



AUG 27 1996

Memorandum

Date

June Gibbs Brown

From

Inspector General

Subject

Report on the ~~Audit~~ of the Public Health Service, Service and Supply Fund for
Fiscal Year 1995 (A-17-95-00053)

To

Philip R. Lee, M.D.
Assistant Secretary for Health

The attached report presents the results of audit by the certified public accounting firm Clifton, Gunderson and Company (CG) in its examination of the Public Health Service, Service and Supply Fund (Fund) financial statements for the fiscal years (FY) ended September 30, 1995 and 1994. The Office of Inspector General exercised technical oversight and quality control of the audit.

We engaged CG to audit the financial statements and to express an opinion on them. The firm issued a "qualified" opinion on the Fund financial statements because of the omission of (1) a statement of cash flows; and (2) a statement of budget and actual expenses. These statements were omitted because the Office of Management and Budget (OMB) granted a governmentwide waiver for presenting them. The waiver, however, does not take precedence over the basic requirement (specified in OMB Bulletin 94-01 and mandated by Government Auditing Standards issued by the Comptroller General) that agencies include these among 'their financial statements. Accordingly, CG determined that except for the omission of the cash flow and budget statements, the financial statements present fairly, in all material respects, the financial position of the Fund as of September 30, 1995 and 1994.

As part of the audit engagement, CG also rendered separate reports on internal controls and on compliance with laws and regulations. In the report on internal controls CG noted three reportable conditions (none of them a material weakness):

(1) understatement of liabilities in the amounts of \$479 thousand (FY 94) and \$1.8 million (FY 95); (2) adjustments to revenue, receivable, and related accounts totaling \$16.3 million; and (3) improvements needed in security access to computer systems data. In the report on compliance with laws and regulations, CG noted no instances of noncompliance required to be reported under Government Auditing Standards.

Managers of the Fund adjusted the liability, receivable, and revenue accounts in preparation of the FY 94 and FY 95 financial statements, and concurred with other recommendations made by CG designed to strengthen internal controls.

Page 2- Philip R. Lee, M.D.

In our oversight of the audit, we found nothing to indicate that CG'S work is inappropriate or that CG'S reports cannot be relied upon.

We would appreciate being advised within 60 days on the status of corrective actions. Should you wish to discuss the report, please call me or have your staff contact Joseph E. Vengrin, Assistant Inspector General for Audit Operations and Financial Statement Activities, at (202) 619-1157. Please refer to the Common Identification Number A-17-95-00053 in all correspondence relating to this report.

Attachment

Department of Health and Human Services

**OFFICE OF
INSPECTOR GENERAL**

**REPORT ON THE AUDIT OF THE
PUBLIC HEALTH SERVICE,
SERVICE AND SUPPLY FUND
FOR FISCAL YEAR 1995**



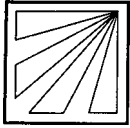
**JUNE GIBBS BROWN
Inspector General**

**AUGUST 1996
A-17-95-00053**

**PUBLIC HEALTH
SERVICE, SERVICE
AND SUPPLY FUND**

**INDEPENDENT
AUDITOR'S REPORT
AND
FINANCIAL
STATEMENTS**

September 30,
1995 and 1994



**Clifton
Gunderson I.L.C.**
Certified Public Accountants & Consultants

To the Office of Inspector General
of the Department of Health and Human
Services and the Board of Governors of
the Public Health Service

Independent Auditor's Report

Executive Summary

We **have** audited the accompanying statements of financial position of the Public Health Service, Service and Supply Fund (the Fund), **a** filed within the Department of Health and Human Services, and **the** related statements of operations and changes in net position (the "Principal Financial **Statements**") **as of** and for the years ended September 30, 1995 and 1994. Our audits were **performed in accordance with** generally accepted auditing **standards; Government Auditing Standards**, issued by the Comptroller **General; and** Office of Management and Budget (OMB) Bulletin 93-06, "Audit Requirements for Federal Financial Statements" and included related tests of the financial **reporting**, internal control **structure** policies and procedures, and of compliance with laws **and regulations**. **Our report on the financial** statements and our reports and findings regarding the **internal** control structure and compliance **with** laws and regulations follow this **summary**. This report also includes a description of management's responsibilities, of our responsibilities under the above standards and guidance, **and** of our methodologies for **fulfilling** these responsibilities.

In summary, we found:

- o The Fund's statements of financial position as of September 30, 1995 and 1994 and the related statements of operations and changes in net position for the years then ended were presented **fairly**, in all material respects, in **conformity** with the basis of accounting described in the Summary of Significant Account Policies accompanying the financial statements.
- o No material internal control weaknesses; however, we noted three reportable conditions described later in this report;
- o No material noncompliance with the selected provisions of applicable laws and regulations tested; and
- o No material conflicts **with** management's report on internal controls prepared under the Federal Managers' Financial Integrity Act of 1982.

