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BY THE COMPTROLLER GENERAL
**Report To The Chairman, Legislation And
National Security Subcommittee, House
Committee On Government Operations
OF THE UNITED STATES**

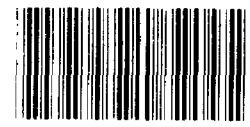
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**Federal Agencies Negligent In
Collecting Debts Arising From Audits**

Each year, auditors detect and report hundreds of millions in questionable expenses charged to the Government by contractors and grantees. Agencies are required to collect without delay all expenditures determined to be improper.

Despite Federal laws and regulations, as well as congressional hearings and other GAO reports on debt collection problems in recent years, Federal agencies still have not developed adequate systems to properly settle audit-related debts. GAO found that Federal agencies have (1) ineffective collection systems, (2) poor management practices, and (3) little assurance that amounts collected are not in fact Government money.

GAO makes specific recommendations for improving agencies' collection systems.



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

B-200473

January 22, 1982

The Honorable Jack Brooks
Chairman, Legislation and
National Security Subcommittee
Committee on Government Operations
House of Representatives

Dear Mr. Chairman:

This report is in response to your October 20, 1981, request that we examine procedures of Federal departments and agencies for collection of audit disallowances.

This is the third in a series of reports on how Government agencies follow up and resolve findings identified through the audit process. Our two previous reports showed inadequate systems for tracking audit findings and excessive delays in determining the propriety of costs questioned during audits. This report concentrates on the debt collection phase of the audit resolution process which begins once questioned costs are disallowed.

We found that Federal agencies generally are doing a poor job of managing and collecting these debts. Most agencies do not know the total amount of audit-related debt owed to them, nor do they collect known debts promptly or charge interest, as required, when payments are late. And, when debts are paid, agencies usually do not know whether the amounts received have been taken from their own or other Federal programs. Furthermore, some Federal agencies avoid altogether the collection of some debts. For various reasons they assume the responsibility for terminating debts rather than collecting them.

As you requested, we did not obtain agencies' official comments on this report. As arranged with your office, we plan no further distribution of this report until 30 days from its date unless you advise otherwise or publicly announce its contents earlier. At that time, we will send copies to interested parties and make copies available to others upon request.

Sincerely yours,

A handwritten signature in cursive script that reads "Charles A. Bowsher".

Comptroller General
of the United States

COMPTROLLER GENERAL'S REPORT
TO THE CHAIRMAN, SUBCOMMITTEE
ON LEGISLATION AND NATIONAL
SECURITY, HOUSE COMMITTEE ON
GOVERNMENT OPERATIONS

FEDERAL AGENCIES NEGLIGENT
IN COLLECTING DEBTS ARISING
FROM AUDITS

D I G E S T

Federal agencies are doing a poor job of managing and collecting audit-related debts owed by contractors and grantees such as State and local governments. Most agencies do not know the total amount owed to them, nor do they collect debts promptly or charge the required interest when payments are late. When they are paid, agencies usually do not know whether the amounts received have been taken from their own or other Federal programs. Also, some Federal agencies avoid collecting some of their debts altogether.

POOR ACCOUNTING AND COLLECTION
CONTROL SYSTEMS

GAO found that Federal agencies' collection systems are so inadequate that the total amount of audit-related debt due the Government cannot be determined, and the small portion that can be identified (\$374 million) remains uncollected for years. Much of this delay in collection is because Federal agencies lack an aggressive collection effort. Some debt is never collected; for instance, one agency dismissed over \$2.4 million in audit-related debts based on its view that the debts had become uncollectible because of the statute of limitations.

Based on (1) a questionnaire sent to the 36 agencies with the largest dollar amounts of monetary audit findings and (2) a detailed audit at seven Federal agencies, GAO concluded that agencies

- are slow to determine the amount of the debt so it can be pursued (see p. 7),
- do not promptly bring debts under accounting control (see p. 7),
- do not effectively monitor collections (see p. 9), and

--rarely pursue collection of debts incurred when subrecipients misspend funds (see p. 14).

POOR MANAGEMENT CONTROL PRACTICES

In addition to system problems, GAO noted a number of poor management practices at most Federal agencies which significantly contribute to their inability to collect audit-related debts promptly and effectively. Specifically, GAO noted that agencies

--are inappropriately "forgiving" millions of dollars of audit-related debts without a reasonable collection effort as required by the Federal Claims Collection Standards (see p. 19),

--have allowed legitimate appeal processes to be used by grantees to delay payment of their debts, thus retaining Federal funds at a cost to the Government of millions of dollars (see p. 21), and

--have not charged interest over the last 3 years on hundreds of millions of dollars in delinquent debts although required to charge interest by the Federal Claims Collection Standards (see p. 23).

NO ASSURANCE REQUIRED THAT GRANTEE PERFORMANCE IS MAINTAINED WHEN DEBTS ARE PAID

In addition to the widespread lack of accounting and collection controls and the poor management practices cited throughout this report, GAO found that Federal agencies can unknowingly accept their own or other Federal funds as payment of audit-related debts at the expense of intended program objectives. Agencies use two primary methods to recover audit disallowances--offset and cash recovery. When agencies settle debts by offsetting grantees' indebtedness against grant advance payments, they usually do not have adequate assurance that the program itself is not reduced. When audit-related debts are repaid in cash, agencies are often unaware of the effect. Payments may reduce funds available for other Federal programs. GAO believes (1) that Federal agencies should require assurance from grantees that payments do not diminish performance of Federal programs and (2) that this should be verified during future program managers' visits and future audits. (See p. 26.)

RECOMMENDATIONS

GAO recommends that the head of each department or agency implement policies and procedures that:

- Require a written determination of the allowability of all questioned costs within 6 months of audit report issuance.
- Ensure establishment of accounts receivable for all disallowed costs within 30 days of the written determination of indebtedness.
- Ensure aggressive collection action in accordance with the Claims Collection Standards, which include written demands for payment at 30-day intervals, affecting the debtor's credit rating, offsetting the debt against amounts due from other Federal programs, and suspension or termination of funding.
- Hold grantees fully responsible for the debts of their subgrantees and apply the Claims Collection Standards in collecting these amounts from grantees.
- Ensure compliance with the Claims Collection Standards to preclude the termination of any debts over \$20,000 and ensure that all Claims Collection Standards concerning compromise and termination are met before settling debts of \$20,000 or less.
- Streamline the audit disallowance appeal process to ensure that unnecessary delays are eliminated and that interest is charged on all amounts under appeal.
- Require interest to be charged and collected on all debts at the rate specified by the Treasury Fiscal Requirements Manual, beginning no later than 30 days from establishment of the debt and continuing until collection or final disposition.
- Require grantees to certify that their payment of audit-related debts does not reduce the level of benefits of any Federal program and institute program and audit followup.

GAO also recommends that the Director, Office of Management and Budget incorporate these recommendations into the management circular on audit

resolution and follow up to ensure that agencies are complying.

AGENCY COMMENTS

At the request of the Legislation and National Security Subcommittee, House Committee on Government Operations, GAO did not obtain agencies' official comments on this report.

C o n t e n t s

	<u>Page</u>
DIGEST	i
CHAPTER	
1	INTRODUCTION 1
	Costs disallowed through the audit process are debts due the Government 2
	Federal collection legislation and regulations 3
	Claims Collection Act 3
	Accounting and Auditing Act 3
	Objectives, scope, and methodology 4
2	POOR ACCOUNTING AND COLLECTION CONTROL SYSTEMS CAUSE INEFFECTIVE DEBT COLLECTION 6
	Agencies are still slow to determine amount of debt 7
	Accounting control is not established promptly if at all 7
	Some agencies have no accounting control over audit-related debts 8
	Weak collection monitoring leads to costly delays 9
	Debt remains outstanding too long because of ineffective monitoring 10
	Collection actions are lax 12
	Collection of subgrantee debts is also inadequate 14
	Federal agencies are not requiring grantees to repay subgrantee debts promptly 15
	Conclusions 17
	Recommendations 17
3	POOR MANAGEMENT PRACTICES CONTRIBUTE TO INEFFECTIVE DEBT COLLECTION 19
	Agencies inappropriately terminate debts rather than collect them 19
	Department of Agriculture disregards Claims Collection Standards 19
	Debt appeals process provides grantees opportunity to delay 21
	Most disallowed costs are appealed 21
	The appeals process is time consuming 21
	Interest should be accrued on debts under appeal 23

	<u>Page</u>
Charging interest on delinquent debts would improve collections	23
Regulation requires interest charges on delinquent debt and installment payments	23
Interest is seldom, if ever, assessed on audit-related debts	24
Agencies have not charged interest for various reasons	24
Conclusions	25
Recommendations	25
 4	
NO ASSURANCE IS PROVIDED THAT PROGRAM PERFORMANCE IS NOT REDUCED WHEN DEBTS ARE PAID	26
Debt collection by offset may have negative consequences	26
Performance level may not be maintained when debts are paid in cash	27
Assurance is needed that benefits are being maintained	28
Conclusion	28
Recommendation	28

APPENDIX

I	October 20, 1981, letter from the Chairman, Subcommittee on Legislation and National Security, House Committee on Government Operations	29
II	Agency magnitude and disposition of disallowed costs	30
III	Agency variances in procedures for handling disallowed costs	40

ABBREVIATIONS

CETA	Comprehensive Employment and Training Act
FNS	Food and Nutrition Service
GAO	General Accounting Office
OMB	Office of Management and Budget
HUD	Housing and Urban Development
EPA	Environmental Protection Agency
HHS	Health and Human Services

CHAPTER I

INTRODUCTION

Each year, auditors detect and report hundreds of millions of dollars in misspent funds. It is the responsibility of agency management to see that these funds are accounted for and collected without delay. Failure to effectively follow up and collect audit-related debts results in a loss of funds as well as a waste of audit resources.

This is the third in a series of reports on how Government agencies follow up on and resolve findings identified through the audit process. Our first report 1/ identified at 34 agencies nearly 14,000 audit reports containing unresolved findings involving more than \$4.3 billion in potential recoveries, penalties, revenues, or savings. Our second report 2/ showed the problem had worsened.

On February 25, 1981, the Comptroller General testified on both reports before the Subcommittee on Legislation and National Security, House Committee on Government Operations. In September 1981, based on the Subcommittee hearings and our reports, the House Committee on Government Operations issued a report entitled "Continued Failure of Departments and Agencies to Take Effective Action on Audit Findings."

Audit resolution and related debt collection are a significant part of the entire Federal debt collection process. Both GAO and the Congress have been actively seeking improvements in the Government's ability to collect all debts. For example, two bills have been introduced in Congress to help alleviate debt collection problems: the Debt Collection Act of 1981 (S. 1249) and the Debt Collection Improvement Act of 1981 (H.R. 2543).

Primarily as a result of earlier GAO and committee reports on audit resolution, as well as other GAO and congressional work in the broad area of debt collection, the executive branch has attempted to strengthen the entire audit resolution and debt collection process. In December 1979, for example, the Office of Management and Budget (OMB) issued new policy guidance to agency management in a revised Circular A-73. Even more recently, OMB proposed additional changes to its management circulars. OMB also established a special debt collection project under the sponsorship of the President's Management Improvement Council to review

1/"More Effective Action is Needed on Auditors' Findings--Millions Can be Collected or Saved" (FGMSD-79-3, Oct. 25, 1978).

2/"Disappointing Progress in Improving Systems for Resolving Billions in Audit Findings" (AFMD-81-27, Jan. 23, 1981).

the Government's credit management and debt collection policies and practices. In addition, the President's Council on Integrity and Efficiency has recognized the importance of improving debt collection and has made it a priority issue.

