

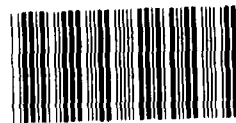
GAO

Report to the Ranking Minority Member,
Committee on Budget, U.S. Senate

May 1987

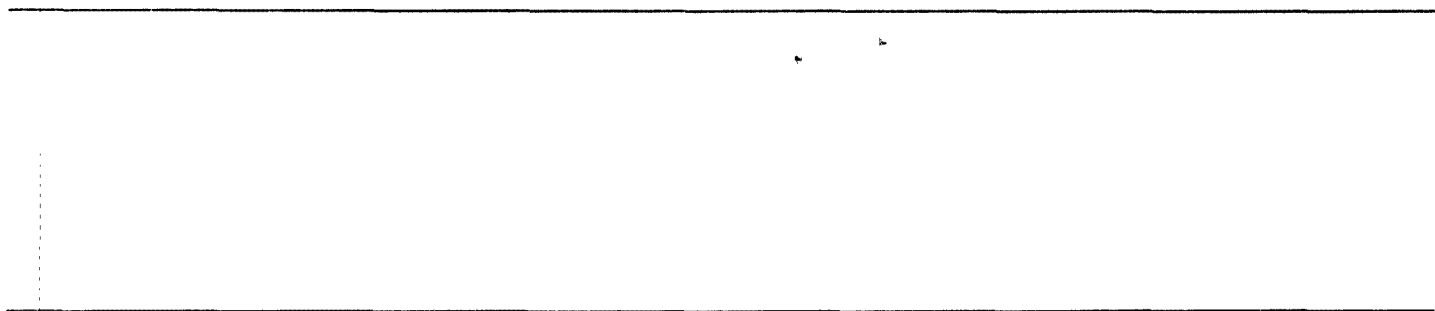
DOD INFLATION

DOD's Inflation Dividends—May 1987 Update



133053

039001



**National Security and
International Affairs Division****B-222917**

May 8, 1987

The Honorable Pete V. Domenici
Ranking Minority Member
Committee on Budget
United States Senate

Dear Senator Domenici:

On April 23, 1987, you asked us to update our estimates of potential excess inflation funds within the Department of Defense's (DOD's) budget. In September 1986, we estimated a \$3.5 billion inflation dividend for fiscal year 1987 nonpay, nonfuel accounts based on the August 1986 Office of Management and Budget (OMB) revised inflation rate estimates and the fiscal year 1987 budget request. Both of these factors have now changed, with appropriation action taken on the budget and OMB having issued revised inflation estimates.

We recalculated the amount of DOD's fiscal year 1987 inflation dividend based on the actual appropriated amounts and the revised OMB inflation projections included in DOD's January 1987 budget submission. Our revised estimate for nonpay, nonfuel accounts is \$3.0 billion. The Congress reduced the fiscal year 1987 nonpay, nonfuel requests by \$2.4 billion for excess inflation. In total, this amount is \$0.6 billion less than the amount we calculated for the fiscal year 1987 nonpay, nonfuel appropriations. Appendix I contains a table comparing the revised estimate of the inflation dividends with congressional reductions for inflation adjustments by account. Appendix II discusses the methodology used to derive these estimates.

We also reviewed the fuel accounts and have determined that they have no further dividends. Our revised estimate for fuel accounts, based on actual amounts appropriated and OMB's January 1987 inflation projections is \$1.4 billion. DOD had reported \$1.8 billion in excess fuel inflation funds for fiscal year 1987 and \$1.3 billion for fiscal year 1986, for a total of \$3.1 billion. The Congress reduced the fiscal year 1987 fuel requests by \$3.0 billion. If OMB's January inflation projections for fiscal year 1987 prove to be correct, the congressional reductions of approximately \$1.8 billion for fiscal year 1987 are in excess of the \$1.4 billion fuel inflation dividend that we calculated.

We discussed the inflation calculations with the Director, Plans and Systems, Office of the Deputy Assistant Secretary of Defense, Program/

Budget, who is responsible for inflation adjustments. The Director agreed with the procedures used to derive the amounts. The Director stressed that the data for fiscal year 1987 is incomplete until all the funds are expended, and the inflation estimates may be revised over that period.

We hope that this information will be of use in your review of the DOD budget. Copies of this report are being sent to the Chairmen, House and Senate Committees on Appropriations, Senate Committee on Governmental Affairs, and House Committee on Government Operations. Copies are also being sent to other interested parties and will be provided to others upon request.

