



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

Accounting and Information
Management Division

B-282660

May 14, 1999

The Honorable Tom Bliley
Chairman, Committee on Commerce
House of Representatives

Subject: Financial Management: Briefing on the Results of the Financial Audit of the National Institutes of Health

Dear Mr. Chairman:

This letter responds to your request that we review the National Institutes of Health's (NIH) fiscal year 1998 financial audit report and brief your staff on the significant issues raised in that report. To meet a requirement for an audited departmental financial statement,¹ the Department of Health and Human Services (HHS) decided to have most of its component's financial statements audited. In our April 26, 1999, briefing to your staff, we discussed the key financial management issues highlighted in the auditor's report on NIH, which are summarized below. The briefing slides are enclosed.

Results in Brief

The independent public accounting firm's² (IPA) audit opinion went from qualified on all NIH principal statements for fiscal year 1997 to unqualified on all principal statements except the Statement of Financing for fiscal year 1998. The IPA qualified its opinion on the fiscal year 1997 principal statements because (1) NIH had not performed a complete physical inventory in the past 4 years and (2) the amount reported as the grant accrual could not be substantiated. For fiscal year 1998, the IPA issued a disclaimer of opinion on the Statement of Financing because NIH could not reconcile differences between its net cost and budgetary obligations.

¹31 U.S.C. § 3515 (a)(1994).

²The HHS Office of the Inspector General contracted with Ernst and Young, L.L.P., an IPA, to perform the fiscal year 1997 and 1998 financial statement audits.

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In its internal control report for fiscal year 1997, the IPA cited material weaknesses³ in financial reporting, property management, and grant management. For fiscal year 1998, the IPA continued to report these three areas as weaknesses, but considered only financial reporting to be a material weakness, particularly in the area of the development and analysis of financial statements.

The IPA stated that while NIH implemented many improvements in fiscal year 1998, significant financial management issues were still affecting NIH's ability to analyze its financial activity and prepare auditable and timely financial information. For example, NIH did not have an integrated financial system to assist in the preparation of its financial statements. NIH's decentralized structure resulted in a labor intensive and time-consuming process in which trial balances from its 22 institutes and centers had to be consolidated. The IPA noted that having an integrated financial system and a sufficient number of properly trained personnel is essential for performing periodic analyses and reconciliations to detect errors and irregularities promptly.

The IPA reported that in fiscal year 1998, NIH performed its first wall-to-wall physical inventory of personal property in 5 years and a complete physical inventory of its real property. The IPA stated that these are important initial steps, but emphasized that NIH's efforts could be wasted if not followed up with the development of formal procedures to ensure proper accountability of assets and the reconciliation of property records to the general ledger. The IPA also noted that while NIH has initiated procedures to reconcile its property records to its general ledger, further improvements are necessary to ensure that differences are researched and adjustments are recorded to the general ledger and related subsidiary records with adequate supporting documentation.

In its report for fiscal year 1998, the IPA noted improvements in grant management. Specifically, NIH improved its documentation supporting the amount of grant accrual reported on the financial statements. Also, through the development of a methodology, it improved its calculation of the liability for expenditures that had been incurred but not reported.

In NIH's response to the IPA's report, management concurred with the findings and stated that they would develop a corrective action plan to address the weaknesses.

We are sending copies of this letter to Representative John D. Dingell, Ranking Minority Member of your Committee, Dr. Harold E. Varmus, Director of NIH, and other interested parties. Copies will also be made available to others upon request.

³A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material to the financial statements may occur and not be detected promptly by employees in the normal course of performing their duties.

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If you have any questions about this letter or the earlier briefing, please contact me at (202) 512-4476. Chinero Thomas and Rosa Ricks Harris were major contributors to this letter.

Sincerely yours,

A handwritten signature in cursive script that reads "Gloria L. Jarmon".