Considerable attention has been focused in recent years on inadequacies in the audit resolution process. Both the Senate and the House of Representatives have held hearings on numerous occasions disclosing inadequate systems for tracking audit findings and excessive delays in determining the amounts to be disallowed. The purpose of this report is to discuss the effectiveness of the debt collection process pertaining to amounts that auditors and Federal program officials agree were misspent by grantees and contractors. It is important to point out that the grantees we refer to throughout this report are typically State or local government entities or community-based organizations, not disadvantaged or underprivileged individuals.

COSTS DISALLOWED THROUGH THE AUDIT
PROCESS ARE DEBTS DUE THE GOVERNMENT

Federal departments and agencies manage hundreds of programs worldwide, including over 1,160 Federal assistance programs funded mostly through grants. In fiscal 1981, Federal grants-in-aid to State and local governments alone exceeded \$95 billion.

It is vital to ensure that the funds the Congress appropriates for these programs are not spent improperly or for unauthorized purposes. When grantees or contractors are handling the money, audit of their records is the Government's principal safeguard against unauthorized expenditures. Federal departments and agencies spend almost half a billion dollars on audits each year. These audits aid management by independently evaluating the effectiveness of controls over program activities and by determining whether funds are spent in accordance with laws, regulations, and program objectives.

Audits often identify sizable amounts that should be returned to the Government by contractors who have claimed costs that are not allowed under Government contracting regulations, or by grantees who have not met the requirements of their grant agreements. The auditors report such amounts as questioned costs to agency management for resolution and collection. If management agrees that the grantee or contractor is not entitled to the questioned costs, the costs are disallowed and become debts due the Government.

Not all audit findings involve potential recovery of funds. Many involve changes in procedures or other improvements that are intended to upgrade the economy, efficiency, or effectiveness of agency operations, thus saving costs in the future.

But when audit findings indicate that grantees or contractors have spent Federal funds for unauthorized purposes, the misspent funds should be promptly recovered. The identification and recovery of debts should proceed as follows:

- The auditors issue a report to agency management questioning any expenditures that appear to violate laws or regulations.
- Program managers resolve the auditors' findings by reviewing their reports and the grantee's or contractor's comments and deciding whether expenditures were indeed improper and should be disallowed.
- Managers notify the grantee or contractor of the need to return the disallowed costs, and establish an accounting record of the debt.
- If the grantee or contractor does not repay promptly, managers take additional steps to collect the debt.

FEDERAL COLLECTION LEGISLATION AND REGULATIONS

Several laws and regulations require the head of each executive agency to aggressively pursue collection of all debts arising from audit disallowances and to establish and maintain systems of accounting and internal controls over the collection of such debts. Two important laws require rigorous accounting and collection controls: the Claims Collection Act and the Accounting and Auditing Act.

Claims Collection Act

The major legislative authority for debt collection in the Federal Government is the Federal Claims Collection Act of 1966 (31 U.S.C. 951). The act requires the Comptroller General and the Attorney General to issue joint regulations implementing the law. The regulations (4 C.F.R. 101-105) are entitled "The Federal Claims Collection Standards," and have the force and effect of law.

The act imposes primary responsibility for collecting debts due the Government on the agencies whose operations give rise to such indebtedness. Furthermore, the Standards require agencies to take aggressive collection action and collect amounts due, when feasible, by offsetting future payments to the debtor.

Accounting and Auditing Act

The Accounting and Auditing Act of 1950 (31 U.S.C. 66a) requires the head of each executive agency to establish and maintain systems of accounting and internal controls. The purpose of this requirement is to provide adequate assurance of the

legality, propriety, and correctness of disbursements and collections of public funds.

Agency accounting systems should conform to the principles, standards, and related requirements prescribed by the Comptroller General. Guidance for developing systems is found in the General Accounting Office Policy and Procedures Manual for the Guidance of Federal Agencies. Title 2 of this manual, entitled "Accounting," sets forth internal financial controls designed to ensure that all debts are accounted for as assets from the time claims arise until they are collected, converted into other resources, or determined to be uncollectible. Accounting for such receivables is an important form of control over agency resources that results in a systematic record of amounts due.

OBJECTIVES, SCOPE, AND METHODOLOGY

During hearings held by the Subcommittee on Legislation and National Security, the seriousness of deficiencies in the collection of audit disallowances received much discussion. Because of continuing concern about this area, the Subcommittee Chairman asked us to give high priority to this audit. Our audit objectives were to

- determine the magnitude of debts attributable to audit disallowances Government-wide;
- evaluate the procedures by which agencies account for, control, and collect these debts;
- identify the causes of any delays in collection; and
- assess the impact of the various collection methods on Federal programs.

To accomplish these objectives, we asked 36 Federal agencies to answer a questionnaire on their policies and procedures for establishing debts for disallowed costs and to provide statistics on the disposition of these debts over the last 3 years. The 36 agencies were selected because they had been identified in our previous report 1/ as having the largest amount of monetary audit findings. One agency did not respond; 3 agencies told us their operation did not lend itself to this type of debt, and the other 32 agencies provided responses to all or some of our questions. We did not verify the accuracy of the data agencies provided. However, where we performed detailed audit work, we found that certain agency responses to the questionnaire conflicted with our findings. A presentation of agencies' responses is in appendixes II and III.

1/"Disappointing Progress in Improving Systems for Resolving Billions in Audit Findings" (AFMD-81-27, Jan. 23, 1981).

In addition to using questionnaires, we audited the debt collection efforts at selected regional offices and headquarters of 7 of the 36 agencies. These agencies were the Departments of Agriculture, Education, Health and Human Services (HHS), Housing and Urban Development (HUD), Labor, and Transportation, and the Environmental Protection Agency (EPA).

At most of the seven agencies we evaluated the effectiveness of debt collection efforts by assessing the agencies' handling and disposition of all amounts they disallowed during fiscal 1978 to 1980. Since some agencies did not have records of disallowed costs, we evaluated audits with questioned costs, tracing these findings through the audit resolution process to determine the disallowed costs. Where it was necessary to begin the evaluation by selecting audit reports, we selected all audit reports issued during fiscal 1978 to 1980 with questioned costs of \$5,000 or more. All assessments involved reviewing and analyzing accounting records and files as well as discussing aspects of debt collection efforts with agency officials. Altogether, we evaluated the effectiveness of actions taken on \$315.4 million of audit-related debts resulting from 1,567 separate audits.

This audit was made in accordance with generally accepted Government auditing standards. Our approach was Government-wide; individual agencies were not the primary focus of this review. Agencies are cited only to illustrate problems found throughout the Government.

CHAPTER 2

POOR ACCOUNTING AND

COLLECTION CONTROL SYSTEMS CAUSE

INEFFECTIVE DEBT COLLECTION

Despite statutory and administrative requirements to carefully control and aggressively collect debts, our audit revealed that Federal agencies are poorly managing audit-related debts. As a result, the total amount of audit-related debt due the Government cannot be determined, and the small portion that can be identified remains uncollected for years because Federal agencies fail to take aggressive action. They lack collection systems that would ensure that audit-related debt is carefully controlled and aggressively pursued as it is processed through agencies.

In a questionnaire we sent in August 1981 to the 36 agencies with the largest amounts of monetary audit findings, we asked agencies to provide the amount of audit-related debt outstanding. We received the following responses:

- One failed to respond (Community Services Administration, which terminated operation on Sept. 30, 1981).
- Three reported that their operation did not lend itself to this type of debt.
- Thirteen reported that they had no such debt or that they were unable to readily determine the amount of audit-related debt outstanding.
- Nineteen reported \$374 million of audit-related debt outstanding as of June 1981.

Because of the widespread lack of adequate systems to control these debts, we believe the figure is grossly understated even by those agencies that did attempt to provide an amount.

After a more detailed review at seven of the agencies responding to the questionnaire, we concluded that the basic reason for ineffective debt collection is that agencies

- are slow to determine the amount of the debt,
- do not promptly bring debts under accounting control,
- do not effectively monitor collections, and
- rarely pursue collection of debts at subrecipient levels.

AGENCIES ARE STILL SLOW
TO DETERMINE AMOUNT OF DEBT

The first step in collecting debts that result from audit findings is determining the amount of debt. We found that the resolution of auditors' findings is still a Government-wide problem despite two previous GAO reports, congressional hearings on four occasions since March 1979, and two House Government Operations Committee reports all dealing with the need to improve audit resolution in the Government.

Our audit disclosed that many agencies are still not complying with the OMB requirement to make written determinations on all audit findings within 6 months after issuance of audit reports. At four of the seven agencies where we performed audit work, it was not uncommon for agencies to take up to 2 years to make these written determinations. Two specific examples typify the delays:

- In August 1978, HUD issued a report on an audit of a Community Development Block Grant in which questioned costs amounted to \$2.3 million. It was not until May 1981 (2-1/2 years later) that HUD determined the amount of costs to be disallowed. As of June 1981, a receivable had not been established and nothing had been collected.
- A March 1975 Department of Transportation audit questioned a grantee's expense of approximately \$1.4 million. The grantee corresponded with the Department several times regarding the audit findings between April 1975 and January 1976, but not until January 1978 was the grantee again asked to respond to the unresolved audit findings. Correspondence between the Department and the grantee began again in February 1978 and lasted over a year. The Department finally disallowed \$265,156 in April 1981, approximately 6 years after the audit. As of November 1981 the debt still was not collected.

ACCOUNTING CONTROL IS NOT ESTABLISHED PROMPTLY
IF AT ALL

OMB Circular A-73 requires Federal agencies to maintain appropriate accounting and collection controls. However, many Federal agencies still have not established basic internal controls to ensure that debts are appropriately accounted for and promptly collected. Debts must be brought under accounting control as soon as possible after the questioned costs have been disallowed. Furthermore, such control must be maintained throughout the collection process to ensure timely repayment.

Some agencies have no accounting control
over audit-related debts

As we said in chapter 1, the Accounting and Auditing Act of 1950 requires the head of each executive agency to establish and maintain systems of accounting and internal controls. The responsibility includes providing adequate assurance of the legality, propriety, and correctness of disbursements and collections of public funds. All amounts determined to be due the Federal Government must be accounted for as receivables from the time claims arise until they are collected, converted into other resources, or determined to be uncollectible.

Four of the seven agencies audited did not even account for audit disallowances as receivables. Nine other agencies, in responding to our questionnaire, also indicated that they did not establish accounts receivable for disallowed costs. This failure to establish accounting control over disallowances understates assets reported on financial statements and has an impact on the collection effort. For example:

--Environmental Protection Agency officials disallowed \$49,206 in August 1978 for improper indirect cost charges. In April 1979, program officials decided to withhold that amount from future grants to minimize hardship on the grantee. ^{1/} However, no accounting controls were established to ensure that the withholding occurred. Officials forgot to reduce the grant awards and it was not until we asked about the debt's status that EPA realized the collection had not been made. As of October 1981, the debt was still outstanding.

--In December 1971, the Department of Agriculture issued an audit report on a county's food stamp program, questioning costs of \$713,272. It is not clear from the available records when the costs were disallowed. No receivable was ever established. In April 1980, the Department's national office sent the grantee a "third billing letter." However, the regional office staff could find no record of a first or second billing in the intervening 8 years. The Department reduced the disallowance to \$52,768 in April 1981 and finally recovered the debt in August 1981, 9-1/2 years after the audit.

--In June 1973, the Department of Transportation issued an audit report with questioned costs of \$68,720 pertaining to unallowable and unsupported grant costs. The grantee responded to the audit report in April 1974, but it was not until July 1979, more than 5 years later, that the

^{1/}This method of settlement may be inappropriate. See ch. 4 for discussion of debt payment methods.

Department sent the first demand for payment of the disallowed amount of \$55,613. No accounting controls were ever established over the debt. When the grantee refused to pay, the Department said it would deduct the debt from \$658,029 which the grantee had requisitioned under another grant. The requisition was then processed. However, Transportation officials not only failed to deduct the disallowance, they also paid the grantee twice for the \$658,029 requisition. In May 1981, the grantee returned the duplicate payment. Finally, in July 1981 the Department deducted the \$55,613 from another requisition, but as we point out in chapter 4, this reduction could have a negative effect on the program.

