plant or a substation, specific lands are needed and ordinarily no purpose would be served by such notification.

d. *Joint use.*—If suitable excess, surplus, or unreserved public domain land is not available, consideration should be given to the possibility of joint use of real property held by other Federal agencies.

e. *Transfer of excess real property.*—As a general rule and where compatible with the general provisions of this Circular, excess real property may be acquired by transfer as provided in General Services Administration's Federal Property Management Regulations, Subchapter H, Subpart 47.2, or as otherwise provided by law.

6. *Permits.*—Permits authorizing the use of property in the custody of an agency by another agency will be issued only when (a) a determination has been made by the accountable agency that the property is not excess, and (b) the proposed use by the requesting agency conforms to the acquisition and use provisions of this Circular. An agency authorized to dispose of real property may make excess or surplus property available for short-term use by permit during the period it is being processed for further use or disposal, providing the requesting agency conforms to the provisions of this Circular.

7. *Financing arrangements and authorizing legislation.*—There may be cases where the application of guidelines 4b and 4c cannot be accomplished without first incurring expenses for which appropriate financing must be obtained or securing the enactment of new authorizing legislation. In these cases appropriate arrangements should be made to complete the necessary studies and to submit such proposals for appropriations or legislation as may be necessary. These proposals should be supported by estimates of replacement costs and ultimate net savings.

8. *Implementation.*—The head of each agency will issue appropriate instructions to assure that:

a. Real property use, retention, and acquisition policies enunciated by this Circular are followed;

b. The guidelines for identification of excess real property are applied in accordance with this Circular;

c. Systematic, thorough reviews of real property holdings are made annually to identify unneeded or uneconomically used properties; and

d. Properties or portions of properties identified as excess are reported or processed as provided in paragraph 3 without delay if continued retention by the agency is not justified under the standards prescribed by this Circular.

9. *Annual report*:

a. *Submission.* The results of the review conducted pursuant to paragraph 8c of this Circular will be summarized in an annual report. The first annual report will be for fiscal year 1968. This report will either be included as an attachment to the agency's annual inventory report or real property owned by the United States, which is submitted to the General Services Administration as of June 30 of each fiscal year, or it may be submitted separately to GSA when the annual inventory report is submitted. When included as part of the annual inventory report, the data concerning the agency's review will be attached to GSA Form 1209, Summary of Number of Installations Owned by the United States.

b. *Coverage.* The report will include the following:

(1) Summary of actions which have been taken during the fiscal year to comply with the provisions of this Circular. A copy of new or revised instructions or criteria developed and issued by the agency should be included.

(2) A statement that all properties under the custody of the agency are needed or, as appropriate, that action is being taken to screen, report excess, or otherwise dispose of unneeded properties. A separate summary will be included for each of the following categories showing the number and cost of properties, acreage and number of buildings, structures and facilities: (a) properties, reported excess for disposition under the Federal Property and Administrative Services Act of 1949, as amended; (b) properties returned to the public domain (see paragraph 3); (c) properties made available by permit to another agency as provided in paragraph 6; (d) leases canceled as a result of the annual agency review; and (e) properties for which other disposition has been made.

(3) In those cases where recommendations have been made to obtain appropriate financing or new authorizing legislation to obtain substitute facilities in accordance with the policy guidelines of this Circular, a reference to such recommendations should be included in the report.

The General Services Administration will transmit the above described report for all agencies accountable for real property to the Bureau of the Budget no later than November 1, of each year.

CHARLES L. SCHULTZE,
Director.

Circular A–2, as now revised, requires Federal agencies to develop criteria to achieve effective and economical use of real property holdings consistent with program requirements. It also provides that agencies are to identify real property, or any separable unit thereof, as unneeded when—

It is not being used by the agency for program purposes, or

There are no approved current plans for future use of the property, or

Substantial net savings to the Government would result if properties used for essential purposes could be sold at their current market values and other suitable properties of substantially lower current values substituted for them, or

The costs of operation and maintenance are substantially higher than for other suitable properties of equal or less value which could be made available by transfer, permit, purchase, or lease.

In addition to the guidelines enumerated in Circular A–2, Circular A–76, on which I commented previously concerning the Government's general policy of relying on the private enterprise system, bears on the problem. Circular A–76 establishes guidance for agencies for reviewing industrial and commercial type activities which may result in real property becoming excess incident to discontinuance of such Government activities.

Circular A–2 provides that all unneeded real property as defined in the Federal Property and Administrative Services Act is to be reported as excess to GSA or, in the case of public domain which is no longer required for the program for which withdrawn, reported to the Bureau of Land Management, Department of the Interior, or, if covered by other statutes, disposed of as provided by applicable law.

We share the committee's concern relative to the growth of Federal real property holdings which totaled $69.4 billion as of June 30, 1966. To assure that acquisitions are kept to an absolute minimum as to area, A–2 instructs Federal agencies to acquire only those amounts of real property necessary for effective program operation. Also, before an agency acquires new property the agency head must make a determination that the best economic use is being made of existing holdings and, in the first instance, attempt to fulfill the need by using property under the agency's jurisdiction. If the need cannot be met by using existing agency holdings, the possibility of utilizing other satisfactory existing Federal properties must be exhausted. Procedures are provided for notifying the General Services Administration and the Bureau of Land Management, Department of the Interior, as appropriate, to ascertain if excess, surplus, or unreserved public domain lands are available which might fill the need. When existing holdings are not available for transfer, agencies then are to consider the possibility of joint use of real property held by other agencies before action can be instituted to condemn, purchase, construct, or lease.

A major feature of the circular is that, beginning with fiscal year 1968, Federal agencies are required to submit an annual report summarizing the results of their implementation of all the provisions of the circular. This report based on annual reviews as required by the circular will indicate whether or not all properties under the custody of an agency are needed, the action which has been and is being taken to screen, report excess, or otherwise dispose of unneeded properties. It will also state the number of properties returned to the public domain. It will indicate properties made available to other agencies by permit. Copies of new and revised instructions of criteria developed and issued by the agency will also accompany the report.

