



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

Accounting and Information
Management Division

B-282496

June 3, 1999

Mr. Richard L. Gregg
Commissioner, Financial Management Service
Department of the Treasury

Subject: Internal Controls: Matters Related to Disbursements

Dear Mr. Gregg:

We recently reported on the U.S. government's financial statements for fiscal year 1998.¹ In connection with fulfilling our requirement to audit these statements, we tested certain internal controls over federal disbursements processed by Department of the Treasury's Financial Management Service (FMS).² For fiscal year 1998, FMS reported processing over 862 million disbursements totaling about \$1.13 trillion. With some exceptions (the largest being the Department of Defense), FMS makes disbursements for all federal agencies. The internal controls we tested related to the delegation and designation of Certifying Officers; the processing of check, electronic fund transfer, and Fedwire disbursements; Automated Standard Application for Payments (ASAP) system enrollments;³ and selected claims and accounting functions. The purpose of this letter is to advise you of certain internal control matters identified during our testing and to suggest improvements.

Results in Brief

Last year, we reported on, and suggested improvements to, FMS' internal controls related to disbursement processing at FMS and its six Regional Financial Centers—Austin, Birmingham, Chicago, Kansas City, Philadelphia, and San Francisco.⁴ FMS'

¹Financial Audit: 1998 Financial Report of the United States Government (GAO/AIMD-99-130, March 31, 1999).

²31 U.S.C. 331(e) (1994).

³The ASAP system, jointly implemented by FMS and the Federal Reserve Bank of Richmond, is an electronic payment and information system. Under this system, organizations can draw federal funds from bank accounts preauthorized by federal agencies. Organizations participating in the ASAP system include recipients of federal domestic assistance programs, such as state agencies, and third party providers—such as Medicare providers—that perform financial services for federal agencies. In fiscal year 1998, FMS reported that federal agencies authorized payments of over \$246 billion using the ASAP system.

⁴Internal Controls: Issues Regarding Disbursements (GAO/AIMD-98-144R, April 30, 1998) and Internal Controls: Issues Regarding Automated Standard Application for Payment System (GAO/AIMD-98-142R, April 30, 1998).

162281

GAO/AIMD-99-157R FMS Disbursements Management Letter

corrective actions resolved our concerns relating to the documentation and review of the delegation and designation of agency Certifying Officers, physical controls over returned checks, and the posting of cancellation activities. However, this year's suggested improvements include matters we reported on last year for which FMS' corrective actions were incomplete and new matters identified during this year's audit work. Specifically, we are reaffirming our prior year suggestions for improvements to (1) the approval, review, and documentation of disbursements and (2) reconciliation of the returned check cancellations. We are also suggesting improvements to processing and documentation of ASAP system enrollments and reconciliation of replacement benefit checks referred to as courtesy disbursements. Although the internal control matters discussed in this letter are not material in relation to the federal government's fiscal year 1998 financial statements, they warrant your attention.

Scope and Methodology

We designed our fiscal year 1998 testing to primarily reconfirm the existence and functioning of manual internal controls and included follow-up tests to determine whether FMS had implemented effective corrective actions to address our prior year's suggested improvements. To reconfirm the existence and functioning of manual internal controls, we examined selected (1) disbursement transactions, (2) ASAP system enrollments, and (3) reconciliations occurring between October 1, 1997, and August 10, 1998. In addition, we performed follow-up tests that involved examination of specific disbursement processing steps for a day subsequent to May 11, 1998, the date FMS officials informed us they had implemented our suggested improvements to their manual internal controls. For the day selected, we examined (1) all paper SF 1166 vouchers for evidence of Center supervisory or independent review, (2) all FMS 1691 Progress Sheets for proper completion and evidence of Center supervisory or independent review, and (3) the Center's reconciliation of returned check cancellations. We performed our audit work in accordance with generally accepted government auditing standards from June 1998 through January 1999.

Approval, Review, and Documentation of Disbursements

We found internal control matters related to the supervisory approval, review and documentation of (1) the verification of the agency Certifying Officer's signature and (2) progress sheets.