Only two of the seven agencies audited routinely accounted for audit disallowances as receivables. Even where procedures had been in effect for some time, agencies ignored them, causing delays in setting up receivables. The Department of Education, for example, took an average of 168 days to set up a receivable for cash collection cases. At the Health Services Administration, HHS, the average time to record 42 audit disallowances as receivables was 81.5 days; for 22 other audit disallowances involving \$490,000, the finance office failed altogether to establish accounts receivable. Two cases illustrate the delays in more detail:

- The agency disallowed \$589,940 in February 1978. A receivable was not established until December 1979. The documents supporting this case were scattered among three separate offices. As of October 1981, the debt was uncollected and the three files had not been consolidated and reconciled to determine the correct amount due.
- The agency disallowed \$163,431 in August 1977. Almost a year later, in June 1978, the finance office was advised to establish a receivable but to delay collection action because of the grantee's appeal. The appeal was denied in June 1979, but collection was not made until July 1980.

One of the reasons for delays in bringing audit-related debts under accounting control is the lack of control over key documents used to establish accounts receivable. At the Department of Education, for example, these documents often were received by the finance office months after the monetary audit findings had been disallowed.

WEAK COLLECTION MONITORING LEADS TO COSTLY DELAYS

At all the agencies we visited, the debt collection function was given low management priority. Collection practices were not adequate to ensure that audit-related debts due the Government were promptly recovered. At each of the agencies audited, some of the following deficiencies were noted: agencies were not

reviewing agency receivable reports, following up promptly on delinquent accounts, assessing debtors' ability to pay before agreeing to installment payments, or referring debts to a higher authority when collection efforts were ineffective. Consequently, grantees and contractors held Federal funds long after it was determined that they were not entitled to them.

Another hindrance to prompt collection was the lack of definition of responsibilities and of an adequate system to coordinate the multitude of players involved in the resolution and collection process. Program offices, finance offices, regional and headquarters offices, audit staffs, appeals resolution boards, and the grantees and contractors themselves, each represent a different perspective and all have an interest in participating in the process. When the responsibilities and authority of each are not clearly defined and when coordination among participants is lacking, audit-related debts can go uncollected for a long time, sometimes permanently.

Debt remains outstanding too long
because of ineffective monitoring

Many audit-related debts are not being collected because agencies lack comprehensive, unified systems for monitoring the collection function. We found that even when agencies established accounts receivable, this frequently was not sufficient to ensure prompt collection. OMB Circular A-73 requires that agencies maintain accurate records of all significant findings until final resolution, including appropriate accounting and collection controls over amounts due the Government, and periodically evaluate whether the audit followup system is adequate for prompt and proper resolution of findings. At the agencies we audited, poor or nonexistent monitoring systems contributed to poor debt collection. For example, at some agencies overlapping responsibilities between program offices and finance offices made collection efforts difficult at best. Furthermore, inadequate monitoring of accounts receivable allows cases to remain outstanding for long periods with no action being taken.

The following cases illustrate the need to improve monitoring of receivables resulting from audit disallowances.

--In May 1980, the Health Services Administration's finance office established \$21,600 in disallowed contract costs as a receivable. In June 1980, the contract office agreed to accept monthly installment payments beginning June 30, 1980, but did not inform the finance office, which sent demand letters for the entire \$21,600 in July and September. The contract office meanwhile received the first installment payment in July. After the second demand letter, the grantee notified the finance office of the installment arrangement. In October 1981, the contractor was behind in its payments, some of which were sent to the contract office and some to

the finance office. Decentralization and lack of coordination delayed collection. The contract office inappropriately performed finance functions and did not evaluate the contractor's ability to pay the debt in one lump sum before authorizing installments.

--At the Department of Education's finance office, we were unable to locate 49 of the 970 accounts receivable records selected for review. Finance office staff could neither locate the files nor tell us the status of each case. As long as these cases are missing from the files, collection controls are nonexistent. Some of these receivables may have been paid and the files closed. Although the total magnitude of the debt in these cases is unknown, we do know that 12 of them involve \$733,132. Without monitoring and reviewing the records, however, it is impossible to determine how much has been collected and how much might be lost as a result of the failure to monitor and control the cases.

Another problem arises because grantees frequently appeal audit disallowances in whole or in part. At some agencies the finance offices place appealed cases in a pending status and do not pursue collection action on them, regardless of the amount appealed. Therefore, even those portions of the disallowances that grantees have not contested are not pursued until a decision is made on the appeal. Furthermore, when appeals are ultimately withdrawn or resolved, the appeals boards often do not promptly advise the finance offices of the outcome. In these situations, collections are further delayed. For example:

--At the Department of Education, the finance office does not resume collection action after an appeal until directed to do so by the program office or the appeals board. In June 1981, the finance section was unaware of several resolved appeals totaling \$101,230 which had been settled in the Government's favor for an average of 4 months.

--At the Health Care Financing Administration, HHS, debts sustained after the appeal were similarly slow to be collected. The average delay between the appeals board decision and the recovery of debts involving \$16,307,698 was nearly a year. Several appealed debts that had been upheld, involving \$8,642,885, remained uncollected for an average of over 5 months as of August 1981. Furthermore, the agency does not adequately monitor withdrawn appeals. As of August 1981, officials were not yet aware that appeals had been withdrawn and collection should be pursued on two debts of \$466,687 and \$69,945, even though this had been the case for 9 and 8 months, respectively.

--The Department of Labor transfers jurisdiction over appealed audits to its Solicitor's Office. However, no debt collection actions are pursued on uncontested portions. In one region, a total of \$170,621 that was unchallenged had been outstanding an average of 9 months as of July 31, 1981.

In response to our questionnaire, 13 of the agencies provided data that clearly confirm the time lag in debt collection. Audit disallowances for these 13 agencies totaled at least \$116 million in fiscal 1978, \$210 million in fiscal 1979, and \$325 million in fiscal 1980. Substantial portions of each year's disallowances were still outstanding as of June 30, 1981--\$9.2 million for fiscal 1978, \$18 million for fiscal 1979, and \$78 million for fiscal 1980. On the whole, 51.6 percent of audit disallowances remain outstanding for more than a year. The following chart shows the average time the 13 agencies estimated their open audit-related debts had been outstanding as of June 30, 1981.

<u>Time outstanding at 13 agencies</u>	<u>Percent of disallowances</u>
Less than 1 year	48.4
1 to 2 years	24.8
2 to 3 years	14.8
3 to 4 years	7.8
4 years or more	<u>4.2</u>
	<u>100.0</u>

Collection actions are lax

The Federal Claims Collection Standards impose primary responsibility for collecting debts due the Government on the agencies whose operations give rise to such indebtedness. These Standards direct agency heads to take prompt, aggressive action, with effective followup, to collect debts due the United States. Prescribed techniques include sending written demands for payment at 30-day intervals, collecting debts through offset against later payments, seeing that credit ratings are affected, charging interest on delinquent debts, and exploring alternatives such as installment collection or compromise. Agencies should document all collection efforts and retain the documentation.

Our audit showed that agency followup efforts have been irregular and infrequent. Even in those cases where costs were disallowed and receivables established, aggressive collection action often was neglected; cases remained outstanding without action for long periods of time.

Finance office and program staff complained that a continued high volume of work and shortage of staff caused the failure to pursue collection activities promptly. Audit-related debts were sometimes left to be collected by chance--as when we brought problem cases to agency officials' attention. Meanwhile, grantees and contractors have no incentive to return the Federal funds in their possession since interest usually is not charged on delinquent debts, as discussed in detail in the next chapter. For example:

--The Department of Education took over a year to settle a debt. In August 1980, Education determined that \$1,312,242

should be disallowed, and established a receivable. After notification in December 1980, the grantee furnished additional information on the disallowance. Education officials, however, took 9 months to evaluate this information and to decide on a course of action. In September 1981, Education finally decided that the amount due the Government should be revised to \$615,159 and the grantee settled the debt within 1 month of this revision.

--In June 1978, the Department of Transportation issued an audit report questioning costs of \$28,995 for overpayments to the same grantee on two projects. Program officials made the first demand for payment in October 1979, after consultation with the grantee and the Department's Chief Counsel. But they took no further action until after we brought the case to their attention. Then they began corresponding with the grantee to determine the status of the disallowance. The grantee repaid the \$28,995 in September 1981, 2 years after the original disallowance.

These disallowed amounts were eventually recovered; however, we found that agencies still have backlogs of open audit disallowances. The following cases illustrate the ongoing problems and lengthy delays in collecting audit-related debts.

--Environmental Protection Agency auditors questioned salary and fringe benefit charges of \$187,071 in a September 1974 audit report. It took 5-1/2 years, until April 1980, to resolve the audit and determine that \$177,001 was unallowable. The first followup after the disallowance was in July 1980. Thereafter the case languished until February 1981, when EPA attached a condition to a 1981 grant that required repayment of the debt within 30 days of acceptance. The grantee subsequently proposed a repayment schedule that EPA officials rejected. EPA officials did not act again until October 1981, when they agreed to a revised proposal for settling the debt by three equal reductions of the grantee's letter of credit. EPA agreed not to charge interest if the reductions were made as scheduled. This debt has been "in the process" for over 7 years and probably will not be completely settled for at least another 2 years. As we point out in chapter 4, offsetting a grantee's letter of credit may not be a satisfactory settlement.

--In April 1974, Department of Agriculture auditors found that a school district was overreimbursed \$1,343,292 because it provided free or reduced-price meals without regard to students' eligibility. In June 1975, a school district official could not support this action and agreed to repay the amount questioned. No collection action was taken, however, until 4 years later, when Agriculture officials contacted the State agency to request payment. In April 1980, Agriculture officials told the State agency to bill the

school district for the \$154,185 and consider the remainder of the claim unresolved. The school district paid this amount in July 1980. In June 1980, Agriculture determined the unresolved portion of the claim to be a debt of \$1,268,892, but did not inform the State agency until March 1981. The debt is still open, with no interest being charged although the case has been outstanding for over 6 years.

--The audit of a Community Development Block Grant in January 1979 questioned \$137,012 for costs not supported by the grantee's records. Fifteen months later, in April 1980, HUD disallowed the costs after receiving no response from the grantee. In September 1980, the HUD program office referred the claim to its claims collection officer in Washington. No receivable was ever established to control the debt, and no interest has been charged. As of June 30, 1981, the case had been outstanding 434 days with no action taken since September 1980.

Unless debts are aggressively pursued and collected, they may become uncollectible because debtors may use the statute of limitations as a defense to Government efforts to collect through the courts. The Department of Education, for example, terminated action to collect over \$2.4 million in debts established as a result of six audits of State education agencies under the Elementary and Secondary Education Act because the statute of limitations had expired.

COLLECTION OF SUBGRANTEE DEBTS IS ALSO INADEQUATE

Grantees frequently solicit the services of subgrantees to help them perform the conditions of Federal grants. To verify the allowability of subgrantees' expenditures, grantees usually hire independent public accountants to audit the subgrantees' accounting records. If subgrantees spend Federal funds for unallowable purposes, Federal agencies must hold grantees accountable for these amounts and aggressively attempt prompt recovery by adjusting amounts available or claim collection. However, we found that agencies are not aggressively pursuing collection because grantees refuse to repay amounts misspent by their subgrantees unless the subgrantees repay them first. Furthermore, if and when grantees collect from subgrantees, it is not uncommon for them to delay for months the transfer of the money to Federal agencies.

By accepting a Federal grant, the recipient enters into a contractual relationship with the Federal Government to spend funds in accordance with the terms of the grant. Thus, the grantee on its own or through others is accountable for seeing that the grant terms and conditions are adhered to.