Report on Principal Financial Statements

As required by OMB Bulletin 94-01, the Summary of **Significant** Accounting Policies accompanying the **financial** statements describes the accounting policies used by the Fund to prepare the financial statements. These policies comprise a comprehensive basis of accounting other than generally accepted accounting principles. Management of the Fund has received a waiver **from** OMB of the requirement to present a statement of cash flows and a statement of budget and actual expenses for the years ended September 30, 1995 and 1994. Accordingly, statements of cash flows and budget and actual expenses for the years ended September 30, 1995 and 1994 are not presented, in these financial statements. Presentation of such statements **summarizing** the operating, investing, and financing activities and budget and actual expenses is required by **OMB** 94-01.

In our **opinion**, except that the **omission** of these statements of cash flows and of budget and actual **expenses results** in incomplete presentations **as** explained in the first **paragraph**, the financial statements referred to above present **fairly, in all** material respects, the financial position of **the** Public Health Service, Service and Supply Fund as of September 30, 1995 and 1994, and the results of its operations for the years ended September 30, 1995 and 1994, in **conformity** with the basis of accounting described in the Summary of Significant Accounting Policies **accompanying** the financial statements.

The financial **information** presented in the accompanying Public Health Service **Introduction**, Overview and Discussion and Analysis: PHS Service and Supply Fund is supplemental **information** required by OMB Bulletin 94-01 and is not a required part of the basic **financial** statements. This information **has** not been subjected to **the auditing** procedures applied **in** the audit of the financial statements and, accordingly, we express no opinion on such information.

Report on Internal Controls

We noted two matters involving the financial reporting internal control structure and its operation that we consider to be reportable conditions under standards established by the American Institute of **Certified** Public Accountants and OMB Bulletin 93-06. We have summarized these reportable conditions below. We believe that these reportable **conditions** are not material weaknesses. We also noted certain minor matters involving the financial reporting internal control structure and its operation that we reported to management of the Fund in a separate letter dated April 30, 1996.

The audit **performed** for the year ended September 30, 1994 reported one **finding** relating to accrued liabilities that was a reportable **condition**. This **condition** has not been resolved and is repeated below.

ACCRUED LIABILITIES

We have continued to note several instances where goods or **services** received as of the end of the year are not being properly accrued in appropriate fiscal year. The following table summarizes the errors noted in accounts payable at September 30, 1995 and 1994:

	<u>1995</u>	<u>1994</u>
Underaccrual for goods and services received	\$2,390,994	\$1,243,000
Overaccrual for goods and services received	<u>(605,399)</u>	<u>(764,000)</u>
Net understatement of accounts payable	<u>\$ 1,785,595</u>	<u>\$ 479,000</u>

The financial statements, provided to us by the Fund's management, have been adjusted as of September 30, 1995 and 1994.

We were informed that many items comprising the net understatement noted above relate to situations where the goods or services relate to a contract that had been **obligated**, but not accrued. Goods or services received under these arrangements are not expensed in the accounting system until paid.

Recommendations

Even though improvement was noted in 1995, we continue to recommend the following:

1. The obligation of the contract under which the invoices are received should have no effect on the timing of recording the liability for CFO financial statement purposes. We recommend that the premise and rationale for the accrual of expenses be emphasized to those assisting in the gathering of information for the close of the **accounting** records. This is especially important at the end of the fiscal year. The distinction between accrual basis accounting and **obligation/budget** accounting must be emphasized. In **addition**, the finance division should solicit input from the various branches to assist them in making year-end accruals.
2. Expenses should only be accrued when the goods or services are received. If certain object codes require automatic accrual for budgetary purposes, these accruals should be reviewed periodically and **especially** at year end to adjust for CFO financial statement purposes.

Auditee Response

1. Division of Fiscal **Services (DFS)** will again include in their year-end closing instructions a request for receiving documents for **all** services provided during the last month of the fiscal year. These receiving documents will be used as the source documents for year-end

accruals. Invoices received at DFS before fiscal year end, which **are** due for payment after the fiscal year ends, will be reviewed for accrual activity as well.

2. DFS will again review the Telecommunications Improvement **Project** Contract at the year end to see if any finds have been obligated/accrued for a **service** period after the appropriate year end. If this exists, an adjusting journal voucher will be prepared for financial statement purposes only to reduce the amount of the accrual.

ACCOUNTS RECEIVABLE/REVENUE - ACCOUNT REVIEW, ANALYSIS AND RECONCILIATION

Accounts **receivable/revenue** required ten adjusting **journal entries** for **the** year ended September 30, 1995. Most of these entries were driven by certain adjustments-that should have been addressed prior to the preparation of the **financial** statements by PHS. **However, certain errors in recording accounts receivable related transactions during the year were also noted. The following** summarizes the most significant adjustments to **the financial** statements relating to accounts receivable and revenue at September 30, 1995:

- **Intra-PHS** activity of approximately \$7 million in revenue and \$1.8 million in receivables required elimination.
- Allowance for **doubtful** accounts and bad debt expense required net adjustments of approximately \$1.7 million and 1.3 **million**, respectively.
- Additional receivables were recorded based upon review of subsequent 'collections in the amount of approximately \$3.7 million.
- A double posting of accounts receivable resulted in a \$653,456 overstatement of the unadjusted balance.
- The incorrect establishment of a receivable for a drawdown (credit) document resulted in a \$107,132 overstatement of the unadjusted balance.