Verification of the Agency Certifying Officer's Signature

Agency Certifying Officers use either an electronic or paper SF 1166, Voucher and Schedule of Payments (SF 1166 voucher), to request that the Centers disburse funds on their behalf. The Treasury Field Operations Manual (FOM) contains the operating procedures used by the six Centers. FOM Sections 1131 and 4114 require the Centers

to verify the Certifying Officer's signature before processing the requested disbursements.⁵

Last year, we found that one of the three paper SF 1166 vouchers tested lacked documentation to support the verification of the Certifying Officer's signature. We suggested supervisory or independent review (and documentation) of the signature verification process for paper SF 1166 vouchers.

Our follow-up testing disclosed that all of the seven paper SF 1166 vouchers examined at the Chicago and Philadelphia Centers had documentation supporting the verification of the Certifying Officer's signature; however, they lacked evidence of supervisory or independent review. Also, we found that the FOM does not require supervisory or independent review of the signature verification process. As we reported last year, without proper controls over the verification of the Certifying Officer's signature, FMS lacks adequate assurance of the validity of the disbursement.

Progress Sheets

To control and track the processing of requested disbursements, the Centers use a Form FMS 1691, Progress Sheet. FMS procedures require the individuals completing each specific task in the disbursement process to initial or sign the Progress Sheet. Last year, at four of the Centers visited, we found no evidence on the numerous Progress Sheets tested that the initial processing steps had been completed, especially the comparison of the number and amount of requested payments, as shown on the SF 1166 voucher, to those to be processed by the Centers, as indicated on the Progress Sheets. We suggested that Center supervisors or independent staff (1) review the Progress Sheets for completeness before disbursing the payment and (2) initial the form to document their review.

Our follow-up testing found no evidence on 2 of the 18 Progress Sheets examined at the Birmingham Center that the Center had completed the initial processing step described above. Our follow-up testing disclosed that the Center had disbursed the payments as requested. In addition, our follow-up testing disclosed that 61 of the 148 Progress Sheets examined at all the Centers, except the Chicago Center, lacked evidence of supervisory or independent review. Also, we found that the FOM does not require supervisors or independent staff to review the Progress Sheets and to document this review. Without fully completed, reviewed, and approved Progress Sheets, FMS lacks adequate assurance that it processed the disbursements as requested.

⁵FMS receives most payment requests using the Treasury Electronic Certification System (ECS). In place of a manual signature, this system uses smartcards and personal identification numbers to authenticate payment requests based on the encrypted keys assigned to each Certifying Officer and agency Security Administrator. We will separately report the results of our contractor's testing of ECS and other FMS systems' electronic data processing (EDP) controls.

Reconciliation of the Returned Check Cancellations

FMS reported that the Centers received almost 2.5 million returned checks in fiscal year 1998. The reconciliation of the number of returned and other checks available for cancellation to the number of checks canceled is essential to ensure that all the checks have been properly accounted for. FMS procedures require clerks to initial the automated check reconciliation report signifying that the Center has canceled all returned and other checks available for cancellation, but the procedures do not describe how to perform or document this reconciliation. Last year, we found that (1) most Centers did not perform a full returned check cancellation reconciliation, (2) some Centers did not document that they had performed the reconciliation, and (3) one Center was unable to provide documentation to allow us to perform the reconciliation. We suggested that FMS issue guidance in the FOM on how to fully perform and document the reconciliation of returned check cancellations

This year, we found that, although FMS had not issued the suggested FOM guidance, all the Centers had developed local reconciliation procedures. However, similar to last year, the Chicago Center did not fully reconcile its returned check cancellations for the day tested. Staff at the Chicago Center performed one part of the reconciliation; however, they did not perform the comparison of various independent reports to the automated check reconciliation report. This comparison is needed to ensure that the automated system had actually canceled, or otherwise accounted for, all the checks. Because of a programming error in the computer-generated automated check reconciliation report, which can contain inaccurate totals, there is a greater need to perform both parts of the reconciliation, including the use of independent reports to reconcile the results of the returned check cancellation process. Also, similar to last year, the Birmingham Center did not fully reconcile its returned check cancellations and, this year, was unable to provide adequate supporting documentation to enable us to perform the reconciliation. If the Centers do not fully perform and document their reconciliation of returned check cancellations, FMS lacks adequate assurance that all returned checks have been canceled.

