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

GENERAL GOVERNMENT
DIVISION

MARCH 25, 1981

B-202562

The Honorable William F. Bolger
Postmaster General



Dear Mr. Bolger:

Subject: Need For Improved Control Over Local
Purchases of Parts, Supplies, and
Services at Post Offices (GGD-81-58)

On July 30, 1980, we issued a report to the Congress on the United States Postal Service's controls over gasoline and diesel fuel. During our review of the Service's fuel controls, we also examined the controls over parts, supplies, and services purchased by local postal facilities. Our work was prompted by the increased interest in preventing fraud, abuse, and waste in the Federal Government as expressed by the Congress in passing the Inspector General Act of 1978.

We concluded that more could and should be done to strengthen control over purchases by local facilities to prevent potential losses from fraud, abuse, and waste. We could not, however, determine whether there have been losses resulting from weak controls because of the incomplete audit trail left by the record-keeping method the Service uses. Nevertheless, we believe you should be made aware of our findings, which are detailed in the enclosure. The enclosure also describes corrective actions planned by the Service, including those resulting from discussions of our findings. Properly implemented, these actions should provide the Service with stronger controls.

Our principal finding was that contrary to good internal control techniques calling for the separation of procurement-related duties, not all critical duties were separated at the postal facilities we visited. Separation of duties is usually not feasible at small facilities, but it should be possible at the Postal Service's 500 or so large facilities (mail processing centers and vehicle maintenance facilities) where the annual obligation authority for supplies and services ranges from \$100,000 to \$400,000 per facility. Even at these facilities, however, we found single employees performing many procurement-related duties, i.e., determining need, ordering, receiving, and, in some instances, certifying invoices for payment.

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Compounding the separation-of-duties weakness is an unreliable inventory control system. A reliable inventory system is needed to enable the Service to insure that all parts and supplies received are properly accounted for. The Service cannot rely on its inventory control systems, because they are maintained in the storerooms by the same employees who are authorized to determine needs, order and receive parts and supplies, certify invoices for payment and also dispense parts and supplies. In addition, storeroom employees are permitted to make adjustments to the inventory records to show the availability of supplies without providing management an explanation of differences between recorded and actual counts.

At nearly all postal facilities we visited, one procurement function--the payment of invoices--was performed separately from other procurement functions. Payments, however, were based on certifications that supplies and services were received, although the certifying employee rarely saw the items and often did not obtain documentation signed by employees who actually received the supplies or services.

In discussing our findings with Service management officials, we were advised that increased emphasis will be placed on controlling parts, supplies, and services obtained for use in postal operations. To this end, officials directly responsible for developing stockroom inventory controls will review and make necessary changes to fleet maintenance, plant maintenance, and supply management manuals to provide better guidance on safeguarding the Service's property. In addition, the Senior Assistant Postmaster General, Operations Group, will reproduce this report and distribute it to appropriate field managers with instructions to correct and strengthen any procedures which fail to provide for adequate control. These actions should go a long way toward improving controls over parts, supplies, and services.

Other actions which were not prompted by our review are being taken to provide the Service with stronger management controls. These actions include

- testing a computerized inventory control system for vehicle parts and supplies to replace the manual system maintained by vehicle maintenance facility storekeepers,
- using a stratified inventory sampling technique for plant maintenance operations to quickly identify stock shortages, and

--a strengthening of followup procedures by the
Postal Inspection Service.

We appreciate the cooperation and courtesies extended
to our representatives during the course of their work.

Sincerely yours,

W. J. Anderson

William J. Anderson
Director

Enclosure

Postal Service Parts, Supplies, And
Service Activities Are Susceptible
To Fraud, Abuse, And Waste

In fiscal year 1980 the Postal Service spent about \$300 million for parts, supplies, and services to keep the mail moving. This amount consisted of about \$93 million for general office supplies and services; \$54 million for parts and services to maintain buildings and sophisticated mail sorting equipment; \$34 million for parts to maintain approximately 125,000 vehicles; \$100 million for gasoline and diesel fuel; and about \$15 million for miscellaneous items such as materials for repairing mailbags.