The transfer of grant funds from a grantee to its subgrantees does not change what costs are allowable. At some agencies, this principle is specifically defined in the regulations. For example, Labor regulations state that prime sponsors are responsible for

ensuring that their subgrantees expend CETA (Comprehensive Employment and Training Act) funds only on allowable costs. At other agencies this concept is implied in the grant requirements. Many Federal agencies also give the grantee responsibility for auditing its subgrantees and determining whether costs are allowable. When funds spent by subgrantees are for unauthorized expenses, the grantee is accountable to the Federal Government for these funds.

Federal agencies are not requiring grantees to repay subgrantee debts promptly

Despite the fact that Federal agencies must pursue collection from grantees of funds subgrantees have misspent, Federal agencies do not always do so. Agency officials told us that they frequently give up on collecting amounts owed the Government because grantees simply refuse to pay for debts owed by their subgrantees until they have received payment themselves. Often these subgrantees are small, community-based, not-for-profit organizations that use Federal funds as their primary source of money for operation, making it next to impossible to recover misspent Federal funds.

Several examples typify Federal agencies' and grantees' treatment of these situations.

--Officials of a city receiving substantial HUD funding stated the city is not obligated to repay HUD for subgrantee disallowances until the city has recovered the money from the subgrantees or taken all possible legal actions. According to the City Attorney, the city cannot take responsibility for the actions of its subgrantees. We evaluated six audits of five subgrantees conducted by the city in which auditors disallowed \$501,000 between April 1974 and September 1979. As of July 1981, four of the five subgrantees were out of business or defunded by the city, while the city had made no collection and returned no funds to HUD. HUD auditors reviewed these disallowances in June and July 1980 and recommended that the city repay HUD. But as of July 1981, HUD had taken no action to recover the funds.

--At the Department of Agriculture, subgrantee funds totaling \$341,000 were disallowed in January 1979. The Department of Agriculture did not immediately pursue the claim against the State grantee since it had not yet recovered any of the funds and was contemplating legal action against the subgrantee. Finally, Agriculture sent demand letters to the State in February and March 1981; as of September 1981 the debt was still uncollected.

--In still another case at Agriculture, a \$16,000 disallowance was established against the subgrantee of a State agency. Agriculture, however, did not pursue the claim against the State agency. Agriculture officials told us

that unless the grantee can recover disallowed costs from its subgrantee, pursuing the claim can lead to poor relations with the State.

Even if grantees recover disallowed amounts from subgrantees, they have no incentive to return the funds to the Government promptly because Federal agencies usually do not charge interest on amounts outstanding. As a result, grantees hold subgrantee payments for a long time before refunding them to the Federal Government. For example:

- At the Department of Labor a CETA grantee held for up to 20 months at least \$46,844, of Federal funds recovered from subgrantees. At another CETA grantee, a State, no timely effort was made to identify recoveries from subgrantees. Funds were held in accounts for up to 2 years before being reprogramed or returned to Labor. After we identified \$102,000 being held in this way, the State reprogramed or returned the funds to Labor. At another CETA grantee where we sampled subgrantee recoveries, we found \$305,000 had been held from 9 to 18 months before being returned to Labor.
- At Agriculture, a \$205,000 disallowance was established against a State's subgrantee. The claim was not pursued against the State when the subgrantee could not raise the cash to repay the debt. In January 1981, the State received full payment from the subgrantee but as of November 1981 still had not returned the funds to the Federal Government.
- An audit report issued by a State Department of Transportation in September 1979 identified \$49,000 in Federal funds improperly paid to a subgrantee for work the grantee itself had performed. Both the grantee and the subgrantee had been paid by the Federal Highway Administration. It was not until June 1981 that billing adjustments were made to recover disallowed costs.

In spite of grantees' claims that they cannot be held accountable for debts until they recover disallowed costs from subgrantees, Federal agencies have no choice but to hold grantees accountable and take aggressive collection action. If grantees are not held accountable, they will have no incentive to ensure the propriety, legality, and correctness of subgrantees' use of Federal funds. This could cause a serious degradation in Federal financial management.

Federal agencies have several avenues of recourse against grantees who refuse to pay debts promptly. If collection letters do not yield positive results, under the Claims Collection Standards agencies can suspend or revoke eligibility or attempt to offset the amount of the debt by reducing the amount paid to the grantee under another Federal program. The use of offset is discussed in chapter 4.

Agencies should select appropriate, positive steps to aggressively pursue collection in order to comply with the intent of the Claims Collection Act. Agencies have no legal authority to refrain from taking action on debts due the United States. They must take aggressive action to recover these debts, including the interest accrued on any delinquent debts. (See ch. 3.)

CONCLUSIONS

Federal practices to collect debts resulting from audit findings need significant improvement. Because of inadequate accounting controls, inadequate monitoring, and the lack of an aggressive collection effort, the Government too often does not collect or otherwise settle amounts it is rightly owed. When amounts are finally collected, they are unnecessarily late and there is no collection of interest or penalties.

To remedy this situation, Federal managers must become more concerned with the collection of audit-related debts. It is only with management's concern, commitment, and attention that adequate systems of internal control will be established to ensure that (1) the amount of audit-related debt is established quickly, (2) all such debts are promptly brought under accounting control, (3) debts are effectively and aggressively controlled and monitored until collection, and (4) aggressive action is taken to collect from and/or appropriately settle with grantees the audit-related debts at subrecipient levels.

As we have testified and reported on several occasions, we believe that the legislation under consideration in Congress--H.R. 1526, the Financial Managers Accountability Act, and S. 864, the Financial Integrity Act--would help make internal controls in Federal agencies more effective. These two bills would require greater accountability by heads of Federal agencies for the effectiveness of their organizations' systems of internal financial control.

RECOMMENDATIONS

We recommend that the head of each department or agency implement policies and procedures that:

- Require a written determination of the allowability of all questioned costs within 6 months of audit report issuance.
- Ensure establishment of accounts receivable for all disallowed costs within 30 days of the written determination of indebtedness.
- Ensure aggressive collection action in accordance with the Claims Collection Standards, which include written demands for payment at 30-day intervals, affecting the debtor's credit rating, offsetting the debt against amounts due from other Federal programs, and suspension or termination of fundings.

--Hold grantees fully responsible for the debts of their sub-grantees and apply the Claims Collection Standards in collecting these amounts from grantees.

We further recommend that the Director, Office of Management and Budget incorporate these recommendations into the management circular on audit resolution and follow up to ensure that agencies are complying.

CHAPTER 3

POOR MANAGEMENT PRACTICES CONTRIBUTE TO

INEFFECTIVE DEBT COLLECTION

We noted a number of poor management practices which in our opinion significantly contributed to agencies' inability to collect audit-related debts promptly and effectively. Specifically, we noted that

- agencies are inappropriately "forgiving" debts without a reasonable collection effort,
- the appeals process provides incentive to grantees to delay payment, and
- interest is not charged on delinquent debts.

AGENCIES INAPPROPRIATELY TERMINATE DEBTS RATHER THAN COLLECT THEM

Federal administrators are empowered to make final decisions on amounts to be recovered from grantees and contractors. Their authority, however, is limited. Their decisions must be based on Federal laws, regulations, and the terms of grants and contracts. A 1978 Comptroller General decision (B-163922, Feb. 10, 1978) dealt with an agency's responsibility for collecting improper expenditures questioned by auditors. It states that without explicit statutory authority, an agency cannot waive recovery of grant funds spent in violation of its regulations no matter how well-intentioned the grantee may have been. Such expenditures become debts due the Federal Government and therefore must be recovered as required under the Claims Collection Standards. In spite of this, we found that millions of dollars in debts rightfully owed the Federal Government are being purposely terminated rather than collected. At the same time the Government is continuing to provide funds to the same organizations that are misusing Federal funds. The Department of Agriculture has gone to great lengths to avoid collecting millions of dollars it found spent in violation of its own regulations. Other agencies have similarly violated the Claims Collection Standards by terminating debts rather than taking aggressive action to collect them.

Department of Agriculture disregards Claims Collection Standards

The Claims Collection Standards require agencies to take aggressive action to collect all claims of the United States arising from their activities. At one regional office of the Department of Agriculture, however, we found a record of confusion and indecision spanning several years which ultimately resulted in the Department terminating nearly \$12 million in debts without ever

attempting collection. The debts resulted from audits of two State governments' handling of their food stamp programs.

Regarding the first of the two debts, Agriculture auditors issued an audit report in December 1977, which questioned costs of \$16.3 million for "enormous overissuances of food coupons," attributed to poor control over distribution. The audit report pointed out that some of the same deficiencies had existed since 1972. The amount was reduced to \$8.6 million in May 1979 as a result of additional information provided by the grantee. In June 1979, the Acting Administrator of the Food and Nutrition Service (FNS), the agency within Agriculture responsible for administering the Food Stamp Program, recommended that the State be billed. He justified the recommendation on the basis of the large program loss and the State's failure to take corrective action to recover losses and ensure that the problems do not recur. However, no billing was sent to the State. In May 1980, the same official, after his promotion to FNS Administrator, notified the State of his decision not to bill for any of the losses because of the remedial action the State had taken.

On the second debt, involving another State, Agriculture auditors issued four audit reports between January 1976 and February 1978 showing that the State agency had overissued \$3.2 million in food coupons. Citing a history of irregularities dating back to 1968, the FNS regional administrator recommended that the State be charged with gross negligence and billed for all losses. In April 1979, however, the Assistant Secretary of Agriculture, the FNS Administrator, and the Inspector General met with the head of the State agency and agreed that if the State took sufficient corrective action, they would reconsider the gross negligence billing.

A July 1979 followup audit showed that the State had corrected some of the problems cited in the earlier reports, but some areas still needed improvement. In August 1980, another followup audit showed irregularities were decreasing but an unacceptably high level of ineligible participants still existed. In October 1981, the FNS decided to drop attempts to collect any of the \$3.2 million.

Because of the lack of accounting and collection controls at Agriculture, available records do not show clearly when claims were established in both of these cases. Agriculture officials, however, told us they considered both to be claims. They said they terminated the claims on the basis of clear evidence that the States were serious about correcting deficiencies to prevent future abuse. While we would certainly expect corrective action to be taken to avoid future misuse of funds, the Claims Collection Standards do not provide for terminating claims on the basis of present or future compliance with regulations.

DEBT APPEALS PROCESS PROVIDES
GRANTEES OPPORTUNITY TO DELAY

Another factor that contributes to the Government's poor performance in recovering disallowed costs is the process that allows the misuse of appeal rights. When grantees and contractors are faced with paying back audit disallowances, they often appeal in an effort to reverse the agency's decision or reduce the amount. An appeal also suspends the billing process until the case is considered and decided. It provides additional time to grantees and contractors who have no expectations of winning but who want to delay payment without penalty. Not only do these appeals delay collections but they clog the appeals system and delay the settlement of legitimate appeals. As a result, millions of dollars are tied up in lengthy appeals which, in effect, provide grantees and contractors interest-free loans. While we are in no way questioning the right of appeal, we believe changes must be made in the process to discourage groundless appeals and to ensure that legitimate appeals are processed without undue delay.

Most disallowed costs are appealed

The total amount of audit-related debt under appeal is unknown because agencies do not have adequate systems to account for it. Of the 32 agencies responding to our questionnaire, 16 told us they could not readily provide the amount of unrecovered audit disallowances under appeal. At six of the seven agencies where we performed audit work, 1/ the amount under appeal was 81 percent (\$201 million of \$249 million) of the total outstanding audit-related debt at those locations during our review.

The appeals process is time consuming

Unresolved appeals cases had been open an average of 18 months at the agencies we audited. The time required to settle appeals varied from a high of 28 months at Education to 12 months at HHS.