The Bureau of the Budget will evaluate these reports and determine the extent to which follow-up action is required. This new requirement will keep the Bureau currently informed of the effectiveness of agencies' reviews and will alert us to the need for any revision of policies and procedures for further improving the management of real property. We believe that the combination of the program for evaluating the need for Government operated industrial and commercial type activities, together with the new program I have just described under circular A-2, will enable us to achieve effective and economical use of Federal real property in meeting program objectives and encourage the prompt return of real property to local tax rolls.

Management and Acquisition of Automatic Data Processing Equipment

Our efforts in the management of automatic data processing equipment continue to be helped by the provisions of Public Law 89-306 which strengthened the authorities of the General Services Administration and the Department of Commerce for improving the procurement and utilization of this equipment. (See app. VIII, p. 404.)

Under the provisions of this legislation, the Bureau of the Budget exercises fiscal and policy control over the administration of these authorities. Accordingly, within the past year we have provided policy guidance to both the General Services Administration and the Department of Commerce which outlines the specific action programs that are to be conducted and indicates areas for priority attention. The policy guidance was developed with full participation by these agencies and therefore represents a coordinated and unified approach to dealing with the complex management problems that we face. We suggest that copies of this policy guidance be made a part of the record at this point. (See pt. 2, app. VIII, p. 404.)

In many respects, the key to improving the management of our huge investment in computers is the availability of good information on the basis of which effective management actions can be taken. With the help of agencies who are large users of this equipment, we have recently completed the development of a revised information system which will provide more comprehensive and up-to-date information about the current and projected status of our inventory equipment, and related data on personnel and costs. This new system, which is intended to serve the operating departments and agencies as well as the central management agencies, is prescribed by Circular A–83 and becomes effective on June 30, 1967. You will be interested in the fact that the system embraces not only computers operated by Government agencies, but also those operated by certain Government contractors who perform work on a cost-reimbursement basis. This action is consistent with a recent revision in the Armed Services Procurement Regulation which require such contractors to observe certain management practices in the acquisition of this equipment.

Continuing attention is being given to the improvement of the Government's procurement processes. The General Services Administration has initiated a review of the effectiveness of existing policies and procedures to determine whether revisions would be beneficial. In this connection, a recent pilot test of the use of commercial leasing arrangements resulted in rental savings of $69,000 per year for punched-card equipment used by the Department of Agriculture. Consequently, this method of procurement will now be used more extensively, but only when outright purchase of the equipment is not warranted. About 50 percent of our present inventory of computers is currently owned by the Government, with the result that rental expenditures of $200 million per year are being avoided.

In a further effort to hold procurement costs to a minimum, aggressive programs are being conducted to assure that maximum practical use is being made of existing computers before additional ones are acquired. This is being accomplished by the extensive sharing of computers among Government agencies, which is facilitated by a nationwide sharing exchange program administered by the General Services Administration; and by the redistribution of excess equipment which in fiscal year 1966 resulted in the reutilization of equipment valued at $70 million.

One of the major obstacles to the sharing and redistribution of equipment is the incompatibility that exists among equipment of different makes and models, often making it too costly to transfer work from one computer to another. This is one illustration of the importance of the responsibility assigned by Public Law 89–306 to the Department of Commerce for recommending the establishment of appropriate Federal computer hardware and software standards. This objective is being pursued primarily through active participation in the standards program of the United States of America Standards Institute under which American standards are developed and approved for voluntary use. Seventeen such standards have been approved in the field of data processing and are now in various stages of consideration for adoption as Federal standards.

Our efforts to improve the management of automatic data processing equipment have received the full support of the President. On June 28, 1966, he issued a memorandum in which he directed all Federal agencies to (a) seek new and better ways for using computers to do a better job, and (b) to manage computer activities at the lowest possible cost. A summary report of the actions taken through December 31, 1966, in response to his memorandum was recently prepared for his information. A copy of the President's memorandum and a copy of our report is being made available for insertion in the record if the chairman wishes. (See p. 410.)

I should like to mention one other aspect of our work which has grown in importance over the last year. The growth of Federal assistance programs that involve cooperative efforts with State and local governments in such areas as education, housing, urban development, and transportation is creating a heavy demand for information to plan and administer these programs. Much of this information must flow among different agencies within each government and between the levels of government to coordinate the work properly. To facilitate this intergovernmental flow of information, there is a great need for attaining greater compatibility among the data required so that it can be exchanged more efficiently and can be summarized at various levels to permit useful comparisons and evaluations of program effectiveness. There are also possibilities for conserving scarce skills and resources by making good use of pilot systems development efforts and by the joint utilization of data processing facilties. In recognition of these possibilities, we have recently formed an Intergovernmental Task Force on Information Systems which has representation from the Advisory Commission on Intergovernmental Relations, the Federal Government and State and local governments. This task force is meeting periodically in an effort to recommend actions that could be taken at each level of government to bring about the improvements that are needed.

Application of the Buy American Act and Policies Thereunder Incident to Government Procurement

Under existing regulations, all Government agencies apply a 6-percent differential (or 12-percent in certain cases) to the delivered price of foreign products, including duties, for comparison with prices of domestic products. The Department of Defense, for purposes of an alternative evaluation, adds 50 percent of the bid, exclusive of duties, to the foreign bid price, and uses the higher of the two evaluated foreign bid prices for comparison with prices of domestic products. For commodities with ad valorem equivalent duties of 41 percent or more, the 6-percent differential, including duties, results in a greater evaluated foreign bid price than the 50-percent differential excluding duties, and is controlling.

The DOD use of a second evaluation factor began in July 1962 under procedures calling for case by case review and application of differentials centering around 50 percent. In April 1964 the 50-percent evaluation factor was incorporated in the Armed Services Procurement Regulations. While the amount saved for our balance of payments by this action was not large in a relative sense, it was an integral part of a whole series of interim measures designed to reduce the adverse impact of DOD expenditures on the U.S. balance of payments.

The extent of protection offered under the Buy American Act to U.S. firms is a matter of concern to our trading partners, just as their own protective practices are a matter of concern to us. In this connection, the OECD recently published a study of member government purchasing practices. Meetings are continuing in which we are urging the reduction of discrimination through administrative discretion and more open procurement procedures among member states. This summer the OECD expects to have a statistical compilation of member government procurement data available for our review.

