

098131

~~76-0350~~

098131



UNITED STATES
GENERAL ACCOUNTING OFFICE
GENERAL ACCOUNTING OFFICE
JUN 29 1976

Handwritten initials, possibly "CP", in the top right corner.

LIBRARY SYSTEM

Need For Greater Audit Coverage Of Internal Financial Areas

Department of Labor

The Budget and Accounting Procedures Act of 1950 requires the head of each agency to establish and maintain systems of internal control, including appropriate internal audit, in order to provide effective control over and accountability for all funds, property, and other assets for which the agency is responsible.

We found that the current audit effort does not provide adequate coverage of internal financial operations as required by the above act.

FGMSD-76-67

JUNE 25, 1976

703TT6
098131



UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

DIVISION OF FINANCIAL AND
GENERAL MANAGEMENT STUDIES

B-133182

The Honorable
Secretary of Labor

Dear Mr. Secretary:

The Budget and Accounting Procedures Act of 1950 (31 U.S.C. 66a) requires the head of each agency to establish and maintain systems of internal control, including appropriate internal audit, in order to provide effective control over and accountability for all funds, property, and other assets for which the agency is responsible. The act further contemplates that the head of each agency will assure himself of the adequacy of staffing and the scope of internal audit arrangements in his agency.

We reviewed the Department of Labor's internal audit operations to determine the extent to which audits are made to insure the Department is maintaining effective control over revenues, expenditures, assets, and liabilities, and that its financial reports contain accurate, reliable, and useful data.

Our review included areas audited by the Directorate of Audit and Investigations (Directorate) during fiscal years 1973 through 1975, and audits planned, in process, or completed during fiscal year 1976. We also reviewed the Directorate's issue paper for fiscal year 1977 planning.

The Directorate's staff issued 1,357 audit reports during the period covered by our review, of which 39 were audits of internal operations and 1,318 were external audits of the Department's contract and grant programs. Of the 39 internal audit reports, 10 were directly related to financial operations and 4 others included aspects of financial matters. The financial areas reviewed included various aspects of cash, advances, property, and liabilities. No audits had been made of such important areas as accounts receivable, the payroll system, the administrative control of funds, revenues, the examination of financial statements, and the effectiveness of the overall accounting system. An audit of the payroll system is planned to start in late July 1976.

Directorate officials said these areas were not audited because of lack of staff and the need to apply available staff to external audits of the Department's contract and grant programs. Emphasis is being given to the external audit

BEST DOCUMENT AVAILABLE

operations because of the significant dollars appropriated for such programs as the Comprehensive Employment and Training Act (CETA), which are required by regulation to be audited annually, or not less than biennially.

We recognize the need for audits of the Department's grant programs, and that such audits provide important financial control over the billions of dollars disbursed through these programs. However, we believe the current audit effort does not provide adequate audit coverage of internal financial operations as required by the Budget and Accounting Procedures Act of 1950. Much of the Department's operations are not being subjected to the internal control which can be provided by auditors. As a result, opportunities to reduce or eliminate unnecessary or wasteful practices may be lost and potential cost reductions may not be realized.

While it is certainly important to concentrate on Federal assistance programs such as CETA, it is also important that the Directorate determine the extent of the Department's control over funds, property, and other assets for which it is responsible through audits of internal operations.

We recommend that you assess the audit function to determine what action should be taken to provide effective audit coverage of the Department's internal financial operations.

Details of our review follow.

GAO CRITERIA FOR INTERNAL AUDIT
COVERAGE OF FINANCIAL OPERATIONS

Under the Budget and Accounting Procedures Act of 1950, the head of each Federal agency is required to establish and maintain systems of

"* * * internal control designed to provide * * * effective control over and accountability for all funds, property, and other assets for which the agency is responsible, including appropriate internal audit."

The same act requires the Comptroller General to prescribe principles, procedures, rules, and regulations to assist agencies in establishing internal audit organizations.

GAO issued statements of basic principles and concepts of internal auditing for Federal agencies in 1957, 1968,

and 1974. The statements said, with regard to internal audits of financial operations, that the internal auditor should examine financial transactions to the extent necessary to determine whether:

- The agency is maintaining effective control over revenues, expenditures, assets, and liabilities.
- The agency is properly accounting for its resources, liabilities, and operations.
- The agency's financial reports contain accurate, reliable, and useful financial data and are fairly presented.
- The agency is complying with the requirements of applicable laws and regulations.