We believe that these adjustments resulted from reconciliation and analytical review of account balance procedures not being completely performed in a timely manner. In **addition**, once the adjustments were found, the impact of such adjustments on financial reporting was not adequately assessed and communicated to individuals in the Division of Fiscal Services(**DFS**) preparing the financial statements.

Recommendation

Analytical review of accounts and reconciliation procedures should be **performed** timely and expanded to ensure that accounts receivable and revenue are **properly** recorded in the general ledger and, ultimately in the financial statements. Prior to the preparation of PHS'S financial statements, account balances should be reviewed to **identify** possible adjustments in the accounts and the impact of such adjustments on the financial statements. Such review should include an assessment of the reasonableness of all estimates, such as the allowance for uncollectible accounts. Adjustments to account balances should be communicated to appropriate supervisors and DFS in a timely manner.

Auditee Response

We concur with this recommendation. The **Division** of Fiscal Services will **perform** timely periodic **analytical** reviews of account balances and reconciliations which should reduce the “ number of adjusting journal entries needed at year end.

ELECTRONIC DATA PROCESSING

Department of Fiscal Services (**DFS**) of the Health Resources And Service Administration (**HRSA**) maintains accounting systems for the Service and Supply Fund. **DFS** has contracted with Parklawn Computer Center (**PCC**) to operate computerized financial applications at PCC'S data center.

We have noted that the security access and administrative controls of PHS'S financial systems need improvement as follows:

- Some Resource Access Controls Facility (**RACF**) coordinators have implemented the **RACF** security software without requiring users to periodically change passwords. Users can keep the same passwords for years.
- Users can access applications with someone else's ID and attempt to compromise the password. Since there is no maximum invalid access attempts limitation in the application software, users can enter passwords until they guess the correct password.
- Health Accounting System (HAS) has outdated manuals and certain Perry Point Supply Depot inventory users manuals are not current. Manuals are an important control mechanism because they inform the users of the features of the **system**, and assist programmers in making changes to programs that might **affect** other aspects of the system. We understand that PCC plans to implement a **new** accounting system to replace HAS; however, this implementation may take several **years** while DFS still uses the old system that remains not adequately documented.

- OMB Circular A-130, Management of Federal Information Resources states that there must be a periodic risk access and **re-certification** every three years. Periodic reviews have not been completed for several years for the payroll interface, accounts receivable, PHS Financial Management **System**, Health Accounting System and inventory applications.
- There is no specific document or process requiring the personnel office to notify **PCC** for transferred or terminated employees. As a result, PHS is exposed to the risk that **disgruntled** former employees could destroy or change data or programs.
- There is no contingency plan for Health Accounting System (HAS) and PHS Financial Management System. As a result, PHS could not be **sufficiently prepared** to handle potential business interruptions resulting from prolonged computer outages, emergencies, or disasters.

Recommendations

We recommend that the Chief Administrative Officer develop policies and procedures to:

1. Implement the change password feature of RACF to force all users to periodically change their passwords and to **modify** financial applications to inherit the RACF ID.
2. Update the HAS and inventory manuals.
3. Instruct the Personnel departments to notify PHS and PCC departments of **all** terminated and transferred employees.
4. The requirements of OMB A-130 should be implemented for payroll interface, accounts receivable, PHS Financial Management **System**, Health Accounting System and Inventory applications. In February 1996, a revision to OMB A-130 was issued to require an independent review or audit of the security controls in each application at least every three years.
5. Develop a **disaster** recovery plan and coordinate the plan with the PCC computer faculty disaster plan.

Auditee Response

1. We concur with this recommendation and will consult with the current contractor to determine the feasibility of implementing this recommendation.
2. We concur in theory with the recommendation to update HAS manuals. However, since we are scheduled to **implement** the Standard General Ledger (SGL) beginning October 1, 1996, it would be of little benefit to expend the resources to update the HAS manuals.

The user manual has been updated since September 30, 1995 to accommodate the menu structure changes, and is currently being reviewed and revised with continual improvements. Additionally, standard operating procedures governing system processing are also under review and being revised as necessary.

3. We concur with this recommendation and will request that the appropriate personnel offices **inform** the security officer when employees within their accountable areas are terminated or **transferred**.
4. We concur with this recommendation in theory. However, DFS will be implementing the SGL as of October 1, 1996. As part of **the** process of installing the new **system**, DFS will ensure that adequate management and technical controls are in place to, safeguard against misuse, unauthorized access or modification **of** the information contained in **these information** systems. We believe that it would be most cost effective to review the security controls when the new **accounting** system (SGL) is **implemented rather** than **performing** a review of the current controls relating to a system that **will soon be** replaced. We will comply with all relevant OMB guidelines/requirements after we have completed implementing the SGL.
5. We concur with this recommendation. Following the reorganization of DFS, we will develop a disaster recovery plan.

Report on Compliance With Laws and Regulations

The results of our tests disclosed no instances of noncompliance that are required to be reported herein under Government Auditing Standards.

Nothing came to our attention to indicate that the report on internal controls, prepared by the various agency components of the Public Health Service under the Federal Managers' Financial Integrity Act (**FMFIA**), conflict materially with the results of our understanding and tests of the financial reporting internal control structure.