Even though procurement practices of some foreign governments are more restrictive than our Buy American Act policy, foreign government procurement of U.S. goods far exceeds U.S. Government procurement of foreign goods. Total nondefense U.S. Government purchases of foreign products, after application of the 6- to 12-percent Buy American Act policy, amounted to $30 million in fiscal year 1966. Procurement in the United States of nonmilitary goods by governments or government-controlled industries of the European OECD countries and Japan is estimated at $1 billion in 1966.

Part of our current nonmilitary sales to foreign governments includes jet aircraft and other specialized equipment that could not easily be supplied from other sources. On the other hand, millions of dollars of other goods now purchased from the United States could be held by foreign governments for their own domestic procurement under more restrictive practices. Therefore, the results of an escalation of restrictive government procurement practices could be very costly to the United States. In fact, we stand to lose far more in exports than we would save in imports.

While it is difficult to estimate the full budgetary costs of a more restrictive procurement policy, we estimate current budgetary savings of $10 million on the $30 million of foreign procurement under the Buy American Act by nondefense agencies.

We are continuing our surveillance of Government expenditures abroad by all U.S. agencies from the point of view of overall budgetary, international trade, and balance of payments considerations. The dual policy of Defense and other agencies applying different buy American practices to similar products is the result of our attempt at an earlier period to reconcile these somewhat conflicting objectives.

We have requested the Department of Defense and GSA to analyze the balance of payments savings and budgetary costs of their current and alternative buy American differentials. We will also examine the other principal agencies concerned. At the same time, the Department of State will follow closely the developments of the OECD Government procurement evaluation and will recommend appropriate steps for the United States to take.

Improvements in Supply Systems

As stated previously, I will comment but briefly on improvements in the Government's supply systems.

In a little more than 5 years since the creation of the Defense Supply Agency the Department of Defense and the General Services Administration, in my estimation, have made good progress toward an efficient and economical Government-wide system for the procurement and supply of personal property and nonpersonal services. Other witnesses have already described in detail accomplishments and certain deficiencies and the various actions which have been taken and are being taken. I believe the subcommittee is aware that the Bureau of the Budget has played a part in getting some of these actions underway and continues to review progress with special interest. I would like to comment briefly on a few of the recent actions in which the Bureau has been particularly interested.

Even though the Nation's military requirements this past year have brought increasing demands on supply operations, the creation of a national supply system has continued to progress. As you have been told by others, plans have been formulated and agreements obtained for the GSA to assume Government-wide support responsibility for 52 Federal supply classes, effective July 1, 1967, and for DSA to assume Government-wide support responsibility for fuel and electronics to be phased in over the next 2 years. Also, DSA will provide civilian agency support for clothing and textiles on a selective basis where savings can be effected without detriment to the military support capability. The Bureau of the Budget is prepared to work with the agencies concerned to effect the transfer of resources as will be necessary to carry out the plan which has received general agreement.

With respect to long supply inventories, steps are being taken by the GSA to bring to civilian agencies a general procedure for using long supply items to meet procurement requirements. This will enable civilian agencies to affect similar savings as that which the DOD has achieved through its facility at Battle Creek, Mich. A fully coordinated system will not develop as rapidly as we had hoped because of different procedures and different degrees of mechanization of supply records among the civilian agencies.

We have also given special attention to the problems of the storage and utilization of short-shelf-life items of supply. We believe the agreement and the actions which GSA and DSA have reported to you will minimize further losses through deterioration of stocks which was mentioned in last year's hearings.

In January of this year I reported to the President the results of further interagency efforts, in which the Bureau has actively participated, to improve the procurement of hospital perishable subsistence. As the agency representatives have detailed in their testimony, the joint efforts of DSA, GSA, PHS, and the VA have resulted in increased cross-servicing of VA and PHS hospitals by the regional Defense Supply Agency subsistence headquarters. A vital step toward even greater cross-servicing is an effort to maximize standardization of perishable items used by the hospital agencies. We are committed to report the results of this latter effort to the President in a progress report in July of this year.

Mr. Chairman, this concludes my prepared statement. I will be glad to deal with such questions as you may have.

APPLICATION OF BUY AMERICAN ACT

Chairman PROXMIRE. Thank you very much, Mr. Hughes.

Mr. Hughes, I would like to ask about a point that occurred to me while you were speaking on the application of Buy American Act and policies thereunder incident to Government procurement. Is there any figure available on the cost of this 50 percent differential?

HOW MUCH HAS THE 50 PERCENT DIFFERENTIAL COST

How much this has increased the cost to the Federal Government in procurement?

INCREASED COST IS FAIRLY SUBSTANTIAL

Mr. HUGHES. No, sir, there is not. We sought figures from Defense. We have attempted to estimate our own. We are in the process of trying to get some from Defense now but we don't have figures that would be worth putting in the record. There is a cost of course and it is fairly substantial in budgetary terms to offset the balance of payments savings.

Chairman PROXMIRE. This figure of 6 percent differential or 12 percent in certain cases, this antedates the balance of payments effort which was 50 percent?

Mr. HUGHES. That is correct.

Chairman PROXMIRE. Has there ever been a study of that?

6 TO 12 PERCENT DIFFERENTIAL SAVES ABOUT ONE-THIRD

Mr. HUGHES. We have some figures reflecting the savings, the budgetary savings implicit in the 6–12 percentages as compared with the 50 percent differential. They are of the magnitude of one-third of the expenditures. I think the figure $10 to $15 million, depending on the year.

Chairman PROXMIRE. $10 to $15 million?

Mr. HUGHES. Yes, out of a total foreign procurement by agencies affected by that 6–12 differential of the magnitude of $30 million to $45 million. These are civilian agencies we are talking about.

Chairman PROXMIRE. Last year, as I understood Mr. Ignatius in testifying, he said we spent $67.5 million in order to reduce the gold dollars, the gold outflow. So you do not have anything more recent than that?

Mr. HUGHES. We do not. We are not too confident of that figure and we are trying to tie down figures better.

BUDGET CIRCULAR A–76

Chairman PROXMIRE. Mr. Gainsbrugh testified to this subcommittee as follows—he said:

REGARDING BUREAU OF THE BUDGET CIRCULAR A–76

The statement is somewhat weaker than previous statements in terms of underscoring the desirability of purchasing within the private sector.

He called it weaker.