Postal facilities of all sizes procure supplies and services. Expenditures for supplies and services for large facilities are quite high. Some management sectional centers with their associate offices spend in excess of \$1 million a year.

Supplies and services are obtained in a variety of ways. Two area supply centers are a prime source of supplies unique to the Postal Service. Most postal facilities east of the Mississippi River obtain such supplies from Somerville, New Jersey; and all facilities west of the Mississippi use the supply center in Topeka, Kansas. Topeka is also the supply center for all spare parts for equipment and vehicles. For those supplies unique to the Service, facilities usually submit requisitions to the supply centers quarterly, while requisitions for spare parts are made on an as needed basis. In fiscal year 1978 postal facilities requisitioned about \$30 million in supplies and parts from the supply centers. Office supplies are obtained from General Services Administration (GSA) supply centers and stores as well as from private vendors. In 1978 the Postal Service obtained about \$20 million in supplies from GSA.

In 1978 postal facilities purchased parts, supplies, and services valued at about \$150 million directly from vendors. Some of these purchases were made by procurement service

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offices 1/ and regional offices, but local postal facilities also determined their needs and received purchased parts, supplies, and services directly from vendors. Purchases are paid for with (1) checks issued by one of the Service's four data centers, (2) postal money orders issued by the local postal facilities, or (3) cash. Blanket purchase agreements are often used for those vendors from which frequent purchases are made.

Purchases are not limited to local vendors. Many of the supplies are obtained from mail order outlets. One such mail order firm, for example, estimated that its business with numerous postal facilities around the Nation amounts to about \$1.2 million a year.

PRINCIPLES OF GOOD INTERNAL CONTROL
OVER SUPPLIES AND SERVICES

Internal controls are the plan of an organization and all the attendant methods and measures adopted to

- promote efficiency and economy of operations;
- restrict obligations and costs, consistent with efficiently and effectively carrying out the purposes for which the agency exists, within the limits of appropriations and other authorizations and restrictions;
- safeguard assets against waste, loss, and improper or unwarranted use;
- insure that all revenues applicable to agency assets or operations are collected and properly accounted for; and
- assure the accuracy and reliability of financial, statistical, and other reports.

1/A procurement service office performs the contracting activities for local postal facilities if the procurement exceeds \$750.

Much has been written about the principles of internal control and specifically about internal controls over assets, including supplies. The Institute of Internal Auditors in its publication "Internal Control Against Fraud and Abuse" states that the requirements for effective internal control over assets are simple. They include

- insuring that what is paid for has been received,
- providing adequate storage facilities and qualified personnel,
- requiring adequate approval for withdrawals for use, and
- testing that records are accurate through periodic physical inventories.

Perhaps the key technique for providing adequate internal control is through the separation of employees' duties. GAO's Policy and Procedures Manual for Guidance of Federal Agencies states that responsibility for assigned duties and functions should be appropriately segregated. Specifically, responsibilities for authorization, performance, keeping of records, custody of resources, and review should be segregated. Such segregation provides proper internal checks of performance and minimizes opportunities for carrying out unauthorized, fraudulent, or otherwise irregular acts.

The Institute of Internal Auditors publication discusses each of the functions essential for good internal control. It states that the receiving operation should be established as a separate function, detached organizationally from both the purchasing and the consuming responsibility. Supplies should be (1) locked in a storeroom so that only the storeroom staff have access and (2) issued only when authorized by a requisition.

Another critical internal control function is a perpetual inventory system. The Institute of Internal Auditors states that it is a "must" that the perpetual inventory system be maintained outside the storeroom if control is to be effective.

No internal control system can totally eliminate the possibility of fraud, abuse, and waste. The basic ingredient of a good internal control system--separation of duties--can be circumvented by collusion. Therefore, it is important that consideration be given to all aspects of internal control. Price

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Waterhouse and Co., in its publication on enhancing government accountability, points out that an environment having appropriate awareness and discipline about control procedures is important to assure that such procedures will not be overridden.

OBJECTIVE, SCOPE, AND METHODOLOGY

Important as detection of fraud, abuse, and waste is, detection was not our primary concern during this review. Rather, our objective was to evaluate the Postal Service's control systems for preventing fraud, abuse, and waste.

