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BY THE COMPTROLLER GENERAL

Report To The Congress

OF THE UNITED STATES

Continuing And Widespread Weaknesses In Internal Controls Result In Losses Through Fraud, Waste, And Abuse

Billions of Federal dollars are lost annually through fraud, waste, and abuse. This report summarizes a series of earlier reports on internal control weaknesses in 11 Federal agencies. The activities reviewed represent a cross section of Government activities--civilian and military, domestic and overseas.

Repeatedly, GAO found control weaknesses over virtually all aspects of accounting operations--accounts receivable, collections, disbursements, obligations, and imprest funds--that allow monetary losses to occur. The implications are very disturbing: it appears probable that similar problems exist throughout the Federal Government.

The Office of Management and Budget recently urged the heads of Federal agencies to give personal attention to internal controls. GAO believes the Congress should enact legislation currently under consideration that would place greater responsibility on Federal agency heads for the soundness of their organizations' financial control systems. Such legislation would be an important step toward reducing the loss of Federal funds through fraud, waste, and abuse.

UNITED STATES GENERAL ACCOUNTING OFFICE

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

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To the President of the Senate and the
Speaker of the House of Representatives

In the past several years much publicity has been given to cases where Federal money was lost through fraud, waste, and abuse. This report discusses financial and accounting control weaknesses allowing these conditions to exist and demonstrates that these conditions could exist in most Federal agencies.

This report points out that Federal agencies are required to maintain internal control systems that safeguard their financial resources. However, no mechanism now exists to enforce this requirement. Therefore, we are recommending that the Congress enact recently introduced legislation requiring Federal agencies to evaluate and report on the adequacy of their systems of internal control. We have not obtained agency comments because the material contained in the report has been previously accepted by the agencies.

We are sending copies of this report to the Director of the Office of Management and Budget. Because the report contains information that should be useful in evaluating internal control systems, we are also sending copies to the heads of all Federal agencies.

Sincerely yours,

Elmer B. Staats

Comptroller General
of the United States

AGC00027

Charles H. Percy
SEN. Charles McC. Mathias
Thomas F. Eagleton

COMPTROLLER GENERAL'S REPORT TO THE CONGRESS

CONTINUING AND WIDESPREAD WEAKNESSES IN INTERNAL CONTROLS RESULT IN LOSSES THROUGH FRAUD, WASTE, AND ABUSE

D I G E S T

A longstanding law requires the heads of executive agencies to establish and maintain systems of accounting and internal control over, and accountability for, all of the agencies' assets. Despite this requirement, most Federal agencies are operating systems that are vulnerable to physical losses and waste of Federal money as well as fraudulent and otherwise improper uses.

This report summarizes conditions noted in a series of GAO reports, issued between December 1976 and October 1979, covering financial and accounting operations at 157 fiscal offices in 11 major Federal organizations. The fiscal offices were selected to provide a cross section of military and civil Federal activities in the United States and overseas. These reports indicate widespread and serious internal control weaknesses may exist in the operations of the fiscal offices which result in Government money being wasted through mismanagement or fraudulent or abusive practices. We did not obtain agency comments because material contained in the report has been previously accepted by the agencies.

The vulnerability of systems results from a series of weaknesses that go undetected for long periods. Agencies usually correct specific deficiencies pointed out at individual offices, but generally are slow to correct systemwide deficiencies in collection, disbursement, obligation, and imprest fund activities.

FGMSD-80-65

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COLLECTION WEAKNESSES

At 8 of the 11 agencies GAO reviewed, controls were inadequate to ensure that amounts owed the Government were recorded as accounts receivable or that overdue accounts were identified and collected. As a result, millions of dollars went uncollected. For example, Department of Labor fiscal offices had not recorded about $218 million as accounts receivable due the Government and so no efforts were made to collect that amount. (See p. 4.)

The accounts receivable that were collected often were so poorly controlled and safeguarded that the potential for theft, loss, or other misuse was quite high. Further, several agencies were so lax in controlling receivables from travel advances that employees were able to leave their jobs without ever repaying amounts due the Government. (See pp. 12 and 13.)

DISBURSEMENT WEAKNESSES

Controls over disbursement activities were also found to be deficient in many fiscal offices reviewed. To illustrate, the Naval Fleet Finance Center had not preaudited travel vouchers submitted for payment. Because of this it had made over $700,000 in overpayments in 2 months. Also, Army European Command fiscal offices had failed to take advantage of $99,000 in discounts offered in one year. (See pp. 15 and 16.)

Such waste occurred because many fiscal offices had disregarded basic control procedures prescribed in manuals published by GAO, Treasury, and their own agencies. Sometimes agencies were not even using sound judgment in making disbursements. For example, several Environmental Protection Agency offices had routinely made disbursements without determining if the amount of payment and name of payee were correct. (See p. 16.)

OBLIGATION WEAKNESSES

Obligations are financial commitments made by Federal agencies which will require future cash outlays. It is essential that fund availability be established before an obligation is made and that the amount of the obligation be properly calculated.

However, about half of the 157 offices GAO reviewed had serious weaknesses in controls over obligations that could result in improper or illegal payments. For example, five U.S. embassies in Western Europe frequently incurred obligations before availability of funds was established. A Health Services Administration office let $1.3 million in obligations go unrecorded for about a year after they were incurred. (See pp. 19-21.)

IMPREST FUND WEAKNESSES

Perhaps the most widespread deficiencies were noted in imprest fund activities. Imprest funds--"cash on hand" funds advanced to an agency to meet miscellaneous day-to-day needs and composed of checks and cash--are susceptible to misuse and so must be kept to minimum amounts and controlled. The amount of imprest funds ranges from less than $300 to more than $380,000.

Weak controls, combined with susceptibility of funds to misuse, allow substantial losses to the Government. Federal agencies reported to GAO over $1.1 million in fund losses between June 1977 and July 1979.

Several of the agencies in which GAO noted control weaknesses also reported substantial losses. To illustrate, GAO reported weak physical security over imprest funds at several Department of State fiscal offices. In the 22 months ending May 1979, State reported over $290,000 in cashier losses to GAO--over $207,000 of these losses were directly linked to robbery and theft cases. Similarly, the Environmental Protection Agency reported over

$50,000 in losses and in August 1979 the Department of the Army reported a loss amounting to $209,000; GAO had found both agencies lax in controlling their imprest funds. (See pp. 24 and 25.)

INTERNAL AUDIT COVERAGE

Adequate internal audit coverage could have detected most of the deficiencies GAO found, allowing management to correct them earlier. GAO has pointed out in other reports that Federal agencies often do not use their internal auditors to examine their financial operations and when they do, they frequently do not take action on the findings. (See pp. 27 through 30.)

In an October 1978 report, GAO noted that management left unresolved $4.3 billion in audit findings contained in nearly 14,000 internal audit reports at 34 agencies and thus jeopardized or delayed the collection of funds due the Government. Some examples the report cited included the following:

--A Housing and Urban Development official said his staff was too busy approving new housing projects and would not have time for at least another year to collect $270,000 which auditors found HUD had overpaid to grantees.

--Five years after Department of Labor auditors questioned the allowability of $3 million claimed by a contractor, program officials finally agreed with the auditors. Recovery will be difficult, if not impossible, because of the delay and because the agency no longer does business with the contractor.

NEEDED ACTIONS

In responding to GAO's reports, the agencies generally agreed to correct the weaknesses GAO found. GAO remains concerned, however, because maintenance of good internal control systems requires continual concern. The accounting and management systems of which internal controls are a part change rapidly with changes in personnel, equipment such as computers, and operating methods. Thus, an agency's concern must be constant if it is to continuously maintain an effective system of internal control. (See pp. 31 and 32.)

The Office of Management and Budget has also expressed concern over the Governmentwide lack of internal control. In an April 18, 1980, memorandum to agency heads, the Director of the Office of Management and Budget urged heads of Federal agencies to give their personal attention to examining the adequacy of their organizations' systems of internal control. GAO concurs with the need for such examinations and is sending this report to all Federal agencies to assist them in this effort.