He went on to say:

A second area that is mentioned in Bulletin A-76 that is still much discussed in meetings of industry-government representatives is the economic arithmetic to be employed in determination of whether to make or buy, and the particular item here that is in controversy is the cost of money. (See p. 175.)

I wondered how the Budget Bureau feels about this, this kind of criticism and what your response is and how it might be amended to take account of this kind of criticism?

Mr. HUGHES. First, of course, we are aware of Mr. Gainsbrugh's criticisms and comments. Perhaps as he indicated, we did talk with the National Industrial Conference Board before the issuance of the Circular. That is not to say the circular had in any sense its approval, but we did endeavor to seek the views of the wide range of concerned interests both inside and outside the Government. We do not regard the circular, read in its entirety, as any weaker in terms of its emphasis on the utilization of private sources, wherever possible, rather we regard it as more explicit in setting forth the circumstances under which private procurement is desirable. In addition to stating the general policy of private procurement, the circular points out that there are many circumstances in which even if government operations might be more economical short-run, there are real advantages in procurement in the private sector because of the risktaking involved, the possibilities of obsolescence, greater flexibility of private procurement and so on. So we would disagree with Mr. Gainsbrugh's statement and we would urge the subcommittee's attention to the circular to see what its view is. We just feel that the circular is equally strong with respect to its emphasis on procurement from private enterprises.

COST OF MONEY

Chairman PROXMIRE. These are two points he made. One was the cost of money. How do you differentiate? The cost of money to the Federal Government obviously has to be imputed as compared with the cost of money within the private sector, which is very definite, real, and often a very big factor.

Mr. HUGHES. Well, the whole problem of comparing the costs, Government-wise versus private, is exceedingly complex and certainly the interest costs are part of it. Generally speaking the objective of the circular is to identify true costs in the private sector as distinguished from true costs to the Government.

Now, the fact that the Government does obtain money, at least under some circumstances at lower rates than are possible in the private economy, gives the Government an advantage, yet this seems to us under the terms of the circular an advantage which the Government should recognize when it evaluates whether it should make or buy a particular product. There are other areas of argument. I think the interest rate differential is not as difficult a problem in some respects as some of the other areas.

FOREGONE TAXES

Chairman PROXMIRE. I can see that this would be a controversy. One other area which he thinks is most important and that is the area of foregoing taxes as he puts it. He says how shall taxes be treated in a comparison of cost of production in the public sector, and in the private sector, and for reasons which BOB regards as sufficient I believe it is the determination of the Bureau of the Budget to still exclude State and local taxes from such determinations. This exclusion is defended on the basis that it is difficult, if not impossible, to arrive at an estimate of what the State and local taxes would be. That was Mr. Gainsbrugh.

At the same time those State and local taxes are very real and in general we know they are going to be on virtually on everything you are going to purchase and there are taxes.

Mr. HUGHES. State and local taxes were excluded for a variety of reasons from consideration in Circular A-76 as it was originally issued. This is one of the suggestions that we have received from the General Accounting Office, as a matter of fact. I think Mr. Gainsbrugh referred to this and requested that consideration be given to the inclusion of such taxes. They were excluded after a great deal of consideration originally for several reasons, not just the one Mr. Gainsbrugh made. Difficulty of calculation is a part of it. The tremendous range of taxing jurisdictions and so on.

A second consideration was the fact that at least so far as the Federal Government is concerned, State and local taxes do not represent a cost, they are a public sector cost but not a Federal Government cost.

Third, such examination——

Chairman PROXMIRE. What do you mean by that? They are a public sector cost but not a Federal Government cost—why not?

Mr. HUGHES. The Federal Government would not be paying State and local taxes whether or not the enterprise is private or public.

Chairman PROXMIRE. At the same time those taxes do represent a contribution to State and local governments.

Mr. HUGHES. That is correct.

Chairman PROXMIRE. Absent that procurement from a private source which enables them to pay that State and local tax you would have less support for education, for welfare, and so forth.

Mr. HUGHES. That is correct. That's what I was trying to say. State and local taxes are derived by State and local governments but they are not a direct cost, at least to the Federal Government. And this was one of the considerations which moved us to leave them out of the original circular.

A third consideration was the fact that such analysis as we have given to the problem would indicate to us that the effect of the inclusion of State and local taxes on comparisons would be virtually de minimis, of the magnitude of 1 or 2 percent, perhaps, excluding the utilities area.

Chairman PROXMIRE. That low when you consider personal property taxes?

Mr. HUGHES. Yes.

Chairman PROXMIRE. And State income taxes and so forth?

Mr. HUGHES. Yes. This is the best analysis that we have been able to get.

Chairman PROXMIRE. One or two percent?

Mr. HUGHES. Yes.

Chairman PROXMIRE. Astonishing.

Mr. HUGHES. Exclusive of the utility area where they would be more substantial, the best we can appraise it.

Chairman PROXMIRE. I am surprised at that.

Mr. HUGHES. This is something we are looking into.

Chairman PROXMIRE. That could make a difference, could it not? You have some decisions decided at less than 2 percent?

Mr. HUGHES. By and large, it is our judgment as we indicated in the longer statement that the inclusion of taxes in the computation would probably not significantly affect decisions but we are reexamining it in the course of our present review of the circular and we certainly will consider Mr. Gainsbrugh's views in the context of that.

Chairman PROXMIRE. I will have some more questions in connection with that. My time is up.

Congressman Moorhead?

INCOMPATIBILITY IN ADPE

Representative MOORHEAD. I have just two questions.

Mr. Hughes, in your statement you bring out this point about the incompatibility that exists among different types of data processing equipment. Just recently another subcommittee I am a member of visited the Marine headquarters where they are trying to work toward an integrated information center and it seemed to me the key to the success of the operation was—or will be—that each marine will be able to communicate with each other marine and this is of great importance in the Government.

RAPID TECHNOLOGICAL CHANGE CREATES PROBLEMS

Mr. HUGHES. Indeed, it is, Mr. Moorhead. The problem is complicated further by the rapid technological change and evolution in the field data processing. This makes it difficult to even keep track of the equipment and the nature of the equipment that is in the Government, let alone to work toward standardization.