Several factors contributed to delays in appeal settlement. Legal staff priority is one such factor. Appeals boards usually administer the process; however, they often must rely on others to carry out various steps. At any given time, the workload of an agency's office of general counsel determines the availability of staff to handle appeals. When attorneys are not available, the process is delayed.

The structure of the body handling the appeals also influences the timeliness of appeal resolution. For example, at the Department of Education, appeals panels must consist of three secretarial appointees. However, the Secretary of Education had appointed no

1/At HUD we were told the appeals process is not used.

new panel members for many months at the time of our review. Meanwhile, some former appointees had resigned for various reasons, leaving the appeals board with a backlog of cases and few panel members to hear them. This resulted in numerous cases "awaiting initiation" for several months before any appeal resolution procedures even began.

Another cause of slow appeal resolution is the time spent unnecessarily on insubstantial appeals and appeals that are eventually withdrawn. Some grantees appeal for forgiveness, though they readily admit being in the wrong and owing the misspent Federal funds. Although there may be no basis for upholding an appeal, the board must nonetheless take the time to process the case.

Agency officials indicated that grantees have incentive to appeal because they have little to lose by doing so. Grantees retain disallowed funds during the appeal period, interest is not charged, and some agencies even allow the legal fees incurred by the grantee for appeals. Thus, the possibility of postponing payment at no additional cost becomes an incentive for a grantee to appeal regardless of the merit of the case. We found strong support for agency officials' contention that many appeals are frivolous. For example:

--In one Department of Labor region, 64 percent of the appealed, audit-related debts were withdrawn before a hearing, and a settlement was negotiated for the full amount of the debt in over half these cases. Grantees were able to delay payment an average of 7 months by filing, then later withdrawing, an appeal.

--A February 1979 HHS disallowance of \$2 million was appealed by a State government grantee in March 1979. The State requested and was granted four extensions totaling 180 days during June, July, September, and October 1979. Then the agency was granted two extensions which froze the case until April 1980. In May 1980, the State requested one more extension for 45 days. The appeals board continued work on the case but it was not until June 1981 that it issued an Order to Show Cause. The State requested an extension to respond to the order, and was told to reply by August. Then, in October 1981, the State and the agency notified the board that they had reached a final settlement of the dispute and the only matter not finally resolved was the figure to be repaid. The parties did not anticipate any difficulty in arriving at the final figure. Although the case was before it for 2-1/2 years, the board never made a final decision.

Interest should be accrued
on debts under appeal

None of the agencies audited charge interest while cases are under appeal. During the appeals process, debtors typically retain Federal funds for long periods while a decision is being made on their entitlement to the funds. This gives debtors an incentive to file appeals because they can thereby delay payment of their debts at the Government's expense.

We believe a better way to handle appeals would be to let interest accrue on debts under appeal. If the appeal were lost, the amount of the debt plus interest would be due immediately. Not only would this be more equitable, but it also would serve to discourage groundless appeals and help reduce the unnecessary workload of the appeals board, leaving it free to concentrate its efforts on legitimate appeals. While this should unquestionably improve the situation, agencies would have to monitor the workload of those involved in the appeals process to ensure quick processing, so appellants are not penalized for agency delays.

CHARGING INTEREST ON DELINQUENT DEBTS
WOULD IMPROVE COLLECTIONS

Not only does the Government not assess interest while appeals are under consideration; it also does not collect interest when debts are delinquent and not appealed. The Government's failure to collect interest on delinquent audit-related debts is yet another factor that hinders collection, costs the Government millions of dollars, and violates the Claims Collection Standards. Grantees and contractors who owe money to the Government have an incentive to delay payment as long as possible. Agencies are not attempting to collect interest because they are not aware of the requirement or because they have not developed implementing instructions.

Regulation requires interest charges
on delinquent debt and installment payments

Until April 1979, the Federal Claims Collection Standards allowed agencies considerable discretion in determining whether to assess interest charges on delinquent debt and installment payments. However, in April 1979 the Standards were revised, and the provisions regarding assessment of interest were strengthened and made more explicit. The revision requires the charging of interest on delinquent debts as well as debts being paid in installments according to the Treasury Fiscal Requirements Manual, which stipulates:

"If payment is overdue, a late charge will be applied and collected at a percentage rate based on the current value of funds to the Treasury."

Interest is seldom, if ever, assessed on audit-related debts

Although interest charges have been required since April 1979, the agencies we audited have collected practically no interest on audit-related debts. Furthermore, only three agencies responding to our questionnaire reported any interest collected on more than 10 percent of disallowed costs recovered. Most agencies have recently begun to notify grantees and contractors that interest will be assessed on overdue audit-related debts; however, only two agencies that we audited--the Departments of Education and Health and Human Services--have collected any interest. The other five agencies admitted that they had never collected interest on delinquent debts as of June 1981.

The interest loss to the Government as a result of agencies' failure to collect it has been substantial. For example:

- HHS has failed to bill and collect \$2.1 million in interest charges on delinquent debts between June 1979 and June 1981. ^{1/}
- According to an EPA Inspector General report issued in September 1981, EPA has failed to bill and collect an estimated \$1.2 million in interest charges on delinquent debts over a 1-1/2 year period.

Furthermore, agencies responding to our questionnaire reported outstanding audit-related debt totaling \$374 million as of June 30, 1981. They said these debts remained outstanding an average of 1 year. We believe the amount of outstanding debt to be grossly understated. However, if this amount were outstanding for a year at the Treasury rate applicable between April 1 and June 30, 1981, interest due the Government on delayed recoveries of audit-related debts would total \$66.3 million.

Agencies have not charged interest for various reasons

Agencies gave a variety of reasons for their failure to charge interest on audit-related debts. Some agency officials told us they were unaware of the requirement to charge interest, while several others said they were aware of the requirement but had not implemented procedures because their agencies had issued no instructions or guidelines. At all the agencies, management had assigned a low priority to the assessment and collection of

^{1/}Based on rates established by Treasury bulletins in accordance with the Treasury Fiscal Requirements Manual and the Federal Claims Collection Standards, June 1, 1979, through June 30, 1981, as applicable. Debts are defined as overdue, or delinquent, if payment has not been received within 30 days of billing. Debts under appeal are not included.

interest. Furthermore, by not assessing interest, Federal agencies have given debtors an incentive to pay the Government only after all interest-charging creditors have been paid.

CONCLUSIONS

Federal agency management is doing a poor job of collecting the debts it establishes as a result of its own audit findings. Some agencies have terminated debts amounting to millions of dollars rather than collect them. Other agencies provide incentives for debtors to appeal audit disallowances at considerable cost to the Government. Virtually all agencies do not collect interest on delinquent debts even though it is a fundamental debt management principle and a requirement of the Claims Collection Standards. Although the cost of this mismanagement cannot be precisely determined, we believe it is very costly. Furthermore, we believe this mismanagement serves as an invitation to abuse by those who can benefit from such practices. Decisive and meaningful actions by top management are needed to stop the flagrant disregard of the Claims Collection Standards.

RECOMMENDATIONS

We therefore recommend that the head of each department and agency implement policies and procedures that:

- Ensure compliance with the Claims Collections Standards to preclude the termination of any debts over \$20,000 and ensure that all Claims Collection Standards concerning compromise and termination are met before settling debts of \$20,000 or less.
- Streamline the audit disallowance appeal process to ensure that unnecessary delays are eliminated and that interest is charged on all amounts under appeal.
- Require interest to be charged and collected on all debts, at the rate specified by the Treasury Fiscal Requirements Manual, beginning no later than 30 days from establishment of the debt and continuing until collection or final disposition.

We further recommend that the Director, Office of Management and Budget incorporate this requirement into the management circular on audit resolution and follow up to ensure that agencies are complying.

CHAPTER 4

NO ASSURANCE IS PROVIDED THAT PROGRAM PERFORMANCE IS NOT REDUCED WHEN DEBTS ARE PAID

In addition to the widespread lack of accounting and collection controls and the poor management practices cited throughout this report, we found that Federal agencies can unknowingly accept their own or other Federal funds as payment of audit-related debts at the expense of intended program recipients. Agencies use two primary methods to recover audit disallowances--offset and cash recovery. When agencies settle debts by offsetting grantees' indebtedness against grant advance payments, they usually do not have adequate assurance that the program itself is not reduced. When audit-related debts are repaid in cash, agencies are often unaware of the source of the money. Payments may come from advances from other Federal grants--which, in effect, allows the debtor to borrow from the Federal Government without its consent and contrary to the agreement between the Government and the grantees, and without paying interest. Payments may reduce funds available for other Federal programs. We believe that Federal agencies should require assurance from grantees that payments do not diminish performance of Federal programs, and this should be verified during future program visits and audits.

DEBT COLLECTION BY OFFSET MAY HAVE NEGATIVE CONSEQUENCES

The Claims Collection Standards require collection by offset when feasible. However, numerous Comptroller General decisions have stated that offset should not be used where it would have the effect of defeating or interfering with the purposes of the grant. Since most grant funds are made available to grantees before expenditures are incurred, the grantee usually has control of the funds before it has a "claim" for the funds. Therefore, it is normally inappropriate for the Government to offset debts against an advance of funds to a grantee unless there is assurance that the same level of grant performance will be maintained.

In response to our questionnaire, agencies reported the most common method for collecting disallowed costs is by offset against current or future awards. Furthermore, most agencies reported that they do not usually require grantees to certify or otherwise state that non-Federal funds equal to the amount of the offset were reinstated to the Federal programs. When the offset is not replaced with non-Federal funds, there has, in effect, been no repayment. The scope of the program has simply been reduced and the intended recipient of the benefits loses by the amount of the audit disallowance.

The use of offset against advance funding programs is significant. For example, the Department of Health and Human Services

reported it collected \$119 million of a total of \$168 million in audit-related debts over the last 3 years through offset. Two cases we found at HUD illustrate how offset can be inequitable.

--HUD disallowed \$22,495 for ineligible costs of a subgrantee. When the county grantee delayed paying the debt, HUD threatened to reduce the next year's grant by the disallowed amount. County officials found this to be a good option because they told us they would rather have the HUD program reduced than spend county general revenues to maintain it.

--HUD disallowed \$25,880 for ineligible expenditures by a subgrantee in November 1979. In February 1980, the city grantee received partial payment of \$8,500 from the subgrantee, but it was unable to obtain the remainder. In June 1980, the city paid the entire disallowance to HUD by reducing its HUD letter of credit. As of July 1981, the city still had not been able to obtain the remaining \$17,380 from the subgrantee. This subgrantee continues to be funded in full by the city while other subgrantees are short \$17,380.

PERFORMANCE LEVEL MAY NOT BE MAINTAINED
WHEN DEBTS ARE PAID IN CASH

Regardless of the method agencies use to recover audit disallowances, the recovery should not reduce the performance level of the program. This principle applies when the repayments are made with cash, regardless of the source of these funds. All involved program performance must be maintained.

Treasury Circular 1075 requires grantees receiving advance funds to draw only what they need for the program when they need it. Acceptance of the letter of credit by a grantee means it accepts these conditions as well. Accordingly, withdrawals for purposes such as payment of debts resulting from other programs are prohibited. Since interest is not charged on advances, to misuse the advance authority in such a fashion results in an interest-free loan to the grantee from the unsuspecting Federal Government. In fact, during our review we found that a subgrantee paid disallowed costs to HUD by endorsing a check it had received for the CETA program from the Department of Labor. No effort was made by Labor or HUD to verify that performance was maintained on their respective programs.

Most agencies make no attempt to assure themselves that the payment of the debt will not adversely affect the intended objectives of the Federal assistance. Agency officials told us either that they were not concerned about the source of funds used to pay grantee debts or that they had no way of determining the source. For example:

--HUD officials acknowledge they cannot be assured that repayment of audit-related debts by grantees and subgrantees comes from non-Federal funds.