Legislation is under consideration in Congress that would place greater responsibilities on heads of Federal agencies for improving their agencies' financial systems. Basically, this legislation would require them to undertake evaluations of their organizations' systems of internal control and report annually to the Congress, and to the President, the results of such evaluations. This legislation would strengthen the accountability aspects of the Accounting and Auditing Act of 1950. GAO recommends that the Congress enact this legislation.

Contents

ABBREVIATIONS

GAO	General Accounting Office
GTR	Government Transportation Request

CHAPTER 1

INTRODUCTION

This report summarizes the weaknesses in Federal agencies' financial and accounting controls that were previously discussed in 11 reports we issued between December 1976 and October 1979. The reports showed that widespread and serious weaknesses existed over long periods of time in the internal control systems of the agencies reviewed. Because of the prevalence and similarity of weaknesses noted, we believe that they may exist throughout the Federal Government's financial operations. Accordingly, we are sending this report to the heads of all Federal agencies to assist them in determining the reliability of their systems of financial controls and initiating any corrective actions needed.

RESPONSIBILITY AND REQUIREMENTS FOR ACCOUNTING SYSTEMS AND RELATED INTERNAL CONTROLS

Section 113 of 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. This responsibility includes providing adequate assurance of the legality, propriety, and correctness of disbursements and collections of public funds. Further, internal control systems should provide for internal audit coverage of agency financial operations.

The accounting systems should conform to the principles, standards, and related requirements prescribed by the Comptroller General pursuant to 31 U.S.C. 66a. The general guidance for developing systems requirements is set forth in the General Accounting Office Policy and Procedures Manual for Guidance of Federal Agencies. For example, title 2 of the manual, "Accounting," sets forth internal financial controls designed to provide, among other things, assurances that:

--All obligations and costs are kept within the limits of congressional appropriations and other authorizations and restrictions.

--All funds, property, and other assets are safeguarded against waste, loss, misuse, or misappropriation.

--All revenues and expenditures applicable to agency operations are properly recorded and accounted for.

--All financial, statistical, and other reports are accurate and reliable.

SCOPE OF REVIEW

The 11 reviews summarized in this report evaluated controls over receipts, disbursements, and other financial transactions at 157 offices of 11 Federal organizations. Collections and disbursements are controlled through agency fiscal organizations consisting of civil agency accounting stations, Army fiscal disbursing stations, and Air Force, Navy, and Marine disbursing stations. For convenience, all office locations reviewed will be referred to as "fiscal offices" in this report. There are approximately 2,000 such fiscal offices throughout the Federal Government.

The agencies and their fiscal offices reviewed were selected to provide a representative cross section of Federal financial operations. They include civil and military agencies' fiscal offices at domestic and overseas locations. The number of fiscal offices reviewed at each agency is shown on the following chart.

Department or agency reviewed	Fiscal offices reviewed	Date of report
Department of State	9	10/10/79
U.S. Military Airlift Command	12	08/28/79
Department of Health and Human Services (note a) Health Services Administration	19	08/22/79
U. S. Pacific Fleet	21	07/10/79
Department of Labor (note b)		
Employment Training Administration	10	05/21/79
Office of the Assistant Secretary for Administration and Management	10	05/21/79
Environmental Protection Agency	13	05/18/79
U.S. Army, Europe, and Seventh Army	7	12/20/78
Department of Housing and Urban Development	12	12/28/77
Department of Justice Drug Enforcement Administration	14	12/27/77
Department of Health and Human Services (note a) Food and Drug Administration	19	11/08/77
Department of Transportation U.S. Coast Guard	11	12/16/76
Total	157	

a/Department of Health, Education, and Welfare at the time of our review.

b/Fiscal office reviews of the Employment Training Administration and the Office of the Assistant Secretary for Administration and Management were combined and the results were issued in a letter report (FGMSD-79-29).

In performing our reviews, we interviewed key officials, using questionnaires specifically designed to identify potential internal control weaknesses. Our examinations focused on the procedures in day-to-day use at the fiscal offices because experience has shown that, while agencies' written procedural requirements may contain control features, such requirements are often not followed. When questionnaire responses indicated potential weaknesses, we tested transactions to establish whether weaknesses did exist. Payroll operations were excluded from the questionnaire because many Federal agencies have centralized this function.

Because of time constraints, we did not attempt to identify losses resulting from control weaknesses. We concentrated on identifying weaknesses so that needed corrective actions could be promptly taken.

CHAPTER 2

WEAKNESSES ARE EXTENSIVE IN RECORDING, COLLECTING, AND CONTROLLING ACCOUNTS RECEIVABLE

Because of weaknesses in the systems for recording, collecting, and controlling accounts receivable, millions of dollars due the Federal Government were either not being collected at the fiscal offices we reviewed or were being recovered long after they were past due. Slow collections sometimes require agencies to seek appropriations to carry out their programs that are larger than would otherwise be necessary, and those increased appropriations mean added interest costs on Treasury's borrowed funds. Moreover, the weaknesses also contributed to inaccurate and misleading financial statements and unnecessarily exposed Government funds to the risk of loss, theft, and misuse.

ACCOUNTS RECEIVABLE ARE NOT PROMPTLY AND ACCURATELY RECORDED

Accounts receivable represent amounts due from operations and therefore are Government assets to be controlled, safeguarded, and--most importantly--collected. The GAO manual (2 GAO 12.4) emphasizes the importance of controlling accounts receivable, stating they should be recorded accurately and as soon as the acts which entitle an agency to collect the amounts involved are completed.

Thirty fiscal offices we reviewed did not follow procedures to ensure that amounts due were recorded as receivables in the financial records. As a result, the normal billing and collection procedures were not followed, agency financial statements and reports did not reflect the value of the receivables, and no actions were taken to recover substantial amounts owed the Government. To illustrate:

--At Labor's Employment Training Administration, action had not been taken to record auditors' exceptions to costs charged against grants. Such exceptions become receivables once management officials agree with them and should be so recorded in financial records. In May 1978, the agency had, from 1,524 audit reports, about $218 million in questioned costs that had never been recorded.

--Five Employment Training Administration offices had not promptly closed out grants and established the amount of unused funds which, under law, are to be promptly returned to the Government by the grantee.

For example, at one office 11 grants had been completed for periods ranging from 3 to 5 years, but about $355,000 of potential refunds were not recorded.

--Most of the Environmental Protection Agency fiscal offices reviewed had not recorded all their accounts receivable, often because operating divisions had failed to notify financial officials of monies due. For example, one station had not recorded almost $780,000 of disallowed grant costs that it had been owed for periods ranging from 1 to 2 years.

We noted that the agencies generally had adequate written procedures to control receivables. However, no action was being taken to enforce compliance with these procedures. For example, one agency's operating divisions were not following specified procedures to notify the fiscal offices of amounts due. Other offices lacked adequate records to reliably identify amounts due.

COLLECTION EFFORTS ARE NEITHER PROMPT NOR AGGRESSIVE

As specified in the Joint Standards of the Federal Claims Collection Act of 1966 (4CF4-101-105), the heads of Federal agencies, or their designees, should take prompt and aggressive action to collect accounts receivable due the Government. The standards further require that (1) three written demands be made at 30-day intervals, (2) collection be made by offset where feasible, (3) debtors be personally interviewed, (4) the possibility of compromise be explored, and (5) other persistent actions to achieve collection be attempted. Despite these requirements, the fiscal offices at six agencies we reviewed had not taken actions to identify problem accounts and to aggressively follow up on the delinquent ones.

Need to better identify problem accounts

One method of determining and controlling delinquent receivables is through accounts receivable aging schedules. These schedules categorize accounts receivable in chronological order by due date and are useful for identifying problem accounts requiring management attention. Despite the widely recognized value of aging schedules, we noted that:

--Five Coast Guard accounting stations did not have (1) accounts receivable aging reports to identify delinquent accounts and the length of time they have been overdue and (2) uniform criteria to determine when accounts receivable were to be considered delinquent.

Consequently, receivables were from 1 month to 1 year overdue before they were considered delinquent.

--Eleven of the thirteen Environmental Protection Agency fiscal offices and twelve of the nineteen Health Services Administration fiscal offices reviewed did not normally prepare accounts receivable aging schedules.