Management's Responsibilities

Management is responsible for:

- I. designing and maintaining a financial reporting internal control structure that provides reasonable, but not **absolute**, assurance that the following objectives are met:
 - A. transactions **are properly** recorded and accounted for to permit the preparation of reliable and timely financial statements and to maintain accountability over assets;

- B. **funds**, property, and other assets are safeguarded against **loss** from unauthorized use or disposition;
 - c. transactions, including those related to obligations and costs, are executed in compliance with applicable laws and regulations; and
 - D. data that support reported performance measures are properly recorded and accounted for to permit preparation of reliable and complete performance information.
- II. preparing the financial **statements** in conformity with the basis of accounting described in the **Summary** of Significant Accounting Policies accompanying the financial statements.
- III. complying with laws and regulations including those that do not necessarily **affect** financial transactions or financial reporting.

Auditor Responsibilities and Methodologies

Our responsibilities are:

- o to express an opinion on the Principal Financial Statements based on our audit. Accordingly, we planned and performed the **audit** to obtain reasonable' assurance about whether the financial statements are **free** of material misstatement and are presented in accordance with the basis of accounting described in the Summary of Significant Accounting Policies accompanying the financial statements.
- o to report the results of our related tests of the Fund's **financial** reporting internal control structure to the extent that its inadequate design or ineffective **operation**, if applicable, could materially **affect** the Fund's financial statements taken as **a whole**.
- o to obtain an understanding of the internal control structure policies and procedures and assess the control risks applicable to the Fund's reported **performance** measure **data**, but not to test the underlying data.
- o to report the results of our related tests of the Fund's compliance with (1) applicable laws and regulations that could materially affect the financial statements examined by us, taken as a whole, and (2) those specified in **OMB** Bulletin 93-06.

Our tests of applicable internal controls and compliance were performed to determine our auditing procedures for expressing an, opinion on the Principal Financial Statements and to report our findings resulting from our **controls** and compliance testing and not to express, and we do not express, separate opinions about the adequacy of the internal control structure **or** compliance with

laws and regulations. Our reports of findings regarding the internal control structure and compliance are included earlier in this report.

Because of inherent limitations **in** any internal control structure, losses, noncompliance or misstatement may nevertheless occur and not be detected. Also, projection of any evaluation of the internal control structure to **future** periods is subject to the **risk** that controls may become inadequate because of changes in **conditions** or that the degree of compliance with controls may deteriorate.

A reportable condition is a matter coming to our attention related to a significant deficiency in the design or operation of the internal control structure that, in our judgment, could adversely **affect** the organization's ability to record, process, **summarize**, and report financial data consistent with the assertions of management in the financial statements.

A material weakness is a reportable condition in which the design or operation of one or more internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities **in** amounts that would be material in relation to **the** financial statements being audited may occur and not be detected **within** a timely period by employees in the normal course of performing their assigned **functions**.

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be reportable conditions and, accordingly, would not necessarily **disclose** all reportable conditions that are also considered to be material weaknesses as defined above.

To fulfill these responsibilities, we:

- I. obtained an understanding of the Fund's financial reporting internal control structure policies and procedures in order to determine our auditing procedures for the purposes of expressing our opinion on the financial statements,
- II. examined, on a test basis, evidence supporting the amounts and disclosures in the financial statements
- III. assessed the accounting principles used and significant estimates made by management;
- IV. evaluated the overall presentation of the financial statements;
- v. evaluated and tested the operation of the relevant internal control structure policies and procedures designed **by** management to provide reasonable, but not absolute, assurance that

the above management objectives are met for the following significant cycles, classes of transactions, and account balances,

- A Revenue and receipts
- B. Purchases and disbursements
- c. Payroll
- D. Property
- E. **Inventory**

VI. obtained an understanding of the Fund's internal control structure and assessed control risk for data in the Fund's reported **performance measures**;

VII. tested compliance with selected provisions of the following laws and regulations that may materially **affect** the **financial** statements or are specified in **OMB** Bulletin 93-06.

- A Antideficiency Act
- B. Federal Managers' Financial Integrity Act of 1982
- c. Single Audit Act of 1984
- D. Fair Labor Standards Act of 1938
- E. Civil Service Retirement Act of 1930
- F. Civil Service Reform Act of 1938
- G. Prompt Payment Act
- H. Debt Collection Act of 1982
- I. Federal Employees Compensation Act
- J. Federal Employees **Life** Insurance Act of 1980
- K. Federal Employees Retirement System Act of 1986

VIII. compared the most recent **FMFIA** reports on internal controls prepared by the various agency components of the Public Health Service with the results of our tests of internal controls.

This report is intended for the information of management of the Fund, the Department of Health and Human Services Office of Inspector **General**, and OMB. However, this report is a matter of public record and its distribution is not limited.

Clifton Henderson L.L.C.