The GAO statements said that in carrying out this work the internal auditor should evaluate the adequacy of the agency's prescribed policies and procedures and the internal controls related to its financial operations, including the accounting and financial reporting. The internal auditor should be particularly concerned with assets for which the agency is accountable--whether they are fully accounted for and whether procedures being followed adequately protect them from loss, deterioration, or misuse.

In addition, the GAO Policy and Procedures Manual for Guidance of Federal Agencies (title 2) prescribes the principles and standards for agency accounting systems. This document provides (1) a basis for GAO's approval of agency accounting systems, (2) a criterion for GAO audits of agency financial operations, and (3) a basis for each agency to properly plan its internal audit operations to insure adequate coverage.

Appendix I to this report identifies specific financial areas that should be reviewed, as applicable, by an agency's internal audit staff.

FINANCIAL AREAS AUDITED

The Directorate's staff issued 1,357 audit reports during fiscal year 1973 through the third quarter of fiscal year 1976 of which 39 were audits of internal operations and 1,318 were external audits of the Department's contract and grant programs. Of the 39 internal audit reports, 10 were directly

related to internal financial operations and 4 others contained elements of financial matters.

We analyzed these reports to determine if audit coverage had been provided to the Department's nine agencies in the areas of cash, receivables, advances, property, liabilities, administrative control of funds, revenues, costs, and financial reports. We selected these areas because they are considered as being among the most significant in our approval of accounting systems and our reviews of systems in operation.

The Directorate's reports indicated audit coverage in the following areas:

Cash

- Imprest fund--fiscal years 1973 and 1975.
- Working capital fund--fiscal years 1973 and 1974.
- Cash control procedures for the Bureau of Labor Statistics' Publications Sales Program--fiscal year 1975.
- Cash management in the Manpower Administration--fiscal year 1975.
- Cash controls in the mailrooms--fiscal year 1976.
- Special Fund-Longshoremen's and Harbor Worker's Compensation Act--fiscal years 1975 and 1976.

Advances

- Controls over Government transportation requests and administrative employees' knowledge of travel regulations and procedures--fiscal year 1975. The review covered six agencies in Washington and four regional offices.
- Travel advance system--fiscal year 1976.

Property

- Property valuation, physical control over property, and a reconciliation of the physical inventory with

property records--fiscal year 1973 in the Manpower Administration.

--Review of the property management system in the Office of the Assistant Secretary for Administration and Management--fiscal year 1975.

Liabilities

--Review of the recording of liabilities in four regions for four agencies--fiscal year 1973.

--Review of the voucher examination function and accruals for recurring and nonrecurring services made in the Office of the Assistant Secretary for Administration and Management--fiscal year 1975.

Costs

--Collection and allocation of direct and indirect costs-- State Employment Security Administration--fiscal year 1975.

We also noted two reviews of financial operations which did not appear to fall under the above general categories. The first, in fiscal year 1973, involved verification of the system for coding accounting documents in four agencies of the Department in four regions. The second, in fiscal year 1975, involved the processing of accounting documents, and was made in three regional Administration and Management offices.

NEED FOR GREATER AUDIT COVERAGE OF INTERNAL FINANCIAL AREAS

Our analysis of the above audit reports indicated that the coverage should be expanded in some areas. Cash reviews, for example, were directed primarily toward the imprest and working capital funds. There have been no recent reconciliations of cash transactions with Treasury accounts, nor has there been any recent review of the Department's payroll system which disburses hundreds of millions of dollars annually. However, an audit of the payroll system is planned to start in late July 1976.

The property review covered the important elements of valuation, control, and a reconciliation of the physical

inventory with records, but for only one of the Department's nine agencies.

There were no audits of accounts receivable. The Department's June 30, 1975, Statement of Financial Condition, showed accounts receivable of \$372,306,394 from Government agencies and \$34,639,504 from the public, indicating that significant amounts of receivables flow through the Department's accounts. The collection and writeoff of receivables, and the adequacy of controls to insure that customers are properly billed are examples of work which should be considered in this area.

There were no recent audits directed toward the administrative control of funds. Such work should be undertaken and it should be directed toward determining whether the Department is complying with the provisions of Section 1311 of the Supplemental Appropriation Act of 1955 which defines valid obligations and establishes requirements for reporting, certifying, and restricting expenditures. Compliance with the Anti-deficiency Act which restricts the rate of expenditure of appropriations to the period for which they are appropriated should also be determined periodically.

Reviews should be made to insure that controls over revenue and cost accounts are adequate. There should also be periodic verification of financial reports to insure that they are supported by the financial records and make full disclosure of the Department's financial condition.

There are many other areas which deserve consideration in conducting future audits of financial operations as noted in appendix I to this report. While it may not be feasible for the Directorate to provide audit coverage in each of the areas, the appendix provides a framework for future consideration of audits of financial operations.

