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BY THE COMPTROLLER GENERAL

Report To The Congress

OF THE UNITED STATES

Examination Of The Panama Canal Commission's Financial Statements For The Years Ended September 30, 1983 And 1982

GAO examined the financial statements of the Panama Canal Commission for the years ended September 30, 1983 and 1982. The examination was made in accordance with generally accepted government auditing standards.

In GAO's opinion, except for the computation and payment of interest on the U.S. investment in the Panama Canal and application of capitalization and amortization policies on improvement projects, the statements present fairly the financial position of the Commission and the results of its operations and changes in its financial position for the years then ended.

The Commission prepares its statements in accordance with the requirements of the Panama Canal Act of 1979. The statements conform with generally accepted accounting principles except where modified by the Commission to meet requirements of law.

UNITED STATES GENERAL ACCOUNTING OFFICE

GAO/NSIAD-85-26
APRIL 17, 1985

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

B-204078

To the President of the Senate and the
Speaker of the House of Representatives

This report presents our qualified opinion on the Panama Canal Commission's financial statements for the years ended September 30, 1983 and 1982. We made our examination pursuant to the provisions of the Panama Canal Act of 1979 (22 U.S.C. 3601-3871 (1982)) and in accordance with generally accepted government auditing standards. We have issued qualified opinions on the Commission's financial statements since fiscal year 1981.

The Commission is a federal agency which was established on October 1, 1979, to carry out the responsibilities of the United States with respect to the Panama Canal under the Panama Canal Treaty of 1977. In fulfilling these obligations, the Commission manages, operates, and maintains the Canal, its complementary works, installations, and equipment, and provides for the orderly transit of vessels through the Canal. The Commission will perform these functions until the Treaty terminates on December 31, 1999, when the Republic of Panama will assume full responsibility for the Canal.

As required by the Act, we are sending copies of this report to the President of the United States and the Secretary of the Treasury. Additionally, we are sending copies to the Director, Office of Management and Budget, and to the Secretaries of State, Defense, and the Army.

for Henry Eschwege
Comptroller General
of the United States

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

B-204078

To the President of the Senate and the
Speaker of the House of Representatives

We have examined the balance sheets of the Panama Canal Commission as of September 30, 1983 and 1982, and the related statements of operations and non-interest-bearing investment; changes in the investment of the United States government; changes in financial position; status of appropriations; and property, plant, and equipment for the years then ended. Our examinations were made in accordance with generally accepted government auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

As described in note 1 to the financial statements, the Commission's policy is to prepare its financial statements on the basis of accounting practices prescribed by the Panama Canal Act of 1979, which differ in some respects from generally accepted accounting principles. The accompanying financial statements are intended to present the financial position and results of operations in conformity with generally accepted accounting principles except as modified in accordance with the Act. This report fulfills our audit responsibilities to the Congress under section 1313(b) of the Panama Canal Act of 1979.

The Commission has accounting policies, which we have approved, concerning capitalization. These policies provide that major units of property, plant and equipment, including renewals and betterments to such assets, be capitalized. The cost of minor items of property, plant, and equipment is charged to expense as incurred. Additionally, these policies require that the recurring cost of dredging the waterway be charged to expense. Nonrecurring dredging costs for substantial improvements and betterments to the waterway are considered major additions to the Canal and are capitalized and depreciated over their estimated service lives.

Contrary to these policies, the Commission expensed the cost of some projects for the years ended September 30, 1983 and 1982, which provide significant long-term improvements, such as widening and straightening the Canal, and increasing power generation capacity. In our opinion, the Commission's decision to expense rather than capitalize the cost of these projects is neither in accordance with proper accounting nor its approved capitalization policy.

Also, Commission policy is to amortize expenditure of capital advance funds provided by Canal users in an amount which approximately offsets depreciation on assets acquired with such advances. The amount of capital advance funds amortized by the Commission in fiscal year 1983 significantly exceeded the corresponding depreciation because of inappropriate inclusion of immediate writeoff items in the amortization computation, resulting in current year expenses being understated.

Section 1603 of the Panama Canal Act of 1979 requires the Commission to compute interest on the investment of the United States in the Panama Canal and provides a formula for determining and adjusting the amount of that investment. The Commission computes and collects this interest as part of toll revenues representing costs of operating the Canal. However, it does not transfer these interest collections to the general fund of the U.S. Treasury. This has the effect of progressively reducing the U.S. investment on which the Commission computes interest and causes interest collections to be lower than they otherwise would be. (See app. II.) In dollar terms, it has reduced the investment base on which interest is computed by $42.2 million for the period October 1, 1979 to September 30, 1983, and understated recoverable interest costs in the amount of $4.3 million during fiscal year 1983 and $4.9 million during fiscal years 1980 through 1982.

In our opinion, except for the effects of the matters discussed in paragraphs 3 through 6, the financial statements referred to above present fairly the financial position of the Panama Canal Commission at September 30, 1983 and 1982, the results of the Commission's operations, changes in the investment of the United States, and changes in financial position for the years then ended. The statements were prepared on the basis of accounting described in note 1 and applied consistently with preceding years after restatement for changes, with which we concur, in the method of accounting for cost of early retirement benefits and amortization of advances for capital, and repair and maintenance of caissons, as described in note 6.

The Commission takes exception to our position on how interest on the U.S. investment in the Canal should be computed as well as how we view its application of certain capitalization and amortization policies. (See app. V.)

Our examination was made for the purpose of forming an opinion on the Commission's financial statements taken as a whole. The Treaty-related cost schedules (app. IV) are submitted as required by the Panama Canal Act of 1979. The schedules are not part of the Commission's financial statements. We prepared the schedules from data supplied by involved agencies and tested the data for reasonableness as necessary. However, we did not audit the Treaty-related costs and express no opinion on them.

Henry Eschwege
for Comptroller General
of the United States

Appendixes

PANAMA CANAL COMMISSION

REPORT ON INTERNAL ACCOUNTING CONTROLS

As part of our examination of the Panama Canal Commission's financial statements for the years ended September 30, 1983 and 1982, we made a study and evaluation of the system of internal accounting control to the extent we considered necessary to evaluate the system as required by generally accepted government auditing standards. This report pertains only to our study and evaluation of the system of internal accounting control for the year ended September 30, 1983. (Report on our study and evaluation of the system of internal accounting control for the year ended September 30, 1982 is presented in GAO/NSIAD-83-34, 9/2/83.) For the purpose of this report, we have classified the significant internal accounting controls in the following categories.

--Cash

--Revenues

--Expenditures

--Inventory

--Fixed plant and equipment.

Our study included all of the control categories listed above. The purpose of our study and evaluation was to determine the nature, timing, and extent of the auditing procedures necessary for expressing an opinion on the Commission's financial statements. Our study and evaluation was more limited than would be necessary to express an opinion on the system of internal accounting control taken as a whole or on any of the categories of controls identified above.

The management of the Commission is responsible for establishing and maintaining a system of internal accounting control. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of control procedures. The objectives of a system are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with accounting practices prescribed by the Panama Canal Act of 1979.

Because of inherent limitations in any system of internal accounting control, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the system to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the degree of compliance with the procedures may deteriorate.

The Commission evaluated its system of internal accounting and administrative control in accordance with the Federal Managers' Financial Integrity Act of 1982 (Public Law 97-255). The Commission reported in December 1983 that its internal control system in effect during fiscal year 1983, taken as a whole, provided reasonable assurance that agency objectives were achieved within the limits described in paragraphs 2 and 3 above.

Our study and evaluation made for the limited purpose described in the first paragraph would not necessarily disclose all material weaknesses in the system. Accordingly, we do not express an opinion on the system of internal accounting control of the Panama Canal Commission taken as a whole or on any of the categories of controls identified in the first paragraph. However, our study and evaluation disclosed no condition that we believed to be a material weakness.

Although our study and evaluation disclosed no material weaknesses, it disclosed the continuing mislocation of the internal audit function in the Office of Financial Management. (See GAO/ID-83-14, 11/22/82 and GAO/NSIAD-83-34, 9/2/83). We pointed out that the organizational location of the Commission's internal audit function did not meet generally accepted government auditing standards for independence and impartiality. The organizational location of the internal audit function was realigned early in fiscal year 1984 as a separate unit responsible directly to the Administrator of the Panama Canal Commission.

PANAMA CANAL COMMISSION

REPORT ON COMPLIANCE WITH LAWS AND REGULATIONS

We have examined the financial statements of the Panama Canal Commission for the years ended September 30, 1983 and 1982. Our examinations were made in accordance with generally accepted government auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures, including compliance with laws and regulations as we considered necessary in the circumstances. This report pertains only to our review of compliance with laws and regulations for the year ended September 30, 1983. (Report on our review of compliance with laws and regulations for the year ended September 30, 1982 is presented in GAO/NSIAD-83-34, 9/2/83.)

In our opinion, the Panama Canal Commission, except for the matters discussed in the following paragraphs, complied with the terms and provisions of laws and regulations for the transactions tested.

Nothing came to our attention in connection with our examination that caused us to believe that the Commission was not in compliance with the terms and provisions of laws and regulations for those transactions not tested.

The Panama Canal Act of 1979 requires that the $10 million public service payments by the Commission to the Republic of Panama be adjusted for actual costs at the end of the third year of operation, which was September 30, 1982. This year, as in past years, the Republic of Panama did not provide sufficient data to permit either adjustment or meaningful audit. Representatives from the Commission and the U.S. Embassy have met with Panamanian officials to express concern about the absence of adequate data, but, to date, necessary documentation has not been provided. In the absence of the data, the Commission appears to be justified in continuing to pay for public services at the same rate as in past years.

Further, as required by this Act, the Commission collects and deposits into the Panama Canal Commission (PCC) Fund toll revenues representing costs of operating the Canal, including interest on the U.S. investment. However, based on its interpretation of the law, the Commission does not transfer interest collections to the general fund of the U.S. Treasury. Although the act does not expressly state what the Commission should do with respect to interest collections after they are deposited into the PCC Fund, the legislative history indicates that the Commission should transfer the collections into the general fund of the U.S. Treasury (see app. VI).

The effect of this non-transfer of interest collections from the PCC Fund to the general fund of the U.S. Treasury is to progressively reduce the U.S. investment on which the Commission computes interest and causes interest collections to be lower than they otherwise would be. This is because, by law, deposits to the PCC Fund decrease the U.S. investment and expenditures increase it. Thus, the interest deposits are not offset by corresponding "expenditures" (i.e., transfers from the PCC Fund to the general fund of the U.S. Treasury). In dollar terms, it has reduced the investment base on which interest is computed by $42.2 million for the period October 1, 1979 to September 30, 1983, and understated recoverable interest costs in the amount of $4.3 million during fiscal year 1983 and $4.9 million during fiscal years 1980 through 1982.

We believe that the Commission can comply with congressional intent to transfer interest collections into the general fund of the U.S. Treasury within the framework of existing law. However, until the Commission transfers interest collected on the U.S. investment to the general fund of the U.S. Treasury, the investment base for the interest computation and the amount of interest computed thereon will continue to be materially understated.