Baltimore, Maryland
April 30, 1996

FINANCIAL STATEMENTS

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**DEPARTMENT OF HEALTH AND HUMAN SERVICES
PUBLIC HEALTH SERVICE, SERVICE AND SUPPLY FUND
STATEMENTS OF FINANCIAL POSITION
As of September 30, 1995 and 1994
(Dollars in Thousands)**

	1995	1994
ASSETS		
Entity Assets		
Intragovernmental assets:		
Funds with U.S. Treasury (Note 1)	\$ 4,700	\$ 3,745
Accounts receivable, net of allowance for uncollectible accounts of \$1,701 in 1995 and \$425 in 1994 (Note 2)	27,485	22,262
Governmental assets:		
Accounts receivable, net	285	32
Inventories	13,764	10,337
Property and equipment, net (Note 3)	14,740	16,595
Total Entity Assets	60,974	52,971
Total Assets	\$ 60,974	\$ 52,971
LIABILITIES AND NET POSITION		
Liabilities		
Liabilities covered by budgetary resources:		
Intragovernmental liabilities:		
Accounts payable	\$ 3,494	\$ 2,738
Advances from other agencies (Note 4)	30,193	30,336
Governmental liabilities:		
Accounts payable	12,899	8,965
Accrued payroll and benefits	5,483	5,186
Total liabilities covered by budgetary resources	52,069	47,225
Total Liabilities	52,069	47,225
Net Position (Note 5)		
Balances:		
Invested capital	250	250
Cumulative results of operations	8,655	5,496
Total net position	8,905	5,746
Total Liabilities-and Net Position	\$ 60,974	\$ 52,971

These financial statements should only be read in connection with the
accompanying summary of significant accounting policies
and notes to financial statements.

**DEPARTMENT OF' HEALTH AND HUMAN SERVICES
PUBLIC HEALTH SERVICE, SERVICE AND SUPPLY FUND
STATEMENTS OF OPERATIONS AND CHANGES IN NET POSITION
For the Years Ended September 30,1995 and 1994
(Dollars in Thousands)**

	1995	1994
REVENUES AND FINANCING SOURCES		
Revenues from sales of goods and services - intragovernmental	\$ 131,514	\$ 125,681
Total revenues and financing sources	131,514	125,681
EXPENSES		
Operating expenses (Note 6)		
Personal services and benefits	41,100	40,233
Travel and transportation	1,496	1,670
Rental, communication , and utilities	9,689	9,246
Printing and reproduction	785	887
Contractual services	36,985	37,997
Supplies and materials	2,540	2,918
Equipment not capitalized	1,359	1,515
Total operating expenses	93,954	94,466
Cost of goods sold - intragovernmental	29,895	31,539
Depreciation and amortization	3,198	3,327
Provision for bad debts	1,308	425
Total expenses	128,355	129,757
EXCESS (SHORTAGE) OF REVENUES AND FINANCING SOURCES OVER TOTAL EXPENSES	3,159	\$ (4,076)
NET POSITION, BEGINNING BALANCE	\$ 5,746	\$ 9,822
NET POSITION, ENDING BALANCE	\$ 8,905	\$ 5,746

These financial statements should only be read in connection with the
accompanying summary of significant accounting policies
and notes to financial statements.

**DEPARTMENT OF HEALTH AND HUMAN SERVICES
PUBLIC HEALTH SERVICE, SERVICE AND SUPPLY FUND
SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES
September 30,1995 and 1994
(Dollars in Thousands)**

BASIS OF PRESENTATION

These financial statements have been prepared to report the financial position and results of operations of The Public Health Service, Service and Supply Fund (the Fund), as required by the Chief Financial Officers Act of 1990. They have been prepared from the books and records of the Fund in accordance with the form and content for entity financial statements specified by the Office of Management and Budget (**OMB**) Bulletin 94-01, and the Fund's accounting policies which are summarized in this note. The Fund has received a waiver from **OMB** of the requirement to present a statement of cash flows and a statement of budget and actual expenses for the years ended September 30, 1995 and 1994.

ENTITY

The Public Health Service (**PHS**) is a part of the Department of Health and Human Services (HI-IS) which is a Cabinet agency of the Executive Branch of the United States Government. PHS is responsible for a wide variety of health care programs including research and **services**.

The Fund (75X4552) is responsible for administering the operations of a medical supply depot located at Perry Point, Maryland and providing data processing, accounting, facilities management and training services to various PHS agencies. Starting in Fiscal Year 1995, the Fund includes the activities of the Division of Payment Management which transferred **from** the Office of the Secretary **Working** Capital Fund (75X4503).

The Fund is a revolving-type **fund**, which recovers its costs through **billings** to PHS agencies and other organizations. No annual appropriated **funding**, subsequent to the initial \$250 **fund capitalization**, is provided to support the Fund's activities. Accounting services for the Fund are provided by the Division of Fiscal Services of the Program Support Center (**PSC**). The Fund is considered a separate reporting entity for financial reporting purposes to the U. S. Department of **Treasury** (Treasury). PSC reports financial accounting data for the Fund to the Treasury and OMB and also maintains the Fund's general ledger balances in the Health Accounting System.

