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United States General Accounting Office

GAO

Report to the Chairman, Subcommittee on  
Wheat, Soybeans, and Feed Grains,  
Committee on Agriculture, House of  
Representatives

October 1988

# COMMODITY CERTIFICATES

## Backlog of 200,000 Unreconciled Certificates Affects Financial Reporting



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**Resources, Community, and  
Economic Development Division**

B-226558

October 25, 1988

The Honorable Dan Glickman  
Chairman, Subcommittee on Wheat,  
Soybeans, and Feed Grains  
Committee on Agriculture  
House of Representatives

Dear Mr. Chairman:

As requested by your office on March 3, 1988, this report discusses the backlog of redeemed commodity certificates that the Department of Agriculture (USDA) has not reconciled to issuance records and its efforts to resolve this backlog. Also, as requested, the report provides information on the extent to which USDA met a requirement of the Omnibus Budget Reconciliation Act of 1987 (P.L. 100-203) to reduce its commercial storage, transportation, and handling expenditures for fiscal years 1988 and 1989 by \$230 million.

Redeemed certificates are put in an exception category when a discrepancy exists between issuance and redemption records. For example, certificates are reported as redeemed when there is no record of their issuance or certificates are reported as having been redeemed twice. Many of the exceptions may be the result of processing errors, but a potential for fraud also exists.

The Agricultural Stabilization and Conservation Service (ASCS) and the Commodity Credit Corporation (CCC) within USDA are responsible for the issues discussed in this report. CCC, a wholly owned government corporation, has no operating personnel; its day-to-day activities are carried out by ASCS.

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## Results in Brief

Although some exceptions have been resolved, the number of certificates in the exception category has increased from over 170,000 in January 1988 to about 204,000 in April 1988. ASCS officials estimate that the number of certificates with unresolved exceptions could reach 320,000 by October 1988 as additional certificates are issued and redemptions continue. The exceptions currently represent almost \$1.6 billion, which is the total of possible overstatements of \$982 million and understatements of \$584 million in the accounting for certificates. However, the true magnitude of the effect cannot be known until the exceptions are resolved.

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ASCS is addressing some of the exceptions as part of its year-end closing plan for accounting activities. However, ASCS has not identified the root causes of the backlog or developed a specific plan to address the remaining backlog of unresolved exceptions and minimize the occurrence of future exceptions. ASCS also needs to report, in its 1988 annual assessment of internal controls, that a material weakness exists, as required by the Federal Managers' Financial Integrity Act of 1982.

With regard to the mandated reduction in expenditures for commercial storage, transportation, and handling of government-owned commodities, ASCS estimated, in December 1987, that such expenditures in fiscal years 1988 and 1989 will be approximately \$610 million less than projected.

This lower level of expenditures, which would exceed the mandated \$230 million reduction, was achieved because of the significantly lower volume of government-owned grain being stored without the need for ASCS to take any specific cost-cutting actions. Lower production and higher demand, especially for export, has caused the reduction in grain being stored. More details on the background of this issue, as well as USDA's original and revised projections are shown in appendix I.

The remainder of this report discusses the backlog of unresolved commodity certificate exceptions.

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## Background

The Food Security Act of 1985 (P.L. 99-198) authorizes the Secretary of Agriculture to issue negotiable commodity certificates to eligible producers instead of a portion of the cash payments due them for their participation in government price- and income-support programs for wheat, feed grains, cotton, and rice. Certificates are also being used to make payments for other USDA programs. Certificates can be (1) used to purchase government-owned commodities or repay price support loans, (2) redeemed for cash, or (3) sold to other interested parties. Between April 1986 and April 1988, ASCS issued over 16 million certificates valued at approximately \$18.7 billion. Over 13 million certificates were redeemed, valued at approximately \$15.7 billion. Almost 3 million certificates, valued at approximately \$3 billion, remain outstanding.

ASCS' Kansas City Management Office (KCMO) is responsible for accounting for the issuance and redemption of certificates. KCMO uses its Commodity Certificate Accounting System (CERTS) to account for the redemption of certificates. The CERTS incorporates automated internal

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controls that have been designed to identify exceptions such as (1) certificates recorded in the system as being redeemed but never recorded as being issued or (2) redeemed certificates that show a higher or lower dollar value than the value of the certificates when issued. When CERTS identifies such exceptions, an exception listing is generated. Resolution of the exceptions is needed to correct financial statements and ensure that certificates are not being fraudulently redeemed. There are six categories of exception listings as follows.