But the proper utilization of the equipment really increase the need for compatibility, so that agencies can share, and so that a program or problem having one type of equipment which has more than it can handle can utilize another agency's equipment which has, perhaps, some idle time.

We are fully aware of the problem. It is a technical as well as a management problem. One of the purposes of both Public Law 89-306 and the circular I referred to is to improve the degree of compatibility within the equipment. The Bureau of Standards in the Department of Commerce is the technically responsible agency, but we hope that the inventory which our circular will bring about with facilitate achievement of a greater degree of information exchange and compatibility in the equipment.

Representative MOORHEAD. I hope the Bureau of the Budget, with its power over purchases, will keep pushing toward this among agencies.

Mr. HUGHES. We will do our best.

WHEN IS RESOLUTION ON BUY AMERICAN ACT DIFFERENTIALS EXPECTED?

Representative MOORHEAD. On the matter of the differential in the Buy American Act, I know you are working on this, but when can we expect a resolution of this problem?

Mr. HUGHES. I wish I could be more precise, Mr. Moorhead, but I think the best answer is the wording of the Armed Services Procurement Regulation which says that this is an interim measure designed to deal with the unusual problems associated with the expansion of defense activities. It is closely tied in with our general balance-of-payments problem, and our expectation would be that when that problem subsides, the differential will revert to a single standard.

Representative MOORHEAD. You do not see any solution short of a solution of the balance-of-payments problem?

Mr. HUGHES. I think it is difficult to see a solution short of a solution to the balance-of-payments problem. We certainly would not want to see a movement from the 6–12 in the direction of the 50 in the light of the other things we are trying to achieve in the trade area and the encouragement we are trying to give foreign governments to free up their own procurement practices. Part of the consideration here, of course, is that we are, both in terms of Government procurement and in terms of our overall balance of trade, much more the beneficiary than the victim of freeing up trade practices. Whereas our foreign product Government procurement is of the magnitude of $30 million——

Mr. HOLDEN. To civilian agencies——

Mr. HUGHES (continuing). Foreign governments procure of us something of the magnitude of a billion dollars. Now, even leaving out the jet aircraft and equipment that is specialized and which would be hard to procure elsewhere, we are in the several-hundred-million-dollar bracket. That is, we are the beneficiaries to the tune of several hundred million dollars.

Representative MOORHEAD. We have a favorable balance of trade as far as Government procurement here.

Mr. HUGHES. In terms of our Government procurement abroad versus their procurement here.

Representative MOORHEAD. I see. Thank you, Mr. Chairman.

CIRCULAR A–76

Chairman PROXMIRE. Thank you, Mr. Moorhead.

Reverting to Circular A–76, what concerns us, although it is a matter of attitude and language, I suppose, more than specific requirements, is the fact that in the old criteria was a statement giving basic policy of procuring from private rather than commercial sources—rather than Government sources. It says because the private enterprise is basic to the American economy and the basic policy establishes a presumption in favor of private procurement—in favor of the commercial sources, and goes on to indicate the benefits of this.

This is as I understand it—is in Circular 60–2, the old regulation—it is not in Circular A–76. And its absence, it seems to me, raises a question as to whether this notion, that it is desirable on the grounds of, aside and apart from strict arithmetic economic comparison, that it is beneficial, why is it excluded?

Mr. HUGHES. I guess I am repeating myself. I can refer to the words in A–76. We have a policy statement in the circular that the guidelines in this circular are in furtherance of the Government's general policy.

AMENDMENTS TO A–76

Chairman PROXMIRE. I think Mr. Gainsbrugh made a good point; that it is a weaker statement.

Mr. HUGHES. It was not our intent to reflect in the A–76 issuance a revision of Federal policy with respect to private versus public procurement.

Chairman PROXMIRE. Would you have any objections to amending the regulation to reflect that same view?

Mr. HUGHES We certainly will have this point in mind in our forthcoming amendment. We will have a reissuance or an amendment to the circular in the fairly near future dealing with some of these points that the agencies are making to us. This would fit in with the general clarifying nature of these points.

BOB'S USE OF GAO REPORTS

Chairman PROXMIRE. I understand that the Bureau of the Budget has the responsibility for seeing that the various agencies following the constructive proposals to the extent that you feel they are of the GAO, the General Accounting Office. Comptroller General Staats, when he was the Deputy Director of the Bureau of the Budget testified before a congressional committee and quoted President Johnson as having told his Cabinet members about reports by GAO, that honest mistakes can be forgiven, but it is hard to forgive failure to examine and tighten agency procedures and error that are uncovered by GAO or a congressional committee. He told them to look into them properly. If the criticisms are justified, he said he would expect you to take corrective actions so the error is not repeated.

Mr. Hughes, are the President's instructions not being carried out by the Defense Department? As you know, GAO has been repeating this ever since the act, Public Law 87–653 was adopted in 1962. We have been able to put pretty definite and irrefutable documentation that it has been a "dead letter" act as far as the Defense Department has been concerned.

I wonder what position the Bureau of the Budget takes with regard to this.

Mr. HUGHES. I think absent some evidence to the contrary, which you are citing to me, our assumption would be that the Department of Defense is carrying out Presidential instructions. I am not familiar at all with the area that you mentioned. We will look into it further.

Chairman PROXMIRE. I wish you would.

BOB TO LOOK INTO COMPLIANCE OF PUBLIC LAW 87–653

Mr. HUGHES. We will see what can be done about it. I am aware of the earlier testimony of Mr. Staats and the followup testimony by Secretary Ignatius and we do intend to pursue those matters.

Chairman PROXMIRE. This troubles us very deeply because a large portion of the Defense Department procurement is noncompetitive by any standards, by any method of measurement. The Truth in Negotiations Act specifies that the cost of the contractor should be accurate, complete and current. And the testimony that we received, in my judgment, by both the Comptroller General and by Mr. Ignatius, indicated that this had not been the case and furthermore that for this reason it was difficult for the postauditing system to be effective because there had not been established in the first place the cost under which the contracts had been negotiated, and it would seem to me that the Bureau of the Budget with its responsibilities here could be extremely helpful in helping us to arrive at a fair conclusion here.

You are right in indicating that Mr. Ignatius does not take the same viewpoint that the Comptroller General does, but he did seem to me to indicate that this act which has been on the books for more than 4 years now is not being followed.