BUDGETS AND BUDGETARY ACCOUNTING

The Fund is governed by a Board of Directors comprised of representatives from the PHS agencies that are served **by** this Fund. Budgetary control for the Fund is provided by the oversight role of the Board of Directors. Allotment documents are issued in accordance with the annual apportioned budget. **The** allotment and allowance documents provide the budget authority so that activity managers **may** enter into obligations, acquire goods and services and make payments in accordance **with laws** and regulations.

**DEPARTMENT OF HEALTH AND HUMAN SERVICES
PUBLIC HEALTH SERVICE, SERVICE AND SUPPLY FUND
SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES
September 30,1995 and 1994
(Dollars in Thousands)**

BUDGETS AND BUDGETARY ACCOUNTING (CONTINUED)

The Fund's budgetary accounting transactions are serviced by **PSC's** Division of Fiscal Services. Budgetary accounting facilitates compliance with legal constraints and controls over the use of federal **funds**.

BASIS OF Accounting

Transactions **are** recorded using the accrual basis of accounting and a budgetary basis. Under the accrual method, revenues are recognized when earned and expenses are recognized when a liability is incurred, without regard to receipt or payment of cash.

FUNDS WITH U.S. TREASURY

The Fund does not maintain cash in commercial bank accounts. Cash receipts and disbursements are processed by the **Treasury**. Collections of **fees** for supplies and **services** provided to customer agencies and operating outlays are recorded in the Health Accounting System. General ledger cash balances are reconciled monthly with balances reported by the Treasury.

ACCOUNTS RECEIVABLE

External accounts receivable are comprised principally of amounts due from Federal agency customers of the Supply Service Center for medical supplies and drugs. Internal receivables are transfers from PHS agencies. At the end of Fiscal Year 1995, estimated **unbilled** accounts receivable are recorded in the Health Accounting System for several activities.

Agencies that order medical supplies from the Supply Service Center receive bills generated from an Accounts Receivable module. These agencies issue check payments for **medical** supplies upon receipt of the goods. The agencies are not part of Treasury's On-Line Payment and Collection (**OPAC**) System in which billing and collection activity is accomplished through electronic transfer.

**DEPARTMENT OF HEALTH AND HUMAN SERVICES
PUBLIC HEALTH SERVICE, SERVICE AND SUPPLY FUND
SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES
September 30,1995 and 1994
(Dollars in Thousands)**

INVENTORIES

Inventories, which consist principally of medical supplies and drugs held for resale by the Supply Service Center located at **Perry** Point, Maryland, are stated at the lower of cost or market. Cost is determined by using the weighted average valuation method. Adjustments have been made for spoilage, breakage, and other variances.

PROPERTY AND EQUIPMENT

Property and equipment purchases are valued at cost. Equipment is capitalized if the initial acquisition cost is \$5 or more and a **useful life** of 2 years or more. Expenditures for **major** additions, replacements, and alterations are capitalized. Normal repairs and maintenance costs are expensed as incurred.

Depreciation on equipment and improvements is computed using the straight 'line method based on the **useful** life of the assets with one-half year's depreciation taken in year of acquisition. Property and equipment is depreciated as follows: Equipment over **useful** lives ranging from 5 to 15 years; ADP Software for 15 years and the Real Property Improvements over 30 years. **Useful** lives are determined using the Veterans Affairs Federal Supply Catalog classification system.

ANNUAL, SICK, AND OTHER LEAVE

Annual leave is accrued as it is earned and reduced as taken. The balance in the accrued annual leave account is adjusted annually to reflect current pay rates of cumulative annual leave earned but not taken. Sick and other types of nonvested leave are expensed as taken.

REVENUES AND OTHER FINANCING SOURCES

Revenues are generated from **fees** for services and commodities provided to PHS customers and other governmental entities. Activities that generate revenues include medical supply sales, automated data processing services, accounting and fiscal services and various centralized services.

RECLASSIFICATIONS

Certain reclassifications were made to the 1994 financial statements to conform to the 1995 presentation.

This information is an integral part of
the accompanying financial statements.

**DEPARTMENT OF HEALTH AND HUMAN SERVICES
PUBLIC HEALTH SERVICE, SERVICE AND SUPPLY m
NOTES TO FINANCIAL STATEMENTS
September 30, 1995 and 1994
(Dollars in Thousands)**

NOTE 1- FUNDS WITH U.S. TREASURY

At September 30, 1995, the U.S. Treasury reported that the Fund had a **fund** balance of \$8,174, which included \$3,474 relating to an incorrect posting of cash receipts by the U.S. **Treasury**. Accordingly, the corrected balance presented in these financial statements is \$4,700.

NOTE 2- ACCOUNTS RECEIVABLE

The increase in accounts receivable during **Fiscal** Year 1995 is the result of a procedure which increases the time needed to collect the receivable. The receivable is liquidated only upon receipt of an authorized obligation document from the **billed** PHS agency. Also, part of the increase is due to increased sales by the Supply Service Center to Pacific Basin territories, the Peace Corps and to the District of **Columbia**.

An allowance for uncollectible accounts has been established at \$1,701 at September 30, 1995 and \$425 at September 30, 1994. The allowances are based on specific accounts whose collection is unlikely and an estimate of the remaining accounts ultimately becoming uncollectible. Such estimate is based on prior year write-off history of the Fund.