We concentrated on determining how postal facilities obtain, maintain, and dispense parts and supplies and obtain and use services at management sectional centers, local post offices, and vehicle maintenance facilities. In conducting our review we

- examined the Service's control system policies, procedures, reports, and studies;
- gathered operational data and observed operations at several postal facilities--the primary ones were management sectional centers and vehicle maintenance facilities located in or near Merrifield, Virginia; Prince Georges County, Maryland; Kansas City, Missouri; Dallas, Texas; and San Francisco, California; and
- discussed the Service's control system with district, regional, and headquarters officials.

POSTAL SERVICE SHOULD TIGHTEN INTERNAL CONTROLS OVER PARTS, SUPPLIES, AND SERVICES

Good internal control techniques are not always followed at large local postal facilities (annually obligating between \$100,000 and \$400,000 each) to control the procurement of goods and services and the maintaining or dispensing of supplies.

Specifically we found

- minimal separation of duties among those performing the procurement and storeroom functions,
- inventory systems that did not provide adequate control over supply items, and
- payments made without verification that supplies and services were received.

Minimal segregation of procurement-related duties limits ability to detect fraud, abuse, and waste

Good internal control procedures provide for separation of responsibilities among those determining needs, ordering, receiving, posting to inventories, and making payments for supplies and services. We found that this separation of duties was lacking in the supplies and services activities in the management sectional centers and vehicle maintenance facilities we visited.

Separate storerooms are kept for parts and supplies required for (1) general operations, (2) plant maintenance, and (3) vehicle maintenance. General operating supplies and services include such items as paper, pens, and typewriter repairs. Plant maintenance supplies and services include such things as parts to repair mail-sorting equipment; tools; and lumber, nails, and paint for making building repairs or modifications. Vehicle maintenance supplies include such items as repair parts, tires, and batteries.

The Service's accounting system does not distinguish between the cost of supplies and services for operations and plant maintenance. Most of the \$100,000 to \$300,000 spent annually for supplies and services at the six management sectional centers we visited was for plant maintenance rather than general operations. Each of the six vehicle maintenance facilities we visited spent between \$200,000 and \$400,000 annually for parts, supplies, and services.

The Postal Service's supply management manual delineating the responsibilities in each of the three storerooms does not provide for adequate segregation of duties. The manual states the storekeeper is responsible for

- ordering parts or supplies from supply centers, GSA, or local sources;
- receiving parts or supplies;
- issuing parts or supplies;
- inventory control;
- care and preservation of parts and supplies; and
- maintaining good housekeeping practices.

Although the manual makes no distinction between sizes of operations or the amount of funds being spent by the facility, it states that the facility manager still has final responsibility for supply management.

With one exception, the management of facilities we visited permitted the same employees to perform numerous duties, including ordering, receiving, storing, issuing, and inventory control functions. The exception--Kansas City, Missouri, Management Sectional Center--did not have an ideal situation, but it was better than the other facilities in separating employee duties. The Kansas City facility had a separate procurement section which made purchases for the plant maintenance and operations storeroom and paid invoices on the basis of receipt documents. The system was still weak, however, because on occasion, employees of the separate procurement office performed work in the storeroom, such as receiving supplies, then returned to the procurement office and made payments. In addition, the storekeepers received and issued supply items and kept the perpetual inventory system.

The supply practices at the Dallas Vehicle Maintenance Facility typify the lack of separation of duties we found at the facilities we visited. The storekeeper had been given authority to order all parts and supplies necessary to repair postal vehicles, including such items as tires, batteries, and tune-up parts. In total, these repair parts cost \$400,000 in 1978. He also had been given authority to receive, store, and issue parts, keep records of purchases, maintain perpetual inventory records, conduct inventories, and make necessary adjustments to perpetual inventory records. The storekeeper in the Dallas Vehicle Maintenance Facility also certified invoices for payment.