Need to follow up on delinquent accounts

Several fiscal offices we reviewed had not taken actions to collect receivables that were identified as being past due. For example, at the Health Services Administration, five fiscal offices had not developed systematic procedures for vigorously following up on delinquent accounts. At one station, only one bill had been sent to each debtor. When partial payments were received, no second billing was made for the balance due. No action was taken when a debtor paid nothing; the amounts owed were not rebilled, nor was any demand letter or other follow-up communication sent.

At four Department of State installations in Western Europe, we noted a need for more aggressive action to collect overdue accounts receivable. For example, the embassy in Paris had outstanding receivables of over $11,500 for non-business phone services provided its employees. Some amounts had been outstanding for over 9 months and a few individuals owed a large portion of the amount; one owed over $1,700. An April 1978 State Department inspection report called attention to this and recommended that the embassy collect for personal phone calls within 5 working days. Embassy officials agreed, but by the time of our review, had not ensured that the collection procedure was enforced.

At the Department of Labor, some offices' efforts to collect receivables were sporadic; one office had exceptions outstanding since 1969. Because of the low priority assigned to collecting these receivables, only limited followup action had been taken. At another office, lapses from 5 months to over 4 years occurred between attempts to collect amounts due. These infrequent followup contacts obscured problems that might have been resolved and thereby delayed collection of amounts due.

Our findings demonstrate that basic procedures for controlling receivables are not being followed. They also indicate a lack of management emphasis on collecting amounts due the Federal Government.

Other actions to improve the Government's collection efforts

The total amount of receivables due Federal agencies has increased substantially in recent years and this increase has been the subject of growing concern by the Congress and the executive branch. Since the beginning of fiscal 1977, the total amount owed increased from about $69 billion to about $95 billion--a 38-percent increase in just 2 years. This amount is made up of such things as receivables for sales of goods and services, amounts due for student loans, overpayments of supplemental security income benefits, veterans educational assistance, and tax assessments.

The growth of indebtedness has been accompanied by strong indications of inadequacies in the Government's debt collection practices, causing concern in both the Congress and the executive branch. The Comptroller General has testified several times on the Government's collection problems at the request of interested congressional committees. In addition, in 25 reports issued between August 1977 and January 1980 we have discussed the need for improvements in the Government's collection efforts.

These reports discussed serious and widespread shortcomings in collection activities both at individual agencies and Government-wide. In an October 1978 report we pointed out that collection efforts had been hindered by such things as inaccurate recording and accounting and a lack of prompt and aggressive collection actions. It also noted that although agencies often prepared prompt initial billings, they did not collect many receivables within a reasonable period because they did not always follow effective debt collection procedures.

A later report noted that agency collection efforts are not keeping pace with the increase in debts. 1/ It showed that in fiscal 1978, nine major agencies wrote off $428 million in uncollected debts. The report suggested that Federal agencies could collect more debts faster and at less cost by implementing certain commercial practices that make sense and seem to be adaptable to the Government. Such practices include the use of credit bureaus and debtor location services, greater automation in preparing demand letters, and more forceful demand letters.

1/ "The Government Can Be More Productive In Collecting Its Debts By Following Commercial Practices" (FGMSD-78-59, Feb. 23, 1979).

In our other reports on collections, we have made a number of suggestions for improving Federal collection practices. Many of these have been adopted while others are under consideration. The need for the Federal Government to improve its debt collection ability is now widely recognized by the legislative and executive branches. The Congress is considering several bills and the President's Management Improvement Council has, through its Debt Collection Project, begun a comprehensive study of the Government's management of receivables. However, considerable effort will be needed to provide adequate control over the growing dollar amount of debts owed the Government.

MONIES COLLECTED ARE NOT ADEQUATELY CONTROLLED

Both the GAO manual and the Treasury fiscal requirements manual specify that agencies' collections should be promptly recorded, deposited, and adequately safeguarded. Further, the manuals state that responsibilities related to cash collections should be adequately segregated. At several fiscal offices we reviewed, these requirements had not been complied with, thus exposing money that was collected to the risk of loss or misuse.

Weaknesses in recording cash receipts

Cash and checks received through the mails or over the counter are inherently susceptible to loss, theft, or other misuse. Because of this, our manual (7 GAO 11) specifies that agency collections should be placed under appropriate accounting and physical controls as soon as they are received. Such controls should, among other things, provide for the cash and checks to be immediately logged in and verified by an individual other than the one opening the mail. This establishes immediate control and provides a permanent check to determine whether all receipts are subsequently processed and deposited. The controls should also provide for use of prenumbered receipt forms that are properly safeguarded and accounted for.

The required controls had not been established by many of the fiscal offices we reviewed and some of the offices had serious weaknesses in their procedures to control large amounts of cash receipts. Seven Army fiscal offices in Europe had not logged in amounts of cash received by their mailrooms, and only one office had a different person verifying mail collections. These offices were collecting over $62.4 million monthly.

We did not establish the amount of money controlled at each fiscal office reviewed; however, we did note a number of control deficiencies in most of the offices. Some examples follow:

--Nine Health Services Administration fiscal offices had serious weaknesses in their controls. Six had not required all mail containing remittances to be opened at a central control point. One office required the mail to be opened at a central point, but had not logged in all collections. Two offices had mail opened and collections logged in by the person responsible for processing collections and making deposits; these collections had not been verified by another person. Six offices had not used prenumbered receipt forms for all over-the-counter collections and thus lacked assurance that all collections were accounted for. At eight offices, prenumbered forms had been used but such forms had not been adequately controlled or safeguarded.

--At 11 Department of Labor fiscal offices, the employees opening the mail had not immediately recorded or accounted for collections. Ten offices also had not used receipts to accompany checks forwarded from one processing point to another.

--Five Coast Guard locations had not required all mail clerks to open and log in letters specifically addressed to the collection clerks. In a Seattle fiscal office, the mail had been delivered unopened to the collection clerk who sorted and delivered it to the accounting branch before remittances were recorded in the proper register.

Weaknesses in depositing cash receipts

When collections are not deposited promptly, access to the funds by Treasury is delayed and the potential for loss, theft, or misuse of the funds is increased. Undue delays in depositing monies collected mean that the Treasury is denied use of the funds, and as a result, must borrow--increasing the Government's interest costs.

At 73 of the 157 fiscal offices we reviewed, procedures had not been established to insure that all collections are deposited promptly. The GAO manual (7 GAO 12.2) stipulates that collections be deposited daily if possible. The Treasury Department provides more specifics on deposit frequency in its Fiscal Requirements Manual for Guidance of Departments and Agencies (1 TFRM 6-8030), which states that collections of $1,000 or more should be deposited daily but that smaller collections may be accumulated and deposited when they total $1,000. Still, deposits must be made at least weekly regardless of the amount accumulated.

Fiscal offices at nine of the agencies we reviewed had not promptly deposited collections. For example, at the Environmental Protection Agency, one fiscal office normally made deposits at the end of each month, even though monthly deposits ranged from $65,000 to $335,000 over 5 months in 1978. Another office usually made deposits once or twice a month, and two other offices made only weekly deposits even though collections often exceeded $1,000 daily. Two other offices did not immediately deposit large amounts received daily. At one of these offices, a $50,000 check was not deposited until 8 days after it was received.

The importance of prompt deposits is well illustrated by an actual occurrence at one Health Services Administration fiscal suboffice. Early in 1977, an audit at the suboffice revealed a $12,000 shortage in undeposited collections of patients' funds (personal funds of hospitalized patients entrusted to the Government for safekeeping). An analysis of collections and deposits at this activity disclosed that collections of patients' funds had been routinely accumulated for several weeks, in some cases for months, before being deposited. Had these collections been deposited promptly, a loss of this magnitude could not have occurred.

Failure to provide separation of duties

As specified in the GAO Manual (7 GAO 11.2), a basic principle of internal control is dividing critical functions between two or more persons, a technique referred to as separation of duties. Experience has shown that fraudulent activities are less likely to be successful if their commission requires two or more individuals. Yet, at 43 of the 157 fiscal offices we reviewed, duties related to collections had been assigned without regard to these widely recognized internal control practices.

Duties were not properly separated in fiscal offices of 7 of the 11 agencies we reviewed. Poor practices were widespread within several agencies as illustrated by the following conditions noted at the Health Services Administration's fiscal offices.