Processing and Documentation of ASAP System Enrollments

We identified internal control matters related to supervisory review over and segregation of duties for ASAP system enrollments.

Enrollment and Supervisory Review

FMS enrolls federal agencies and organizations (users) into the ASAP electronic payment and information system.⁶ FMS' ASAP Enrollment Guidelines require users

⁶We will separately report the results of our contractor's testing of the ASAP and other FMS systems' EDP controls.

that want to participate in the ASAP system to complete and submit various enrollment forms—such as delegations of authority, user identifications requests, and requestor bank information—prior to FMS granting them ASAP system access. The Centers review the accuracy and completeness of the forms and maintain them in user folders. The enrollment tracking forms guide staff in reviewing, tracking, and accepting the various enrollment forms from which Center staffs input information into the ASAP system. The required supervisory review, which should be documented on the enrollment tracking forms, reduces the risk of errors and irregularities occurring during the ASAP enrollment process. Last year, we found that none of the user's folders selected for review showed evidence of supervisory review and approval of the enrollment procedures performed by the staff.

This year, we reviewed two ASAP enrollments at each of the three Centers—Kansas City, Philadelphia, and San Francisco—processing these enrollments. We found that supervisors' reviews at two Centers were not always ensuring that staff adhered to ASAP enrollment policies and procedures. For example, (1) the San Francisco Center processed one enrollment application form signed by someone other than the official(s) specifically authorized by the user organization, (2) the Kansas City Center finalized one enrollee based upon a verbal bank confirmation and the enrollment tracking form lacked documentation that the supervisor verified the subsequent written confirmation, and (3) a San Francisco enrollment folder indicated that the supervisor reviewed the enrollment tracking form after the ASAP enrollment had been finalized. Centers that do not adhere to ASAP enrollment policies and procedures and fail to perform adequate supervisory reviews of the key user enrollment forms prior to enrolling the users into the ASAP system increase the risk of errors or fraud occurring and not being detected in a timely manner.

Inadequate Segregation of Duties

As part of the ASAP enrollment process, the Centers send a bank confirmation letter to the users' financial institutions to independently confirm the users' bank account data. At all three Centers that process ASAP enrollments, we found that Center staff who process enrollments, including inputting bank data into the system, could also prepare, receive, and reconcile the bank confirmation letters, thus creating inadequate segregation of duties. The Comptroller General's Standards for Internal Controls in the Federal Government (1983) require that key duties and responsibilities in authorizing, processing, recording, and reviewing transactions should be separated among individuals to reduce the risk of error or fraud.

Reconciliation of Courtesy Disbursements

Courtesy disbursements are replacement benefit checks issued by FMS at the request of an agency when the intended recipient notifies the agency that he/she has not received a benefit check. Courtesy disbursements, which are issued in conjunction with the cancellation of the original benefit check, are charged to a special FMS

account rather than to the agency. When the cancellation of the original check is processed, the special FMS account is then credited, resulting in a zero balance. In certain instances, the agency can request that FMS issue the courtesy disbursement check prior to the cancellation of the original check, raising the possibility that both checks could erroneously or fraudulently be negotiated. When both checks are negotiated, FMS does not receive the cancellation credit and charges the agency for the courtesy disbursement. In such cases, the agency becomes responsible for investigating and recovering the duplicate payment.

FMS produces a monthly report of the outstanding courtesy disbursements for the Centers to reconcile. Reconciling the outstanding items on this report is essential to ensure that FMS timely and properly accounts for all activity on its special account. Last year, we found the Philadelphia and San Francisco Centers were not consistently reconciling their courtesy disbursement reports.

This year, we found that, although each Center has local procedures to reconcile its courtesy disbursement reports, the reconciliations were not being performed consistently. For example, the San Francisco Center did not reconcile all items on the two monthly courtesy disbursement reports we tested. In addition, we were told that the Austin, Kansas City, and San Francisco Centers did not perform reconciliations for certain months because they did not receive reports for these months from FMS' Financial Analysis Branch.