NOTE 3- PROPERTY AND EQUIPMENT, NET

Class of Fixed Assets	Acquisition cost	Accumulated Depreciation	B o o k Value
<u>September 30, 1995</u>			
Real property improvement	\$ 564	\$ 61	\$ 503
ADP software	10,080	2,861	7,219
Equipment	<u>19,992</u>	<u>12,974</u>	<u>7,018</u>
Total	<u>\$ 30,636</u>	<u>\$ 15,896</u>	<u>\$ 14,740</u>
<u>September 30, 1994</u>			
Real property improvement	\$ 418	\$ 33	\$ 385
ADP software	10,080	2,189	7,891
Equipment	<u>19,074</u>	<u>10,755</u>	<u>8,319</u>
Total	<u>\$ 29,572</u>	<u>\$ 12,977</u>	<u>\$ 16,595</u>

Real Property consists of **capital** improvements to the Supply Service Center warehouse and loading dock.

DEPARTMENT OF HEALTH AND HUMAN SERVICES
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 NOTES TO FINANCIAL STATEMENTS
 September 30, 1995 and 1994
 (Dollars in Thousands)

NOTE 4- ADVANCES FROM OTHER AGENCIES

At September 30, 1995 and 1994, the Fund had a projected balance due to the U.S. Treasury for payment requirements of a **completed** contract with Computer Data Systems, Inc. for accounting and **financial software** aggregating \$10,080, increases in inventory held for sale, and a slowdown in the collection of receivables. The **software** cost will be recaptured from its customers over 15 years of **billings**. Advances were received from five component agencies of **HHS** of \$30,000 through September 30, 1995 and 1994. Each agency advance was calculated based on its planned **future** activity with the Fund. The advances will be liquidated upon **completion** of the billing and collection cycles.

NOTE 5- NET POSITION

Undelivered orders were \$52,647 at September 30, 1995 and \$45,906 at September 30, 1994.

NOTE 6- OPERATING EXPENSES BY PROGRAM

	<u>1995</u>	<u>1994</u>
Supply Service Center	\$ 5,850	\$ 4,208
Parklawn Computer Center	9,256	14,663
Division of Fiscal Services	11,563	9,166
Parklawn Semites	32,033	34,588
Division of Commissioned Personnel	5,674	6,353
Central Personnel Services	3,623	3,019
Regional Activities	1,010	2,192
Telecommunications Improvement Project	19,803	20,277
Division of Payment Management	<u>5,142</u>	<u> </u>
Totals	<u>\$ 93,954</u>	<u>\$ 94,466</u>

NOTE 7- RETIREMENT PLAN

Fund employees participate in three different retirement plans. Civil service employees participate in the Civil Service Retirement System (**CSRS**), or the Federal Employees Retirement System (**FERS**) (for most employees hired after December 31, 1983). Commissioned Corps personnel participate in the **retirement** plan for **Uniformed** Services. The Fund does not report CSRS, FERS, Uniformed Services, **assets**, accumulated plan benefits, or **unfunded** liabilities, if any, applicable to its employees. Reporting such amounts is the responsibility of the Office of Personnel Management.

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NOTE 8- COMBINING STATEMENTS

The Combining Statement described in **OMB** Bulletin 94-01 is designed to present the information found in the financial statements by major program activities or **funds**. As the financial activities of the Fund are not allocated by programs or finds, but rather on an **agency-**wide basis, a combining statement is not applicable and is not presented.

This information is an integral part of
the accompanying financial statements.

Public Health Service

Overview

The mission of the Public Health Service (PHS) is the improvement and advancement of the health of **all** citizens. To accomplish this mission, PHS programs are designed to:

- Develop **knowledge** leading to the prevention and treatment of **disease**;
- Control and promote **health**;
- Gather data that measure the status of the Nation's **health**;
- Improve the health care system,
- Assure the quality and accessibility of health care;
- Improve the mental health of the Nation;
- Assure safe and effective drugs and **healthful** foods;
- Respond to emergency health needs; and
- Expand health resources.

Since its origin in 1798, PHS has been making important contributions to the Nation's health.

- The Marine Hospital Service was established in 1798 under the Treasury Department with the signing by President John Adams of an act for the relief of sick and disabled seamen. The first temporary hospital was started in rehabilitated barracks on Castle Island in Boston Harbor in 1799.
- Congress **officially** established the Public Health Service Commissioned Corps in 1889 along military lines **with titles** and pay corresponding to Army and Navy grades. The Commissioned Corps was established

as a mobile force of professionals subject to duty anywhere upon assignment.

- The Hygienic Laboratory was established in 1891, the forerunner of the National Institutes of Health.
- After 141 years in the Treasury Department the Public Health Service, in 1939, became part of the newly created Federal Security Agency, later to become the Department of **Health, Education, and Welfare**, and subsequently in 1980, the Department of Health and Human Services.
- In response to its increased responsibility, PHS has grown from a small nucleus of health professionals to more than 5,700 commissioned corps officers, plus 44,000 professional, technical, and support personnel in civil **service**, working in a wide variety of health programs.