--In 10 offices, the same employees had responsibility for receiving and recording collections, preparing deposit tickets, and making all bank deposits without verification against collection records by other employees.

--In six offices, the collection officer received the money and actually prepared transactions for input into the accounting records, and in two of these offices the collection officers also maintained the accounts receivable records.

--In 11 offices, the custodian of imprest funds also received, recorded, and deposited collections, including collections of patients' funds at 10 stations.

When cash receipts are handled by an imprest fund custodian, the opportunity is provided for the cash receipts to be used to cover shortages in imprest funds, thereby increasing risk of fraud or misuse of funds. This is particularly true when collections are allowed to accumulate over a period of time before being deposited.

Failure to safeguard cash receipts

Currency and checks are highly susceptible to improper conversion or loss. Thus, the accounting controls should include physical security measures to safeguard them.

As illustrated in the following examples, many fiscal offices we reviewed had not instituted adequate physical controls over checks and currency.

--Two Environmental Protection Agency fiscal offices sometimes left collections overnight in mail slots and on desk tops in an unlocked room. Another office stored collections in an unlocked desk drawer.

--Seven Department of Labor offices had a variety of physical control problems. For example, at one office collections remained on the desk of an employee who was on leave. Four offices stored collections overnight in locked desk drawers and files; only one of these offices had a safe, but it was not used to store collections. Another office stored collections in an open file cabinet that was accessible to eight employees during regular working hours. Still another office stored its collections in a safe but failed to change the combination annually.

--At five Pacific Fleet offices more than one person had access to funds, safe combinations were known or available to more than one person, or collections were placed in unlocked containers.

We noted that agencies' manuals normally contained adequate procedures for physically controlling the cash and checks. The Navy Comptroller Manual, for example, requires that all cash in possession of an accountable person be kept in a safe or security container with the combination known only to that person. In most cases, the weaknesses we noted can be corrected by simply requiring people to follow the procedures prescribed.

TRAVEL ADVANCES ARE NOT PERIODICALLY REVIEWED OR PROMPTLY RECOVERED

The GAO manual (7 GAO 25.6) provides that agency accounting systems should include procedures for periodic review and analysis of outstanding travel advances. All advances determined to be in excess of immediate needs should be promptly recovered to keep outstanding balances to a minimum. Eight of the agencies reviewed did not exercise proper control over travel advances, allowing the advances to remain outstanding for excessive periods. This practice unnecessarily ties up funds needed for travel and increases the risk that travel advances might never be recovered.

Some fiscal offices were extremely lax in monitoring and recovering travel advances. In fact, we noted cases where employees had left the Government without repaying sizable travel advances. The following examples illustrate situations we found:

--Four Department of Labor offices had not exercised proper control over travel advances. At two offices, advances shown on travel vouchers were not being periodically reconciled to the amounts listed on travel advance control cards. Other offices failed to collect outstanding travel advances from employees before employment was terminated. Regional officials in one of these offices wrote off advances amounting to $922.45 during fiscal 1977 because some former employees could not be located.

--Three Environmental Protection Agency fiscal offices had not analyzed travel advances at frequent, regular intervals even though data to perform such analyses was readily available. Further, aggressive collection action had not been taken on advances known to be excessive and outstanding for long periods. The offices' records showed many advances to be over a year old and in some instances as high as $1,000. The records at one office showed outstanding travel advances for some former employees. We also noted that one office gave additional advances to employees who had not cleared previous advances.

--Travel advances at three Housing and Urban Development fiscal offices were outstanding for an excessive period of time. Two offices had unpaid travel advances of $8,600 from 38 former employees. In addition, records at several fiscal offices indicated that travel advances for employees moving from one location to another had been outstanding for several years.

--The Pacific Fleet offices we visited had, as of August 1978, over 18,000 advances for more than $1 million that were more than 60 days old. When asked about the problem, a Navy official said the Naval Audit Service had recently found that the Pacific Fleet's Naval Air Force had excessive travel advances. According to the Audit Service, travel advances remained outstanding too long because periodic listings of travel were not reviewed promptly.

Travel advances represent sizable amounts of Government funds. Accordingly, they should be as well controlled as other types of accounts receivable.

CHAPTER 3

SAFEGUARDS AND CONTROLS OVER DISBURSEMENTS ARE INADEQUATE

Many agency disbursing operations we reviewed did not conform to Treasury and GAO requirements, and as a result, Federal funds were being unnecessarily exposed to the risk of loss, theft, or other misuse. Moreover, the Federal Government's indebtedness and related interest costs had unnecessarily increased because disbursement activities did not conform to recognized principles of sound cash management.

TIMING OF DISBURSEMENTS SHOULD BE BETTER REGULATED

Fiscal offices in several agencies reviewed had not scheduled their disbursements to coincide with invoice due dates or to take advantage of discounts offered by some vendors for prompt payments. Payments had been made either too late or too early, which increased the Government's operating costs.

Specifically, our manual (7 GAO 24.8) provides that (1) procedures be established to ensure that vendors' invoices offering discounts for prompt payment are handled quickly so that payments may be made within the time prescribed and (2) failure to take cash discounts be fully explained on appropriate documents. Further, the Treasury requires that agencies schedule the issuance and mailing of checks as close as possible to the due date of the invoice, contract, or other agreement.

Early payments unnecessarily accelerate the flow of cash from the Treasury. This increases the amounts Treasury must borrow from the public and adds to the national debt and related interest costs. For example, in a 1978 report we estimated that at least $118 million might have been saved Government-wide over a 6-month period if all the early payments had been made exactly on the due date. 1/ Late payments, on the other hand, are not only contrary to good business practices but also prevent the Government from taking advantage of cash discounts offered by vendors for prompt payment. Explanations of discounts missed enable financial managers to evaluate disbursing and cash management activities and help them identify and eliminate the problems that prevent discounts from being taken.

1/"The Federal Government's Bill Payment Practices Are Good But Could Be Better" (FGMSD-78-16, Feb. 24, 1978).

Twenty-five fiscal offices did not systematically schedule the payment of vendors' invoices to coincide with due dates or to take advantage of discounts offered. Furthermore, we found that 55 fiscal offices did not document the reasons why the discounts were not taken. For example:

--Seven fiscal offices of the U.S. Army European Command had not taken advantage of discounts amounting to about $99,000 over 1 year.

--Twelve Health Services Administration offices neither explained the reasons for lost discounts nor maintained records showing the amount of discounts lost. Officials at most of these offices were unable even to estimate the amount of discounts lost. One official, however, estimated that his office had lost $5,000 in discounts during 1978 because of a continual backlog of unprocessed invoices and the lack of a procedure to give priority processing to invoices involving discounts.

Fiscal office employees at several agencies we visited had paid invoices without first checking for due dates and discounts offered. Because invoices were not preaudited, many offices lost the opportunity to take discounts. For example, one Department of Labor fiscal office lost discounts amounting to about $1,532 in 1 fiscal year on 303 invoices that had not been preaudited. We sampled 50 invoices in another office and found that only 4 of 13 available discounts had been taken.

We noted that eight Environmental Protection Agency fiscal offices had paid their bills either too early or too late. One office paid 52 percent of its bills from 5 days to 3 weeks earlier than the due date. These early payments can unnecessarily increase interest costs on the public debt. On the other hand, 28 percent of the office's payments had been made too late to meet the due date and take advantage of discounts. Another office paid 46 percent of its bills from 9 days to 23 days early and paid 38 percent from 4 to 192 days late.

LEGALITY, PROPRIETY, AND ACCURACY OF DISBURSEMENTS SHOULD BE CHECKED BEFORE PAYMENTS ARE MADE

Because disbursement transactions are susceptible to misuse and diversion, GAO and Treasury provide extensive guidance to help ensure the propriety, accuracy, and legality of disbursements. The guidance requires the preaudit of vouchers, controls to prevent duplicate payments, and adequate accounting for disbursement transactions. We noted that even when such controls are required by agencies' written procedures, the requirements were often not followed in practice. As a result, Federal disbursements were not adequately protected against fraud, waste, and other abuse.