Mr. HUGHES. I certainly think out of the earlier hearings and discussions that we have responsibility to pursue this matter and we do intend to do it.

BOB RESPONSIBILITY AS TO INVENTORY REPORTS

Chairman PROXMIRE. Also how about inventory reports—inventory by the GAO? For instance, one of the things that really troubled me was the notion that so many of the tools and equipment owned by contractors—I mean held by contractors and used are really owned by the Federal Government and the GAO testified that on the basis of their investigation that these contractors did not know what their inventory was, they had not taken a regular inventory, they did not know how much of the time they used this Government-owned inventory for profit operations, how much they used it for public, and it was a very, very disturbing situation.

Mr. HUGHES. Is this one in the Defense area, also?

Chairman PROXMIRE. Yes, sir.

Mr. HUGHES. We will try in both of these areas, through the budget handle, if you will, to get a little better information than we have. We don't have much and we will see if we can be of some assistance to the committee and to the cause of good government.

Chairman PROXMIRE. Senator Percy?

INCENTIVES VS. PRESSURE AND POLICY

Senator PERCY. On the same question of inventory control, the Federal Government does own billions and billions of dollars of inventory scattered all over the world. I am certain that your department is doing everything you can to put pressure on the various agencies to dispose of this. But pressure and policing never have worked as well as incentives.

Is there any incentive that exists in the Federal Government now for a department really on their own initiative, to root out and dig out those items that they are not fully utilizing and somewhat get credit for that against the current operating budget, or to give them some incentive for optional programs that have been turned down but where they might have some reason to get rid of this stuff hanging around? Because unlike old wine it does not improve with age.

Mr. HUGHES. I think, Senator Percy, anyone looking at the problems of property disposal would have to acknowledge that the incentives tend to be the other way. There are actually advantages, frequently, in retaining property because of the flexibility in management that that provides or because of the additional services that otherwise makes possible.

The counterincentive I think simply is the incentive to good management which we are committed to and which the administration throughout I think is committed to. It sometimes seems an inadequate counter to some of the pressures the other way. Some of them are within the executive branch, some are within the Congress, some of them in the private economy. Notwithstanding the counterpressures there are some quite impressive figures with respect to the amount of property declared excess, particularly in recent years. I am not maintaining we found it all or declared it all excess, but there have been some substantial increases in the inventory of excess property declared for transfer and disposal and these increases reflect a great deal of pain and strain—base closings-wise and otherwise. They come about through a great deal of attention on the part of a wide range of Agencies and Departments, much of it being Defense. But the incentives frequently tend to be the other way, I suspect not only in the public, but in the private economy.

REVENUES FROM SURPLUS PROPERTY

Senator PERCY. I am just wondering, when we get these estimates now of the deficit, and I understand Mr. Fowler gave a new estimate yesterday following some of the "ball park" figures thrown out at Hot Springs where I was this weekend. When we get figures like that there are only a few things we can do—increase the debt, which endangers the soundness of our fiscal policy; or we can try to increase taxes which is going to be difficult if the economy is at all soft; or we can try to somehow or other to dispose of certain inventories that we might have. What if you took a figure and said we are going to try to find $10 billion out of surplus disposal and give a quota to the department? You give them a quota when you cut their budget. Is it feasible to say to many of these departments where you guess there is a lot of stuff just sitting around. "We expect you to find in one department $2 billion and that is a goal for you to dispose of"? We are getting to the stage where we are going to have to find new techniques and resort to new approaches rather than just let a lot of this sit around, even though I know you have made progress in recent years trying to dispose of surplus property, including a film company I happen to be familiar with.

Mr. HUGHES. We may be to some extent confusing unlike things in somewhat different orders of magnitude. We are a little bit sensitive to the subject of assets disposal to deal with budget deficit problems, off our participation certificate sale controversy.

Senator PERCY. It is a problem of increasing the debt.

Mr. HUGHES. To the extent that surplus property can be disposed of it represents Federal budget income and is an offset against any expenditures. I think the orders of magnitude here, however, the potential orders of magnitude are somewhat out of proportion. I think even an optimistic estimate of the potential for surplus property disposal does not on a continuing basis offer a great deal of comfort as an income-producing device.

Senator PERCY. You are talking hundreds of millions, not billions.

Mr. HUGHES. I suspect so.

COORDINATION OF GRANT-IN-AID PROGRAMS

Senator PERCY. One last question raised by the recent statement made by the Governor of Missouri on a public television program that he feels that he is now dealing with about 220 different Federal Government agencies. He must set up counterpart State agencies to deal with each of these Federal agencies. Is any major effort being made in this grant-in-aid program to somehow streamline the overall supervision? They all have to be audited, they all have to be supervised in some way. I suppose trips by HEW, HUD, Agriculture people have to be made out for these audits from possibly Washington. Is there any coordination that can be done to reduce cost?

Mr. HUGHES. Several things. The problem is a general one. It reflects the rapid growth of individual programs in response to particular needs, and to meet the pressures, if you will, of particular interest groups.

On the audit side arrangements have been evolved under which audits are taking place on a joint basis, that is, one agency audits for several where there is an overlap and where there is an adequate relationship to make that possible.

Also, in the last Congress there was approved a measure, "Partnership for Health" which consolidated a number of grants in the health area, and it reduced from perhaps 10 to 15 to 1 the actual grant programs. It achieved a substantial consolidation of individual grants which simplifies administration and makes for more flexibility in the use of money in the States.

We are also exploring at present with our agencies and with State and local people the possibility of a statute which would permit combined administration of separate programs without altering the basic authorization statutes. The idea would be, for instance, in a situation where a neighborhood center embracing employment, Health and Welfare and other types of community service activities, in that kind of circumstance, to permit a single administration at the Federal level and locally with proper attention to the individual statutory requirements, but with a maximum blending of administrative and audit arrangements.

COORDINATION OF MILITARY PROCUREMENT

Senator PERCY. One last question in the area of real "pay dirt" in the Defense Department. My own experience in procurement in the Navy goes back 23 years when the duplication, overlapping, rivalry between the services was nothing less than scandalous in the way it worked as far as procurement was concerned. Since then I know there has been a major effort to coordinate, designate one agency as the principal procurement agency for the three services.