Public Law 98-63 appropriated $378,635 to the Commission in July 1983 for payment of fiscal year 1982 net operating revenues to the Republic of Panama, with the proviso that none of the funds could be expended prior to validation by GAO audit. The Commission made the payment to Panama in September 1983, shortly after issuance of our report (GAO/NSIAD-83-34). That report concludes that the Commission may have materially understated its fiscal year 1982 expenses, depending on how the Congress determines that interest on U.S. investment should be computed. The Congress has not clarified whether it intended that interest should be computed on the total or net direct U.S. investment. Absent such clarification, we now do not disagree with the Commission's practice to compute interest on the net direct U.S. investment. However, our qualifications regarding computation of interest on a declining U.S. investment base and application of capitalization policies remain. Since they are not resolved, GAO has not validated the Commission's payment to Panama.

The Commission holds that it has correctly interpreted existing legislation and states that it is inconceivable that the Commission would be expected to withhold payment to Panama indefinitely based on some uncertainty that we perceive in the law. We believe that the Congress intended for the Commission to transfer interest revenues on the U.S. investment to the general fund of the Treasury. It is primarily this issue that led to our qualified opinion. Our uncertainty pertained to how the Congress intended interest to be computed, whether on the total or net direct U.S. investment. We no longer disagree with the Commission's practice to compute interest on the net direct U.S. investment.

These conditions were considered in determining the nature, timing, and extent of the audit tests to be applied in our examination, and these conditions, except for the matters of computing interest on U.S. investment and applying capitalization/ amortization policies discussed in our opinion on the financial statements, do not affect our opinion on the Commission's financial statements.

PANAMA CANAL COMMISSION
Balance Sheet
September 30, 1983 and 1982

APPENDIX III

ASSETS	1983	1982
PROPERTY, PLANT AND EQUIPMENT:		
At cost (Note 1c)............................	$869,818,221	$853,314,309
Less accumulated depreciation and valuation allowances (Notes 1e, 2 and 3)...............	402,676,579	386,676,308
	467,141,642	466,638,001
CURRENT ASSETS:		
Cash and fund balances (Notes 4 and 5):		
Deposit funds and undeposited receipts:		
Postal fund..............................	158,657	167,723
Trust fund...............................	1,132,860	1,015,983
Cash receipts for deposit into U.S. Treasury..............................	282,793	576,536
	1,574,310	1,760,242
Unexpended appropriated funds:		
Operating funds..........................	45,222,217	74,440,013
Capital funds............................	28,517,883	21,424,115
Emergency fund...........................	10,000,000	10,000,000
	83,740,100	105,864,128
	85,314,410	107,624,370
Accounts receivable, less allowance for doubtful accounts of $ 50,612, for fiscal year 1982 (Note 1f)...........................	11,043,545	9,987,875
Other receivables (Note 7)....................	826,867	826,867
	11,870,412	10,814,742
Inventories, less allowance for obsolete and excess stock of $750,154 and $800,000, respectively (Note 1g).......................	42,010,283	34,580,616
Other current assets..........................	354,383	203,737
	139,549,488	153,223,465
OTHER ASSETS:		
Deferred charges:		
Cost of early retirement benefits (Note 1h)..................................	312,960,000	332,520,000
Retirement benefits to certain former employees of predecessor agencies (Note 1h).	10,776,000	11,940,000
Other..	612,319	816,426
	324,348,319	345,276,426
Unrecovered costs due from subsequent revenues (Notes 1b and 8)............................	4,132,804	-
	328,481,123	345,276,426
TOTAL ASSETS..................................	$935,172,253	$965,137,892

The accompanying notes are an integral part of this statement.

PANAMA CANAL COMMISSION
Balance Sheet
September 30, 1983 and 1982

APPENDIX III

LIABILITIES	1983	1982
INVESTMENT OF THE UNITED STATES GOVERNMENT:		
Invested capital:		
Interest-bearing (9.885% and 9.178%, respectively) (Note 9)	$108,905,590	$ 89,763,345
Non-interest-bearing	268,748,245	258,511,310
	377,653,835	348,274,655
Current budgetary accounts (Note 4):		
Obligated operating funds	45,222,217	74,440,013
Obligated capital funds	18,031,685	15,705,670
Unobligated capital funds	10,486,198	5,718,445
Unobligated emergency fund	10,000,000	10,000,000
	83,740,100	105,864,128
	461,393,935	454,138,783
CURRENT LIABILITIES:		
Accounts payable:		
U.S. Government agencies (Note 10)	3,914,323	22,808,314
Government of Panama	6,205,923	7,090,498
Other	4,708,282	6,197,843
	14,828,528	36,096,655
Accrued liabilities:		
Employees' leave	38,075,806	36,427,154
Salaries and wages	6,124,362	5,624,977
Cost of early retirement benefits (Note 1h)	19,560,000	19,560,000
Retirement benefits to certain former employees of predecessor agencies (Note 1h)	1,364,000	1,483,000
Employees' repatriation	1,457,000	1,743,000
Ship accident claims (Notes 7 and 11)	9,818,560	11,032,030
Net revenue payable to Government of Panama (Note 12)	-	378,635
Other	2,432,361	2,027,612
	78,832,089	78,276,408
Other current liabilities:		
Unfunded ship accident claims (Notes 7 and 11)	17,890,038	20,553,489
Advances for capital-unexpended (Notes 1d and 13)	13,231,035	11,379,967
Other	1,114,088	916,418
	32,235,161	32,849,874
	125,895,778	147,222,937
DEFERRED CREDIT:		
Advances for capital being amortized (Notes 1d, 6d and 13)	14,437,009	11,956,238
LONG-TERM LIABILITIES AND RESERVES:		
Cost of early retirement benefits (Note 1h)	293,400,000	312,960,000
Retirement benefits to certain former employees of predecessor agencies (Note 1h)	9,412,000	10,457,000
Employees' repatriation	10,200,000	10,998,000
Lock overhauls (Note 1i)	7,607,574	8,294,198
Casualty losses (Notes 1j and 14)	12,825,957	9,110,736
	333,445,531	351,819,934
TOTAL LIABILITIES	$935,172,253	$965,137,892

The accompanying notes are an integral part of this statement.

PANAMA CANAL COMMISSION
Statement of Operations and Non-Interest-Bearing Investment
Fiscal Years Ended September 30, 1983 and 1982

APPENDIX III

	1983	1982
OPERATING REVENUES:		
Tolls (Note 1b)	$287,791,023	$325,589,097
Advances for capital (Note 1d)	(4,078,000)	(681,000)
Net tolls revenue	283,713,023	324,908,097
Other	111,417,549	112,946,382
Advances for capital (Note 13)	(1,173,549)	(5,870,015)
Net other revenue	110,244,000	107,076,367
Total operating revenue	393,957,023	431,984,464
OPERATING EXPENSES:		
Payments to the Government of Panama (Note 12):		
Public services	10,000,000	10,000,000
Fixed annuity	10,000,000	10,000,000
Tonnage	51,190,136	61,193,887
	71,190,136	81,193,887
Maintenance of channels and harbors	35,970,930	45,203,812
Navigation service and control	72,452,357	79,067,472
Locks operation	45,641,090	45,998,340
General repair, storehouse, engineering and maintenance services	9,625,198	11,305,378
Transportation and utilities	42,104,531	36,403,300
Housing operations	8,871,031	8,136,555
General and administrative (Note 15)	69,126,899	72,226,412
Interest on interest-bearing investment (Note 9)	9,943,192	9,123,826
Other	33,164,463	42,029,589
Total operating expenses	398,089,827	430,688,571
NET OPERATING REVENUE (LOSS) (Notes 1b, 8 and 12)	(4,132,804)	1,295,893
INVESTED CAPITAL - NON-INTEREST-BEARING:		
Unrecovered costs (recovered) deferred (Notes 1b and 8)	4,132,804	(917,258)
Net revenue payable to Government of Panama (Note 12)	-	(378,635)
Investment at beginning of fiscal year	258,511,310	249,101,935
Miscellaneous receipts deposited into the U.S. Treasury	576,536	368,145
Due U.S. Treasury for undeposited receipts	(282,793)	(576,536)
Plant reactivations	-	493,940
Interest on interest-bearing investment (Note 9)	9,943,192	9,123,826
INVESTED CAPITAL - NON-INTEREST-BEARING AT END OF FISCAL YEAR	$268,748,245	$258,511,310

The accompanying notes are an integral part of this statement.

PANAMA CANAL COMMISSION
Statement of Changes in the Investment of the United States Government
Fiscal Year Ended September 30, 1983

	Invested Capital Interest-Bearing	Invested Capital Non-Interest-Bearing	Emergency Fund	Operating Funds	Capital Funds	Total
INVESTMENT AT OCTOBER 1, 1982	$ 89,763,345	$258,511,310	$10,000,000	$ 74,440,013	$ 21,424,115	$ 454,138,783
Appropriation by the Congress for fiscal year 1983	-	-	-	405,378,634	29,024,000	434,402,634
	89,763,345	258,511,310	10,000,000	479,818,647	50,448,115	888,541,417
INCREASES IN INVESTMENT:						
Plant reactivations	-	-	-	-	-	-
Prior year receipts deposited into the U.S. Treasury	-	576,536	-	-	-	576,536
Disbursements from capital appropriations	21,930,232	-	-	-	(21,930,232)	-
Disbursements from operating appropriations	395,875,547	-	-	(395,875,547)	-	-
Funds covered into U.S. Treasury (Note 9)	(28,200,421)	-	-	-	-	(28,200,421)
Repayment to the U.S. Treasury of FY 1980 appropriation lapsed (Note 9)	28,200,421	-	-	(28,200,421)	-	-
Interest on interest-bearing investment	-	9,943,192	-	-	-	9,943,192
Property transferred from other U.S. Government agencies	3,356	-	-	-	-	3,356
Unrecovered costs deferred (Notes 1b and 8)	-	4,132,804	-	-	-	4,132,804
	417,809,135	14,652,532	-	(424,075,968)	(21,930,232)	(13,544,533)
DECREASES IN INVESTMENT:						
Funds to be covered into the U.S. Treasury	-	-	-	10,520,462	-	10,520,462
Receipts deposited into the U.S. Treasury	398,461,068	-	-	-	-	398,461,068
Due U.S. Treasury for undeposited receipts	-	282,793	-	-	-	282,793
Property transferred to the Government of Panama	141,303	-	-	-	-	141,303
Property transferred to other U.S. Government agencies	64,519	-	-	-	-	64,519
Net loss (Notes 1b, 8 and 12)	-	4,132,804	-	-	-	4,132,804
	398,666,890	4,415,597	-	10,520,462	-	413,602,949
INVESTMENT AT SEPTEMBER 30, 1983	$108,905,590 (Note 9)	$268,748,245	$10,000,000	$ 45,222,217	$ 28,517,883	$ 461,393,935

The accompanying notes are an integral part of this statement.