The GAO manual (7 GAO 24.2) states that vouchers should be preaudited before they are certified for payment. Preaudits are reviews which check and verify the accuracy of the data on the disbursement voucher. Some of the items to be verified are: the amount of the payment and the name of the payee; whether the payment duplicates another; and the quantities, prices, and amounts on the voucher. Furthermore, vouchers are checked for proper authorization, legality, and determination that the goods and services received are in accordance with the agreement.

In our review of 157 fiscal offices, we found 23 offices not adequately supporting or reviewing disbursement vouchers. For instance:

--Employees at the Pacific Fleet averaged about a 13-percent error rate when processing vouchers during a 2-month test in 1978, resulting in about $710,300 in overpayments and about $17,600 in underpayments.

--Employees at Environmental Protection Agency fiscal offices made disbursements without first determining whether the amount of payment and the name of payee were correct. At one of the offices, employees had not determined before payments were made whether quantities, prices, and amounts were accurate, or whether goods received and services rendered were in accordance with purchase agreements.

--One Labor fiscal office had processed unaudited travel vouchers which contained erroneous payments. Travel expenses had been paid without proper authorization documents, such as a standard travel authorization or purchase order. And invoices for consulting contracts had been paid without review of documentation or certification by the project officer.

The serious consequences of failing to perform adequate preaudits are illustrated by a recent fraud case that occurred at a Department of Transportation office in Washington, D.C. In 1977 a financial clerk embezzled over $856,000 in Federal funds by falsifying vouchers instructing the Treasury Department to issue checks for specified amounts. The clerk substituted his name on the voucher for that of a mass transit authority. The vouchers were routinely approved and certified by the clerk's supervisor, the certifying officer, and later processed along with other approved payments against mass transit grants. Because the supervisor did not properly preaudit vouchers before signing them, the financial clerk was able to successfully process six fraudulent vouchers totaling $856,557. We believe this embezzlement would have been avoided if the supervisor had adequately preaudited the vouchers.

CONTROLS OVER GOVERNMENT TRANSPORTATION REQUESTS SHOULD BE IMPROVED

Government Transportation Requests (GTRs), when presented to a carrier, authorize the carrier to issue tickets to Government travelers. In addition, GTRs authorize the carrier to bill the Government agency for services provided. By their nature, these documents are readily convertible to improper use so it is essential that they be placed under adequate safeguards and controls.

A recently discovered illegal conversion of GTRs amounting to over $30,000 at a Federal agency's fiscal office in Washington, D.C., illustrates the consequences of inadequate controls. At this office, one employee was given total control of the acquisition, custody, issuance, and accounting for GTRs without any intervention or reconciliation by other employees. Further, this employee also received the invoices from airlines for travel authorized by the GTRs.

Because of this total absence of checkpoints, the employee was able to issue GTRs and obtain airline tickets for personal nonbusiness use by the employee and several acquaintances. The individual concealed the illegal travel by disposing of invoices for such travel sent in by the airlines. This continued for 2 years, during which time airline tickets valued at over $30,000 were illegally obtained and used. The activity was discovered in June 1979 only because investigations were begun as a result of other improper activities by the employee.

The potential for similar misuse of GTRs existed at two of the agencies we reviewed; to illustrate:

--Five Department of Labor fiscal offices had not followed departmental procedures for safeguarding and controlling GTRs. One office designated 12 employees as primary GTR custodians, although Labor regulations specify that only 1 employee should be so designated. At another office, seven employees knew the combination of the safe containing the GTRs and, by writing the combination on a desk note pad, made it readily accessible to anyone else. Furthermore, the combination had not been changed in over 5 years. Three offices had not periodically reconciled used, unused, and voided GTRs, thus limiting the effectiveness of accountability records.

--Four Environmental Protection Agency fiscal offices had not adequately controlled or safeguarded GTRs. The primary custodian and subcustodians of requests at one office had not periodically reconciled requests issued, used, and on-hand and did not know whether requests had been used, lost, or stolen after they were issued. At another office, officials had not properly completed and periodically reviewed the forms used to record requests issued and to reconcile requests. For example, 14 of 25 GTRs issued in February 1978 had not been accounted for by October 10, 1978. Nine of the GTRs had been issued to an employee who had not been employed by the agency since February 1978. Requests at two stations had been stored in unlocked credenzas or desk drawers. Unused requests, like cash, should be maintained under proper physical control at all times.

The easy convertibility of GTRs for personal use makes them prime targets for abuse. Accordingly, they should be controlled in the same manner as other valuable, easily converted assets.

CHAPTER 4

WEAK CONTROLS OVER OBLIGATIONS ALLOW

INACCURATE RECORDS AND IMPROPER EXPENDITURES

Of the 157 fiscal offices we visited, 73 had weaknesses in documenting, recording, or controlling obligations which could cause inaccuracies in the Federal Government's financial records and statements and even allow improper and illegal expenditures.

Obligations specify the amounts of orders placed, contracts awarded, services rendered, or other financial commitments made by Federal agencies that will require cash outlays during the current or some future period. Our guidance to agencies emphasizes that funds must be available before the Government is committed to an obligation and that obligations must be properly recorded in agencies' financial records.

One consequence of failing to control obligations can be the obligating of amounts in excess of those appropriated by the Congress, a practice specifically prohibited by the Anti-Deficiency Act (31 U.S.C. 665). In a 1976 report, we noted that such an anti-deficiency violation amounting to almost $1 million occurred at the Equal Employment Opportunity Commission. 1/ More recently, in a draft report to the Secretary of the Interior, we discussed Anti-Deficiency Act violations amounting to at least $186,000 but possibly as high as $13 million. We attributed these violations to control weaknesses.

CONTROLS OVER RECORDING OF OBLIGATIONS SHOULD BE STRENGTHENED

Fiscal offices at four of the agencies reviewed did not adequately control the recording of obligations. As a result, they incurred and recorded obligations without establishing the availability of funds, did not always record valid obligations, and recorded as obligations amounts which did not meet the criteria for validity.

One of the agencies with weak controls was the Department of State. At its fiscal offices we found several instances where the availability of funds was certified after the obligation was recorded. Four American embassies, as shown in

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1/ "Violations of the Anti-Deficiency Act and Other Management Problems at the Equal Employment Opportunity Commission" (FGMSD-76-12, Apr. 5, 1976).

the following table, also frequently incurred obligations before funds were certified as available.

Embassy location	Obligation documents reviewed	Funds certified available after obligation incurred
Athens	41	11
London	49	10
Madrid	43	15
Paris	163	38

At a fifth embassy, we noted several instances where the availability of funds was certified after the obligation was incurred. Embassy personnel said this was a recurring problem and estimated that it happened in about 20 percent of the cases. While we found no instances where this practice resulted in an embassy being overobligated at fiscal yearend, such practices reduce management's awareness of unobligated funds and indicate poor fiscal management and control.

We noted similar problems at the Department of Labor. One of its fiscal office's obligations had been recorded even though they did not meet the criteria for valid obligations. Similarly, valid obligations had not been promptly recorded in several instances. We noted that at another office, obligations were not promptly recorded and, as a result, employees in this office paid some invoices without adequate supporting documents.

These conditions are serious; they can lead to overobligation of funds, violations of the Anti-Deficiency Act, and inaccuracies in agency financial statements.

OBLIGATIONS SHOULD BE REVIEWED

The GAO manual (7 GAO 17.3) specifies that obligation documents should be reviewed at the end of each fiscal year to (1) establish the validity of recorded obligations, (2) determine the continuing validity of older obligations, and (3) determine if recently recorded obligations are valid.

Despite the widely recognized value of such reviews, they were not performed at fiscal offices in three of the agencies we reviewed. To illustrate:

--Four Environmental Protection Agency offices had a large number of obligations recorded against grants for which no disbursements had been recorded in 2 years. For instance, a grants administration office had 285 such grants, totaling $8.9 million. None of the four offices had tried to confirm the current validity of the prior year's obligations.

--Two Food and Drug Administration offices did not periodically review prior year unliquidated obligations. At one office, the unliquidated obligation listing in two accounts included several transactions totaling almost $400,000 that extended from fiscal 1973 through 1975.

--A Health Services Administration fiscal office had about $1.3 million in obligations that were recorded more than a year after they were incurred. As a result, fiscal 1977 obligations of the Indian Health Service were understated by more than $1 million.