Sincerely yours,

David W. Little
Frank C. Conahan *for*
Assistant Comptroller General

Contents

Letter 1

Appendix I 6
Estimated Inflation
Dividend Amounts for
Fiscal Year 1987

Appendix II 9
Methodology for
Determining DOD's
Inflation Dividend for
Fiscal Year 1987

Abbreviations

DOD Department of Defense
GAO General Accounting Office
OMB Office of Management and Budget

Estimated Inflation Dividend Amounts for Fiscal Year 1987

Dollars in millions			
Account	Dividend Calculated in April 87	Amount of Congressional Inflation Reduction	Difference Between Dividend and Reduction
Summary			
Operations & Maintenance	\$604.8	\$621.8	\$(17.0)
Military Construction	67.7	.0	67.7
Major Commodities	1,332.4	820.3	512.1
Nonmajor Commodities	337.1	243.5	93.6
Family Housing	43.4	.0	43.4
Military Personnel	111.7	39.0	72.7
Research, Development, Test, and Evaluation	488.5	699.0	(210.5)
Total	\$2,985.6	\$2,423.6	\$562.0
Operations & Maintenance (Nonpay, Nonfuel)			
Army	\$156.3	\$135.1	\$21.2
Navy	170.2	230.6	(60.4)
Marine Corps	17.2	13.2	4.0
Air Force	154.9	153.7	1.2
Defense Agencies	58.1	47.3	10.8
Army Reserve	6.6	5.3	1.3
Navy Reserve	10.1	6.3	3.8
Marine Corps Reserve	.8	.0	.8
Air Force Reserve	6.5	6.3	.2
Army National Guard	13.7	11.5	2.2
Air National Guard	10.4	12.5	(2.1)
Total	\$604.8	\$621.8	\$(17.0)
Military Construction (Nonpay)			
Army	\$17.6	\$.	\$17.6
Navy	19.2	.	19.2
Air Force	17.2	.	17.2
Defense Agencies	6.7	.	6.7
Army National Guard	2.1	.	2.1
Air National Guard	2.1	.	2.1
Army Reserve	1.2	.	1.2
Navy Reserve	.7	.	.7
Air Force Reserve	.9	.	.9
Total	\$67.7	\$.	\$67.7

**Appendix I
Estimated Inflation Dividend Amounts for
Fiscal Year 1987**

Account	Dividend Calculated in April 87	Amount of Congressional Inflation Reduction	Difference Between Dividend and Reduction
Major Commodities			
Army-Aircraft	\$63.1	\$48.0	\$15.1
Army-Missiles	50.1	40.1	10.0
Army-W&TCV	87.9	58.0	29.9
Navy-Aircraft	231.1	122.0	109.1
Navy-Weapons	121.1	72.0	49.1
Navy-Shipbuilding	200.1	124.0	76.1
Marine Corps	33.0	22.0	11.0
Air Force-Aircraft	378.1	212.2	165.9
Air Force-Missiles	167.9	122.0	45.9
Total	\$1,332.4	\$820.3	\$512.1
Nonmajor Commodities			
Army-Ammunition	\$29.0	\$24.0	\$5.0
Army-Other	73.1	72.0	1.1
Navy-Other	84.6	40.0	44.6
Air Force-Other	129.0	92.5	36.5
Defense Agencies	21.4	15.0	6.4
Total	\$337.1	\$243.5	\$93.6
Family Housing (Nonpay, Nonfuel)			
Army-Construction	\$4.9	\$	4.9
Navy-Construction	2.5		2.5
Air Force-Construction	1.4		1.4
Def Agencies-Construction	.0		.0
Army-Debt	17.0		17.0
Navy-Debt	7.5		7.5
Air Force-Debt	9.9		9.9
Defense Agencies-Debt	.2		.2
Total	\$43.4	\$	\$43.4
Military Personnel (Nonpay)			
Army	\$24.5	\$12.9	\$11.6
Navy	23.7	5.8	17.9
Marines	5.8	3.0	2.8
Air Force	19.6	11.4	8.2
Army Reserve	10.1	2.2	7.9
Navy Reserve	5.3	.8	4.5
Marine Reserve	1.6	.2	1.4
Air Force Reserve	3.4	.5	2.9
Army National Guard	14.3	1.9	12.4
Air National Guard	3.4	.3	3.1
Total	\$111.7	\$39.0	\$72.7