APPENDIX III

PANAMA CANAL COMMISSION
Statement of Changes in the Investment of the United States Government
Fiscal Year Ended September 30, 1982

	Invested Capital					
	Interest-Bearing	Non-Interest-Bearing	Emergency Fund	Operating Funds	Capital Funds	Total
INVESTMENT AT OCTOBER 1, 1981...............	$128,419,111	$249,101,935	$10,000,000	$ 59,433,349	$ 25,475,158	$ 472,429,553
Appropriation by the Congress for fiscal year 1982..............................	-	-	-	400,754,000	19,766,000	420,520,000
	128,419,111	249,101,935	10,000,000	460,187,349	45,241,158	892,949,553
INCREASES IN INVESTMENT:						
Plant reactivations.......................	-	493,940	-	-	-	493,940
Prior year receipts deposited into the U.S. Treasury...........................	-	368,145	-	-	-	368,145
Expenditures from capital appropriations..	23,817,043	-	-	-	(23,817,043)	-
Expenditures from operating appropriations	379,957,490	-	-	(379,957,490)	-	-
Interest on interest-bearing investment...	-	9,123,826	-	-	-	9,123,826
Property transferred from other U.S. Government agencies......................	72,421	-	-	-	-	72,421
Net revenue (Notes 1b and 8).............	-	378,635	-	-	-	378,635
	403,846,954	10,364,546	-	(379,957,490)	(23,817,043)	10,436,967
DECREASES IN INVESTMENT:						
Funds to be covered into the U.S. Treasury	-	-	-	5,789,846	-	5,789,846
Receipts deposited into the U.S. Treasury.	440,139,216	-	-	-	-	440,139,216
Due U.S. Treasury for undeposited receipts	-	576,536	-	-	-	576,536
Property transferred to the Government of Panama...............................	1,790,580	-	-	-	-	1,790,580
Property transferred to other U.S. Government agencies......................	572,924	-	-	-	-	572,924
Net revenue payable to the Government of Panama (Notes 1b, 8 and 12)..............	-	378,635	-	-	-	378,635
	442,502,720	955,171	-	5,789,846	-	449,247,737
INVESTMENT AT SEPTEMBER 30, 1982...........	$ 89,763,345 (Note 9)	$258,511,310	$10,000,000	$ 74,440,013	$ 21,424,115	$ 454,138,783

The accompanying notes are an integral part of this statement.

APPENDIX III

Statement of Changes in Financial Position
Fiscal Years Ended September 30, 1983 and 1982

	1983	1982
SOURCE OF FUNDS:		
From Operations:		
Revenue	$ 393,957,023	$ 431,984,464
Less operating expenses:		
Interest on interest-bearing investment	9,943,192	9,123,826
Payments to the Government of Panama (Note 12)	71,190,136	81,193,887
Other expenses	316,956,499	340,370,858
Total operating expenses	398,089,827	430,688,571
Net operating revenue (loss)(Notes 1b, 8 and 12)	(4,132,804)	1,295,893
Unrecovered costs for fiscal year 1981 (recovered) deferred (Notes 1b and 8)	-	(917,258)
Net revenue payable to Government of Panama (Notes 1b, 8 and 12)	-	(378,635)
Unrecovered costs for fiscal year 1983 deferred (Notes 1b, 8 and 12)	4,132,804	
Add transactions not requiring outlay of funds:		
Depreciation (Note 1e)	18,514,996	18,754,070
Provision for lock overhauls (Note 1i)	4,354,000	3,544,000
Provision for casualty losses (Note 1j)	3,117,088	12,200,000
Other	1,970,819	6,454,007
	27,956,903	40,952,077
Change in investment of the U.S. Government:		
Interest on interest-bearing investment	9,943,192	9,123,826
Receipts deposited into U.S. Treasury	(398,461,068)	(440,139,216)
Disbursements from appropriated funds	446,006,200	403,774,533
Repayment to the U.S. Treasury of the FY 1980 appropriation lapsed	(28,200,421)	-
Net property transfers	(202,466)	(2,291,082)
Other	293,744	285,548
	29,379,181	(29,246,391)
Amortization of advances for capital	919,711	-
Advances for capital being amortized (Notes 1d, 6d, and 13)	2,480,771	11,956,238
Total source of funds	60,736,566	23,661,924
APPLICATION OF FUNDS:		
Lock overhauls expenditures	5,040,623	3,214,853
Casualty losses	4,214,134	12,288,023
Accrued capital expenditures	21,704,598	24,903,322
Total application of funds	30,959,355	40,406,198
INCREASE (DECREASE) IN WORKING CAPITAL	$ 29,777,211	$ (16,744,274)
ANALYSIS OF CHANGES IN WORKING CAPITAL:		
Increase (decrease) in current assets:		
Cash	$ (185,931)	$ 26,439
Receivables	1,055,670	(1,665,437)
Inventories	7,429,667	(5,703,715)
Other	150,646	(156,336)
	8,450,052	(7,499,049)
Decrease (increase) in current liabilities:		
Accounts payable	21,268,127	(4,658,980)
Accrued liabilities	(555,681)	(3,587,824)
Other	614,713	(998,421)
	21,327,159	(9,245,225)
INCREASE (DECREASE) IN WORKING CAPITAL	$ 29,777,211	$ (16,744,274)

The accompanying notes are an integral part of this statement.

PANAMA CANAL COMMISSION
Statement of Status of Appropriations
Fiscal Years Ended September 30, 1983 and 1982

SOURCE OF APPROPRIATIONS:	1983	1982
Operating funds:		
Current year operating appropriation..............	$405,378,634	$400,754,000
Obligated operating funds brought forward:		
Fiscal year 1980................................	23,684,912	27,699,623
Fiscal year 1981................................	5,623,556	31,733,726
Fiscal year 1982................................	45,131,545	-
	74,440,013	59,433,349
	479,818,647	460,187,349
Capital Funds:		
Current year capital appropriation (no year).......	29,024,000	19,766,000
Obligated capital funds brought forward:		
Fiscal year 1980................................	358,549	4,162,768
Fiscal year 1981................................	4,618,448	13,208,244
Fiscal year 1982................................	10,728,673	-
	15,705,670	17,371,012
Unobligated capital funds (no year) brought forward:		
Fiscal year 1980................................	599,957	1,288,708
Fiscal year 1981................................	845,934	6,815,438
Fiscal year 1982................................	4,272,554	-
	5,718,445	8,104,146
	50,448,115	45,241,158
Emergency fund (no year)............................	10,000,000	10,000,000
TOTAL SOURCE OF APPROPRIATIONS.......................	$540,266,762	$515,428,507

The accompanying notes are an integral part of this statement.

PANAMA CANAL COMMISSION
Statement of Status of Appropriations
Fiscal Years Ended September 30, 1983 and 1982

APPLICATION OF APPROPRIATIONS:	1983	1982
Operating funds:		
Expenditures from operating appropriations:		
Repayment to the U.S. Treasury of the FY 1980 appropriation lapsed	$ 28,200,421	$ -
Fiscal year 1980	21,121,981	4,927,818
Fiscal year 1981	2,830,821	26,279,322
Fiscal year 1982	38,274,112	348,750,350
Fiscal year 1983	333,648,633	-
	424,075,968	379,957,490
Obligated operating funds:		
Fiscal year 1980	2,543,398	23,684,912
Fiscal year 1981	3,424,423	5,623,556
Fiscal year 1982	4,717,168	45,131,545
Fiscal year 1983	34,537,228	-
	45,222,217	74,440,013
Unobligated operating funds lapsed	10,520,462	5,789,846
	479,818,647	460,187,349
Capital Funds:		
Expenditures from capital appropriations:		
Fiscal year 1980	483,026	4,492,971
Fiscal year 1981	3,088,345	14,559,299
Fiscal year 1982	11,799,504	4,764,773
Fiscal year 1983	6,559,357	-
	21,930,232	23,817,043
Obligated capital funds:		
Fiscal year 1980	273,632	358,549
Fiscal year 1981	2,058,558	4,618,448
Fiscal year 1982	924,503	10,728,673
Fiscal year 1983	14,774,992	-
	18,031,685	15,705,670
Unobligated capital funds (no year):		
Fiscal year 1980	201,848	599,957
Fiscal year 1981	317,480	845,934
Fiscal year 1982	2,277,219	4,272,554
Fiscal year 1983	7,689,651	-
	10,486,198	5,718,445
	50,448,115	45,241,158
Unobligated emergency fund (no year)	10,000,000	10,000,000
TOTAL APPLICATION OF APPROPRIATIONS	$540,266,762	$515,428,507

The accompanying notes are an integral part of this statement.

PANAMA CANAL COMMISSION
Statement of Property, Plant and Equipment
September 30, 1983 and 1982

	1983		1982	
	Cost	Depreciation and valuation allowances	Cost	Depreciation and valuation allowances
Titles and treaty rights.................	$ 14,728,889	$ 3,774,278	$ 14,728,889	$ 3,406,056
Interest during construction.............	50,892,311	50,892,311	50,892,311	50,892,311
Canal excavation, fills and embankments...	347,536,452	88,974,673	336,893,372	74,355,710
Canal structures and equipment...........	223,188,786	107,678,797	226,696,154	109,506,598
Supporting and general facilities.........	159,531,771	98,621,330	157,669,770	95,231,887
Minor items of plant and equipment........	10,081,037	10,081,037	10,629,593	10,629,593
Facilities held for future use...........	3,166,947	2,508,355	3,166,947	2,508,355
Plant additions in progress..............	20,546,230	-	12,491,475	-
Suspended construction projects..........	40,145,798	40,145,798	40,145,798	40,145,798
TOTAL..................................	$869,818,221	$402,676,579	$853,314,309	$386,676,308

The accompanying notes are an integral part of this statement.

APPENDIX III

PANAMA CANAL COMMISSION

Notes to Financial Statements

1. Summary of Significant Accounting Policies.

The Comptroller General of the United States approved the Accounting Principles and Standards Statement of the Panama Canal Commission in his letter dated September 14, 1982. A summary of significant accounting policies follows:

a. Accounting and reporting. As required by section 1311(a) of the Panama Canal Act of 1979, hereinafter referred to as the Act, the accounts of the Commission are maintained pursuant to the Accounting and Auditing Act of 1950. This requires that the principles, standards and related requirements for accounting be met, as prescribed by the Comptroller General of the United States, after consulting with the Secretary of the Treasury and the Director of the Office of Management and Budget concerning their accounting, financial reporting and budgetary needs. The Accounting and Auditing Act of 1950 also requires that the accounts be maintained on an accrual basis.

b. Cost recovery. As required by section 1341(e)(1) of the Act, the application of generally accepted accounting principles to the Panama Canal Commission, a United States Government agency comparable to a rate-regulated public utility, determines the manner in which costs are recognized. The basis for tolls rates is prescribed in section 1602(b) of the Act. This section of the Act, known as the "statutory tolls formula," provides that:

> "Tolls shall be prescribed at rates calculated to produce revenues to cover as nearly as practicable all costs of maintaining and operating the Panama Canal, together with the facilities and appurtenances related thereto, including unrecovered costs incurred on or after the effective date of this Act, interest, depreciation, payments to the Republic of Panama pursuant to paragraph 5 of Article III and paragraph 4(a) and (b) of Article XIII of the Panama Canal Treaty of 1977, and capital for plant replacement, expansion, and improvements. Tolls shall not be prescribed at rates calculated to produce revenues sufficient to cover payments to the Republic of Panama pursuant to paragraph 4(c) of Article XIII of the Panama Canal Treaty of 1977."