Are you satisfied that this tremendous effort put in a few years ago is now being carried forward and that that program is a very active program of coordination of procurement between the services just as we tried in General Services throughout the Government?

Mr. HUGHES. Our business, Senator, is not to be satisfied, and therefore I would have to say negative to the first part of your question.

However, the Defense Supply Agency is a single supply agency for the Department of Defense. It deals for all three—all four services, I guess, if you include the Marines, and it is in truth, as we look at it, a consolidated procurement and supply operation.

Mr. HOLDEN. I think that is a fair statement.

Senator PERCY. Standard items that are used in civilian agencies as well as Defense—let us say typewriters—there is a complete coordination there?

NATIONAL SUPPLY SYSTEM

Mr. HUGHES. The coordination of the Defense Supply Agency activity with GSA activities is progressing.I think I mentioned in the statement there are 52 or 53 categories of items, including the kinds of things which you mentioned which are scheduled the first of July or thereabouts to be transferred from Defense Supply to GSA.

Senator PERCY. That is being done this year?

Mr. HUGHES. That is being done this year.

Senator PERCY. That is a good step.

Thank you, Mr. Chairman.

TRUTH IN NEGOTIATIONS ACT

Chairman PROXMIRE. I am going to be brief, but I would like to button up this area in the Truth in Negotiations Act.

I understood you to say you were not aware of the argument that the truth in negotiations law has not been complied with by the Defense Department. I would like to give you the documentation we developed. (See p. 62.)

Mr. Staats said that he had undertaken a study of the truth in negotiations law to find out whether or not it had been carried out in accordance with the intent of Congress. I quote from his testimony.

> Chairman PROXMIRE. Would you agree there is a serious lack of compliance?
> Mr. STAATS. Yes.
> Chairman PROXMIRE. And a comprehensive lack of compliance?
> Mr. STAATS. Yes. We felt the matter was so important that we were not willing to rest just on a few isolated cases, and that is the reason it took 242 cases of either prime or first tier subjects.
> Chairman PROXMIRE. What were the results of your findings in some of these cases?
> Mr. STAATS. In our report which we sent to the Congress, which was January 16, it indicated very widespread noncompliance with the law. Let me just read you one paragraph.

And then he read the paragraph.

Then he goes on and say:

> This is for the period after October 1964, so we picked a period when the law had been in effect for two years, so there would be adequate time for somebody to issue the regulations. We found 185 of the 242 procurements examined in the first phase were awarded under requirements of the law and procurement regulations for submission of cost or pricing data and certificate that the data submitted was accurate, complete and current.

Then he said:

However, in 165 of these awards we found that the Agency officials and prime contractors had no records identifying the cost or pricing data submitted and certified by offerers in support of significant cost estimates. We also find that of the remaining 57 of the 242 procurements examined Agency and contractor records of the negotiated procurements that cost or pricing data were not obtained apparently because the prices were based on adequate price competition or on an established catalog or market price or commercial items sold in substantial quantities to the general public.

Then I asked if this would involve any burden, any big serious burden on their part, on the Defense Department, and he said not in their opinion. And then I asked if it is possible for the Defense Department to determine, especially in view of the lack of competition, was it possible for the Defense Department to determine the real cost on these contracts without having accurate, up-to-date cost data. And Mr. Staats said that not on a central basis or a post audit review, it cannot be done.

This is why I say in my judgment the law is not being enforced by DOD. The Comptroller General is honest and competent.

Mr. HUGHES. I happen to like him and certainly agree.

Chairman PROXMIRE. In my judgment this represents a law which has become a dead letter. This is on pages 80 to 83 of the transcript. It has not been edited but I think it is a fair recitation.

BOB WILL PURSUE COMPLIANCE WITH PUBLIC LAW 87–653

Mr. HUGHES. We will pursue that.

Chairman PROXMIRE. Good.

Now, I would like to ask—we had a proposal for a third Hoover Commission which I think may be appropriate. The old Hoover Commissions were very helpful to us. Mr. Gainsbrugh documented the reasons for it and I wondered if you would favor the idea of a Presidential Commission to study the scope of Government business activities and to cope with the problem.

Mr. HUGHES. Well, I think, Senator, as I understand the charter of the original Hoover Commission vis-a-vis Mr. Gainsbrugh's proposal, his was a somewhat more limited proposition. I read only his statement with reference to that and I think he was dealing primarily with the competition with business areas.

Chairman PROXMIRE. That is correct.

BOB PREFERS TO WORK WITH A–76

Mr. HUGHES. I personally would like to try and struggle with Circular A–76 and see if we could, by our amendments to it, and restatement of policy along the lines that you suggested, Mr. Chairman, perhaps, or amplification of the policy, if we couldn't one way or another deal with the kind of problems that concern Mr. Gainsbrugh.

Chairman PROXMIRE. Mr. Gainsbrugh is a responsible economist. Let me read a short part of what disturbs him.

He said:

The first one then is, is Government business activity increasing or diminishing? Second, a catalog, as it were, of the original purposes for each of these invasions into the private sector, an examination as to whether the original purposes are still controlling.

What is the deep, long-run significance of the growing entrance of Government into sectors of business previously reserved for the private economy?

How should public policy be defined with respect to justifiable Government business enterprises as compared with those that are engaged in competition with the private sector?

What steps are required to see that such policy is respected after it enunciated by the various Agencies including the Bureau of the Budget. We have followed with a great deal of interest the laudatory work the Bureau of the Budget has done in exploring some of these areas. The question that then comes up about the implementation of this, insofar as the circulars of the Bureau of the Budget are prepared, distributed to the various governmental agencies. (See pp. 171–2.)

This seems to me to be something that regulations may not be able to cope with. Because it does involve the gathering of information. And also making a judgment on that information not by people who are witch hunting but are trying to get at the facts.

Mr. HUGHES. Certainly the commission, an independent commission is one approach to the problem. It is hard to object to a review of the facts with regard to a problem of this importance. I would like to point out, though, that A–76 does provide for an inventory of the Government's commercial and industrial type activities and sets forth certain standards for establishing, or for that matter for maintaining them. Our efforts would be, through the circular, through our own efforts, through the attention, if you will, of this committee and the Comptroller General who is very much an interested party in the enforcement of A–76, that we could achieve the same kind of objectives that the commission might achieve. If we don't, then the commission is certainly an alternative or second line defense—and in some sense maybe a first line, a prime line of defense.