- Department of Agriculture officials said they had no controls to check the source of funds. Officials suspected it would be easy for the Department to end up paying its own debt.
- Transportation officials told us they lack adequate staff and procedures to determine the source of funds.
- EPA officials said other priorities prevent them from determining the source of recovered funds.

ASSURANCE IS NEEDED THAT BENEFITS ARE BEING MAINTAINED

We recognize that it is not practical for agencies to immediately verify grantees' performance level in every disallowed cost collection or settlement. However, the level of performance should be verified during future visits by agency program officials to grantees as well as during future audits. Federal agencies should also require a statement from grantee officials certifying in each instance that their payment of disallowance costs has not been made at the expense of any Federal program. This would provide some assurance to Federal managers that grantees are aware of the level-of-performance requirement and some indication that the requirement has been met.

CONCLUSION

When audit-related debt is settled with funds taken from a Federal program, the Government may be accepting its own money at the expense of the intended program beneficiaries. When this happens, no debt has been settled at all. Yet, Federal agencies do not seek assurances that grantees are maintaining the level of performance in Federal assistance programs. We believe that agencies should seek this assurance whenever debts are settled and periodically verify the level of performance through grant management and audit followup.

RECOMMENDATION

We recommend that heads of departments and agencies require grantee debtors to certify that their payment of audit-related debts has not reduced the level of performance of any Federal program. We further recommend that a followup system be established whereby grant management staff closely monitor performance of grantees to ensure that settlement of debts does not adversely affect grantee performance. This system should also include provision for audit followup, whereby routine verification is made part of the subsequent audit of grantees paying off audit-related debts.

We further recommend that the Director, Office of Management and Budget incorporate this recommendation into the management circular on audit resolution and follow up to ensure that agencies are complying.

1981-10-20
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NINETY-SEVENTH CONGRESS

Congress of the United States

House of Representatives

LEGISLATION AND NATIONAL SECURITY SUBCOMMITTEE

OF THE

COMMITTEE ON GOVERNMENT OPERATIONS

RAYBURN HOUSE OFFICE BUILDING, ROOM B-373

WASHINGTON, D.C. 20515

October 20, 1981

Mr. Charles A. Bowsher
 Comptroller General
 U.S. General Accounting Office
 441 G Street, N.W.
 Washington, D.C. 20548

Dear General:

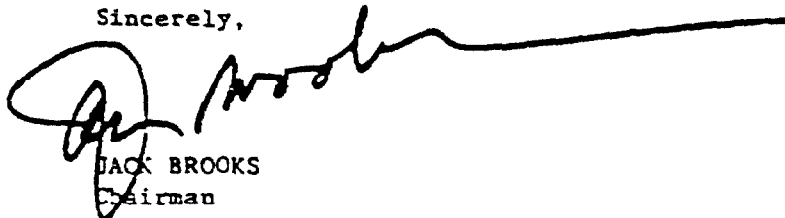
In March 1979, this Subcommittee held the first in a series of hearings on the failure of Federal departments and agencies to follow-up and resolve audit findings. More recently the Subcommittee conducted a follow on review and held hearings in February, June, and July 1981 on the continued failure by these same agencies to take effective action on audit findings. GAO has been most helpful to us throughout this period and I look forward to our continuing to work together to improve management in government.

Repeatedly during the Subcommittee hearings, the matter of collection procedures over audit disallowances was raised as an area where serious deficiencies appeared to exist. Therefore, I was particularly pleased to learn, as expressed in my letter to Mr. Staats on June 10, 1980, of the GAO review underway examining federal departments' and agencies' collection procedures over audit disallowances. In that same letter, I also expressed my hope that the review would be given priority and that the Subcommittee would be kept informed of its progress.

As I understand, members of your Accounting and Financial Management Division recently briefed my staff on the preliminary results of this review. Because of the deficiencies and significant problems uncovered in Federal agencies' audit disallowance collection procedures, the Subcommittee hopes to schedule hearings on the results of your findings in mid-February. So that we can properly study the results of your findings and prepare for the likelihood of these hearings, I would appreciate having a draft of your report by the third week in January.

Thank you for your cooperation.

Sincerely,



JACK BROOKS
 Chairman

Agency Magnitude and Disposition of Disallowed Costs
(All data as of June 30, 1981 unless otherwise noted.)

REPORTED MAGNITUDE OF AUDIT DISALLOWANCES (note a)

Agency	Disallowed costs outstanding as of June 30, 1981 (thousands)	How long outstanding				
		Less than 1 year	1 year to less than 2 years	2 years to less than 3 years	3 years to less than 4 years	4 years or more
		----- (percent) -----				
Department of Agriculture	*					
Department of Commerce	*					
Department of Defense	b/Does not apply	-	-	-	-	-
Department of Education (note x)	\$ 71,203	*				
Department of Energy	10,900	33	50	14	2	1
Department of Health and Human Services	156,455	38	28	6	3	25
Department of Housing and Urban Development	c/ 42,200	*				
Department of the Interior	8,400	47	15	34	1	3
Department of Justice	7,820	65	27	4	1	4
Department of Labor	52,712	74	10	16	-	-
Department of State	733	*				
Department of Transportation (note x)	d/ 322	e/ Varies by division				
Department of the Treasury	None	-	-	-	-	-
ACTION	194	38	48	-	3	11
Environmental Protection Agency	1,520	*				
General Services Administration	None	-	-	-	-	-
National Aeronautics and Space Administration	*					
Small Business Administration	None	-	-	-	-	-
Veterans Administration	*					
International Communications Agency	101	-	17	83	-	-
National Science Foundation (note x)	37	100	-	-	-	-
Nuclear Regulatory Commission	None	-	-	-	-	-
Office of Personnel Management	19,665	33	34	11	11	11
Smithsonian Institution	None	-	-	-	-	-
Civil Aeronautics Board	38	100	-	-	-	-
Consumer Product Safety Commission	None	-	-	-	-	-
Equal Employment Opportunity Commission	386	-	13	6	81	-
Federal Emergency Management Agency	c/ 1,260	*				
Legal Services Corporation	47	1	80	19	-	-
National Endowment for the Humanities	None	-	-	-	-	-
Tennessee Valley Authority	6	100	-	-	-	-
United States Postal Service	None	-	-	-	-	-
Total	<u>\$373,999</u>					

*No data available.

REPORTED MAGNITUDE OF APPEALS

<u>Agency</u>	<u>Appealed</u>	<u>Settled</u>	<u>Settled in favor of Government</u>	<u>Settled in favor of auditee</u>
	----- (thousands) -----			
Department of Agriculture	*			
Department of Commerce	*			
Department of Defense	*			
Department of Education (note x)	*			
Department of Energy	*			
Department of Health and Human Services	\$162,341	\$72,080	\$68,313	\$3,767
Department of Housing and Urban Development	**			
Department of the Interior	*			
Department of Justice	*			
Department of Labor	*			
Department of State	*			
Department of Transportation (note x)	d/ 131	d, w/ 126	d/ 68	d/ 63
Department of the Treasury	*			
ACTION	195	w/ 195	113	81
Environmental Protection Agency	g/ *			
General Services Administration	None	-	-	-
National Aeronautics and Space Administration	*			
Small Business Administration	None	-	-	-
Veterans Administration	*			
International Communications Agency	84	-	-	-
National Science Foundation (note x)	22	22	17	5
Nuclear Regulatory Commission	None	-	-	-
Office of Personnel Management	3,369	2,890	250	2,640
Smithsonian Institution	None	-	-	-
Civil Aeronautics Board	*			
Consumer Product Safety Commission	None	-	-	-
Equal Employment Opportunity Commission	314	314	-	314
Federal Emergency Management Agency	*			
Legal Services Corporation	35	-	-	-
National Endowment for the Humanities	None	-	-	-
Tennessee Valley Authority	2,727	2,727	2,050	677
United States Postal Service	*			
Total	<u>\$169,218</u>	<u>\$78,354</u>	<u>\$70,811</u>	<u>\$7,547</u>

*No data available.

**No formal appeals process.

DISALLOWED COSTS APPEALED AND SETTLED, BY NUMBER OF CASES

<u>Agency</u>	<u>Time from appeal to settlement</u>				
	<u>6 months or less</u>	<u>6 months to 1 year</u>	<u>1 to 2 years</u>	<u>2 to 3 years</u>	<u>More than 3 years</u>
	----- (percent) -----				
Department of Agriculture	*				
Department of Commerce	*				
Department of Defense	*				
Department of Education (note x)	*				
Department of Energy	*				
Department of Health and Human Services	7	26	27	30	10
Department of Housing and Urban Development	None	-	-	-	-
Department of the Interior	*				
Department of Justice	*				
Department of Labor	*				
Department of State	*				
Department of Transportation (note x)	d,e/Varies by div.				
Department of the Treasury	*				
ACTION	47	36	17	-	-
Environmental Protection Agency	g/ *				
General Services Administration	None	-	-	-	-
National Aeronautics and Space Administration	27	21	24	10	18
Small Business Administration	None	-	-	-	-
Veterans Administration	*				
International Communications Agency	None	-	-	-	-
National Science Foundation (note x)	33	67	-	-	-
Nuclear Regulatory Commission	None	-	-	-	-
Office of Personnel Management	23	23	-	39	15
Smithsonian Institution	None	-	-	-	-
Civil Aeronautics Board	*				
Consumer Product Safety Commission	None	-	-	-	-
Equal Employment Opportunity Commission	None	-	-	-	100
Federal Emergency Management Agency	*				
Legal Services Corporation	None	-	-	-	-
National Endowment for the Humanities	None	-	-	-	-
Tennessee Valley Authority	50	-	-	50	-
United States Postal Service	*				

*No data available.

DISALLOWED COSTS APPEALED AND SETTLED, BY AMOUNT

<u>Agency</u>	<u>Time from appeal to settlement</u>				
	<u>6 months or less</u>	<u>6 months to 1 year</u>	<u>1 to 2 years</u>	<u>2 to 3 years</u>	<u>More than 3 years</u>
	----- (percent) -----				
Department of Agriculture	*				
Department of Commerce	*				
Department of Defense	*				
Department of Education (note x)	*				
Department of Energy	*				
Department of Health and Human Services	5	19	34	34	8
Department of Housing and Urban Development	None	-	-	-	-
Department of the Interior	*				
Department of Justice	*				
Department of Labor	*				
Department of State	*				
Department of Transportation (note x)	d,e/Varies by div.				
Department of the Treasury	*				
ACTION	52	30	18	-	-
Environmental Protection Agency	g/ *				
General Services Administration	None	-	-	-	-
National Aeronautics and Space Administration	*				
Small Business Administration	None	-	-	-	-
Veterans Administration	*				
International Communications Agency	None	-	-	-	-
National Science Foundation (note x)	14	86	-	-	-
Nuclear Regulatory Commission	None	-	-	-	-
Office of Personnel Management	36	21	-	37	6
Smithsonian Institution	None	-	-	-	-
Civil Aeronautics Board	*				
Consumer Product Safety Commission	None	-	-	-	-
Equal Employment Opportunity Commission	None	-	-	-	100
Federal Emergency Management Agency	*				
Legal Services Corporation	None	-	-	-	-
National Endowment for the Humanities	None	-	-	-	-
Tennessee Valley Authority	3	-	-	97	-
United States Postal Service	*				

*No data available.