DIRECTORATE'S EVALUATION OF AUDIT EFFORT

Directorate officials concurred in the analyses of the areas reviewed and the need to extend their audits of internal financial matters. They stated that only limited coverage had been provided for internal operations because of lack of staff and the need to apply available staff to external audits of the Department's contract and grant programs. Emphasis is being given to external audit operations because of the significant dollars appropriated for such programs as CETA which are required by regulation to be audited annually or no less than biennially.

Directorate officials pointed out that external audits have a significant impact on the Department's financial operations because they provide important financial control over the billions of dollars disbursed annually to contractors and grantees.

A Directorate issue paper, which set forth a projection for deploying 139 auditors during fiscal year 1977, indicated that about 268 auditors would be required annually to carry out an effective audit program in the Department as follows.

<u>External</u>	<u>Projected use of available staff years</u>	<u>Estimated additional staff years needed</u>	<u>Total</u>
CETA prime sponsors	61	57	118
CETA subsponsors	12	11	23
Employment security/ unemployment in- surance/work in- centive	16	14	30
Occupational Safety and Health Admin- istration	2	2	4
National agency con- tracting offices	<u>12</u>	<u>11</u>	<u>23</u>
Total	103	95	198
<u>Internal</u>			
Organizational	24	22	46
Functional (including financial)	<u>12</u>	<u>12</u>	<u>24</u>
Total	<u>36</u>	<u>34</u>	<u>70</u>
Total	<u>139</u>	<u>129</u>	<u>268</u>

CONCLUSIONS

We agree with the Directorate's statement that much of the external audit work has a significant impact on the Department's financial control over the billions of dollars disbursed through its grant programs. However, we believe the current audit effort does not provide adequate audit coverage of the internal financial operations of the Department as required by the Budget and Accounting Procedures Act of 1950. Many of the Department's operations are not being subjected to the important internal control which can be provided by auditors. As a result, opportunities to reduce or eliminate unnecessary or wasteful practices may be lost and potential cost reductions may not be realized.

While it is important to concentrate on Federal assistance programs such as CETA, it is also important that the Directorate determine the extent of the Department's control over funds, property, and other assets for which it is responsible through audits of internal operations.

RECOMMENDATION

The Budget and Accounting Procedures Act of 1950 contemplates that the head of an agency assure himself of the adequacy of staffing and the scope of internal audit arrangements in his agency; therefore, we recommend that you make an assessment of the audit function to determine what action should be taken to provide effective audit coverage of the Department's internal financial operations.

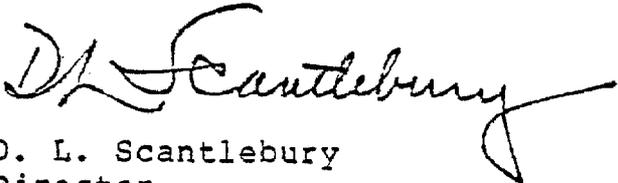
As you know, section 236 of the Legislative Reorganization Act of 1970 requires the head of a Federal agency to submit a written statement on actions taken on our recommendations to the House and Senate Committees on Government Operations not later than 60 days after the date of the report and to the House and Senate Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of the report. We would appreciate receiving copies of these statements.

We are sending copies of this report to the Director, Office of Management and Budget; the Chairmen of the House and Senate Committees on Appropriations and on Government Operations; the Assistant Secretary for Administration and Management; and the Directorate of Audit and Investigations of the Department of Labor.

B-133182

We appreciate the courtesies and cooperation extended to our representatives during our review. We are looking forward to receiving your comments concerning the matters discussed in this report.

Sincerely yours,

A handwritten signature in cursive script that reads "D. L. Scantlebury". The signature is written in dark ink and is positioned above the typed name and title.

D. L. Scantlebury
Director

BEST DOCUMENT AVAILABLE

SUMMARY OF MAJOR AREAS
OF FINANCIAL INTEREST FOR REVIEW AND
EVALUATION BY AGENCY INTERNAL AUDIT ORGANIZATIONS

Cash

General

- Internal control procedures
- Adequacy of records and procedures
- Cash accounts identified by appropriation and/or fund
- Periodic or surprise cash counts
- Reconciliation of cash with the Treasury Department
fund balances
- Compliance with laws and regulations
- Reports

Collections

- Physical control
- Cash recorded immediately after receipt
- Timely deposit of cash receipts
- Excessive funds on hand
- Cash in transit--cutoff dates

Disbursements

- Pre-audit prior to approval for disbursement
- Disbursement recorded promptly in records
- Disbursement in transit at time of cutoff

Imprest Funds

- Compliance with fund restrictions
- Advances
- Reimbursements--service provided
- Adequacy of invested capital

Other

- Investments

Receivables

- Internal control procedures
- Compliance with laws and regulations
- Receivables identified by appropriation and/or fund

Receivables (con.)