BASIS FOR COMPUTATION OF OBLIGATIONS SHOULD BE RECORDED

The GAO manual (7 GAO 17.1) requires agencies to estimate the amount of an obligation if the exact amount is not known when it is incurred, and to show the basis for and computation of the estimate on the obligating document. These requirements had not been followed by 55 fiscal offices in 9 of the 11 agencies we reviewed.

The deficiencies noted usually related to cases where estimates had been used to record obligations. For instance, 11 of the 13 Environmental Protection Agency fiscal offices had not explained the basis for estimates.

At the Coast Guard's Honolulu district office, however, neither the basis for nor computation of estimates had been recorded on obligating documents. At this service's Portsmouth district office, the official responsible for obligating funds did not know the method used to estimate obligations. Under these circumstances, management cannot always exercise proper control over funds.

Agency officials are responsible for maintaining proper fund controls to ensure that obligations and expenditures do not exceed the amounts authorized. Recording correct information on obligations helps ensure that established estimating methods are consistently applied and provides management with a basis for evaluating the methods.

CHAPTER 5

IMPREST-TYPE FUNDS NEED BETTER MANAGEMENT

Imprest funds are "cash on hand" funds comprised of currency, coin, or Government checks advanced by a U.S. Treasury disbursing office to agency imprest fund cashiers. Our reviews showed that not all Federal agencies reviewed were adequately controlling, safeguarding, or managing millions of dollars in such funds. As a result, they were unnecessarily exposed to the risk of loss, theft, or misuse, and the Government's borrowing costs were increased.

GAO and Treasury have provided extensive guidance on controlling, safeguarding, and managing imprest-type funds. Our Policy and Procedures Manual for Guidance of Federal Agencies (7 GAO 27) sets forth the requirements for the use of imprest funds by the various departments and agencies. Treasury's Fiscal Requirements Manual and its Manual of Procedures and Instructions for Cashiers specify procedures for agencies to follow when handling imprest funds. Also, many Federal agencies' regulations and procedures manuals provide guidelines for the proper operation of such funds. However, Federal agencies incurred large losses because they simply disregarded basic management techniques, such as performing unannounced audits, physically securing money, and limiting the size of the fund to actual needs.

FUNDS ARE EXPERIENCING LARGE LOSSES

Imprest funds are usually designed to meet the day-to-day miscellaneous financial needs of a particular department or agency. They are used for a variety of disbursing needs such as payments to vendors for goods and services, payments for travel advances, employee reimbursements for authorized expenditures, and routine office expenses.

These funds are inherently susceptible to misuse because the cash and checks they contain are easily converted and substantial losses do occur. Between June 1977 and July 1979, Federal agencies reported to us over $1.1 million in losses in imprest funds. As of July 1979, over $397,000 of such losses remained unexplained. We have no assurance that all imprest fund losses are reported to us, and the true amount of losses may be higher than that cited above.

UNANNOUNCED AUDITS OF FUNDS SHOULD BE PERFORMED

Forty fiscal offices had not protected funds in their custody by performing unannounced audits and examinations. Such audits and examinations, as provided for in the GAO and Treasury manuals, are a primary deterrent to improper operation of imprest funds.

Their purpose is to determine whether (1) funds are properly accounted for, (2) the amounts of the funds are in correct proportion to cash requirements, (3) the procedures followed protect funds adequately from loss or misuse, and (4) the funds are used for authorized purposes only. Further, in our view, the knowledge that unannounced audits are frequently performed serves as a deterrent to irregular acts.

Despite the widely recognized benefits of such audits, fiscal offices at some agencies had not performed them as required. For example:

--Seven Food and Drug Administration fiscal offices had not performed the required audits of their imprest funds.

--Two Environmental Protection Agency fiscal offices had verified their fund balances on the same day of each quarter rather than at irregular intervals as required. Advance knowledge of precisely when fund examination will take place greatly diminishes the value of the examinations. During our review, we noted that one cashier had commingled personal money with imprest funds. Another cashier improperly made direct purchases with imprest funds.

--The State Department failed to audit or verify imprest fund balances at all nine of the embassies we reviewed. We noted at most embassies visited that cashiers had routinely disbursed money in excess of the Department's usual authorized limit of $250 for a single transaction. For instance, such payments had included $15,000 in residence expenses for officials and a $1,000 hotel bill.

PHYSICAL SECURITY OVER IMPREST FUNDS SHOULD BE IMPROVED

Our reviews noted weaknesses in physical security over imprest funds at 56 of the 157 fiscal offices examined. These weaknesses consisted of such things as inadequate storage facilities and failure to change safe combinations as required.

Security over storage and transportation of funds

In 4 of the 11 agencies we reviewed, several fiscal offices had failed to provide adequate safekeeping facilities for the storage and transportation of funds. The GAO and Treasury manuals specify standards of security that should be employed over funds, and this guidance is often supplemented by Federal agencies' own regulations and established procedures.

This guidance generally provides that imprest funds containing cash, checks, and other negotiable instruments should be placed in a suitable safe or vault within the office under the exclusive control of the fund custodian. File cabinets with key locks are not considered to provide adequate security, but those with a bar and combination locks can be considered acceptable in some circumstances. Perhaps most importantly, prudence and due regard for the responsibility to safeguard public funds should guide those to whom such funds are entrusted.

Many fiscal offices we reviewed had not followed this guidance. For example:

--One State Department fiscal office had stored $18,000 in a key-lock file cabinet. At another location, we found the door to the cashier's cage unlocked, thus allowing anyone to enter. The cashier of an imprest fund at another location had been robbed of over $50,000 while returning from a bank. Yet, at the time of our visit embassy officials had not implemented the security measures recommended by the official who investigated the theft. Similarly, at another State location personnel had transported imprest funds up to $30,000 without needed security services. From July 1976 through December 1978, the State Department had reported to us over $290,000 in cash losses. The majority of these losses, totaling $207,000, were being linked directly to robbery and theft cases.

--An Environmental Protection Agency cashier had failed to keep imprest funds in a lockable fire-resistant strongbox and instead had placed the money in envelopes in an unlocked metal changebox. The Environmental Protection Agency reported to us $51,712 in losses for fiscal 1979.

--The Food and Drug Administration had one cashier sharing a safe with two other employees and leaving the cashbox unlocked and unattended. Another cashier had left unreimbursed imprest fund receipts on a desk unattended.

--The Army had one fiscal office maintaining imprest funds in an unlocked cashbox stored in a safe which was accessible to several people other than the cashier. On August 7, 1979, another Department of the Army fiscal office reported to us a loss of $209,051 in public funds, resulting from failure to properly safeguard imprest fund cash.

Changing safe combinations

A standard security practice to minimize the potential for losses is to change safe combinations at least annually, but 50 fiscal offices at seven of the agencies reviewed had failed to follow this practice.

Treasury's Manual of Procedures and Instructions for Cashiers (section 4) states that the safe combination should be changed annually and whenever (1) a cashier is replaced, (2) the funds must be reached and a cashier is not available, or (3) the combination has been compromised. This requirement was not enforced at many locations we reviewed. For example:

--Officials at three Department of Labor fiscal offices had not changed safe combinations annually, and two of these offices had no record of the last time they were changed.

--Safe combinations at 11 Food and Drug Administration fiscal offices had not been changed annually.

--The Health Services Administration had not changed safe combinations at 14 of the 19 offices we reviewed.

THE SIZE OF IMPREST FUNDS SHOULD BE LIMITED

Our reviews showed that 27 fiscal offices at 5 of the 11 agencies reviewed maintained balances in imprest funds that exceeded their needs. Maintaining excess cash balances can unnecessarily increase the amount of funds Treasury must borrow from the public, thereby increasing the national debt and related interest costs. Excess balances also increase the amount of funds susceptible to theft, loss, and misuse.

The GAO manual (7 GAO 27.4) states that an imprest fund should be limited to the smallest amount commensurate with the authorized purpose of the fund. Generally, the amount of the fund should not exceed the amount necessary to cover normal disbursements during an administratively established time period. For example, one agency has set the maximum authorized imprest fund level as the amount necessary to meet 3 days' disbursement needs.