Sometimes other storeroom employees at the Dallas Vehicle Maintenance Facility helped the storekeeper with his responsibilities, and any of them could perform any and all of the duties. In many instances different employees performed different functions, but often the same employee performed two or more of the functions. For example, for 138 purchases made under blanket purchase agreements during a 1-month period, the same person

- received and certified for payment 78 of the purchases,
- posted 47 of the 78 purchases to the inventory records, and
- recorded 27 of the 78 purchases on the controlling call register (a document which consolidates purchases made under blanket purchase agreements so that the postal payment centers can issue one check to the vendor).

The Shawnee Mission, Missouri, Vehicle Maintenance Facility is another example of the lack of separation of duties. The facility spent about \$150,000 annually for supplies and services, including gasoline. About 70 percent of the funds were under the control of the administrative clerk. The clerk's administrative responsibilities included

- determining needs for parts and services,
- ordering items,
- receiving items,
- issuing parts out of the storeroom,
- maintaining the perpetual inventory system,
- maintaining records of purchases made or being made, and
- certifying purchases for payment.

The Prince Georges County, Maryland, Vehicle Maintenance Facility was similar to the others in that one person could perform all functions. One difference, however, was that at the time of our review a signature stamp of the vehicle maintenance facility manager was being used rather than an actual signature for certifying that invoices were proper for payment. The manager kept the signature stamp but his assistant also had access to it in the manager's absence. We were assured that other employees were not using the stamp, but this could not be verified. During our review, this practice was changed and the manager began signing the certifications as required.

We found a different twist to the separation-of-duties problem at an associate office of the Prince Georges County Management Sectional Center. A part-time clerk ordered and had full control over annual purchases of about \$110,000 worth of supplies obtained from GSA. For years, the part-time clerk had been ordering supply items using Standard Form 344 by signing for the postmaster and without review by any other postal official. The clerk received most shipments and was responsible for stock control. He did not maintain an inventory system (postal regulations do not require a system at associate offices) and could not estimate how much stock was available or how long the stock had been on hand.

With no guidance or control, this employee could purchase whatever he wanted and was not accountable to anyone for his actions. Postal regulations limit Standard Form 344 purchases to supply items. However, some of the items the clerk obtained from

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GSA using Standard Form 344 were accountable property, such as a \$1,300 set of tools, file cabinets, desks, and chairs. Per employee, this associate office spent twice as much for supplies as any other associate office in the surrounding area.

Inventory system ineffective
for internal control purposes

A good inventory control system could provide the Postal Service with accountability for the supplies it purchases to insure that all supplies received are available for postal operations. The Service cannot rely on its inventory systems for the operations, plant maintenance, and vehicle maintenance storerooms to provide adequate control because

- the perpetual inventory systems are maintained in the storerooms by parts and supplies clerks, thereby circumventing the control features of a perpetual inventory system; and
- inventory adjustments are made only to show the availability of supplies without providing management with an explanation of differences between the records and actual counts.

The perpetual inventory records for operations and plant and vehicle maintenance are kept by storeroom employees, which makes the perpetual inventory system ineffective as an internal control technique. Ideally, perpetual inventory systems should provide an independent check of stock levels. Therefore, the records should be kept outside the storeroom. All receipts should be entered into the system from receipt documents signed for by storeroom employees. Issues from the storerooms should be entered into the system from requisitions or work orders. With such a system, a determination can be made at any time as to what supplies are supposed to be available in the storeroom and shortages shown by physical inventories can be investigated. Likewise, auditors could identify potential fraud and abuse by independently taking physical inventories. The Service's present system does not provide these control features.

Plant maintenance storerooms in the 115 largest postal facilities are tied into a nationwide computer system known as the National Maintenance Information and Control System (NMICS). Under NMICS, all data is entered by storekeepers. The system produces information on the nature and extent of maintenance problems in mail processing centers and provides information on stock items received and issued. NMICS provides an added dimension to manual inventory control systems as it is preprogrammed for acceptable stock levels so that when stock levels reach a certain point, they are automatically reordered from the supply center.

Plant maintenance storerooms not tied to NMICS and all vehicle maintenance and operation storerooms maintain manual inventory systems which provide information on stock items received and issued. Under these systems, storeroom clerks are responsible for maintaining sufficient stock levels to meet the facilities' needs.