Classification of receivables:

a) Interagency/fund

b) External

Price established on documentation for:

a) Actual cost

b) Estimated cost

Accounts reviewed, delinquent accounts identified

Provisions for doubtful accounts

Control--adjustments and writeoffs

Collection and liquidation of receivables

AdvancesTravel

Internal control procedures

Administrative control over travel

Compliance with travel regulations

Control over Government travel regulations

Timely settlement of employees' travel advances

Authorized expenses

Contractors

Liquidation--services provided/returned

Grantees

Liquidation--services provided/returned

Property

Internal control procedures

Policy, procedures, and recordkeeping

Integrated property and financial records

Account classification:

a) Furniture/fixtures

b) Equipment

c) Plant and equipment

d) On assignment--other

e) On assignment--from others

f) Supplies and materials

Property (con.)

Property valuation established on documentation for:

- a) Cost
- b) Estimated
- c) Salvage

Compliance with laws and regulations

Physical control:

- Acquisition
- Removal
- Utilization of property
- Excess property
- Identification

Timely recording in the property/financial records

Control over loss/writeoffs

Reconciliation of physical inventories with property records/financial

Depreciation/obsolescence

Evaluation of maintenance costs and economic value

Liabilities

Internal control procedures

Account classification:

- a) Accounts payable
- b) Contract provisions
- c) Accruals
- d) Intergovernmental/fund
- e) Advance payments
- f) Contingencies
- g) Unfunded
- h) Long-term debts

Timely recording of liabilities

Accounts identified by appropriation/fund

Liquidation of liabilities

Support/pricing of liabilities

Administrative control of funds

Internal control procedures

Separation of accounts by appropriation/fund

- a) Apportionment
- b) Subdivision of funds
- c) Obligations
- d) Disbursements
- e) Reporting

Administrative control of funds (con.)

Compliance with laws/regulations
 Incurrence of obligations:
 a) Authority
 b) Availability of funds:
 Precertification
 Commitment accounting
 c) Compliance with 1311 criteria
 d) Timely recording
 Policy and procedures
 Liquidation and recoument of excess obligations
 Use of "M" accounts
 Reprograming/transfer of funds
 Accounting for proceeds
 Status of funds reports

Revenues

Internal control procedures
 Revenue accounts identified by appropriation/fund
 a) Fees, fines
 b) Reimbursements to appropriation
 Authorized services
 Established fees:
 a) Total costs--supported by accounting records
 b) Estimated/negotiated
 c) Statutory
 Timely recording of billings
 Adjustments/writeoffs
 Compliance with laws and regulations
 Comparison amounts billed/cost of services provided

Costs

Internal control procedures
 Timely recording in accounts
 Separation of costs
 a) Pay and allowance
 b) Direct
 c) Indirect
 d) Depreciation
 e) Contracts/grantees
 f) Unfunded

Costs (con.)

System integrated with financial records
Basis for costs
Cost reports--full disclosure and useful to management
Comparison of costs to standards of measurements
Compliance with laws and regulations
Allocation of costs

Reports

Full disclosure of financial condition
Compliance with laws and regulations
Supported by accounting system
Usefulness to management
Timeliness of reports
Accurate, reliable, truthful
Comparison of budgeted/programed costs with actual
Footnoted as required

Other

Approved systems implemented
Followup prior recommendations

Copies of GAO reports are available to the general public at a cost of \$1.00 a copy. There is no charge for reports furnished to Members of Congress and congressional committee staff members. Officials of Federal, State, and local governments may receive up to 10 copies free of charge. Members of the press; college libraries, faculty members, and students; and non-profit organizations may receive up to 2 copies free of charge. Requests for larger quantities should be accompanied by payment.

Requesters entitled to reports without charge should address their requests to:

U.S. General Accounting Office
Distribution Section, Room 4522
441 G Street, NW.
Washington, D.C. 20548

Requesters who are required to pay for reports should send their requests with checks or money orders to:

U.S. General Accounting Office
Distribution Section
P.O. Box 1020
Washington, D.C. 20013

Checks or money orders should be made payable to the U.S. General Accounting Office. Stamps or Superintendent of Documents coupons will not be accepted. Please do not send cash.

To expedite filling your order, use the report number in the lower left corner and the date in the lower right corner of the front cover.