Some agencies' accounting manuals instruct imprest fund cashiers to hold only the minimum amount of funds needed for immediate disbursement needs. Yet we noted that many fiscal offices maintained funds far exceeding their reasonable needs. Some examples follow:

--Rhein-Main Air Force Base in West Germany was authorized $267,000 in imprest funds. Our analysis showed that this amount was excessive and we were later informed that a $103,000 reduction in the fund level was approved by Air Force officials.

--The Environmental Protection Agency had six locations with excess imprest funds. At one fiscal office, a fund of $20,000 had about $6,000 more than the maximum amount allowed by Treasury regulations. Over 6 months the fund had about $10,000 to $15,000 on hand each time a reimbursement was sought. In addition, a field office of one of those fiscal offices had continued to maintain a $500 fund even after Treasury said the amount was excessive.

--The Department of Health and Human Services had one imprest fund that had an authorized balance of $20,000, although disbursements from the fund averaged only about $6,000 a month.

--A Pacific Fleet headquarters fund had a $1,000 balance when its expenditures were much less. The balance was later reduced to about $190.

The size of imprest funds should be limited both to minimize the amounts exposed to the risk of misuse or loss and to conform to sound cash management principles. The number of fiscal offices with excessive balances indicates this is a Government-wide problem.

CHAPTER 6

MORE EFFECTIVE USE OF INTERNAL AUDITORS

WOULD STRENGTHEN INTERNAL CONTROLS

In our view, adequate internal audit coverage could have detected most of the control deficiencies discussed in previous chapters, thus providing agency management with the opportunity to correct them. As we have reported earlier, Federal agencies' internal auditors spend only a small portion of their time evaluating financial controls. Also, agencies tend to react slowly to recommendations contained in internal auditors' reports.

EMPHASIS ON INTERNAL FINANCIAL OPERATIONS SHOULD BE INCREASED

As noted previously, we believe the prevalence of noted weaknesses is largely attributable to the absence of recent internal audit coverage. Federal agencies could substantially enhance their control over financial resources and operations if programs for periodic, cyclical reviews by internal auditors were established.

Internal audits are recognized as a part of an agency's system of financial controls. Under section 113 of the Accounting and Auditing Act of 1950, agency heads are required to establish accounting and internal controls, including internal audit. Since passage of that act we have issued guidance to Federal agencies on their internal audit activities. For example, we issued statements on the basic principles and concepts of internal audit in 1957, and updated them in 1968 and 1974. These statements stress the need for internal auditors to examine financial transactions to determine whether their agencies are (1) maintaining effective controls over assets, liabilities, revenues, and expenditures and (2) complying with applicable laws and regulations. In 1972 we issued a pamphlet, "Standards for Audit of Governmental Organizations, Programs, Activities, and Functions." Also, between 1976 and 1979, we issued nine reports discussing internal audit utilization by Federal agencies. In those reports we made recommendations for strengthening the internal audit function itself and for better utilization of internal audit capabilities.

The potential benefits from increased use of internal auditors are many. For example, internal auditors can provide the following services to agency management:

--Identify and bring to management's attention weaknesses in established procedures.

--Point out specific locations needing management's attention to ensure compliance with established procedures.

--Evaluate the design of accounting and control systems and recommend improvements.

--Provide guidance, advice, and technical assistance to offices being reviewed.

--Identify conditions allowing potential for fraud, waste, and abuse.

--Encourage agency operating units to conform to established procedures.

A primary reason that agencies have not realized these benefits is that many assign their internal auditors to perform program-type reviews and reviews of outside contractors and grantees at the expense of their own agency's financial auditing needs. On November 29, 1976, we reported that some Federal agencies spend a relatively small percentage of their efforts on internal financial matters. 1/ For example, we noted:

--At the Departments of Labor and Health and Human Services, internal audit staffs spent only about 20 percent of their audit time on the Departments' internal functions.

--At the Environmental Protection Agency, virtually all of the audit staff was occupied with external audits of construction and other grant programs.

Similarly, in a June 6, 1978, report we discussed a questionnaire survey on financial audits of operating units in cabinet-level departments and independent executive agencies, international organizations, Government corporations, and other committees, commissions, and boards. 2/ We analyzed responses from 489 such units and noted that 133--roughly one-third--said they did not receive an audit of their accounts and financial records during a 3-year period.

1/"An Overview of Federal Internal Audit" (FGMSD-76-50).

2/"Financial Audits in Federal Executive Branch Agencies" (FGMSD-78-36).

We believe Federal agencies' financial management would benefit from increased emphasis on internal reviews of financial operations. These reviews, however, can be worthwhile only if appropriate actions are taken when deficiencies requiring management's action are reported. As noted below, even though the majority of some agencies' audit efforts are devoted to external audits of contractors or grantees, management often does not act when its auditors do uncover findings involving substantial amounts.

FOLLOWUP ACTIONS ON FINDINGS REPORTED BY INTERNAL AUDITORS SHOULD BE STRENGTHENED

Our reviews noted several instances in which agencies' internal auditors reported findings involving hundreds of thousands of dollars in potential savings that management did not act upon. Failure to act on such findings results in losses to the Government and wastes the productive efforts of internal auditors.

One of our recent reports revealed that this type of problem exists Government-wide; millions of dollars in potential savings and collections are not being followed up. 1/ Among other conditions, the report noted that $4.3 billion in audit findings from nearly 14,000 audit reports at 34 agencies were unresolved, thus jeopardizing or delaying the collection of funds due the Government. We estimated that 80 percent of this amount could be collected with proper followup action by management.

The report contained many examples of potential recoveries and savings that were not acted on; to cite a few:

--Five years after Labor's auditors questioned the allowability of $3 million claimed by a contractor, program officials finally agreed with the auditors. Recovery will be difficult, if not impossible, because of the delay and because the agency no longer does business with the contractor.

--Labor administrators had not taken the necessary time to promptly collect $3 million overpaid to a contractor.

--Six months after sending the initial demand letter, a Housing and Urban Development administrator had taken no further action to collect $185,000 which auditors found a grantee owed the agency.

1/"More Effective Action Needed On Auditors' Findings--Millions Can Be Collected Or Saved" (FGMSD-79-3, Oct. 25, 1978).

--Two Environmental Protection Agency officials had cited the crush of other duties as the reason for not seeking resolution of two transactions--one involving $300,000 and the other, $90,000.

--Because of other duties, a Health and Human Services official had decided his staff did not have time to collect funds or correct a deficiency which had led to an earlier overpayment of $155,000.

--A Housing and Urban Development official said his staff would be too busy approving new housing projects for at least another year to collect $270,000 which auditors found the agency overpaid to grantees.

--A Commerce official failed to collect $45,000 overpaid to a contractor. He attributed the slow action to his limited attention to resolving audit findings and his heavy workload. For the same reason, he was not seeking resolution of another $40,000 in costs claimed by a contractor and questioned by auditors.

The same report contained a number of recommendations for insuring that auditors' findings are dealt with effectively. Implementation of these recommendations would result in (1) establishing accountability for the resolution of auditors' findings, (2) developing formal procedures for tracking actions to resolve findings, and (3) setting deadlines for corrective actions to be taken.

The types of deficiencies noted in our reviews indicate that agencies need to use internal auditors to a greater degree to review their own financial operations. Such reviews, however, will be of no value unless management also makes a commitment to act on findings resulting from them.

CHAPTER 7

CONCLUSIONS

Our 11 reviews of Federal agency fiscal offices showed widespread, similar, and prevalent financial control weaknesses. The fiscal operations reviewed represented a cross section of the major activities carried out by the Federal Government. The implications of this cause us to believe that similar problems exist throughout the Government.

In response to our reports, fiscal officials generally concurred with our conclusions and agreed to implement appropriate corrective actions. Such actions, however, will result in significant benefits only if implemented in all fiscal offices rather than just at the ones we reviewed. Additionally, experience has shown that constant vigilance by management is necessary to insure continued effective operation of internal controls. We therefore believe that stronger measures are needed to bring about lasting improvements.

On an individual basis, any one weakness at a single fiscal office would not be likely to have significant impact upon the Government's financial condition. In the aggregate, however, we believe such weaknesses are detrimental to the Government's overall financial operations and corrective actions must be taken to ensure that the systemwide deficiencies are corrected.