We also found that the Kansas City Center procedures only require reconciliation of items over 60 days old on the presumption that month-end timing differences caused many discrepancies that would automatically clear by the next monthly report. While month-end timing differences will likely occur, this delay postpones the Center providing assurance that the financial records are as complete and accurate as possible. Monthly reconciliations also enhance FMS' ability to detect in a timely manner whether the original and courtesy disbursements checks were properly processed.

The Comptroller General's Standards for Internal Controls in the Federal Government require that documentation of transactions or other significant events be complete, accurate, and facilitate tracing the transactions or events. In addition, these standards require written evidence of an agency's internal control objectives and techniques. Without complete and timely monthly reconciliations of courtesy disbursements, FMS does not have adequate assurance that its financial records are complete and accurate and that the special courtesy disbursement account is in balance.

Suggestions

We reaffirm our suggestions from our prior year audit regarding (1) the approval, review, and documentation of disbursements and (2) reconciliation of the returned

check cancellations. We also suggest that you direct the Assistant Commissioner for Regional Operations to (1) require supervisors to adequately review and document their approval of staff's work prior to enrolling a user in the ASAP system to ensure staff follow enrollment policies and procedures, (2) require that a person independent of the enrollment process be the initial recipient of the returned bank confirmations letters and perform a reconciliation to the system data, and (3) develop and implement policies and procedures for the monthly reconciliation of courtesy disbursements, including steps to ensure that the Centers consistently receive outstanding courtesy disbursement reports needed to perform the monthly reconciliations. In addition, we suggest that guidance for all these areas be incorporated in the FOM to ensure consistent and uniform operating procedures among all Centers. Further, we suggest that you direct the Assistant Commissioner for Regional Operations to monitor the implementation of the corrective actions and take steps to ensure compliance.

Agency Comments


In commenting on this letter, the Commissioner of FMS generally concurred with our findings and suggestions for improvements. He stated that FMS has already taken corrective actions on all of the findings except one, which he expects will be completed before the end of fiscal year 1999. We plan to follow up on these matters during our audit of the federal government's fiscal year 1999 consolidated financial statements.

This letter is intended for use by Treasury's management and the Inspector General. We are sending copies of this letter to Senator Fred Thompson, Chairman, and Senator Joseph Lieberman, Ranking Minority Member, Senate Committee on Governmental Affairs; Representative Dan Burton, Chairman, and Representative Henry Waxman, Ranking Minority Member, House Committee on Government Reform; Donald Hammond, Fiscal Assistant Secretary, Department of the Treasury; and Mr. Lawrence Rogers, Acting Inspector General of the Department of the Treasury. This letter is a matter of public record and its distribution is not limited. Consequently, copies will be available to others upon request. We appreciate the cooperation and assistance of FMS management and staff during our fiscal year 1998

B-282496

audit. If you have any questions, please contact me at (202) 512-3406 or Brian Huchro, Assistant Director, at (415) 904-2243.

Sincerely yours,



Gary T. Engel
Associate Director
Governmentwide Accounting and
Financial Management Issues

(919359)

Ordering Information

The first copy of each GAO report and testimony is free. Additional copies are \$2 each. Orders should be sent to the following address, accompanied by a check or money order made out to the Superintendent of Documents, when necessary. VISA and MasterCard credit cards are accepted, also. Orders for 100 or more copies to be mailed to a single address are discounted 25 percent.

Orders by mail:

**U.S. General Accounting Office
P.O. Box 37050
Washington, DC 20013**

or visit:

**Room 1100
700 4th St. NW (corner of 4th and G Sts. NW)
U.S. General Accounting Office
Washington, DC**

**Orders may also be placed by calling (202) 512-6000
or by using fax number (202) 512-6061, or TDD (202) 512-2537.**

Each day, GAO issues a list of newly available reports and testimony. To receive facsimile copies of the daily list or any list from the past 30 days, please call (202) 512-6000 using a touchtone phone. A recorded menu will provide information on how to obtain these lists.

For information on how to access GAO reports on the INTERNET, send an e-mail message with "info" in the body to:

info@www.gao.gov

or visit GAO's World Wide Web Home Page at:

<http://www.gao.gov>

**United States
General Accounting Office
Washington, D.C. 20548-0001**

**Bulk Rate
Postage & Fees Paid
GAO
Permit No. G100**

**Official Business
Penalty for Private Use \$300**

Address Correction Requested