Under this statutory tolls formula, any unrecovered costs are to be recovered from subsequent revenues. The amount for recovery from subsequent revenues is transferred from Invested Capital to an account within the Other Assets classification. Unrecovered costs are charged back to Invested Capital to the extent subsequent annual revenues exceed annual costs.

c. Property, plant and equipment. Property, plant and equipment are recorded at cost or, if acquired from another Government agency, at the value determined by the Director of the Office of Management and Budget. Administrative and other related general expenses are recovered currently and therefore not capitalized. The cost of minor items of property, plant and equipment is charged to expense as incurred.

d. Advances for capital. A portion of tolls in excess of depreciation recoveries may be programmed annually by the Board of Directors for plant replacement, expansion, or improvements. Such funds are considered capital advances from Canal users. Upon utilization, these advances are amortized through an offset to depreciation expense in an amount calculated to approximate the depreciation on assets acquired with such advances.

e. Depreciation. Property, plant and equipment are depreciated over their estimated service lives at rates computed using a straight-line method with additional annual depreciation, identified as composite, to provide for premature plant retirements.

f. Accounts receivable. Uncollectible accounts receivable of the Panama Canal Commission are recognized as a reduction in revenue when written off. Any subsequent collections of Commission accounts receivable previously written off are recorded as revenue. The allowance for doubtful accounts which appeared on the Commission books at September 30, 1982, was applicable only to the receivables of predecessor agencies.

g. Inventories. Operating materials and supplies are stated at average cost, plus cost of transportation to the ultimate destination on the Isthmus of Panama. An allowance has been established to reflect the estimated cost of obsolete and excess stock.

h. Retirement benefits. Employer payments to the contributory United States Civil Service Retirement System and to the Republic of Panama Social Security System are charged to expense. The Commission has no liability for future payments to employees under these systems.

Non-United States citizen employees who retired from predecessor agencies prior to October 5, 1958, are not covered by the United States Civil Service Retirement System but do receive benefits under a separate annuity plan. Payments made under this annuity plan are recorded as a current year expense. The liability of the Commission for future annuity payments to these former employees or their eligible widows is reflected in the balance sheet as "Retirement Benefits to Certain Former Employees of Predecessor Agencies" and an equal amount is recorded as a Deferred Charge.

As required by the Act, the Panama Canal Commission is liable for the increase in the unfunded liability of the United States Civil Service Retirement Fund which is attributable to benefits payable from that fund to, or on behalf of, employees and their survivors under the early retirement provisions of the Act. The annual installment to liquidate the increased liability is determined by the Office of Personnel Management.

i. Reserve for lock overhauls. A reserve is provided through an annual charge to expense to cover the estimated cost of periodic lock overhauls.

j. Reserve for casualty losses. A reserve is provided through an annual charge to expense to cover the estimated cost of marine accidents and other casualty losses.

k. Housing use rights. No monetary value is assigned to the rights granted to the United States Government by the Republic of Panama to use Canal Area housing transferred to the Republic of Panama under the terms of the Panama Canal Treaty of 1977. The cost to manage, maintain and provide livability improvements to these quarters is charged to expense. Rental income is included in other revenues.

2. Plant Valuation Allowances.

At July 1, 1951, certain valuation allowances for property, plant and equipment transferred from the Panama Canal (agency) to the Panama Canal Company and the Canal Zone Government were established, to reduce to usable value the costs of the assets transferred. At October 1, 1979, such valuation allowances as were applicable to the assets transferred from the Panama Canal Company and the Canal Zone Government to the Panama Canal Commission were carried forward. At September 30, 1983 and at September 30, 1982, these valuation allowances amounted to $99.3 million comprised of: (a) $5.6 million to reduce to usable value the cost of property, plant and equipment transferred; (b) $50.9 million to offset interest costs imputed for the original Canal construction period; and (c) $42.8 million to offset the cost of defense facilities and suspended construction projects, the latter being principally the partial construction of a third set of locks abandoned in the early part of World War II.

Property, plant and equipment offset by valuation allowances, when fully or partially reactivated, are reinstated by a reduction in the valuation allowance and by an increase to the non-interest-bearing investment of the United States Government in proportion to the value to the Commission of the reactivated asset.

3. <u>Depreciation as a Percentage of Average Cost of Plant</u>.

The provision for depreciation, expressed as a percentage of average cost of depreciable plant exclusive of valuation allowances, was 2.55% for fiscal year 1983 and 2.49% for fiscal year 1982.

4. <u>Cash and Fund Balances</u>.

As of September 30, 1983, the cash and fund balances of $85,314,410 are made up of $80,721,975 on deposit in the United States Treasury, $1,647,360 on deposit in commercial banks, and $2,945,075 on hand. Of the total, $83,740,100 is comprised of current budgetary accounts which include appropriated funds for operations, capital and the emergency fund.

As of September 30, 1982, the cash and fund balances of $107,624,370 were made up of $104,375,796 on deposit in the United States Treasury, $2,021,770 on deposit in commercial banks, and $1,226,804 on hand. Of the total, $105,864,128 was comprised of current budgetary accounts which included appropriated funds for operations, capital and the emergency fund.

The emergency fund represents the amount on deposit in the United States Treasury which is to be used "... to defray emergency expenditures and to insure the continuous efficient and safe operation of the Panama Canal when funds appropriated for the operation and maintenance of the Canal prove insufficient for such purposes...."

The postal fund consists of outstanding money orders, postal savings and interest accrued thereon. This fund will remain available until liquidated. The trust fund primarily includes deposits made by customers for future tolls and other service payments.

5. Panama Canal Commission Fund.

The Panama Canal Commission Fund as established by the Panama Canal Act of 1979 (Public Law No.96-70) is made up of receipts deposited in the United States Treasury less appropriation warrants issued during the fiscal year. The balance in this account, $146.3 million as of September 30, 1983 and $143.9 million as of September 30, 1982, is available for future appropriations.

Section 1302 of the Panama Canal Act of 1979 (Public Law No. 96-70) provides that all appropriations necessary to operate the Panama Canal shall be issued from the Panama Canal Commission Fund. The appropriations for fiscal year 1980 were issued to the Commission from the General Fund of the United States Treasury. The status of the amount still owed to the General Fund of the United States Treasury for fiscal year 1980 is as follows:

	Millions of Dollars	
Operating Appropriation	$ 427.2	
Capital Appropriation	36.6	$ 463.8
Repaid to General Fund (07/81)	(350.0)	
Repaid to General Fund (12/82)	(28.2)	(378.2)
Amount owed General Fund of U.S. Treasury as of September 30, 1983		$ 85.6

6. Accounting Changes.

a. "Unobligated operating funds to be returned to the U.S. Treasury" was deleted in fiscal year 1982. This change has no impact on the financial position or operating results of the Commission.

b. The cost of early retirement provisions of the Panama Canal Act of 1979 was added to the balance sheet in fiscal year 1982 as a liability of the Commission for future payments to the United States Civil Service Retirement Fund and an equal amount was recorded as a Deferred Charge. This change has no impact on the financial position or operating results of the Commission.

c. Effective with fiscal year 1982, there was a change in the method of applying the accounting policy for dredging costs. The effect of this change was to increase expense and reduce the capital advance requirement. The precise dollar magnitude of this change cannot be measured since these amounts were not isolated in the Commission's operating accounts. However, the change did not have any impact on net operating revenue. The recurring costs of dredging the waterway are charged to expense. Non-recurring dredging costs for substantial improvements and betterments to the waterway are considered additions to plant and are capitalized and depreciated over their estimated service lives.

d. Amortization of Advances for Capital (see Note 1d) was implemented in fiscal year 1983 based on the following procedure: At the beginning of each fiscal year, an amount equivalent to any capital advance funds disbursed for plant replacement, expansion, or improvement during the previous fiscal year is reclassified and amortized over the average accounting life of assets acquired in the fiscal year in which the funds were expended.

e. The intent of the lock overhauls reserve policy is to normalize costs directly related to the periodic repair and maintenance of the locks. Repair and maintenance costs of caissons, which are used exclusively for lock overhauls, have increased dramatically in recent years. To minimize significant fluctuations in results of operations, these costs are now charged to the reserve. In fiscal year 1983, $754,136 for repair and maintenance of caissons was charged to the reserve for lock overhauls.

7. <u>Other Receivables</u>.

Other receivables represent services provided in connection with ship accidents for which the vessel is considered to be responsible awaiting final settlement. This amount is also included in the computation of estimated liabilities established for ship accident claims.

8. <u>Unrecovered Costs Due from Subsequent Revenues</u>.

Pursuant to the provisions of section 1602(b) of the Panama Canal Act of 1979 (Public Law No. 96-70) the fiscal year 1983 net loss from operations of $4.1 million was deferred as an unearned cost to be recovered from subsequent revenues. Also, in accordance with section 1341(e) of that Act such unearned costs must be deducted from any future net operating revenues due the Government of Panama.

Pursuant to the provisions of Section 1341(e) and Section 1602(b) of the Panama Canal Act of 1979 (Public Law No. 96-70) the net loss of $0.9 million from fiscal year 1981 operations was recovered from fiscal year 1982 operating revenue and the net amount of $0.4 million was paid to the Government of Panama in fiscal year 1983.

9. Interest-Bearing Investment of the United States Government.

The interest-bearing investment of the United States Government in the Panama Canal is determined based on section 1603(a) of the Panama Canal Act of 1979. The interest-bearing investment of the United States Government at September 30, 1983 and September 30, 1982, was determined as follows:

	Millions of Dollars	
Investment at September 30, 1981		$ 128.4
Fiscal year 1982 transactions:		
Disbursements	$ 403.8	
Receipts	(440.1)	
Net property transfers	(2.3)	
Net change		(38.6)
Investment at September 30, 1982		$ 89.8
Fiscal year 1983 transactions:		
Disbursements	$ 446.0	
Receipts	(398.5)	
Repayment to United States Treasury of FY 1980 lapsed funds	(28.2)	
Net property transfers	(0.2)	
Net change		19.1
Investment at September 30, 1983		$ 108.9

10. Accounts Payable - United States Government Agencies.

Included in the accounts payable to United States Government agencies are ship accident and other claims in the amount of $19.1 million for fiscal year 1982 that were forwarded to the Department of Justice in Washington, D. C. after reaching a settlement or receiving a judgment for approval for payment.

11. Ship Accident Claims.

Liabilities arising from ship accident claims are divided into fund and non-fund categories. The fund category is made up of the following:

a. Accidents which occurred prior to October 1, 1979.

b. Accidents which occurred within the locks after September 30, 1979.

c. Accidents which occurred outside the locks after September 30, 1979, for which the claim or estimated liability is $120,000 or less per ship per accident.

Settlement of liabilities for ship accidents which occurred outside the locks where the claim exceeds $120,000 requires specific Congressional approval. Until Congressional action is completed, liabilities for these accidents are booked as non-fund.

12. Payments to the Government of Panama.

Based on Article III and Article XIII of the Treaty, the Government of Panama has received payment for public services, fixed annuity and thirty cents per Panama Canal net ton. In addition to these payments, an amount of $0.4 million was paid to the Government of Panama during fiscal year 1983 in accordance with paragraph 4(c) of Article XIII, which states that an annual amount of up to $10 million will be paid out of operating revenues to the extent that such revenues exceed expenditures of the Commission. This amount is subject to the limitations set forth in section 1341(e) of the Panama Canal Act of 1979 (Public Law No. 96-70).

13. Advances for Capital - Transit Booking System Fees.

During fiscal year 1982, with approval of the Board of Directors, the Commission tested a system whereby shippers, for a fee, could make an advance reservation for vessel transit. The test continued for approximately four months generating funds of $5.9 million. The system was activated in fiscal year 1983 and generated funds of $1.2 million. Such funds are considered capital advances from Canal users. By direction of the Board of Directors, these fees are set aside for capital improvements.

14. Reserve for Casualty Losses.

The reserve for casualty losses at September 30, 1983, of $12.8 million includes $12.5 million for marine accidents and $0.3 million for other casualty losses. As a result of a management analysis of accident frequency and severity, the regular monthly accrual of $0.8 million was adjusted downward to recognize in the reserve account balance the decreased loss trend for larger vessels and the reduced potential loss exposure resulting from the significant drop in overall transit levels. Accordingly, the reserve for marine accidents was adjusted during the fiscal year to maintain a balance of $12.5 million in the account.