At all facilities we visited, the inventory systems were in place as prescribed by Postal Service manuals. Storekeepers received and issued stock and also maintained the perpetual inventory records. Losses have been identified at these facilities, but because of the Service's recordkeeping practices, the extent of losses could not be determined. Whether the losses resulted from recordkeeping errors or theft also could not be determined.

In July 1977, the Postal Inspection Service issued a report on its review of the inventory practices of the Merrifield, Virginia, plant maintenance operation. The review identified shortages of between \$35,000 and \$55,000, or between 15 and 23 percent of the value of the inventory. The Inspection Service recommended a complete inventory be initiated to reconcile the inventory listing and to insure the records reflect the actual balances on hand. Management of the sectional center agreed with the Inspection Service's conclusions that a lack of aggressive supervision and a failure to establish proper internal controls were the causes of the shortages. It agreed to complete an inventory of the stock items before the end of Summer 1977. Management also agreed to have maintenance operations personnel strictly adhere to procedures for the control of parts and tools. (The procedures require storeroom employees to conduct daily inventories to correct the records for shortages and overages as they occur.)

About 1 year after this report was issued, the Inspection Service began a second review of the inventory control practices at Merrifield as part of a review of all NMICS offices in the Eastern Region. The report, issued in December 1978, stated that the Merrifield storeroom had shortages of about \$45,000, or about 19 percent of the total value of the inventory. The reported causes of the shortages were the failure of storeroom employees to enter and remove information from NMICS as transactions occurred and the failure to enter accurate data into NMICS.

Similarly, the Inspection Service reported in May 1978 that the Prince Georges County, Maryland, Vehicle Maintenance Facility had shortages of \$5,773, or 20 percent of the book value of the inventory. This was offset somewhat by a \$1,572 overage, but the Inspection Service was still highly critical of the operation, noting that adjustments had been made to inventory records just 6 months earlier and that all stock records were correct at that time.

At each of the facilities we visited, adjustments were being made to the inventory records by storeroom employees on the basis of physical count of stock items. The following explanations for adjustments made to inventory records at the Dallas Vehicle Maintenance Facility provide some insight about the nature of the adjustments.

--Storeroom employees remembered transactions they failed to record earlier.

--Entries were made to the wrong stock cards.

--Storeroom employees did not believe the parts recorded on the work order adequately reflected the parts actually obtained from the stockroom.

Such adjustments are to be reported to management, but this was not always done.

Keeping inventory records in the storerooms defeats the intended control features of a perpetual inventory system because the records are maintained by the personnel accountable for the supplies. Accountability for parts and supplies is lacking in the Service's system, and alteration of the records to avoid detection of losses or theft is a strong possibility. This situation, however, must be balanced against the cost of providing ideal internal control features.

Payments made without verification
that supplies or services were received

Payments were made for supplies and services on the basis of employees' certification of receipt even though the certifying employee often had no assurance that the items were, in fact, received. This practice does not represent good internal control. An acceptable internal control system would provide that payments for parts, supplies, and services be based on the signature of the employee who personally verified receipt.

Postal Service regulations on receiving parts, supplies, and services vary depending on whether the receipt is for operating; plant maintenance; or vehicle maintenance parts, supplies, and services. The Service's supply management manual states that acceptance of operating supplies and services should be supported by a signed receiving document. The manual does not discuss procedures for receipt of parts, supplies, and services for plant and vehicle maintenance. Headquarters officials, however, stated that receiving requirements for operating supplies and services apply to the other storeroom activities.

The plant maintenance manual for facilities operating under NMICS states that whenever an order is received, the stock clerk will make appropriate entries on Form 4801 (Parts/Supplies Receipt) used for entry into NMICS. The receiving employee is not required to sign the receiving document used as a basis for payment. Postal facilities which do not have NMICS operate under a different plant maintenance manual, but again this manual has no requirement that receiving documents be signed by the employee who verifies receipt of the order.

Regulations for receipt of parts, supplies, and services in vehicle maintenance facilities are similar to those for plant maintenance operations which are not under NMICS. There is no requirement that employees who verify receipt of parts, supplies, and services sign a receiving document.

