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

FILE: B-149858 **DATE:** OCT 12 1978

MATTER OF: Definition of "Impairment" in 15 U.S.C. § 278b(f)

DIGEST:

National Bureau of Standards finances operations in part by charges to users of its services, paid into Working Capital Fund. Earned net income of the Fund must be paid into Treasury annually, except that it "may be applied first to restore any prior impairment" of the Fund. 15 U.S.C. § 278b (1976). Impairments contemplated by this provision are operating losses. Bureau may not retain profits to offset increased costs--caused by inflation--of replacing equipment or facilities, nor can Bureau calculate depreciation of equipment and facilities based on replacement cost.

This decision is in response to a memorandum from David S. Nathan, Controller of the Department of Commerce asking whether the term "prior impairment," as used in 15 U.S.C. § 278b(f) could include impairment caused by inflation.

The National Bureau of Standards, Department of Commerce (NBS), performs services for the United States Government, State or municipal governments, and others. It is authorized to charge for these services based on fixed prices or costs. 15 U.S.C. §§ 273, 275 (1976). NBS finances its activities with a working capital fund established by statute. The statute requires that the amount of any earned net income resulting from the operation of the working capital fund (NBSWCF) at the close of each fiscal year be paid into the general fund of the Treasury. However, prior to such deposit, the net income may be applied first to "restore any prior impairment of the fund." 15 U.S.C. § 278b(f) (1976).

Equipment or facilities acquired for carrying out functions of NBSWCF are capitalized to the fund and their cost allocated by including an amount for depreciation, in fees charged users. However, due to inflation, the amounts recovered are insufficient to permit replacement of the equipment or facilities at the end of their useful lives. Therefore, the Controller asks whether the phrase, "to restore any prior impairment," can be interpreted to mean impairment caused by inflation, and whether the NBSWCF may retain profits to offset increased costs in replacing equipment or facilities. For the following reasons, our answer is no to both the questions asked.

The inquiry assumes that the increased cost of equipment is the result of inflation and not attributable to other factors (e.g., product improvement) and also that NBS will still have a need for the equipment or facility at the end of its useful life (i.e., that it will in fact be replaced.) Such assumptions might not be warranted in every case. However, we direct the following discussion to those cases where such assumptions are correct.

"Impairment" is not a word of art with a well-defined meaning in the practice of accounting. The dictionary definition of "impair" is to "make worse; to diminish in quantity, value, excellence or strength; to do harm to." Webster's Third New International Dictionary of the English Language, Unabridged (Springfield, Mass., G&C. Merriam Co., 1966), p. 1131. While it could be argued that the Congress, by appropriating a specific amount of money to establish a working capital fund, intended that the amount in the fund be periodically redetermined to reflect changes in the value of the dollar (up or down) so that the buying power of the fund could remain constant vis-a-vis price levels on the date of its establishment, we doubt that the Congress would impose such a complex accounting requirement on agencies without expressly stating such an intention. Thus we doubt that the impairment contemplated was the lessening of the value of the fund by means of a lessening in the value of the dollar. However, this is in effect what NBS is suggesting in its proposal.

The NBSWCF was initially established by the Deficiency Appropriation Act of 1950, approved June 29, 1950, 64 Stat. 279, and funded in the amount of $3 million. (As a result of subsequent appropriations by the Congress, the NBSWCF is now capitalized in the amount of $24.3 million.) Subsequently, this provision was amended and added to the Organic Act of the NBS (Act of March 3, 1901, ch. 872, 31 Stat. 1449), by section 2 of the Act of August 3, 1956, ch. 906, 70 Stat. 959 (1956 Act), 15 U.S.C. § 278b (1976).

Section 3 of the NBS Organic Act, as amended by the 1956 Act, provides in pertinent part as follows:

> "The bureau shall exercise its functions for the Government of the United States and for international organizations of which the United States is

a member; for governments of friendly countries; for any State or municipal government within the United States; or for any scientific society, educational institution, firm, corporation, or individual within the United States or friendly countries engaged in manufacturing or other pursuits requiring the use of standards or standard measuring instruments * * *." 15 U.S.C. § 273 (1976).

Section 7 of the Organic Act, as amended by the 1956 Act, requires the Secretary of Commerce to:

"* * *charge for services performed under the authority of section 273 of this title, except in cases where he determines that the interest of the Government would be best served by waiving the charge. Such charges may be based upon fixed prices or costs. The appropriation or fund bearing the cost of the services may be reimbursed, or the Secretary may require advance payment subject to such adjustment on completion of the work as may be agreed upon." 15 U.S.C. § 275a (1976).