The reserve for casualty losses at September 30, 1982, of $9.1 million included $8.8 million for marine accidents and $0.3 million for other casualty losses. The monthly accrual for the reserve for marine accidents in fiscal year 1982 was $1.0 million per month for a total of $12.0 million.

15. Extraordinary Retirements.

During fiscal year 1982, the retirement of SIP-7 Emergency Gates and Miter Gate Latching Devices was approved at the March 1982 meeting of the Board of Directors. The retirement of these systems was recommended by the United States Army Corps of Engineers and reviewed by selected specialists of the Panamanian Society of Engineers and Architects at the request of the Panamanian Board members. The specialists also recommended the elimination of these systems. The net amount charged to operations was $2.6 million.

16. Contingent Liabilities and Commitments.

In addition to recorded liabilities, the estimated maximum contingent liability which could result from pending claims and lawsuits was $9.8 million at September 30, 1983 and $10.9 million at September 30, 1982. In the opinion of management and Commission counsel, these pending claims and lawsuits will be resolved with no material adverse effect on the financial condition of the agency.

Commitments under uncompleted construction contracts and unfilled purchase orders amounted to $30.8 million at September 30, 1983, and $36.4 million at September 30, 1982. Of this amount, $0.2 million in unfilled purchase orders were prepaid as of September 30, 1983 and $0.1 million as of September 30, 1982. In addition, the Panama Canal Commission is liable for an indeterminable amount with respect to death and disability payments under the Federal Employees' Compensation Act.

Cash and negotiable securities of a kind acceptable by the United States Government in the amount of $6.5 million were held by United States depositories designated by the Panama Canal Commission at September 30, 1983 and $7.0 million at September 30, 1982 to guarantee payment by third parties of their obligations.

The Panama Canal Treaty of 1977, Article XIII, paragraph 4(c), provides that an annual amount of up to $10 million per year be paid to the Government of Panama out of operating revenues to the extent that such revenues exceed expenditures. Payment to the Government of Panama is subject to the limitations set forth in section 1341(e) of the Panama Canal Act of 1979 (Public Law No. 96-70). In the event operating revenues in any year do not produce a surplus sufficient to cover this payment, the unpaid balance shall be paid from operating surpluses in future years up to the amount available from these surpluses. As of September 30, 1983, the balance contingently payable to the Government of Panama amounts to $36.9 million. As of September 30, 1982, the balance contingently payable to the Government of Panama amounted to $26.9 million.

17. Treaty Impact.

On September 7, 1977, the United States of America and the Government of Panama signed the Panama Canal Treaty of 1977. The Treaty provided for the establishment of the Panama Canal Commission on October 1, 1979, to assume certain operational responsibilities for the Canal until December 31, 1999. When the Treaty terminates on December 31, 1999, the Government of Panama shall assume total responsibility for the management, operation, and maintenance of the Panama Canal, which shall be turned over in operating condition and free of liens and debts, except as the two Parties may otherwise agree. The effects of these long-range requirements are not considered in the financial statements.

DOD TREATY-RELATED COSTS (SAVINGS) THROUGH FISCAL YEAR 1983

Unaudited

Agency	Prior FY costs	FY 1982 costs[a]	FY 1983 costs
U.S. Army[b]			
Base Operations	$25,550,762	$13,104,872	
Communications	3,818,974	2,335,099	
Commissary	3,275,663	1,132,301	
Transportation	1,711,028	376,918	
Technical Assistance	186,940	15,660	
Health Services	21,608,408	8,769,824	
Disposal of Remains	389,126	230,311	
Criminal Investigations	76,411	44,846	
Tropic Test Center	35,408	-	
Procurement of Equipment	2,958,978	87,811	
Military Construction	34,834,641	958,889	
Military Pay	11,591,617	11,665,596	
Ports	165,868	-	
Total Army	$106,203,824	$38,722,127	c
U.S. Air Force	6,139,241	3,035,890	c
U.S. Navy	452,612	(92,636)	c
DOD Dependents' Schools	4,520,000	304,000	c
Defense Mapping Agency/IAGS	1,158,764	-	c
Total DOD	$118,474,441	$41,969,381	

[a]Includes prior year adjustments
[b]Obligations incurred rather than actual expenditures
[c]Not reported

NON-DOD TREATY RELATED COSTS (SAVINGS) THROUGH FISCAL YEAR 1983

Unaudited

Agency	Prior FY costs [a]	FY 1982 costs	FY 1983 costs	Total costs
State Department	$(3,218,925)	$ [b]	$(1,782,935)	$(5,001,860)
Federal Aviation Administration	(3,563,900)	(3,461,300)	(4,034,800)	(11,060,000)
American Battle Monuments Comm.	392,637	551,120	513,763	1,457,520
Panama Canal Commission	300,000	-	-	300,000
Smithsonian Tropical Research Inst.	560,042	176,421	342,590	1,079,053
Gorgas Memorial Laboratory	(10,572)	(5,808)	(5,829)	(22,209)
Canal Area Court System				
-U.S. Attorney	-	(97,500)	(101,400)	(198,900)
-U.S. Marshall	(118,881)	(10,200)	(43,740)	(172,821)
-Clerk of Court	(129,348	(217,276)	(465,590)	(812,214)
Bureau of Prisons	36,586	160,435	187,000	384,021
Foreign Broadcast Info. Service	9,733	2,500	6,158	18,391
National Oceanic and Atmospheric Admin.	1,377	442	442	2,261
Total Non-DOD	$(5,741,251)	$(2,901,166)	$(5,384,341)	$(14,026,758)

[a]Includes prior year adjustments
[b]Not reported

PROPERTY TRANSFERRED BY THE PANAMA CANAL COMMISSION AND PREDECESSOR ORGANIZATIONS TO THE REPUBLIC OF PANAMA SINCE OCTOBER 1, 1979

Unaudited

Acquisition Cost

Agency	Prior transfers	FY 1982 transfers	FY 1983 transfers	Total transfers
Canal Zone Government and Panama Canal Company	$168,317,629	$ -	$ -	$168,317,629
Panama Canal Commission	3,558,420	5,509,831	442,995	9,511,246
TOTAL	$171,876,049	$5,509,831	$442,995	$177,828,875

Net Book Value

Agency	Prior transfers	FY 1982 transfers	FY 1983 transfers	Total transfers
Canal Zone Government and Panama Canal Company	$ 84,886,222	$ -	$ -	$ 84,886,222
Panama Canal Commission	1,997,412	1,790,579	141,303	3,929,294
TOTAL	$ 86,883,634	$1,790,579	$141,303	$ 88,815,516

PROPERTY TRANSFERRED BY THE DEPARTMENT OF DEFENSE AND THE FEDERAL AVIATION ADMINISTRATION TO THE REPUBLIC OF PANAMA SINCE OCTOBER 1, 1979

Unaudited

Agency	Acquisition Cost			
	Prior FY transfers	FY 1982 transfers	FY 1983 transfers	Total transfers
Department of Defense				
-U.S. Army	$29,175,942	$2,907,116	$ 62,358	$32,145,416
-U.S. Navy	4,698,687	-	-	4,698,687
-U.S. Air Force	-	275,874	-	275,874
TOTAL DOD	$33,874,629	$3,182,990	$ 62,358	$37,119,977
Federal Aviation Administration	829,912	536,476	95,571	1,461,959
TOTAL	$34,704,541	$3,719,466	$157,929	$38,581,936

PANAMA CANAL COMMISSION

APO MIAMI 34011

OFFICE OF THE ADMINISTRATOR

JUL 30 1984

Mr. Frank C. Conahan, Director
National Security and International
Affairs Division
U.S. General Accounting Office
Washington, D.C. 20548

Dear Mr. Conahan:

We have reviewed the GAO draft report entitled "Examination of the Panama Canal Commission's Financial Statements For The Years Ended September 30, 1983 and 1982." The following comments address certain aspects of the draft report. The Commission requests that these comments be included as an attachment to the final report.

Investment of the United States

On pages 2 and 3 of the draft report, GAO discusses its opinion that the Panama Canal Act of 1979 ". . . is not clear on what constitutes the investment on which interest is to be computed." The draft report does not include the Commission's position that ". . . it has correctly interpreted legislation pertaining to computation of interest on investment and has applied it in accordance with the intent of Congress."

The full text of the Commission position, which is germane to this issue and should be available to all report addressees, is set forth below. The comments address whether interest is computed on the total investment of the United States in the Panama Canal or on the net direct investment. These comments are essentially the same as those previously furnished to GAO on four separate occasions. In providing these comments, however, the Commission recommends that GAO update its draft report to reflect actions recently taken on this issue by the House of Representatives.

These actions, which were prompted by the issues raised in GAO report entitled "Return on U.S. Investment in the Panama Canal," (GAO/ID 83-36) dated March 22, 1983, included the conduct of a public hearing on May 16, 1984 by the Merchant Marine and Fisheries Subcommittee on Panama Canal/Outer Continental Shelf at which both GAO and the Commission testified, and passage by the House of Representatives on June 25, 1984 of H.R. 5655, a bill amending the Panama Canal Act of 1979 regarding the payment of interest on the U.S. investment in the Panama Canal. By providing for a prospective change in how interest and the U.S. investment are to be computed, H.R. 5655 upholds the Commission's

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position that it has correctly interpreted legislation pertaining to interest on investment and has applied it in accordance with the intent of Congress. Moreover, passage of the bill by the House of Representatives should resolve GAO's uncertainty on this issue. Accordingly, there would appear to be no further basis for GAO to qualify its opinion on the Commission's financial statements relative to the interest issue.

Section 1603(a) of the Panama Canal Act of 1979 (the Act) provides that:

> ". . . interest shall be computed . . . on the investment of the United States in the Panama Canal as shown in the accounts of the Panama Canal Company at the close of business on the day preceding the effective date of this Act, ..."

While the Act does not specifically mention interest- and non-interest-bearing investment, the legislative history is quite clear in the intent to continue the net direct investment principle established by Section 62, Title 2 of the Canal Zone Code. In House Report No. 96-98 issued by the Committee on Merchant Marine and Fisheries of the House of Representatives to accompany H.R. 111, which became the Act, the following comments are made on page 73 of the sectional analysis.

> "Section 413. Calculation of Interest. — This section defines the basis for computation of interest to be included in the formula for tolls rates in section 412(b), and to be shown in the accounts of the Commission under section 234. In general the base on which interest is calculated will be the same as that established by present law for the Panama Canal Company (2 CZ Code 62), that is the investment of the United States in the Panama Canal as reduced by payments into the Treasury and increased by new appropriations."

Section 413 of H.R. 111 and Section 1603 of the Act are basically the same as they refer to the beginning investment in the Panama Canal; that is, it shall be the amount shown in the Company's accounts on the day preceding the effective date of the Act. In the final conferences there were some changes in this section concerning the rate of interest to be charged but no rejection of the concept of the investment base. The conference report of September 24, 1979 (Report 96-473) had the following comments on page 62:

> "Interest Rate - (Section 1603)
>
> Section 202 of the Senate amendment provided that the rate of interest to be paid by the Panama Canal Commission to the Treasury on the net direct interest-bearing investment of the United States in the

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canal enterprise should be determined by the Secretary of the Treasury. Section 413(d) of the House bill repeated the requirement that interest be paid, but stipulated that it should be calculated at the 'average market yield' rate. (Underscoring supplied.)