- Unmatched redeemed—redeemed certificates that do not match an issued certificate.
- Excessive redemptions—redeemed certificates recorded at a higher value than issued.
- Unmatched cancellations—cancelled certificates that do not match an original issued certificate.
- Potential duplicates—redeemed certificates that match a certificate number that is already recorded as issued and redeemed.
- Unmatched redemption reversals—redeemed certificate transactions that have been reversed for correction purposes, but the reversal does not match the original redemption transaction.
- Other exceptions—redeemed certificates that were recorded at a lower value than when they were issued or that appear to have been redeemed more than once.

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## The Backlog of Redeemed Certificates With Unresolved Exceptions Is Increasing

The backlog of redeemed certificates with unresolved exceptions is increasing. As of April 30, 1988, the backlog was over 204,000 certificates, an increase of over 34,000 certificates from the January 31, 1988, level.

The 11 KCMO personnel who are assigned to research and correct the six exception listings were working primarily on unmatched redeemed certificates because of the large backlog in this category. Although KCMO does not keep detailed records of the number of exceptions that occur or are resolved each month, the KCMO official responsible for resolving the discrepancies estimates that about 25,000 exceptions are corrected each month. However, as shown in table 1, the number of unresolved exceptions continues to increase, even in the unmatched redeemed category which the KCMO considers to be its highest priority.

**Table 1: Backlog of Unresolved Exceptions**

<b>Exception category<sup>a</sup></b>	<b>Jan. 31, 1988</b>	<b>Apr. 30, 1988</b>	<b>Increase/Decrease</b>
Unmatched redeemed	51,048	70,314	19,266
Excessive redemptions	13,715	16,432	2,717
Unmatched cancellations	16,932	38,188	21,256
Potential duplicates	43,041	42,900	(141) <sup>b</sup>
Unmatched reversals	6,079	6,223	144
Other exceptions	39,176	30,369	(8,807) <sup>b</sup>
<b>Total</b>	<b>169,991</b>	<b>204,426</b>	<b>34,435</b>

<sup>a</sup>Listed in order of ASCS' priority for resolution.

<sup>b</sup>Corrections made in the unmatched redeemed listing caused the decrease.

Source: ASCS.

KCMO officials estimate that the backlog of redeemed certificates with unresolved exceptions will increase from over 204,000 in April 1988 to approximately 320,000 by October 1988. According to these officials, this increase will result from the redemption of the 3 million outstanding certificates and the issuance and redemption of additional certificates.

## KCMO's Plan to Reduce the Backlog

As of May 1988, when we completed our field work, KCMO management did not have a plan to resolve the increasing backlog of exceptions. Therefore, we suggested that one approach would be to give priority to correcting high-dollar exceptions to maximize the dollar benefit from KCMO's efforts. Currently, a certificate with exceptions at \$10 can receive the same consideration as one valued at \$10,000 within each exception listing.

As shown in table 2, for example, about 18 percent (30,622) of the 169,156 certificates with exceptions totaling to \$5,000 or more accounted for 90 percent (approximately \$1.4 billion) of the total dollar discrepancy. Exceptions totaling \$1,000 or more represent 50 percent of all certificates with exceptions and about 98 percent of the total dollar discrepancy.

**Table 2: Number and Dollar Amount of Discrepancies on Unresolved Certificates as of April 30, 1988**

Range of discrepancy	Unresolved certificates			
	Number	Percent	Amount	Percent
\$0-99	15,814	9.3	\$822,078	0.05
\$100-499	42,151	24.9	11,451,426	.73
\$500-999	25,895	15.3	18,712,089	1.19
\$1,000-4,999	54,674	32.3	124,596,224	7.95
\$5,000-9,999	13,762	8.1	90,842,175	5.80
over \$10,000	16,860	10.0	1,319,998,023	84.27
<b>Total</b>	<b>169,156<sup>a</sup></b>	<b>99.9<sup>b</sup></b>	<b>\$1,566,422,015</b>	<b>99.99<sup>b</sup></b>

<sup>a</sup>These figures do not include certificates from the potential duplicate listing.

<sup>b</sup>These figures do not total 100 percent due to rounding.

KCMO officials agreed that resolving high-dollar exceptions first would be an additional method to rank their work until they get the backlog of unresolved exceptions under control.