Section 12 of the Organic Act, as amended by the 1956 Act, provides in pertinent part that:

"(d) Credits.

"The fund may be credited with advances and reimbursements, including receipts from non-Federal sources, for services performed under the authority of section 273 of this title.

"(e) Cost defined.

"As used in this chapter, the term 'cost' shall be construed to include directly related expenses and appropriate charges for indirect and administrative expenses.

"(f) Distribution of earnings; restoration of prior impairment.

"The amount of any earned net income resulting from the operation of the fund at the close of each fiscal year shall be paid into the general fund of the Treasury: Provided, That such earned net income may be applied first to restore any prior impairment of the fund." 15 U.S.C. § 278b (1976).

In explaining the addition of subsections 12(d), (e) and (f) to the NBS Organic Act, the report of the Senate Interstate and Foreign Commerce Committee, states in pertinent part that:

> "Subsection (d) will also provide authority, not now provided, to make payments to the fund in advance of performance of services. This authority will enable the Bureau to avoid shortages in operating cash without receiving additional appropriations to increase the working capital. During periods of emergency increases in program activity, the Bureau has been faced with a serious shortage of operating cash which occasionally has necessitated delays in payment of vouchers for services received.
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> "Subsection (e) presents a more general definition of the term 'cost' than is presently incorporated in the authority for the use of the fund. The act which originally established the working capital fund provided that reimbursements shall include handling and related charges, reserves for depreciation of equipment and accrued leave, and building construction and alterations directly related to the work for which reimbursement is made. Subsection (e) will permit the inclusion of any or all of these elements in the determination of costs of services performed but would not preclude the charging of other items. Accordingly, the accounting system to be followed in connection with the use of the working capital fund would be left to the administrative discretion of the Department of Commerce, subject, of course, to the requirements of the Bureau of the Budget, the Treasury Department, and the Comptroller General.
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> "Since a significant part of the work performed by the Bureau would be paid for on the basis of fixed prices or fees, the procedure for handling surpluses or deficits in the capital of the fund is needed. Subsection (f) provides for the depositing of any earned net income in the general fund of the Treasury after first restoring any deficit in working capital due to prior operating losses." S. Rep. No. 1171, 84th Cong., 1st Sess., p. 4 (1955).

Thus the "impairment of the fund" contemplated appears to be the operating losses sustained by providing services to other agencies at a fixed price which might not recover the total cost of performing the service. See also Hearings before a Subcommittee of the Senate Committee on Interstate and Foreign Commerce on S. 2060, 84th Cong., 1st Sess. 8 (1955). Furthermore, this interpretation is consistent with the earlier law and legislative history dealing with the operation of working funds. For example, Congress imposed on the Bureau of Engraving and Printing Fund, established under section 2 of the Act of August 4, 1950, ch. 558, 64 Stat. 409, the following requirement:

> "(e) Any surplus accruing to the fund in any fiscal year shall be paid into the general fund of the Treasury as miscellaneous receipts during the ensuing fiscal year: Provided, That any such surplus may be applied first to restore any impairment of the capital of the fund by reason of variations between the prices charged for work or services and the amount determined to be the actual cost of performing such work or services." (Emphasis supplied.) 31 U.S.C. § 181a (1970).

Also, when the Treasury General Supply Fund was reconstituted into the General Services Administration General Supply Fund by section 109 of the Federal Property and Administrative Services Act of 1949, approved June 30, 1949, ch. 288, 63 Stat. 382, the Congress provided in pertinent part that:

> "(e) Annual audit; surplus; report to Congress.
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> "The Comptroller General of the United States shall make an annual audit of the General Supply Fund as of June 30, and there shall be covered into the United States Treasury as miscellaneous receipts any surplus found therein, all assets, liabilities, and prior losses considered, above the amounts transferred or appropriated to establish and maintain said fund, and the Comptroller General shall report to the Congress annually the results of the audit, together with such recommendations as he may have regarding the status and operations of the fund." 40 U.S.C. § 756 (1970).

Section 109 of the 1949 Act originated in S. 2020 as reported by the Senate Committee on Expenditures in the Executive Departments. See H.R. Rep. No. 935, 81st Cong., 1st Sess. 33 (1949).