"The conferees adopted the House provision on interest but with the Senate language allowing the Secretary of the Treasury to determine the rate. It is the intention of the conferees that the Commission should continue to pay interest at the 'coupon' rate, the rate paid by the Panama Canal Company before October 1, 1979.

"The conferees also modified the language of this section (new Sec. 1603(b) (2)(B) and (C)) to make it clear that those subsections cover non-capital as well as capital assets."

The cited conference report did not change the definition of the base on which interest is computed; it continued the requirement that interest be computed on the "net direct interest-bearing investment." Since conference reports have been recognized by the Comptroller General as the most authoritative single source of legislative history (B-142011, April 30, 1971), the definition of the interest base contained in the House Report No. 96-98 and continued in Conference Report No. 96-473 stands as the intent of Congress. Thus, the Commission believes the legislative history contains a clear statement of Congressional intent.

Further definition and interpretation of the investment base can be obtained from Senate Reservation 6, incorporated in the Resolution of Ratification of the Treaty. Reservation 6 states, in part, that:

"For purposes of this reservation, the phrase 'funds or other assets directly invested' shall have the same meaning as the phrase 'net direct investment' has under section 62 of title 2 of the Canal Zone Code."

Section 62 of Title 2 of the Canal Zone Code specifically provided for interest-bearing and non-interest-bearing elements of the United States investment in the Panama Canal Company.

In prior reports[1/] GAO, by implication, took exception to the Commission classifying the retained earnings of the Panama Canal Company, the predecessor agency, as part of the non-interest-bearing investment. GAO's position was that retained earnings were invested in Canal improvements and since improvements enhance Canal operations, it was

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1/ GAO/NSIAD-83-34 dated September 2, 1983 and GAO/ID-83-36 dated March 22, 1983.

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proper that the U.S. Government expect a return on any such investment. This position appears to contradict principles of interest cost recognition in the GAO Policy and Procedures Manual for Guidance of Federal Agencies which states: "Accumulated net income or deficit should not be included in the interest base."

It should be recognized that the retained earnings invested in the Canal were derived from shipping in the form of profits which, under the law, should not have accrued in the first place since the Canal operation was mandated to break-even. Any additional "investment" on the part of the United States in the waterway would have been properly subject to interest chargeable to users. However, extensive capital programs were accomplished without any appropriation or borrowing of funds from the U.S. Treasury because they were paid for and financed directly by shipping. As such, it would be inappropriate to require the users to pay interest on capital they themselves contributed. This logic conforms with the practice followed by the Canal since 1951 that interest be calculated only on the direct capital contribution or investment of the United States in the waterway. Also it is in line with the guidelines established by GAO for Federal agencies. The relationship between users of the Canal and the United States, as operator of the Canal, has not changed with the treaty and there is no apparent reason to change the traditional method of calculating interest.

In summary, the Commission established the investment base in compliance with Section 1603 of the Act recognizing the intent of Congress specified in the legislative history of the Act and Reservation 6 to the Treaty. The Commission sees no need for clarification of the existing law regarding this issue. Additionally, the interest-bearing and non-interest bearing elements of the net direct investment were recognized in the Commission's Accounting Principles and Standards Statement approved by the Comptroller General on September 14, 1982.

GAO comment:

Our opinion that the act is not clear on what constitutes the U.S. investment on which interest is to be computed encompasses two separate and distinct issues. The first concerns whether interest should be computed on the total or net direct U.S. investment. Although we continue to believe it would be desirable for the Congress to clarify its intent with respect to whether the Commission should compute interest on the total or net direct U.S. investment, we now do not disagree with the Commission's practice to compute interest on the net direct U.S. investment. The second concerns whether interest collections deposited to the Panama Canal Commission Fund should have the effect of reducing the investment base on which interest is computed. It is primarily this issue, which had reduced the interest-bearing investment base by $42.2 million at September 30, 1983 and reduced fiscal year 1983 interest revenue by $4.3 million, that led to our qualified opinion.

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The bill amending the Panama Canal Act of 1979 regarding payment of interest on the U.S. investment in the Panama Canal (H.R. 5655) was not acted on by the Senate in the 98th Congress but was reintroduced in January 1985. If enacted, the legislation would clarify how interest should be computed and prevent further erosion of the U.S. investment. The bill's sponsor, in reintroducing the legislation, stated that it was clearly the intent of the authors of the Panama Canal Act of 1979 that the interest payment on the U.S. investment would be paid directly into the general fund of the U.S. Treasury. He further stated that the bill did not address the broader question concerning disposition of interest (currently in excess of $50 million) already deposited to the Panama Canal Commission Fund and recoupment of lost revenues resulting from the corresponding understatement of the interest-bearing U.S. investment. We believe this matter can be corrected by requiring the Panama Canal Commission to

--request appropriations to transfer to the general fund of the U.S. Treasury those interest collections already temporarily deposited in the Panama Canal Commission Fund, and

--restore the interest-bearing investment account by the amount so transferred.

Capitalization Policy

On pages 1 and 2 of the draft report, GAO discusses its opinion that in regards to certain projects, ". . . the Commission's decision to expense rather than capitalize the cost of these projects is not in keeping with [its] approved capitalization policy." The Commission holds that its capitalization policies have been properly applied.

The projects questioned by GAO are identified as the navigational projects of La Pita Hill, Lirio Point and Mamei Curve and the power generation project at Madden Dam. The La Pita Hill and Lirio Point projects did not contribute to increasing Canal capacity, but were prudent efforts under the Bank Stabilization Program to avoid the possibility of catastrophic landslides into the channel. These two projects constituted earth-moving projects, not dredging, falling under the category of "Civil Works." As a secondary benefit, these projects also extended the pilots' lines-of-sight at these bends in the channel and added a modicum of safety to their control of vessels. The Mamei

Curve project consisted of piecemeal dredging work accomplished with normal work force and equipment which also did not result in increased Canal capacity.

The power generation project involved the rewinding of generators at Madden Dam hydroelectric power plant. The work was necessary to maintain the unit in an operational state and, as a secondary benefit, provided the opportunity to modify the unit to match the peak generation of the turbines when lake levels permit.

The Commission's accounting policies, including those on capitalization, have been approved by GAO. Present questions hinge on the interpretation of what constitutes a substantial improvement. The Commission clarified its written interpretation by further defining "substantial improvements and betterments" to preclude misunderstandings. This clarification, provided to GAO, was necessary because questions of interpretation or application of the Commission's policy cast an unnecessary doubt on the validity of amounts stated as contingently payable to the Government of Panama under the 1977 Treaty.

Had the Commission considered all or any part of these projects subject to financing through the Capital Program, such action would have been anticipated in its Capital Budget. The resultant change in operating costs would have been offset by a necessary comparable increase in the Advances for Capital and there would have been no change in the amount of net income payable to the Government of Panama.

GAO comment:

We do not take exception with the Commission's capitalization policy, merely with the way it has been applied to certain projects. In our opinion, they provided major long-term improvements and therefore should not have been expensed. The navigational projects in question substantially widened and straightened the canal, removed a one-way traffic restriction, and improved canal pilots' lines of sight for safer operations. The power generation project significantly uprated unit capacity and service life.

Amortization of Capital Advance

On page 2 of the draft report, GAO takes exception to the Commission's method of amortizing expended capital advance funds. The Commission amortizes utilized capital advance funds through credits to operations to prevent Canal users from paying twice for assets acquired, at least in part, from capital advance monies. The time period for this amortization is based upon an average accounting life for all assets acquired including such items as housing improvements funded from capital monies but written off to operations immediately.

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Inclusion of the immediate write-off items in the computation results in a shorter amortization period than the service lives of the majority of assets acquired. This method is considered appropriate since it gives consideration to the actual costs of all capital items acquired with capital advance monies, including those written off in the year of acquisition. In addition, this method serves to smooth the credit to operations after a finite number of years. The Commission believes its method is reasonable in distributing the costs over a span of several years.

It should be noted that housing improvement costs are being included in the Commission's operating expense budget request for fiscal year 1986. This will eliminate the requirement to include these costs in the amortization calculation in the future if approved.

GAO comment:

The Commission should not include immediate write-off items in its amortization of expended capital advance funds. The Commission fully considers these costs in financing its capital program exclusive of its capital advance funding requirement. Since capital items written off in the year of acquisition are not financed by capital advance monies, it is not appropriate to include them in the amortization of such fund expenditures. The shorter amortization period used by the Commission as the result of including immediate write-off items has the effect of understating fiscal year 1983 operating expenses and net operating loss by $421,534. As of October 1, 1983, the method of accounting for the amortization of advances for capital was changed and we concur with the change.

Location of Internal Audit Function

Page 3 of Appendix I of the draft report reiterates GAO's observation that the organizational mislocation of the internal audit function in the Office of Financial Management has not been changed. Earlier this fiscal year, the internal audit function was realigned as a separate independent unit responsible directly to the Administrator of the Panama Canal Commission. The Commission requests that the draft report be revised to show the independent status of the internal audit function.

GAO comment:

The report was revised to show the organizational change.

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Compliance with Laws and Regulations

In Appendix II of the draft report, GAO states its opinion that the Commission in 1983 had not complied with the terms and provisions of laws and regulations concerning the public service payments to Panama, the payment of 1982 net operating revenues to Panama, the recovery of costs of capital assets, and the determination of the investment base. For reasons presented below, the Commission does not agree with GAO's opinion and requests that the adverse opinion concerning the Commission's noncompliance with laws and regulations be deleted from the report.

Public Service Payments to Panama. The draft report characterizes the Commission as being in violation of the Panama Canal Act of 1979 by continuing to pay Panama for public services at the same rate as in past years. Since the Commission's responsibility under the Act is for the making of the payments only, the Commission is in full compliance with the law with respect to meeting its responsibility. The Department of State, representing the U.S. Government, has responsibility for reaching agreements with Panama on the reimbursement to be made for each three-year period following the initial three years, with the Comptroller General being responsible for annual audits of payments against the actual costs incurred by Panama in providing the service. The decision to continue paying Panama at the $10 million annual rate was made after consultation with both the Department of State and the GAO. That decision, which can be said to have Congressional approval as the result of the authorization and appropriation process for three fiscal years, takes into account that (1) in the absence of meaningful cost data being provided by Panama, there can be no basis for adjustment of the $10 million annual payment, and (2) since these public services are being received from Panama, payment must continue as the services are critical to the efficient operation of the Canal. If the discussion of public service payments is left in the report, it should recognize that the Commission is meeting its responsibilities in this regard.

GAO comment:

It is not our intent to characterize the Commission as being in violation of law by continuing to pay Panama for public services at the same rate as in past years. Rather, the purpose of the report comments is to point out not whether, but how, the Commission is meeting its payment responsibilities in the absence of meaningful cost data being provided by Panama. To alleviate the Commission's concerns, we have revised our discussion of the matter to eliminate any suggestion of wrongdoing on the Commission's part.

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Payment of Net Operating Revenues to Panama. In its draft report GAO takes exception to the Commission proceeding with the $378,635 net revenue payment to Panama without having GAO's validation of the amount due Panama from 1982 operations. Further, the draft report states that GAO is, at this date, still unable to validate this payment to Panama. The cited reason for being unable to validate an operating result for an accounting period ending close to 21 months ago is that there may be a material understatement of expense depending on how the Congress determines that interest on the U.S. investment should be computed. It is inconceivable that the Commission would be expected to withhold payment to Panama indefinitely based on some uncertainty that GAO perceives in the law, particularly one which requires legislation to eliminate.