After we completed our field work, the Director of KCMO requested, in a June 15, 1988, letter, that ASCS management approve KCMO's year-end closing plans for its accounting activities. Included in this plan was an outline of eight proposals to reduce the backlog of unresolved exceptions. Six of these proposals deal with developing computer programs to help generate corrections for the exception categories, including writing-off all exceptions of less than \$5,000 in the unmatched redeemed category. This proposal would reduce the backlog by about 65,000 certificates and the dollar amount of exceptions by about \$55 million. The remaining two proposals deal with (1) developing a one-time write-off of exceptions (in categories other than unmatched redeemed) that have a net value of less than \$200 (this method would remove 23,082 certificates with a credit amounting to about \$431,354) and (2) giving priority to errors with a net value of over \$1,000 in the excessive redemption category that KCMO has designated as its second highest priority. On August 11, 1988, ASCS approved KCMO's year-end closing plan, including these proposals.

While we did not review KCMO's proposals in detail because they were developed after completion of our work, we believe the proposals outlined by KCMO are the first step toward resolving the backlog. However, the proposals may need additional development before they are workable. For example, it may be inappropriate to use the net dollar value rather than the total value as a criterion for writing off exceptions.

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The net dollar value of a certificate is the difference between two or more discrepancies that may exist for a redeemed certificate. The true value of the discrepancy cannot be determined, however, until the certificate exceptions are researched and processing errors corrected. For example, the dollar amount of the certificate may be recorded incorrectly for either issuance or redemption or the certificate number may be incorrectly recorded. Additionally, it is possible that the certificate has been altered and fraudulently redeemed. As such, we believe that using the total value of all exceptions for a given certificate would be a better method to use if ASCS decides to write-off some exceptions. Using the total value of all exceptions would ensure that even in the worst case the dollar amount written-off would be relatively small while still removing thousands of exceptions from the backlog. We also believe the same procedures should be followed when using the dollar value of exceptions to rank certificates for corrective action.

In addition, while ranking certificates in the second most important category of exceptions—excessive redemptions—will also help to reduce the backlog, there will still remain a backlog of about 116,000 certificates with exceptions. The proposal outlined by KCMO does not address this portion of the backlog, identify specific funding or resources to be employed, or establish milestones for corrective actions. Finally, the proposal does not address the need to identify and correct the root causes of the exceptions to minimize the occurrence of future exceptions.

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## ASCS Has Not Met All Financial Integrity Act Requirements

The Federal Managers' Financial Integrity Act of 1982 (FIA) requires government agencies to annually evaluate their internal controls and report whether they comply with prescribed internal control standards and provide reasonable assurance that (1) obligations and costs are in accordance with applicable laws, (2) assets are safeguarded against waste, fraud, or abuse, and (3) revenues and expenditures are properly recorded and accounted for so that reliable financial reports may be prepared and accountability of assets may be maintained. To the extent systems do not comply, any material control weaknesses, along with plans for their correction, must be reported in an agency's FIA statements.

The Office of Management and Budget Circular A-123 defines material control weaknesses, in part, as those which significantly weaken safeguards against waste, loss, unauthorized use or misappropriation of funds, property, or other assets. Additional guidance provided for the



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annual 1988 FIA reports requires, in part, that a material weakness should risk or result in the actual loss of either \$10 million or 5 percent of the resources of a budget line item.

In June 1987, the KCMO unit responsible for correcting the certificates with unresolved exceptions reported in an annual review assessment that the backlog of unresolved exceptions needing corrections was large. The assessment also stated that KCMO expected to reduce the number of unresolved exceptions by one-half by the end of June 1987, which was not done. However, ASCS did not identify the causes of the backlog, develop plans to correct the problem, or report that a material weakness existed in its November 1987 FIA statement.

In March 1988, the KCMO unit again reported that a large backlog of certificates with unresolved exceptions existed. The backlog has increased since that time. KCMO's internal control coordinator, who has reviewed the 1988 assessment, believes that the backlog is evidence that a material weakness needing correction exists and should be reported as such in ASCS' 1988 FIA statement.

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## Conclusions

A large and growing backlog of certificates with unresolved exceptions exists. The exceptions, generated as part of the CERTS internal controls, were designed to identify discrepancies between records of certificate issuance and redemption to aid in preparing reliable financial statements and in detecting any fraudulent certificates.