In most cases, such corrective actions would not involve appreciable increases in personnel or expenditures, and could be made relatively easily. In many cases, the agencies' own procedures manuals or regulations--implementing standards published by Treasury and GAO--specify the controls needed; but the controls had not been incorporated into fiscal offices' day-to-day operations.

Compliance with financial control requirements would be greatly aided by better utilization of Federal agencies' internal audit organizations. In earlier reports, we noted that Federal agencies do not effectively use their audit staffs to review their own financial operations. We believe that most of the weaknesses identified could have been readily detected and corrected had Federal managers made greater use of their internal audit staffs. Cyclical audit coverage not only identifies problem areas, but the knowledge that such audits will take place provides an incentive for operating personnel to conform to established procedures.

Although the cost of correcting the types of weaknesses noted is minimal, the cost of not correcting them can be significant. First, the direct costs--as illustrated in the examples cited throughout this report--are not individually large but are significant when projected Government-wide. Secondly, when these weaknesses result in inaccurate accounting records, erroneous financial statements are produced and financial decisions are based on the incorrect data. Inaccurate accounting data, along with other control deficiencies, can lead to the purchase of goods and services for which funds are not available or authorized. This is not only clearly illegal, as pointed out in chapter 5, but is an extremely poor business practice as well.

Finally, the failure to control accounts receivables, collections, and disbursements reduces funds otherwise available to the Government for operating agency programs. This reduced availability must be made up for by borrowing, which is becoming increasingly more expensive. Additional funds must be appropriated to pay such interest costs.

Our concern is shared by the Director, Office of Management and Budget. In his April 18, 1980, memorandum to the heads of departments and agencies, the Director discussed the need for adequate internal controls. (See app. II.) He pointed out that few agencies have comprehensive systems of internal control and that the controls required by existing systems may not be properly observed. The memorandum instructed the heads of departments and agencies to direct their personal attention to examining the adequacy of their organization's internal control systems. We agree with the need for such examinations and, accordingly, we are sending this report to the heads of Federal departments and agencies to assist them in undertaking this effort.

In our view, the Congress' oversight responsibility can be exercised to a greater and more effective degree by strengthening existing law. Consideration is currently being given in the Congress to legislation known as the Financial Integrity Act of 1980 (S-3026), which would require greater accountability by heads of Federal agencies for the effectiveness of their organizations' systems of internal financial control. This legislation would require agency heads to undertake annual evaluations of their organizations' internal control systems and report the results of such evaluations to the Congress and the President. GAO would participate in this process by providing guidance for conducting the examinations and by reviewing the results. We believe this legislation would contribute to the development of adequate internal control systems in the Federal Government.

RECOMMENDATION TO THE CONGRESS

We recommend that the Congress enact the legislation to place greater responsibility upon the heads of Federal agencies for the soundness of their organizations' systems of internal financial control.

APPENDIX I

CONSOLIDATED SUMMARY OF GAO'S OBSERVATIONS AT

157 FEDERAL DEPARTMENT AND AGENCY FISCAL OFFICES

	DEPARTMENT OR AGENCY											
	Justice (DEA)	Transportation (Coast Guard)	U.S. Army (Europe)	U.S. Air Force (MAC)	State Department (Europe)	HEW (Health Services Admin.)	Labor (ETA) (OASAM)	EPA	U.S. Pacific Fleet	HEW (FDA)	HUD	TOTAL FISCAL OFFICES
NUMBER OF OFFICES EXAMINED	14	11	7	12	9	19	20	13	21	19	12	157
CONTROL WEAKNESSES NOTED												
ACCOUNTS RECEIVABLE AND COLLECTIONS:												
Procedures to bill and record receivables not followed				2		5	12	10		1		30
Prompt and timely action not taken on delinquent receivables					4	5	5		4			18
Receivable aging schedules not prepared properly		5				12		11				28
Collections not recorded or logged in by mail clerk	10	5	7	1		9	12	10		9	3	66
Receipt documents not used or controlled	3	1		2	5	14	10	12			3	50
Lack of separation of duties				1	8	15	3	5	8		3	43
Collections not safeguarded as required						5	7	2	5	3	5	27
Procedures to deposit collections not followed	10			2	5	10	11	9	7	16	3	73
Travel advances not controlled or reviewed	3		1		5		4	3	5	4	7	32
(Subtotals)	(26)	(11)	(8)	(8)	(27)	(75)	(64)	(62)	(29)	(33)	(24)	(367)
DISBURSEMENTS:												
Invoices not paid in accordance with due dates or cash discounts			7			10		8				25
Lost discounts not explained in writing	6	3		2	2	12	5	10		9	6	55
Vouchers and invoices are not adequately supported or reviewed						2	4	5	2	9	1	23
Disbursements made in excess of approved limit or authorization					8							8
GTR's not safeguarded or properly accounted for							5	4				9
(Subtotals)	(6)	(3)	(7)	(2)	(10)	(24)	(14)	(27)	(2)	(18)	(7)	(120)
OBLIGATIONS:												
Estimates of obligations not adequately supported	6	1	2	10		11	5	11		4	5	55
Obligations not recorded or reviewed properly						3	4	4		2		13
Funds not certified before obligations incurred					5							5
(Subtotals)	(6)	(1)	(2)	(10)	(5)	(14)	(9)	(15)	(0)	(6)	(5)	(73)
IMPREST FUNDS:												
Unannounced audits and cash verifications not performed					9	7	4	4		12	4	40
Imprest funds used improperly						2		4			4	10
Funds commingled or shared with other cashiers		1				7	3	3		9	8	31
Fund procedures not reviewed or followed by cashiers				1	8	10		3	5		2	29
Safe combinations not changed annually or not accessible		3	2		6	14	3	8		14	12	62
Fund levels exceed their required need				3	3	1		6	14			27
Duties of cashiers not separated	8											8
Alternate cashiers not appointed		4								1		5
(Subtotals)	(8)	(8)	(2)	(4)	(26)	(41)	(10)	(28)	(19)	(36)	(30)	(212)
GRAND TOTALS	(46)	(23)	(19)	(24)	(68)	(154)	(97)	(132)	(50)	(93)	(66)	(772)

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

APR 18 1980

MEMORANDUM FOR HEADS OF SELECTED DEPARTMENTS AND AGENCIES

SUBJECT: Improving Internal Controls

Last May we launched the Financial Priorities Program to resolve major weaknesses in agency systems of financial management and control.

One of the issues addressed by the program was Internal Control. Our objective was to upgrade internal control systems to reduce the risk of fraud, abuse, waste, and inefficiency. Some progress has been made. For example, using the authority of the Antideficiency Act, we called upon the major departments and agencies to upgrade their fund control systems, and submit them for our approval. Thus far, 20 such systems have been approved, and a number of additional approvals are expected shortly.

In addition, the new Offices of Inspector General in fifteen departments and agencies have increased the awareness of top management to internal control issues. Several of the Inspectors General made recommendations for improving internal controls in their semiannual reports to the Congress. But audit and investigation cannot, by themselves, resolve these problems.

Much more needs to be done by program and policy managers to meet their responsibilities for assuring the adequacy of internal control systems. Recent Congressional testimony indicates that an astonishing total of 130,000 cases of alleged fraud and related illegal acts have been found in 21 major departments and agencies over a two-and-a-half-year period. Individual losses range from under $100 to over $1 million. The fact that most of this information comes from field offices, with little awareness of these problems in Washington, indicates weakness in policy level oversight.

Our own review of reports submitted under Bulletin 80-1, "Information on improvements in financial systems," shows that very few agencies have comprehensive systems of internal control. Moreover, the controls required by existing systems may not be properly observed. In light of the President's proposals for increased budget discipline, developing better controls to get the most out of Federal spending is essential.

Accordingly, we urge you to direct your personal attention to examining the adequacy of your internal control systems. We will help by developing uniform guidelines to insure that comprehensive, systematic internal controls are established and followed in every agency. We are working closely with the Comptroller General in this. Also, we are creating a task force to assist us on a part-time basis. Please provide the name of a candidate for the task force from your agency to John Lordan, Chief, Financial Management Branch, (395-6823) by May 15, 1980.

James T. McIntyre, Jr.
James T. McIntyre, Jr.
Director

(905017)

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