Nearly all payments to vendors are made by the administrative services sections of management sectional centers or one of the Service's four data centers. The documents used as a basis for these payments are vendors' invoices certified by a postal employee stating "I certify that the goods and services shown on this invoice have been received and that this invoice is proper for payment." We found, however, that often the employees certifying the invoices were not the same employees who received the supplies or services and often had no assurance that the items were received.

Employees who actually receive supplies and services for plant maintenance and vehicle maintenance storerooms do not always sign the receiving document because there are no requirements to that effect. Payments made by the Dallas Management Sectional Center provide a good example of this. We reviewed 92 payments made over a 4-week period and found that 28 invoices (30 percent) were certified for payment without supporting documentation showing that the billed items were actually received. Similarly, of 270 payments made for purchases by the San Francisco Management Sectional Center during a 4-week period, 101 (37 percent) were made without supporting documentation evidencing receipt.

INTERNAL AUDITS ALSO IDENTIFIED
CONTROL WEAKNESSES

Procurement and supply operations of postal facilities are periodically reviewed by management review teams and the Postal Inspection Service. These reviews consist of onsite evaluations of the facilities' compliance with prescribed regulations, as well as assessments of internal controls. The results of these reviews are reported to management sectional center managers and district managers with summaries being supplied to regional and headquarters officials.

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Information furnished to us by the Inspection Service showed that its audits frequently identify internal control problems. For example, the Inspection Service reported that in 52 percent of the 65 vehicle maintenance facility audits it performed in fiscal year 1980, inadequate stockroom and tool controls were identified as problems. Similar problems at vehicle maintenance facility were reported by the Inspection Service in summary reports as far back as 1976 and 1977.

CONCLUSIONS

Local postal facilities' procurement, receipt, and use of parts and supplies should be better controlled. Contrary to good internal control techniques, the Postal Service does not require separation of duties at local postal facilities where most supplies and services are obtained and used. Hence, a single employee at any given facility may perform several or all procurement-related duties, i.e., determining need, ordering, receiving, and, in many instances, certifying invoices for payment.

Compounding the inadequate separation of duties is an unreliable inventory control system. A reliable inventory control system would provide the Service with accountability for parts and supplies it purchases to better insure that all parts and supplies are received and used for postal operations. The Service cannot rely on its inventory systems to provide internal control, because the perpetual inventory systems for operations, vehicle maintenance, and plant maintenance are maintained in storerooms by the same employees who are authorized to determine needs, order and receive parts and supplies, certify invoices for payment, and also issue supplies. In addition, inventory adjustments made to reflect the availability of parts and supplies are not always reported to management, which allows inventory shortages to go unexplained.

At nearly all postal facilities we visited, one procurement function--the payment of invoices--was maintained separately from other procurement functions. Payments, however, were based on certifications that parts, supplies, and services were received, although the certifying employees rarely saw the items and often saw no documentation signed by the employee receiving the parts, supplies, or services.

POSTAL SERVICE ACTIONS
AND OUR EVALUATION

Postal Service officials plan to take the following actions to strengthen the Service's control over parts, supplies, and services:

- Appropriate fleet management and plant maintenance manuals will be reviewed and revised, where necessary, to insure proper and complete reference to control features contained in the Administrative Support Manual, Supply Handbook, and Fiscal Handbook. These references should provide guidance to the users of the manuals so that proper controls are maintained to safeguard the Service's property.
- Revision of the Supply Handbook to clearly delineate the procedures for receipt of parts, supplies, and services.
- Distribution of this report to field managers with instructions to correct and strengthen any procedures which fail to provide for adequate control.

These actions should go a long way toward improving controls over parts, supplies, and services. Other actions underway which were not prompted by our review include

- testing a computerized inventory control system for vehicle parts and supplies to replace the manual system maintained by vehicle maintenance facility storekeepers,
- a stratified inventory sampling technique for plant maintenance operations to quickly identify stock shortages, and
- a strengthening of followup procedures by the Postal Inspection Service.

These additional actions, if properly implemented, should provide the Service with stronger controls.