While KCMO has developed a proposal, as part of its year-end closing plan for accounting activities to address a portion of the current backlog of certificates with unresolved exceptions, it has not developed, nor has ASCS approved, any specific plans to address the remaining backlog. Further, neither KCMO or ASCS has identified the root causes of the backlog or developed plans for corrective action to minimize the number of exceptions that might occur in the future. As a result, ASCS is unable to assure the integrity of the certificate accounting system, resolve discrepancies (both positive and negative) that represent almost \$1.6 billion on its financial statements, or assure that certificates are not being fraudulently redeemed. Finally, ASCS needs to report, as required by law and Office of Management and Budget guidelines, that a material weakness exists in its 1988 FIA statement.

## Recommendations

We recommend that the Secretary of Agriculture direct the ASCS Administrator to develop a plan to address the remaining backlog of certificates with unresolved exceptions that ensures the accountability for commodity certificates and reduces the potential that undetected fraud could be occurring. This plan should

- clearly establish priorities so that high dollar value certificates are researched and corrected first regardless of the exception category;
- be as specific as possible with regard to the methods that will be used, the resources to be allocated, and a schedule for completion; and
- include steps to identify and correct the root causes of the exceptions to minimize the number of exceptions that may occur in the future.

We also recommend that the Secretary of Agriculture direct the ASCS Administrator to report in its annual Financial Integrity Act statement that a material weakness exists and provide an assessment detailing (1) the impact of the backlog of certificates with unresolved exceptions on its financial statement and (2) management's plan to correct the problem.

## Objectives, Scope, and Methodology

Our work was performed, in accordance with generally accepted government auditing standards, between April and June 1988, with updates through August 1988. Our objectives were to identify the size of the backlog in redeemed certificates with unresolved exceptions and ASCS' plan for resolving the backlog and to determine whether USDA had achieved the mandated reduction in storage expenditures. To accomplish our objectives, we interviewed ASCS officials in Washington, D.C., and at its Kansas City Commodity and Kansas City Management Offices; visited two ASCS county offices in Kansas; reviewed exception reports produced by the Commodity Certificate Accounting System; and identified the process to correct the exceptions. We did not evaluate ASCS' accounting system or internal controls. However, we did discuss with appropriate ASCS officials the requirement to report material weaknesses in internal controls under the Federal Managers' Financial Integrity Act. Finally, we reviewed the provisions of the Omnibus Budget Reconciliation Act of 1987 dealing with the reduction of storage, transportation, and handling expenditures in fiscal years 1988 and 1989 and reviewed, but did not independently verify, USDA's revised budget estimates for 1988 and 1989.

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The views of responsible officials were sought during the course of our work and are included where appropriate. As requested, we did not obtain official agency comments on a draft of this report. We plan to distribute this report at the same time it is presented to you. At that time, we will send copies to the Director, Office of Management and Budget; the Secretary of Agriculture; and other interested parties. Copies will be made available to others upon request.

Major contributors to this report are listed in appendix II.

Sincerely yours,

A handwritten signature in black ink that reads "J. Dexter Peach". The signature is written in a cursive style with a large, prominent initial "J".

J. Dexter Peach  
Assistant Comptroller General

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## Abbreviations

ASCS	Agricultural Stabilization and Conservation Service
CCC	Commodity Credit Corporation
CERTS	Commodity Certificate Accounting System
FIA	Financial Integrity Act
GAO	General Accounting Office
KCMO	Kansas City Management Office
USDA	U.S. Department of Agriculture



# Status of Congressionally Directed Storage Cost Reduction

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The Omnibus Budget Reconciliation Act of 1987 required the Secretary of Agriculture to reduce commercial storage, transportation, and handling expenditures by \$230 million from the amounts projected under the budget base for fiscal years 1988 and 1989. Section 1106 of the act states:

“For the fiscal years 1988 and 1989, the Secretary of Agriculture shall ensure that expenditures of the Commodity Credit Corporation for commercial storage, transportation, and handling of commodities owned by the Corporation (excluding storage payments made in accordance with section 110 of the Agricultural Act of 1949 (7 U.S.C. 1445e) are reduced by \$230,000,000 in such fiscal years from the amount of funds otherwise projected to be expended in fiscal years 1988 and 1989 under the budget base determined under section 251 of the Balanced Budget and Emergency Deficit Control Act of 1985 (2 U.S.C. 901) for commercial storage, transportation, and handling of such commodities. In order to achieve the savings required by this section, the Secretary shall adjust storage, handling, or transportation expenditures paid by the Corporation or take other appropriate actions.”

Under the budget base established in August 1987, ASCS estimated that commercial storage, transportation, and handling expenditures would be \$3 billion in fiscal years 1988 and 1989. However, in December 1987, ASCS estimated that such costs would be about \$600 million less than its earlier estimate.