As discussed above, the Commission holds that it has correctly interpreted legislation pertaining to the investment base and has applied it in accordance with the intent of Congress. The GAO has reported its opinion on this issue to the Congress on several occasions in the past and until recently Congress has chosen to let the legislation stand as is. Recent Congressional hearings on this matter, passage of H.R. 5655, and even GAO's testimony and recommendations during the aforementioned hearings clearly indicate that any change in the treatment of interest is to be made prospectively and not retroactively. For these reasons, the Commission holds that it was in compliance with Public Law 98-63 in making the subject payment to Panama. Accordingly, the Commission recommends that the GAO draft report be updated to recognize these facts.

GAO comment:

The report has been revised to add that legislation is pending which would change how interest and the interest-bearing U.S. investment are computed. Since this legislation resolves only part of our uncertainty on this issue and our qualification on the capitalization issue remains, we cannot validate the Commission's $378,635 net revenue payment to Panama from 1982 operations.

Recovery of Costs of Capital Assets. Although not altogether clear, GAO seems to be alleging that the appropriations currently being spent by the Commission for the acquisition of new assets for the Canal will not be recovered by the end of the Treaty. If so, GAO is in error since by law all appropriations to the Commission must be derived from receipts of the Canal. This has the effect of requiring Canal users to pay for the cost of capital assets in advance of their actual acquisition. Accordingly, it is inconsequential, except for bookkeeping purposes, whether the depreciable service lives of new assets extend beyond December 31, 1999 or not.

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GAO comment:

The Commission correctly assumes we are making the point that its acquisition of new capital assets funded by current appropriations will result in costs that will not be fully recovered by the end of the Treaty. However, we do not intend this as criticism that the Commission is not complying with existing law, but rather to show what the effect is of the Commission depreciating new acquisitions over their estimated service lives. We acknowledge that the Commission finances its capital appropriations from Canal receipts. It should be noted, though, that a major portion of these receipts represents depreciation cost recoveries of capital assets acquired by the predecessor Panama Canal Company. If receipts representing cost recovery of assets funded by the predecessor Panama Canal Company are excluded as a financing source for the Commission's capital improvement program, the cost of newly acquired assets will not be fully recovered.

GAO note: This matter has been deleted from this report. It will be the subject of a separate GAO report.

Other Matters

On page 4 of the draft report, the opinion paragraph should recognize the policy change concerning the repair and maintenance costs of caissons as described in note 6e to the financial statements.

GAO comment:

Our opinion paragraph was revised to recognize this policy change.

Thank you for providing us the opportunity to comment on the draft report before its publication. The Commission appreciates your efforts to have the report published at the earliest possible date.

Sincerely yours,

D. P. McAuliffe
Administrator

UNITED STATES GOVERNMENT

GENERAL ACCOUNTING OFFICE

Memorandum

December 26, 1984

TO : Director, NSIAD - Frank C. Conahan

FROM : General Counsel - Harry R. Van Cleve

Harry R. Van Cleve

SUBJECT: Return on U.S. Investment in Panama Canal- B-214242-O.M.

This responds to a request from the Development Assistance group of your division and the Latin America Office for our opinion on two questions concerning how interest should be computed and paid on the United States investment in the Panama Canal.1/ Our findings have been discussed informally with your staff, and the issues were discussed in testimony by Associate Director Samuel W. Bowlin ("GAO Views Concerning Return on U.S. Investment in the Panama Canal") presented on May 16, 1984, before the Subcommittee on Panama Canal/Outer Continental Shelf, House Committee on Merchant Marine and Fisheries. Since the issues are likely to be recurring ones in view of the Panama Canal Commission's apparent disagreement with GAO's position, the purpose of this memorandum is to set forth in more detail the basis of and support for our conclusions.

As will be discussed in more detail below in answer to the specific questions presented, the Panama Canal Treaty and the Panama Canal Act of 1979 both contemplated that an amount representing interest on the investment of the United States should be included in tolls charged by the Panama Canal Commission. The Treaty and the Act also contemplate that such interest would inure to the benefit of the United States taxpayer by being deposited into the Treasury. However, on the basis of a literal reading of the Act, the

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1/ The original request (dated January 20, 1984) raised several additional questions as well. However, in subsequent discussions between our respective staffs it was agreed that our response would be limited to the two questions addressed in this memorandum.

Panama Canal Commission has retained interest payments in the Panama Canal Commission Fund in the Treasury instead of depositing them in the general fund of the Treasury. Retention in the Panama Canal Commission Fund results in the interest payments not accruing to the benefit of the U.S. taxpayers but being used instead to gradually repay the amount previously invested in the Canal by the United States.

The Commission's treatment of interest on the United States investment has resulted in qualified GAO opinions on Commission financial statements and reports to the Congress suggesting clarification of the Panama Canal Act. Although legislative clarification would be desirable, this memorandum explains how the Commission can comply with the evident congressional intent under the existing law.

The specific questions and our answers are set forth below.

Question 1: If interest collections (along with other receipts) are to be deposited to the Panama Canal Commission Fund, is the PCC required to subsequently pay/transfer the interest collections to miscellaneous receipts of the Treasury? If so, when?

Answer: The Panama Canal Act of 1979 (Act) requires the Panama Canal Commission to deposit its toll collections into the Panama Canal Commission Fund (Fund). Toll rates include interest on the United States investment in the Canal. Although not expressly stated in the Act, Congress intended that the Commission transfer the interest receipts from the Fund into the general fund of the Treasury as miscellaneous receipts.

By way of background, it should be understood that technically, the Panama Canal Commission Fund exists as an account in the United States Treasury. 22 U.S.C. § 3712(a). Although in the Treasury, the Fund constitutes a distinct pool of funds which are used exclusively to pay the Commission's expenses. Section 1602 of the Act provides, in effect, that all of the costs of maintaining and operating the Canal are to be covered by the tolls the Commission collects. 22 U.S.C. § 3792(b). The Congress established the Fund as part of a statutory scheme designed to insure that the Canal's operations would be self-sustaining.

To facilitate the Canal's operation on a self-sustaining basis, the Fund operates as a revolving fund. At the same time, the Congress controls Commission expenditures from the Fund through the appropriations process. The Act requires the Commission to deposit all tolls collected into the Fund. 22 U.S.C. § 3712(b). The Congress must appropriate the amounts collected as tolls "out of the fund" before the Commission may expend them. 22 U.S.C. § 3712(c)(1). Consistent with the self-sustaining concept, the Act limits the amounts of Commission appropriations which may be derived from the Fund for a fiscal year to the amount of revenues deposited into it during that fiscal year plus the amount of unexpended deposits from prior years. 22 U.S.C. § 3712(c).

Thus, although situated in the Treasury, the Fund represents monies which are separate and apart from those normally appropriated by the Congress to fund the Government's activities--the general fund. Accordingly, what is under discussion here is the Commission's authority to deposit interest collections into the Fund and whether it is required to transfer them from the Fund into the general fund as miscellaneous receipts.

Two Act provisions, read together, clearly indicate that the Commission is required to deposit interest collections into the Fund. As noted, section 1602(b) of the Act, 22 U.S.C. § 3792(b), provides that the Commission is to prescribe tolls for use of the Canal at rates calculated to produce revenues to cover as nearly as practicable all costs of maintaining and operating the Canal, including interest on the United States investment. Section 1302(b), 22 U.S.C. § 3712(b), specifies that tolls for the use of the Panama Canal "shall be deposited in the Treasury in the Panama Canal Commission Fund." Thus, under the Act, the Commission receives as part of its toll collections an amount sufficient to cover the interest on the United States investment, and it is required to deposit that amount into the Panama Canal Commission Fund along with the rest of its toll collections.

The Act does not state what the Commission should do with respect to interest collections after they are deposited into the Fund. However, the legislative history indicates that they should be transferred from the Fund into miscellaneous receipts, because the Congress intended that interest collections should inure to the benefit of the U.S. taxpayer.

Before the Panama Canal Treaty was executed in 1977, the Panama Canal Company, which operated the Canal, was required to pay interest on the U.S. investment into the Treasury. C.Z. Code tit. 2, § 62(e) (1962). When the Senate ratified the Treaty, it did so with the express reservation that:

> "After the date of entry into force of the Treaty, the Panama Canal Commission shall, unless otherwise provided by legislation enacted by the Congress of the United States of America, be obligated to reimburse the Treasury of the United States of America, as nearly as possible, for the interest cost of the funds or other assets directly invested in the Commission by the Government of the United States of America and for the interest cost of the funds for other assets directly invested in the predecessor Panama Canal Company by the Government of the United States of America and not reimbursed before the date of entry into force of the Treaty. * * *" Panama Canal Treaty, September 7, 1977, United States-Panama, annex, TIAS 10030.

After the Senate ratified the Treaty, it became necessary for the Congress to enact legislation implementing it. The implementation bill introduced on behalf of the Administration, H.R. 1716, contained a provision which would have eliminated the right of the United States to receive interest on its investment in the Canal. H.R. 1716, 96th Cong., 1st Sess. § 202 (1979). The administration recommended elimination of the interest obligation because it believed that this would help keep the Commission self-sustaining and would avoid an uneconomic increase in tolls. H.R. Doc. No. 39, 96th Cong., 1st Sess. 75 (1979). The Congress considered the administration's proposal but did not adopt it.

The Act's provisions governing the inclusion of interest in the toll base and the calculation of interest come from the House bill, H.R. 111. The bill's primary sponsor, Representative Murphy, was the Chairman of the House of Representatives subcommittee with oversight responsibilities over the Canal, the Subcommittee on the Panama Canal and Outer Continental Shelf, Committee on Merchant Marine and Fisheries. In explaining his bill's interest provisions during the floor debates, Chairman Murphy stated:

> "The question has been raised in the course of deliberations on H.R. 111 as to whether interest on the investment of the United States in the canal organization is a proper element in the tolls formula. The discontinuance of this element in the tolls formula, as provided in the administration draft of legislation, would have deprived the Treasury of some $400 million over the next 20 years. Testimony received by the committee in the hearings on the bill overwhelmingly supports the view that interest is a normal cost of operation that should be recovered from user charges. Furthermore collection of interest by the United States constitutes one of the very few benefits that can be provided to U.S. taxpayers under a treaty arrangement that is oriented primarily to satisfaction of the financial goals of Panama.
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> "Interest on the cost of capital in the canal enterprise has been considered a cost not just since the formation of the present corporate organization that operates the canal but rather since the time the canal was completed and opened to traffic. According to documentation introduced into the record of the hearings on H.R. 111, before 1950 canal tolls were calculated to cover a return of interest at 3 percent per annum upon the investment of the United States in the canal enterprise as a whole. Provision for payment of interest by canal users recognized that the Panama Canal was more than a public works project for the benefit of the United States but that the benefits were also enjoyed by the interoceanic commerce of the entire world." 125 Cong. Rec. 11953 (1979).