REPORT ON TRUTH IN NEGOTIATIONS ACT

Chairman PROXMIRE. I wonder if it would be possible for you to report to this committee on your findings on this Truth in Negotiations Act. I consider this to be extremely serious.

Mr. HUGHES. I would like to do that.

Chairman PROXMIRE. I am sure you would. It involves billions and billions of dollars every year and I would appreciate that very much.

Mr. HUGHES. We will.

FACE REVIEW OF PENDING MATTERS

Chairman PROXMIRE. It has been suggested by Mr. Ward that it may be necessary to have a fall review of some of these pending matters.

Without objection all pertinent matters will be placed in the record unless Senator Percy has additional questions.

Senator PERCY. I only had one.

DESTRUCTION OF MEDICAL SUPPLIES

You might well have covered that—this question of the destruction of $24.5 million worth of medical supplies between 1964 and 1967. Did you cover that?

Chairman PROXMIRE. We did not cover it in the question period because I had to step out for almost an hour to appear before the Agricultural Committee. I have a bill pending, S. 1717.

Senator PERCY. I am a cosponsor.

Senator PROXMIRE. Yes.

Senator PERCY. I am the only Christian Scientist who is a cosponsor of the medical bill. Is there any reason why the Bureau of the Budget should see why this would not be done to have a tag system so that the supplies do not run obsolescent and become unusable and disposed of through poverty programs or other agencies prior to the necessity of destroying them?

Mr. HUGHES. I don't see any reason why we shouldn't minimize losses from this.

Senator PERCY. We should have your support, certainly.

Mr. HUGHES. At some point, you have the problem of mechanics and where the administrative cost of doing some of these things may be greater than the cost of not doing it. But as a generalization it seems to me we ought to try—for a lot of reasons—social as well as economic, to minimize destruction and try to make full use of the equipment and drugs.

SAME PROBLEM AS DATED FILM

Senator PERCY. It is the same sort of program I have seen all over the world in the film industry. You have dated film, tens of thousands at retail are going to have to go and you have to figure out if they are going to destroy it before the expiration date at a 55-percent reduction in price. I should think if retailers could do it with the small amount of accounting they have that Government agencies could be alerted to it and I commend the chairman that this is the kind of bill that would save money.

Chairman PROXMIRE. What is going to happen to the $176 million worth of medical supplies in inventory? We have them all over because of civil defense procedures. I am just delighted that Senator Percy brought that up because as I say, in my absence—that was the reason I failed to do so.

Senator PERCY. I have no further questions.

Chairman PROXMIRE. It is my understanding that the GAO supported my bill last year. I put this in last year and the GAO supported it and suggested it be broader to include all other perishable items. It seems to me we did not get a recommendation from the Bureau of the Budget for some reason. I could be wrong about that.

Mr. HUGHES. Let me talk with Mr. Holden and see if I can find out, Mr. Chairman. I don't know.

Again, we will look into it and see what problems we had and I will send you a letter or add something for the record on this point.

Chairman PROXMIRE. Very good.

(The information referred to follows:)

EXECUTIVE OFFICE OF THE PRESIDENT,
BUREAU OF THE BUDGET,
Washington, D.C., May 27, 1967.

Hon. WILLIAM PROXMIRE,
U.S. Senate, Washington, D.C.

DEAR SENATOR PROXMIRE: In my recent appearance before the Subcommittee on Economy in Government of the Joint Economic Committee, you inquired as to whether the Bureau of the Budget had reported on your bill S. 3328, 89th Congress, relating to the disposal of medical supplies. I have reviewed the legislative file on this bill and found that we did not submit a Bureau report, basically for two reasons.

First, the Bureau normally waits until it receives the comments of other agencies whose views have been requested before formulating its own position. This permits the Bureau to draw on the expertise within the Executive Branch and to determine whether there are possible differences among the agencies concerned. In the case of S. 3328, only one of the five agencies asked by the Committee to comment submitted a draft reply prior to adjournment.

Second, during the period that S. 3328 was before the Congress, the Bureau was participating with other agencies in a thoroughgoing review of the emergency health program. One of the major objects of that review was the system of stockpiling of medical supplies—not least because of the problems of disposal to which your bill was addressed. That review has been completed, and the procedures pertaining to the emergency health program, as well as the materials provided through it, have been significantly changed. Continued attention is being given to the composition and quantities of materials in the six months' medical stockpile. These efforts are all designed to minimize the problem of obsolescence, although some problems still remain. Not knowing in advance, however, what changes might result from the review, we believed it best to await its outcome before defining the Bureau's position on your bill.

I assure you we and the other agencies concerned will carefully consider the bill you introduced in this session of the Congress (S. 1717).

Sincerely,

PHILLIP S. HUGHES, *Deputy Director.*

Chairman PROXMIRE. This concludes 4 days of hearings on economy in Government. We have concentrated our efforts generally on the subcommittee's long-term program aimed at securing greater economy and efficiency in the broad field of property management.

As Comptroller General Staats pointed out, "in fiscal year 1966, the Federal Government procured $77 billion worth of goods and services. This amounts to 10.4 percent of the NPG of $739.5 billion."

I also want to point out that the annual expenditures augment the enormously large investments in real and personal property.

> The worldwide cost of Federal real property holdings in 1966 was $69.3 billion.
>
> The DOD real property holdings alone were $38.390 billion and personalty property $145.180 billion.
>
> The DOD supply systems stock was valued at $37.661 billion.

The subcommittee is not only interested in the scope of these activities but in the *quality* of the management of them.

The evidence presented to the subcommittee appears to me to be conclusive that while some progress has been made the past few years it has not been sufficient. I am fearful that there has been a serious gap in top management.

It is possible that the subcommittee may reconvene sometime late in autumn to see what progress has been made as a result of these hearings and the upcoming report.

Without objection all relevant matters pertinent to these hearings may be incorporated therein. Members will be given 2 days in which to submit additional questions which will be referred to the appropriate witnesses for replies. The record will be held open for 7 days.

Thank you very, very much.

(Whereupon, at 12:45 p.m., the subcommittee adjourned.)

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