In commenting on section 109, the report of the Senate Committee on Expenditures in the Executive Departments states, in pertinent part as follows:

> "(e) This subsection alters the previous requirement that all surplus in the fund, as determined in the annual audit by the Comptroller General, must be covered into the Treasury as miscellaneous receipts, by permitting losses incurred by the fund in prior years, as well as all assets and liabilities, to be considered in ascertaining the amount of such surplus. This change takes cognizance of the fact that such prior losses represent impairments of the fund capital, unless made good from earnings, and also will counteract any tendency to establish prices at too high a level. Also, there is added the requirement that the Comptroller General report to the Congress annually the results of the audit. Such reports, and his recommendations as to the status and operations of the fund, should be helpful to the Congress in its consideration of supply activities." (Emphasis supplied.) S. Rep. No. 475, 81st Cong., 1st Sess. 11 (1949).

See also the Civil Service Commission revolving fund established by the Third Supplemental Appropriation Act of 1952, Act of June 5, ch. 369, 66 Stat. 107. Thus it is clear that the Congress, prior to adoption of the 1956 Act, used "impairment" to indicate the detriment to the working capital fund if reimbursements based on fixed fees failed to recover the full cost of providing the service. We therefore find no basis for NBS to retain profits in order to offset increased replacement costs.

The Deficiency Appropriation Act of 1950, supra, establishing the NBSWCF, required that "reimbursements" recovered for the services provided include "reserves for depreciation." See 64 Stat. 279. When the NBSWCF was incorporated into the NBS Organic Act in 1956, the definition of "cost" provided in 15 U.S.C. § 278b(e) (1976) was clearly intended to permit the inclusion of "reserves for depreciation" as required by the 1950 Act. See S. Rep. No. 1171, supra, p. 4, and H.R. Rep. No. 2809, 84th Cong., 1st Sess., p. 4 (1955). The question now is, what method of depreciation accounting is required for depreciating equipment and facilities capitalized into the NBSWCF. In turn, if the value ascribed to the item depreciated can be stated in terms of replacement cost, then amounts could be retained in the NBSWCF equal to the replacement value. The NBSWCF could then, by including in its charges to users an element based on replacement cost, achieve the same objective sought to be achieved by the proposal to retain profits--i.e., the accumulation of amounts sufficient to replace equipment or facilities at current, inflated, values. However, such a procedure is not authorized.

Generally, depreciation is a means by which a cost incurred is allocated over the useful life of the asset. In Paton and Paton, Asset Accounting (New York; MacMillan Co., 1952) pp. 236-237 it is stated that:

> "* * * the primary purpose of depreciation accounting is the orderly charging of plant costs to operation; that recognizing depreciation, like the acknowledgement of other costs, has as its principal objective reasonable income accounting rather than the accumulation of funds for replacement." (Emphasis added.)

See also Eldon S. Hendriksen, Accounting Theory, rev. ed. (Homewood, Ill.; Richard D. Irwin, Inc., 1970), in which the author states "historical acquisition cost" is the most common method for valuing plant and equipment. Hendriksen, id., p. 363. Furthermore, see 2 GAO Policy And Procedures Manual for Guidance of Federal Agencies § 12.5(d), concerning acquisition cost.

We believe that the term "cost," absent something in the law or its legislative history indicating otherwise, means historical cost, and not replacement cost. Thus, when capitalizing fixed assets in the fund, the value of the asset is determined by historical cost (e.g., acquisition cost) and it is this value that depreciation allocates over the useful life of the asset.

In a similar circumstance, we indicated in our Report to the Congress, entitled "Examination of Financial Statements-Bureau of Engraving and Printing Fund For Fiscal Years 1974 and 1975-Shows Need for Statutory Authority To Increase Capitalization," FOD-76-22, March 7, 1977, that the Secretary of the Treasury lacked authority to charge fees for services of the Bureau which included a surcharge based on replacement costs of equipment (even though he possessed express authority to establish reserves for depreciation based on original cost or appraised value). Further, he could not retain in the fund such surcharges as collected. The Congress subsequently in effect authorized such a surcharge and its retention. Treasury, Postal Service, and General Government Appropriation Act, 1978, Pub. L. No. 95-81, July 31, 1977, 91 Stat. 342.

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Consequently, should it be deemed necessary for NBS to include in its fees cost items which include a factor for increased replacement costs of equipment due to inflation, specific statutory authority should be obtained. Without such authority, additional appropriations for the NBSWCF, as authorized by 15 U.S.C. § 278b(a) (1976), must be requested.

[Deputy] Comptroller General
of the United States