Comments by other members of the House of Representatives during debate on H.R. 111 further indicate that the House did not intend to follow the Administration's proposal, but rather intended to legislate the payment of interest on the U.S. investment into the U.S. Treasury for the benefit of the taxpayer. For example, in the course of remarking upon the extent to which the Treaty and the bill would place a financial burden on the taxpayer, Representative Dannemeyer stated:

"* * * H.R. 111 improves upon the President's original proposal to the extent that the United States would still collect the $20 to $25 million a year interest it has been collecting on its canal investment * * *." 125 Cong. Rec. 15760 (1979).

Similarly, Representative Levitas remarked:

"It is interesting to note several things at this point. One, the Panama Canal Commission has been completely self-sufficient financially since it began in 1951. Although it is authorized to seek appropriations to cover both losses and capital needs and to borrow up to $40 million, it has never done so. Also, during its 28 years of existence, the Commission has paid back to the U.S. Treasury $40 million in dividends as a return on the Government's investment in the canal.

"As a matter of fact, under this legislation, the United States will continue to receive interest payments on our investments in Panama into the Treasury for the next 20 years so that, at the end of that period, we will have made a profit of $382 million on all our nonmilitary outlays in Panama." 125 Cong. Rec. 16015 (1979).

Representative Bowen stated during debate on the bill:

"I would like to point out to some of you, those of you who have read the ads that have circulated around the Nation--you know, the gold brick ads, the ones that talk about $4 billion, $20 billion, all the different amounts of money that somehow are alleged to be a part of the cost of this operation--to remind you that if we pass the legislation we will still receive interest on our investments in Panama.

"Currently they are running at about $20 million a year. At that rate by the end of the century we will have received a profit of some $262 million on all our nonmilitary outlays in Panama since 1903, and I call that a good deal.

* * * * *

"If we pass this legislation, we get continued payments of interest to us, interest payments which, as I say, by the turn of the century will make us a substantial profit on all of our investments down there. Just count all the investments. Count the $387 million we paid to construct the canal, count the $40 million we paid to France for the concession, count the first $10 million we paid to Panama for the right to use the canal. Count every piece of property we bought down there, every stick and stone we spent a dime on, count every bit of it, and then count the revenues that have come into our Treasury. Count the profits that came in up until 1950 when we put profits directly into the Treasury. Count the interest payments after that time that have come and still will come in, and when you add them up, by the end of this century your taxpayers and mine, the citizens of this country will be making a profit of somewhere between $200 million and $300 million on the canal enterprise." 125 Cong. Rec. 17563 (1979).

These excerpts from the House debate indicate clearly that the intention of the House of Representatives was that interest on the U.S. investment be paid into the Treasury for the benefit of the United States.

The language of the interest provisions in the Senate bill was somewhat different. Nevertheless it clearly indicated that the Senate's intent with respect to the treatment of interest on the U.S. investment was the same as that of the House of Representatives. The Senate bill would have amended 2 CZC § 62(e), the provision cited above which required the Panama Canal Company to pay interest into the Treasury, so as to make the payment requirement applicable to the Commission. It provided as follows:

"(a) Subsection (e) of section 62 of title 2 of the Panama Canal Code is amended to read as follows:

"(e) In order to reimburse the Treasury, as nearly as possible, for the

> interest cost of the funds or other assets directly invested in it, the Commission shall pay interest to the Treasury on the net direct investment of the Government in it as defined by subsections (a), (c), and (d) of this section, and shown by the receipt described therein at a rate determined by the Secretary of the Treasury." H.R. 111, 96th Cong., 1st Sess., § 202, 125 Cong. Rec. 20759 (1979).

The conference committee adopted the House provisions, which were less explicit on the issue of payment of interest by the Commission. In commenting on the "calculation of interest" provision, which is now 22 U.S.C. § 3793, the conference report stated:

> "Interest Rate--(Section 1603)
>
> "Section 202 of the Senate amendment provided that the rate of interest to be paid by the Panama Canal Commission to the Treasury on the net direct interest-bearing investment of the United States in the canal enterprise should be determined by the Secretary of the Treasury. Section 413(d) of the House bill repeated the requirement that interest be paid, but stipulated that it should be calculated at the 'average market yield' rate.
>
> "The conferees adopted the House provision on interest but with the Senate language allowing the Secretary of the Treasury to determine the rate. It is the intention of the conferees that the Commission should continue to pay interest at the 'coupon' rate, the rate paid by the Panama Canal Company before October 1, 1979." H.R. Rep. No. 473, 96th Cong., 1st Sess. 62, reprinted in 1979 U.S. Code Cong. & Ad. news 1137, 1145.

Thus, the conference report suggests that the conferees accepted what both Houses had intended--that the Commission pay interest collections into the Treasury for the benefit of the United States.

In order to carry out Congress' intent that interest on the U.S. investment in the Panama Canal accrue for the benefit of the United States Treasury, the Commission should transfer interest collections from the Panama Canal Fund into the appropriate miscellaneous receipts account of the Treasury. Although the Panama Canal Fund is technically "in the Treasury," when interest collections stay in the Fund they do not benefit the Treasury in the sense Congress intended. The legislative history discussed above shows that the Congress included interest on the U.S. investment in the Canal toll base so that the Treasury would receive a return on funds appropriated from it for investment in the Canal which would ultimately benefit the taxpayers.

As we discussed earlier, the financial system established for the Commission is designed to make its operations self-sustaining. The Canal users provide the funds for the Commission's expenses through their toll payments. The tolls collected from the Canal users are deposited into the Fund and then appropriated out of the Fund to pay the Commission's expenses. Thus, monies in the Fund are used only to pay the Commission's operating expenses--something which was not intended to be the responsibility of the Treasury or the taxpayers.

If interest collections are not transferred from the Fund to miscellaneous receipts, they could be appropriated along with other collections only for the purpose of paying the Commission's expenses. Using interest collections for that purpose does not benefit the Treasury or alleviate the burden of the taxpayer since the Canal users, and not the taxpayer, are supposed to bear the expenses of the Commission's operations. If the interest collections are not appropriated but remain in the Fund, they similarly do not benefit the taxpayer. It is only when the funds are transferred into miscellaneous receipts so that they can then be reappropriated for some other purpose that they really inure to the benefit of the taxpayer in the sense that Congress intended. Accordingly, we conclude that the Commission should transfer interest collections in the Panama Canal Fund to miscellaneous receipts.

No amendment to the Panama Canal Act is necessary in order for the Commission to make the interest collection transfers.[2] In our view, the provisions of the Act discussed above provide sufficient authority. Generally, the Commission receives an annual lump-sum appropriation derived from the Panama Canal Fund for its expenses. Since a lump sum appropriation is available for any authorized purpose of the agency receiving it, the Commission could, based on the authority of the cited Panama Canal Act provisions, transfer interest collections in the Fund into miscellaneous receipts pursuant to its annual appropriation.

To remove any doubt in this area, the Commission could specifically request that the Congress provide for interest transfers when it annually considers the Commission's authorization and appropriations bills. This would be in accord with the suggestion made in Mr. Bowlin's May 16 testimony referred to earlier. Alternatively, an amendment to the Panama Canal Act would seem desirable in view of the long-standing disagreement between our Office and the Commission on the transfer question.

With regard to your question as to when the Commission should make such transfers, we do not believe that there is any legally mandated time period in which interest collections must be transferred from the Fund into miscellaneous receipts. However, in light of the congressional intent that such collections inure to the benefit of the taxpayer, we believe transfers should be made as soon as is reasonably practical for the Commission to do so. This would also be consistent with the intent of 31 U.S.C. § 3302(b) (1982).

<u>Question 2</u>: If interest collections are not required to be transferred from the Fund to miscellaneous receipts, is it reasonable to interpret (as the Commission has done) that the interest-bearing investment base--on which future interest is computed--should be decreased for interest

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2/ Page 12 of GAO's report "Examination of the Panama Canal Commission's Fiscal Year 1980 Financial Statements and Treaty-Related Issues" (ID-81-49, June 29, 1981) states that an amendment to the Panama Canal Act would be necessary in order for the Commission to transfer interest recovered through tolls into miscellaneous receipts. After further considering this question in preparing this memorandum, we are now of the opinion that legislation is not necessary from the strictly legal perspective, although it may be desirable in practical terms because of the Commission's disagreement with our conclusion.

collections deposited to, but not paid out of, the Panama Canal Commission Fund? Are other interpretations more reasonable?

<u>Answer</u>: We concluded in answering Question 1 that interest collections should be transferred from the Fund into miscellaneous receipts. Nevertheless, whether or not the Commission effects the transfer, its interpretation that the computation base on the U.S. investment should be decreased for interest collections deposited into the Fund is consistent with the Act's language. As explained below, the Commission's interpretation appears to be unreasonable because it is erroneously failing to transfer interest collections as the Act contemplates. If the Commission made the transfers, then decreasing the investment base not only technically follows the Act's provisions but is logical as well.

Section 1603 of the Act, 22 U.S.C. § 3793, prescribes how the Commission is to determine the investment base. It provides in part:

> "(a) For purposes of sections 3721 and 3792 of this title, interest shall be computed, at a rate determined by the Secretary of the Treasury, on the investment of the United States in the Panama Canal as shown in the accounts of the Panama Canal Company at the close of business on the day preceding October 1, 1979, and as adjusted in accordance with subsections (b) and (c) of this section. Capital investment for interest purposes shall not include any interest during construction.
>
> "<u>Increases and decreases in investment of United States</u>
>
> "(b) <u>The investment of the United States described in subsection (a) of this section</u>--
>
> "(1) shall be increased by--
>
> "(A) the amount of expenditures from appropriations to the Commission made on or after October 1, 1979, and
>
> "(B) the value of property transferred to the Commission by any other department or agency of

the United States, as determined in accordance with subsection (c) of this section; and

"(2) shall be decreased by--

"(A) the amount of the funds covered into the Treasury pursuant to section 3712 of this title.

"(B) the value of property tranferred to the Republic of Panama pursuant to this chapter or any other Act on or after October 1, 1979, and

"(C) the value of property transferred by the Commission to any other department or agency of the United States." (Emphasis added.)

Section 3712 indicates that toll revenues, including interest collections, are to be considered "covered into the Treasury" for purposes of decreasing the U.S. investment under section 3793(b)(2) when they are deposited into the Panama Canal Commission Fund. Section 3712(b) provides:

> "[T]olls for the use of the Panama Canal and all other receipts of the Commission * * * shall be deposited in the Treasury in the Panama Canal Commission Fund." (Emphasis added.)

The inclusion of the phrase "in the Treasury" in conjunction with the reference to the Panama Canal Commission Fund indicates that for purposes of determining the U.S. investment base, Congress considered deposits into the Fund to be deposits into the Treasury. Accordingly, the Commission is technically correct when it decreases the U.S. interest-bearing investment base on its books for interest collections deposited into but not transferred out of the Fund.

The problem is that the Commission's failure to transfer interest collections to miscellaneous receipts artificially lowers the U.S. investment base. This in turn causes the Commission's interest collections which are calculated upon that base to be too low. As noted, 22 U.S.C. § 3793(b)(2) provides that the investment base should be decreased for interest collections deposited into the Fund. Section 3793(b)(1)(A) provides that the investment base should be increased for expenditures from appropriations (from the Fund). Since interest collections are deposited into the Fund the base is decreased, but since currently they are not expended from the Fund (into miscellaneous receipts, as we think Congress intended) there is no corresponding increase in the investment base. What results is a disproportionate decrease annually in the interest base, which means that the Commission is not collecting as much interest on the U.S. investment as it should. This problem could be corrected simply by the Commission's transferring interest from the Fund into miscellaneous receipts, as discussed above.

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