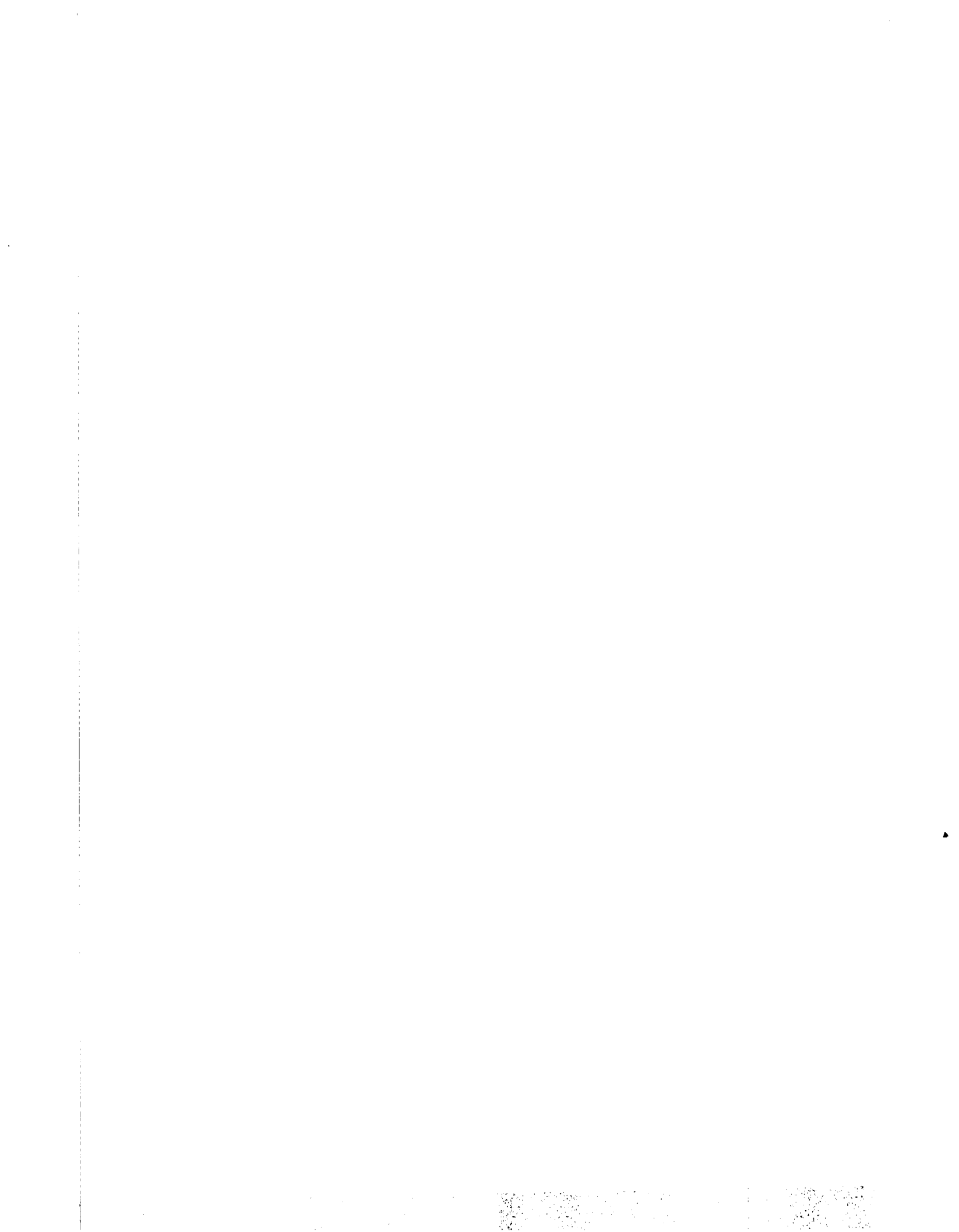
**Appendix I
 Estimated Inflation Dividend Amounts for
 Fiscal Year 1987**

Account	Dividend Calculated in April 87	Amount of Congressional Inflation Reduction	Difference Between Dividend and Reduction
Research, Development, Test, and Evaluation			
Army	\$52.4	\$82.0	\$(29.6)
Navy	131.2	182.9	(51.7)
Air Force	210.2	288.6	(78.4)
Defense Agencies	94.7	145.5	(50.8)
Total	\$488.5	\$699.0	\$(210.5)

Methodology for Determining DOD's Inflation Dividend for Fiscal Year 1987

We used the following steps to compute the fiscal year 1987 inflation dividend. These procedures are described in chapter 5 of the National Defense Budget Estimates for FY 1987.

1. For the fiscal year 1987 budget, fiscal year 1985 was the assumed base year in order to account for inflation changes during fiscal year 1986 that would affect the current fiscal year.
2. For each year in which fiscal year 1987 funds could be expended, that is, fiscal years 1987 through 1993, we developed an index showing the total inflation occurring between the base year and that fiscal year. This index was developed with the inflation rates used by DOD in preparing the fiscal year 1987 budget. These rates are shown in table 5-2 of the National Defense Budget Estimates for FY 1987. Separate indexes were developed for inflation in the purchases of fuel, major commodities, and all other defense purchases.
3. We multiplied the inflation index for each year by the corresponding spendout rate for each account. We summed the products of the inflation index and the spendout period to obtain an escalation factor which measures the amount of inflation funding in each account.
4. The appropriated amount for fiscal year 1987 was divided by this original escalation factor yielding an estimate of the total unescalated funding in the original fiscal year 1987 budget.
5. Steps 2 and 3 were repeated using the new inflation rates issued by OMB as guidance for preparation of the fiscal year 1988 budget. The result was multiplied by the total unescalated funding in step 4 above to derive a revised escalated estimate of the funding that is required in the fiscal year 1987 budget using current inflation projections.
6. The potential dividend was then determined by subtracting the revised escalated estimate from the original escalated estimate.



Requests for copies of GAO reports should be sent to:

U.S. General Accounting Office
Post Office Box 6015
Gaithersburg, Maryland 20877

Telephone 202-275-6241

The first five copies of each report are free. Additional copies are \$2.00 each.

There is a 25% discount on orders for 100 or more copies mailed to a single address.

Orders must be prepaid by cash or by check or money order made out to the Superintendent of Documents.

United States
General Accounting Office
Washington, D.C. 20548

Official Business
Penalty for Private Use \$300

Address Correction Requested

First-Class Mail
Postage & Fees Paid
GAO
Permit No. G100