The act did not specify what actions USDA was to take to reduce the level of expenditures. Therefore, ASCS could have (1) negotiated reduced rates, (2) reduced the volume of commodities stored, handled, and shipped, or (3) taken some other actions. In fact, the lower level of expenditures was achieved without the need for any specific cost-cutting actions by ASCS. Rather, the reductions occurred because of the significantly lower volume of government-owned grain, primarily corn and wheat, that is currently being stored. The lower volume of grain being stored has resulted from lower annual production and higher demand for grain, especially for export, that has taken place in the last few years. As such, ASCS officials believe that the projected reduction of \$600 million more than meets the requirements of the act to reduce such expenditures by \$230 million.

**Appendix I  
Status of Congressionally Directed Storage  
Cost Reduction**

**Table I.1: Storage/Handling and Transportation Estimates Fiscal Years 1988 and 1989** (Dollars in Thousands)

Commodity	August 1987 (baseline) review estimates			December 1987 budget estimates			Change
	Storage/Handling	Transportation	Total	Storage/Handling	Transportation	Total	
Corn	\$1,566,941	\$126,947	<b>\$1,693,888</b>	\$1,243,788	\$53,047	<b>\$1,296,835</b>	\$(397,053)
Grain Sorghum	360,877	19,375	<b>380,252</b>	434,453	26,241	<b>460,694</b>	80,442
Barley	68,745	4,844	<b>73,589</b>	84,893	2,352	<b>87,245</b>	13,656
Oats	2,257	117	<b>2,374</b>	3,247	170	<b>3,417</b>	1,043
<b>Total feed grain</b>	<b>1,998,820</b>	<b>151,283</b>	<b>2,150,103</b>	<b>1,766,381</b>	<b>81,810</b>	<b>1,848,191</b>	<b>(301,912)</b>
Wheat	495,198	36,335	<b>531,533</b>	299,623	20,992	<b>320,615</b>	(210,918)
Rice	27,300	415	<b>27,715</b>	9,577	126	<b>9,703</b>	(18,012)
Rye	11,643	6,975	<b>18,618</b>	11,130	4,990	<b>16,120</b>	(2,498)
Soybeans	175,476	840	<b>176,316</b>	70,456	20,882	<b>91,338</b>	(84,978)
Honey	445	2,551	<b>2,996</b>	1,056	3,550	<b>4,606</b>	1,610
Sugar	0	0	<b>0</b>	1,132	83	<b>1,215</b>	1,215
Cotton, Upland	852	0	<b>852</b>	405	0	<b>405</b>	(447)
Cotton, ELS <sup>a</sup>	339	0	<b>339</b>	185	0	<b>185</b>	(154)
Peanuts	1,600	0	<b>1,600</b>	1,600	0	<b>1,600</b>	0
Supply Program	20	0	<b>20</b>	20	0	<b>20</b>	0
<b>Total other commodities</b>	<b>712,873</b>	<b>47,116</b>	<b>759,989</b>	<b>395,184</b>	<b>50,623</b>	<b>445,807</b>	<b>(314,182)</b>
Butter	4,330	15,042	<b>19,372</b>	7,992	15,785	<b>23,777</b>	4,405
Butter Oil	22	25	<b>47</b>	264	1,865	<b>2,129</b>	2,082
Cheese	7,471	25,869	<b>33,340</b>	16,936	24,164	<b>41,100</b>	7,760
Dried Milk	8,758	34,720	<b>43,478</b>	6,973	37,312	<b>44,285</b>	807
Mozzarella Cheese	0	132	<b>132</b>	0	93	<b>93</b>	(39)
UHT Milk <sup>b</sup>	0	0	<b>0</b>	0	2	<b>2</b>	2
Red meat	9,377	2,650	<b>12,027</b>	2,691	915	<b>3,606</b>	(8,421)
<b>Total dairy and red meat</b>	<b>29,958</b>	<b>78,438</b>	<b>108,396</b>	<b>34,856</b>	<b>80,136</b>	<b>114,992</b>	<b>6,596</b>
<b>Total (feedgrain, dairy, other)</b>	<b>\$2,741,651</b>	<b>\$276,837</b>	<b>\$3,018,488</b>	<b>\$2,196,421</b>	<b>\$212,569</b>	<b>\$2,408,990</b>	<b>\$(609,498)</b>

<sup>a</sup>Extra long Stable (ELS)

<sup>b</sup>Ultra high temperature (UHT)

Source: ASCS.

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