Gloria L. Jarmon
Director, Health, Education, and Human Services
Accounting and Financial Management

Enclosure

GAO

**Accounting and Information
Management Division**

NATIONAL INSTITUTES OF HEALTH

Briefing on Financial Statement Audits

April 26, 1999

GAO Major Legislation

- **CFO Act**

- **GMRA**

- **FFMIA**

GAO Financial Statement Audits

- Opinions on financial statements
 - unqualified, qualified, adverse, dis
- Report on Internal Control
 - material weaknesses and reportab
 - conditions
- Compliance with Laws and Regulat
- Management letter

GAO Audit History

- FY 1997
 - Qualified opinion on financial statements because amounts for fixed assets and grant advances payable could not be substantiated

GAO Audit History (cont.)

- Report on Internal Control identified weaknesses in
 - fixed assets
 - grant accrual
 - grant advances
 - financial reporting
 - grant monitoring

GAO Audit History (cont.)

- **Report on Compliance with Laws and Regulations**
 - instances of noncompliance with **FFMIA**

GAO Audit History (cont.)

- FY 1998
 - Unqualified opinion on the balance statements of net costs, custodial and budgetary resources, and changes position
 - Disclaimer on the Statement of Financial due to unreconciliable differences between net costs and budgetary obligations

GAO Audit History (cont.)

- Report on Internal Control identified weaknesses in
 - financial reporting
 - fixed assets
 - Fund Balance with Treasury (FBWT)

GAO Audit History (cont.)

- Report on Compliance with Laws and Regulations identified
 - instances of noncompliance with FFMIA
- Management letter identified weaknesses in
 - grant accrual
 - grant monitoring

GAO Scope and Methodology

- Reviewed the audit reports on NIH's FY 1997 and FY 1998 financial statement audits

GAO Significant FY 1998 Audit Issues

- Financial Reporting
- Fixed Assets
- Fund Balance with Treasury
- Grant Accrual
- Grant Monitoring

GAO IPA Audit Results

FY 1998 Audit Report

- **Financial Reporting**

- no integrated financial reporting system to facilitate preparation of reliable financial statements

- lack of timely reconciliation between the general ledger and subsidiary records

GAO IPA Audit Results

- **Financial Reporting (cont.)**
 - lack of periodic analysis of revenue, expenses, and other account balances to ensure that balances reported in the general ledger are accurate and reasonable
 - inadequate documentation of accounting and internal control procedures and processes

GAO IPA Audit Results

- **Fixed Assets-PP&E**

- physical inventory of personal property identified \$27 million in capitalized assets which could not be located

- no subsidiary system to account for real property activity prior to FY 1999

GAO IPA Audit Results

- **Fixed Assets (cont.)**
 - no up-to-date formalized policies and procedures to ensure that building-related expenditures which meet criteria for capitalization are recorded appropriately

GAO IPA Audit Results

- **Fund Balance With Treasury**
 - lack of timely posting of adjustments to the general ledger
 - lack of periodic reconciliation to Treasury records
 - lack of supporting documentation for unreconciled suspense account differences

GAO IPA Audit Results

- **Grant Accrual**

- information in the Payment Management System not sufficient to calculate an estimate of incurred but not reported grant expenditures

- **Grant Monitoring**

- inadequate system to ensure all single audit reports are received

- lack of timely notification for the receipt of single audit reports at the Census Bureau

GAO IPA Recommendations

- Strengthen controls to improve the reliability and documentation of financial information
 - perform and oversee monthly reconciliation of all major financial balances

GAO IPA Recommendations

- Update current policies and procedures to ensure that capitalized asset activity is properly recorded in the property management information system and the general ledger; and property records are reconciled to the general ledger

GAO IPA Recommendations

- Develop standardized inventory procedures, assign inventory dates, attend selected inventory counts, and monitor inventory results
- Develop formalized policies and procedures for real property and train personnel to ensure proper accounting for real property

GAO IPA Recommendations

- Improve current procedures to ensure timely reconciliations and adjustments for FBWT
- Consider whether changes should be made to current grant recipient reporting requirements in order to refine the grant accrual estimate

GAO IPA Recommendations

- Develop a system to track the submission of Single Audit reports by grantees and identify those that are delinquent
- Coordinate with the Census Bureau to ensure that notification of the receipt of Single Audit reports are received promptly and information is accurate

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