STATUS OF COSTS DISALLOWED DURING FISCAL 1978, 1979, AND 1980
(AS OF JUNE 30, 1981)

Agency	Total questioned costs established as disallowed (A)	Amount of Disallowed Costs in A					Still outstanding as of 6/30/81 (F)	Still outstanding and under appeal (G)
		Recovered as of 6/30/81 (B)	Determined on basis of appeal to be not a debt (C)	Written off as uncollectible (D)	Determined on basis other than appeal to be not a debt (E)			
Department of Agriculture	h/ *							
Department of Commerce	*							
Department of Defense	b, i/ None	-	-	-	-	-	-	-
Department of Education (note x)	\$ 76,623	\$ 20,156	*	\$583	*	*	\$44,961	
Department of Energy	j/ 16,180	j/ 7,053	*	*	*	\$ 9,127	*	
Department of Health and Human Services	262,603	179,815	\$2,296	217	\$11,486	82,788	63,915	
Department of Housing and Urban Development	135,300	*	*	*	*	*	*	
Department of the Interior	55,200	k/ 36,000	*	*	*	*	*	
Department of Justice	k/ 41,085	*	*	*	*	3,661	*	
Department of Labor	l/ *							
Department of State	*							
Department of Transportation (note ::)	d/ 3,564	d/ 3,292	d/ 31	d/ -	d/ -	d/ 153	d/ 83	
Department of the Treasury	e/ 155	e/ 155	-	-	-	-	-	
ACTION	250	75	82	-	-	90	14	
Environmental Protection Agency	m/ 40,891	m/ 15,356	*	*	*	*	11,309	
General Services Administration	1	1	-	-	-	-	-	
National Aeronautics and Space Administration	*							
Small Business Administration	*							
Veterans Administration	*							
International Communications Agency	108	6	-	-	-	101	-	
National Science Foundation (note x)	*							
Nuclear Regulatory Commission	None	-	-	-	-	-	-	
Office of Personnel Management	11,955	2,439	776	-	-	8,740	4,932	
Smithsonian Institution	44	44	-	-	-	-	-	
Civil Aeronautics Board	36	36	-	-	-	-	-	
Consumer Product Safety Commission	None	-	-	-	-	-	-	
Equal Employment Opportunity Commission	386	-	-	-	-	386	314	
Federal Emergency Management Agency	n/ 61	n/ 6,061	*	*	*	n/ 29	*	
Legal Services Corporation	47	-	-	-	-	47	35	
National Endowment for the Humanities	17	15	-	1	-	-	-	
Tennessee Valley Authority	7,868	7,191	677	-	-	-	-	
United States Postal Service	*							
Total (note y)	\$652,374	\$277,695	\$3,862	\$801	\$11,486	\$105,122	\$125,563	

*No data available.

35

AMOUNTS OF DISALLOWED COSTS RECOVERED BY VARIOUS METHODS

<u>Agency</u>	<u>Return of cash</u>	<u>Offset against cur- rent letter of credit</u>	<u>Offset against future grant/ contract awards</u>	<u>Perform- ance of services in-kind</u>	<u>Reprogram- ming to other eligible expenses</u>	<u>Other</u>
	----- (thousands) -----					
Department of Agriculture	*					
Department of Commerce	*					
Department of Defense	b,i/ None	-	-	-	-	-
Department of Education (note x)	\$ 6,518		\$ 7,626			o/ \$ 5,989
Department of Energy		j,r/ \$ 7,053				
Department of Health and Human Services	46,493	15,893	103,062	**		q/ 2,700
Department of Housing and Urban Development	*					
Department of the Interior	*					
Department of Justice	*					
Department of Labor	*					
Department of State	*					
Department of Transportation (note x)	d/ 2,897	d/ 221				d,r/ 173
Department of the Treasury	f/ 114				\$41	
ACTION	49	20				
Environmental Protection Agency	*					
General Services Administration	1					
National Aeronautics and Space Administration	*					
Small Business Administration	*					
Veterans Administration	*					
International Communications Agency	6					
National Science Foundation (note x)	*					
Nuclear Regulatory Commission	None	-	-	-	-	-
Office of Personnel Management			2,439			
Smithsonian Institution		35	9			
Civil Aeronautics Board				\$36		
Consumer Product Safety Commission	None	-	-	-	-	-
Equal Employment Opportunity Commission	None	-	-	-	-	-
Federal Emergency Management Agency						s/ 6,061
Legal Services Corporation	t/ 2					
National Endowment for the Humanities	15					
Tennessee Valley Authority	7,191					
United States Postal Service	*					
Total	<u>\$63,286</u>	<u>\$23,222</u>	<u>\$113,136</u>	<u>\$36</u>	<u>\$41</u>	<u>\$14,923</u>

*No data available.

**Cannot compute value.

RECOVERIES RETURNED TO THE TREASURY AND INTEREST COLLECTED

<u>Agency</u>	Amount of recovered cash returned to U.S. Treasury as of June 30, 1981	Amount of interest collected on disallowed costs as of June 30, 1981
	----- (thousands) -----	
Department of Agriculture	*	*
Department of Commerce	*	(v)
Department of Defense	b,i/ Does not apply	*
Department of Education (note x)	\$ 6,541	*
Department of Energy	Does not apply	(v)
Department of Health and Human Services	6,015	u/\$3,173
Department of Housing and Urban Development	*	(v)
Department of the Interior	*	(v)
Department of Justice	*	*
Department of Labor	*	*
Department of State	*	*
Department of Transportation (note x)	d/ 2,641	-
Department of the Treasury	f/ 114	(v)
ACTION	47	(v)
Environmental Protection Agency	*	*
General Services Administration	1	(v)
National Aeronautics and Space Administration	*	*
Small Business Administration	*	None
Veterans Administration	*	*
International Communications Agency	None	(v)
National Science Foundation (note x)	*	(v)
Nuclear Regulatory Commission	Does not apply	-
Office of Personnel Management	(do.)	*
Smithsonian Institution	"	(v)
Civil Aeronautics Board	"	*
Consumer Product Safety Commission	"	(v)
Equal Employment Opportunity Commission	"	(v)
Federal Emergency Management Agency	"	(v)
Legal Services Corporation	None	(v)
National Endowment for the Humanities	15	-
Tennessee Valley Authority	*	(v)
United States Postal Service	*	(v)
	<hr/>	<hr/>
Total	\$15,374	u/\$3,173
	<hr/>	<hr/>

*No data available.

Footnotes to appendix II

- a/ Questionnaires were sent to 36 Federal agencies. One agency, the Community Services Administration, did not respond. Three agencies (Federal Communications Commission, Federal Deposit Insurance Corporation, and the Federal Reserve System) responded but did not answer the questionnaire. They stated that the questionnaire did not apply to their operations. A total of 32 agencies answered some or all of our questions.
- b/ According to Defense, disallowed costs would seldom involve establishing an account receivable. Contractors are not paid until payment has been earned. Any disallowances are handled by rate adjustments or offset against holdbacks as subsequent payments due the contractor before the contract is closed out and final funds are released under the terms of the contract.
- c/ Reported as of March 31, 1981.
- d/ Many Department of Transportation administrative divisions could not provide the data.
- e/ Transportation returned questionnaires from its various administrative divisions, so the responses within the Department vary for many questions.
- f/ At some Treasury bureaus the data were not available.
- g/ EPA determined that audit-related appeals totaling \$11,308,574 were open as of September 4, 1981. In fiscal 1979 and 1980, 166 appeals were filed--both audit and nonaudit. They estimate that of this amount, two-thirds are audit related.
- h/ Agriculture stated it could not develop the data because its accounts receivable system does not distinguish between audit-related claims and others. However, in fiscal 1979 and 1980, disallowances for collection purposes amounted to \$17 million; for other than collection purposes, disallowances totaled \$52 million.
- i/ The Defense Contract Audit Agency reported its incurred cost exceptions sustained, for 1978 through 9 months of 1980, in two categories: costs questioned (\$1,470,252,000) and cost avoidance (\$579,573,000). The Department of Defense noted that "Incurred Exceptions Cost Questioned Sustained" do not generally represent an amount to be set up as a receivable. Most of this amount is withheld from contractor billings. The cost avoidance sustained reflects estimated costs that contractors have avoided through improved management techniques and practices.
- j/ At the Department of Energy, no centralized audit followup system existed in fiscal 1978. Column A equals the sum of amounts recovered in column B and amounts disallowed and still outstanding in column F.

Footnotes to appendix II (cont.)

- k/ No data available for 1978.
- l/ The Department of Labor states that it will be able to develop this information in the future.
- m/ The Environmental Protection Agency had no accounts receivable subsidiary ledger before fiscal 1980. The data provided covers eight of the EPA regions and shows as of March 31, 1980, the status of collections of disallowed costs from audit reports issued in fiscal 1979 and the first 6 months of fiscal 1980.
- n/ Figures for the Federal Emergency Management Agency cover the period April 1, 1980, through September 30, 1980, only. No data are available for earlier periods.
- o/ Grantees restored amounts to program bank accounts.
- p/ At the Department of Energy the audit followup system does not indicate how disallowed costs are recovered. In most cases, the amounts are recovered by offset to an invoice or current letter of credit.
- q/ Reimbursement to program account (applicable to Office of Human Development Services only).
- r/ Deducted from another pay project request.
- s/ Offset against a current billing.
- t/ Funds were returned in July 1981.
- u/ Of \$3,173,000 in interest reported as collected by HHS, only \$3,100 was actually interest. The rest was the principal repaid on one audit disallowance.
- v/ Agencies do not charge interest on disallowed costs. (See app. III, p. 45.)
- w/ Amount settled is not the total of columns entitled "Settled in favor of Government" and "Settled in favor of auditee" because of inconsistent or incomplete agency responses.
- x/ Subsequent to our writing the report, additional data were received from the Department of Education, the National Science Foundation, and two administrative divisions of the Department of Transportation (Federal Railroad and Federal Highway Administrations). We did not include these data in the report.
- y/ Columns B through F do not total to column A due to inconsistent or incomplete responses from agencies.

Agency Variances in Procedures for Handling
Disallowed Costs

AGENCY PROCEDURES FOR HANDLING AND CONTROLLING DISALLOWED COSTS (note a)

<u>Agency</u>	<u>Control of Disallowed Costs</u>		
	<u>At what point are disallowed costs established as a debt?</u>	<u>Does organization establish accounts receivable for disallowed costs?</u>	<u>If no accounts receivable, how does organization control disallowed costs? -</u>
Department of Agriculture	Set up account receivable	Yes	
Department of Commerce	Disallowance sustained	Yes	
Department of Defense	Varies	Yes	
Department of Education	Disallowance sustained	Sometimes	Finance tracks
Department of Energy	Disallowance sustained	Sometimes	Program tracks
Department of Health and Human Services	Disallowance sustained	Yes	
Department of Housing and Urban Development	Payment requested	Yes	
Department of the Interior	Disallowance sustained	No	Program tracks
Department of Justice	Claim determined by OGC	Sometimes	Audit tracks
Department of Labor	Disallowance sustained	Yes	
Department of State	Inspector General determines	Yes	
Department of Transportation	<u>b/</u> Varies by division	Sometimes	<u>b/</u> Varies by division
Department of the Treasury	<u>c/</u> Varies by bureau	Sometimes	<u>c/</u> Varies by bureau
ACTION	Disallowance sustained	No	Program tracks
Environmental Protection Agency	Payment requested	Yes	
General Services Administration	Payment requested	No	Program tracks
National Aeronautics and Space Administration	Payment requested	Yes	
Small Business Administration	Disallowance sustained	Yes	
Veterans Administration	At final negotiation	Sometimes	No response
International Communications Agency	Payment requested	Yes	
National Science Foundation	Disallow. sust./paymt. req.	No	Program and grants office tracks
Nuclear Regulatory Commission	Auditee agrees	No	Program tracks
Office of Personnel Management	Disallowance sustained	No	Audit or program tracks
Smithsonian Institution	Disallowance sustained	Yes	
Civil Aeronautics Board	Depends on audit	No	Finance tracks
Consumer Product Safety Commission	Costs negotiated	No	Program tracks
Equal Employment Opportunity Commission	Final audit released	Yes	
Federal Emergency Management Agency	Payment requested	Yes	
Legal Services Corporation	Audit division determines	Yes	
National Endowment for the Humanities	Disallowance sustained	Yes	
Tennessee Valley Authority	Disallowance sustained	Yes	
United States Postal Service	Disallowance sustained	No	Program tracks

41

FREQUENCY WITH WHICH VARIOUS METHODS ARE USED TO ENSURE THAT REPAYMENTS BY GRANTEES OF DISALLOWED COSTS COME FROM NON-FEDERAL FUNDS

<u>Agency</u>	<u>Conduct special audit review of auditee</u>	<u>Include audit procedures to check source of funds on next regularly scheduled audit</u>	<u>Instruct auditee in demand letter that payment must be from non-Federal funds</u>	<u>Require auditee to certify that funds are from non-Federal sources</u>	<u>Other</u>
Department of Agriculture	Occasionally	Frequently	Rarely	Rarely	
Department of Commerce	Rarely	Occasionally	Rarely	Rarely	
Department of Defense	Frequently	Frequently	Rarely	Rarely	
Department of Education	Rarely	Frequently	Always	Rarely	
Department of Energy	Rarely	Occasionally	Always	Rarely	
Department of Health and Human Services	Rarely	Always	Always	Rarely	(d)
Department of Housing and Urban Development	Occasionally	As often as not	Always	Occasionally	
Department of the Interior	No response	Always	No response	No response	
Department of Justice	Rarely	Occasionally	Rarely	Rarely	
Department of Labor	Rarely	Frequently	Frequently	Occasionally	
Department of State	Occasionally	Always	Always	As often as not	
Department of Transportation	Rarely	Rarely	Rarely	Rarely	
Department of the Treasury	Does not apply	Does not apply	Does not apply	Does not apply	
ACTION	Rarely	Rarely	Always	Rarely	
Environmental Protection Agency	Rarely	Rarely	Rarely	Rarely	
General Services Administration	Rarely	Rarely	Rarely	Rarely	(e)
National Aeronautics and Space Administration	No response	No response	No response	No response	
Small Business Administration	Rarely	Rarely	Rarely	Rarely	
Veterans Administration	No response	No response	No response	No response	
International Communications Agency	Rarely	Occasionally	Rarely	Rarely	
National Science Foundation	Does not apply	Does not apply	Does not apply	Does not apply	
Nuclear Regulatory Commission	Rarely	Rarely	Rarely	Rarely	
Office of Personnel Management	Rarely	Rarely	Rarely	Rarely	
Smithsonian Institution	Occasionally	Frequently	Rarely	Rarely	
Civil Aeronautics Board	Does not apply	Does not apply	Does not apply	Does not apply	
Consumer Product Safety Commission	No response	No response	No response	No response	
Equal Employment Opportunity Commission	Rarely	Always	Does not apply	Does not apply	
Federal Emergency Management Agency	Rarely	Rarely	Rarely	Rarely	
Legal Services Corporation	Rarely	Rarely	Rarely	Rarely	(f)
National Endowment for the Humanities	Rarely	Rarely	Rarely	Rarely	
Tennessee Valley Authority	Does not apply	Does not apply	Does not apply	Does not apply	
United States Postal Service	Does not apply	Does not apply	Does not apply	Does not apply	

FREQUENCY WITH WHICH VARIOUS METHODS ARE USED TO ENSURE THAT CONTRACTORS DO NOT
REDUCE THE SCOPE OF THEIR WORK AS A RESULT OF DISALLOWED COSTS

<u>Agency</u>	<u>Conduct special audit review</u>	<u>Include audit procedures to check source of funds on next regularly scheduled audit</u>	<u>Rely on contracting officer to ensure contractor performance of all contract terms</u>	<u>Other</u>
Department of Agriculture	Rarely	Always	Always	
Department of Commerce	No response	No response	No response	
Department of Defense	Frequently	Frequently	Always	(h)
Department of Education	Occasionally	Frequently	Always	
Department of Energy	Rarely	Occasionally	Always	
Department of Health and Human Services	Rarely	Always	Always	
Department of Housing and Urban Development	No response	No response	Always	
Department of the Interior	No response	No response	Always	
Department of Justice	Rarely	Occasionally	Always	
Department of Labor	Rarely	Rarely	Always	(g)
Department of State	Occasionally	Always	Always	
Department of Transportation	b/ Varies by division	b/ Varies by division	b/ Varies by division	
Department of the Treasury	c/ Varies by bureau	c/ Varies by bureau	Always	
ACTION	Occasionally	Rarely	As often as not	(i)
Environmental Protection Agency	Rarely	Rarely	Always	
General Services Administration	Rarely	Rarely	Always	
National Aeronautics and Space Administration	No response	No response	No response	
Small Business Administration	Rarely	Rarely	Always	
Veterans Administration	No response	No response	No response	
International Communications Agency	Rarely	Rarely	Always	
National Science Foundation	Does not apply	Does not apply	Always	
Nuclear Regulatory Commission	Rarely	Rarely	Always	
Office of Personnel Management	Occasionally	Always	Rarely	
Smithsonian Institution	No response	No response	No response	(j)
Civil Aeronautics Board	Does not apply	Does not apply	Does not apply	
Consumer Product Safety Commission	Rarely	Rarely	Always	
Equal Employment Opportunity Commission	Rarely	Rarely	Always	(k)
Federal Emergency Management Agency	Rarely	Frequently	Always	(l)
Legal Services Corporation	Rarely	Rarely	Always	
National Endowment for the Humanities	Rarely	Rarely	Rarely	
Tennessee Valley Authority	Rarely	Rarely	Always	
United States Postal Service	No response	No response	Always	

43

AGENCY PROCEDURES FOR WRITING OFF DEBTS

<u>Agency</u>	<u>Has agency ever written off as uncollectible any portion of sustained audit disallowances?</u>	<u>If any writeoffs are made, at what point are disallowed costs written off as uncollectible?</u>	<u>Has agency referred any audit disallowances to a commercial collection agency?</u>
Department of Agriculture	Yes	No uniform agency procedures	No
Department of Commerce	Yes	If uncollected for specified time and all attempts exhausted	No
Department of Defense	m/ No data		No
Department of Education	Yes	If uncollected for specified time and all attempts exhausted	No
Department of Energy	No		No
Department of Health and Human Services	Yes	When sent to GAO for collection	No
Department of Housing and Urban Development	Yes	No response	No
Department of the Interior	Yes	When sent to GAO for collection	No
Department of Justice	Yes	Exhausted all attempts at collection	No
Department of Labor	Yes	Exhausted all attempts at collection & sent to GAO	No
Department of State	No response	When sent to GAO for collection	No response
Department of Transportation	No		No
Department of the Treasury	No		No
ACTION	No		No
Environmental Protection Agency	Yes	When sent to GAO for collection	No
General Services Administration	Yes	If uncollected for specified time and all attempts exhausted	No
National Aeronautics and Space Administration	No response	According to GAO manual	No response
Small Business Administration	No		No
Veterans Administration	No response	No response	No response
International Communications Agency	No		No
National Science Foundation	No		No
Nuclear Regulatory Commission	No		No
Office of Personnel Management	Yes	When organization becomes insolvent	No
Smithsonian Institution	No		No
Civil Aeronautics Board	No		No
Consumer Product Safety Commission	No		No
Equal Employment Opportunity Commission	No		No
Federal Emergency Management Agency	No		No
Legal Services Corporation	No		No
National Endowment for the Humanities	Yes	When not cost effective to pursue	No
Tennessee Valley Authority	No		No
United States Postal Service	Yes	When all attempts at collection have been exhausted	No

AGENCY PROCEDURES FOR CHARGING INTEREST ON DISALLOWED COSTS

<u>Agency</u>	<u>Does organization ever charge interest on disallowed costs?</u>	<u>If interest is charged, at what point does it begin accruing?</u>	<u>In what percentage of cases where disallowances are recovered is an interest charge collected?</u>	<u>When interest is assessed, how is the rate determined?</u>
Department of Agriculture	Yes	Debt delinquent 28-30 days	Less than 10 percent	(n)
Department of Commerce	No			
Department of Defense	Yes	Debt delinquent 30 days	No data available	Treasury rate
Department of Education	Yes	Debt delinquent 60 days	11 to 40 percent	Treasury rate
Department of Energy	No			
Department of Health and Human Services	Yes	Debt delinquent 30-45 days	Less than 10 percent	Treasury rate
Department of Housing and Urban Development	No			
Department of the Interior	No			
Department of Justice	Yes	Debt delinquent 30 days	Less than 10 percent	Treasury renegotiation board
Department of Labor	Yes	Debt delinquent 30 days	11 to 40 percent	Treasury rate
Department of State	Yes	When auditee informed	No data available	Treasury rate
Department of Transportation	b/ Varies by div.	Debt delinquent 30 days	Less than 10 percent	Treasury rate
Department of the Treasury	No			
ACTION	No			
Environmental Protection Agency	Yes	Debt delinquent 30 days	Less than 10 percent	Treasury rate
General Services Administration	No			
National Aeronautics and Space Administration	Yes	Debt delinquent 30 days	No data available	Treasury rate
Small Business Administration	No			
Veterans Administration	No response	No response	No response	No response
International Communications Agency	No			
National Science Foundation	No			
Nuclear Regulatory Commission	Yes	Debt delinquent 30 days	Less than 10 percent	Terms of contract
Office of Personnel Management	Yes	When auditee informed	More than 90 percent	(o)
Smithsonian Institution	No			
Civil Aeronautics Board	Yes	If no immediate repayment	Less than 10 percent	Current prime rate
Consumer Product Safety Commission	No			
Equal Employment Opportunity Commission	No			
Federal Emergency Management Agency	No			
Legal Services Corporation	No			
National Endowment for the Humanities	Yes	Debt delinquent 30 days	Less than 10 percent	Treasury rate
Tennessee Valley Authority	No			
United States Postal Service	No			

Footnotes to appendix III

- a/ Questionnaires were sent to 36 Federal agencies. One agency, the Community Services Administration, did not respond. Three agencies (Federal Communications Commission, Federal Deposit Insurance Corporation, and the Federal Reserve System) responded, but did not answer the questionnaire. They stated the questionnaire did not apply to their operations. A total of 32 agencies answered some or all of our questions.
- b/ The Department of Transportation returned questionnaires from its various operating administrations, so the responses within the Department varied for many of the questions.
- c/ The Department of the Treasury returned questionnaires from its various bureaus, so the responses within the Department varied for many of the questions.
- d/ The Department of Health and Human Services always uses offset against the quarterly award of funds for Medicaid disallowed costs.
- e/ The General Services Administration always notifies grantees at the beginning of the grant or prior to award what costs are allowable.
- f/ Legal Services Corporation always uses specific follow up procedures to ensure that the disposition of a disallowed cost required by the monitoring office has actually been made by the grantee.
- g/ At the Department of Labor, the contracting officer's representative always certifies performance before payment is initiated. A closeout process is also used to ensure completion of all terms and conditions.
- h/ It is standard practice at the Department of Defense to not pay contractors until payment has been earned.
- i/ ACTION frequently relies on the government project manager.
- j/ At the Smithsonian, the assurance always comes through inspection and acceptance of work as called for in specifications.
- k/ At the Equal Employment Opportunity Commission the contract monitor is always relied on.
- l/ At the Federal Emergency Management Agency, most audits are performed after completion of the contract.
- m/ Debts due from contractors are not classified at Defense in categories that distinguish audit disallowances from others.

Footnotes to appendix III (cont.)

- n/ The interest rate charged by Agriculture is the rate specified in the contract or, if no rate is specified, it is the lower of the State-allowed rate or the quarterly interest rate published by the Department of the Treasury.
- o/ The Office of Personnel Management currently charges interest at the portfolio rate of the contractor, but is changing to the semiannual Treasury rate.
- p/ Subsequent to our writing the report, additional data were received from the Department of Education, the National Science Foundation, and two administrative divisions of the Department of Transportation (Federal Railroad and Federal Highway Administrations). We did not include these data in the report.

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