PHS has undergone significant change in the last two decades. Through enactment of laws, Congress has placed increased responsibility upon PHS in the following sectors:

- Expanding research into the cause, treatment, control, and prevention of disease;
- Launching of frontal attacks on such major killers as cancer, heart disease, and AIDS;
- Promoting healthier lifestyles for all Americans;
- Supplying of health-professional assistance to local, State, national, and

international health organizations to cope with special health needs and challenges;

- Furthering of programs to treat mental illness, to promote better mental health, and to combat drug abuse, alcoholism, and other hazards to **health**;
- Furthering of food and drug programs to safeguard the health of the consuming public;
- Strengthening of communicable disease control at home and abroad;
- Enhancing the quality, appropriateness, and effectiveness of health care services and access to such services; and
- Promoting the responsible conduct of scientific research.

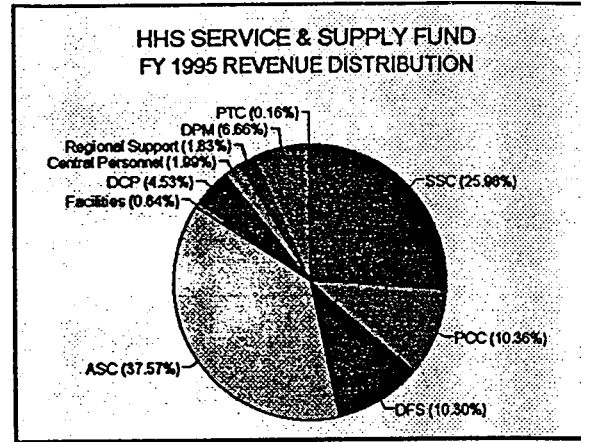
Organizationally, PHS operated through the **Office** of the **Assistant** Secretary for Health and eight major **health** agencies, which were as follows in FY 1995:

- Agency for Health Care Policy and Research (**AHCPR**);
- Agency for Toxic Substances and Disease Registry (**ATSDR**);
- Substance Abuse and Mental Health Services Administration (**SAMHSA**);
- Centers for Disease Control and Prevention (**CDC**);
- Food and Drug Administration (**FDA**);
- Health Resources and Services Administration (**HRSA**);
- Indian Health Service (**IHS**); and
- National Institutes of Health (**NIH**).

Discussion and Analysis: PHS Service & Supply Fund

Mission

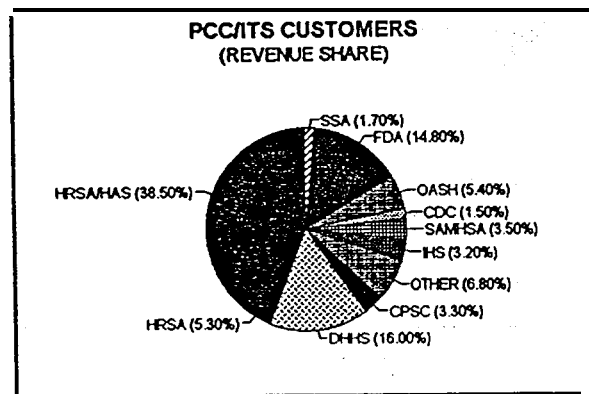
The PHS Service & Supply Fund (SSF) was established under authority of 42 U.S.C. 231, July 3, 1945. The purpose of the fund is to provide consolidated financing and accounting for business type operations involving the provision of common services and commodities to customers in the Public Health Service as well as other government entities. In FY 1995, SSF activities were located organizationally in the following PHS Agencies: the Food and Drug Administration (FDA), the Health Resources and Services Administration (HRSA), the Indian Health Service (IHS), and the Office of the Assistant Secretary for Health (OASH). The mission of the SSF management is to provide their customers with the proper mix of quality service at a reasonable, competitive cost. The SSF Charter outlines the operations and management of the Fund, as well as the purpose, functions, and membership of the SSF Board of Directors. The Board is responsible for making recommendations on all matters concerning activity budget requests, changes in the scope of operation of any activity, changes in charges and fees, policies and procedures governing the operation of the Fund, and any other appropriate items. The Chairperson of the Board is responsible for calling meetings, setting agendas, and keeping all parties informed of issues and decisions.



Service Activities

Parklawn Computer Center

This FDA activity provides automated data processing (ADP) services for HHS and 30 other Federal organizations. In FY 1995, the PCC generated over \$14 million in cost recovery & fee-for-service revenue, 10% of total SSF activity. (see graph above)



Major accomplishments for the year included the implementation of an off-site location for automatic backing-up of

customer data, hot-site disaster recovery program development, and implementation of Electronic Data Interchange (EDI) which gives PCC customers electronic commerce capability. PCC is the first civilian government organization to have EDI capability.

The best measure of PCC performance is the time necessary to process **information**, referred to as the response time. Over the last three fiscal years, PCC has made a priority of continually improving its response time. In FY 1995, PCC successfully completed 99.86% of its batch jobs within the targeted response time goals.

Administrative Services

ASC is the largest **function** within Parklawn Services. With an FY 1995 budget of \$65 million, this OASH activity accounted for **38%** of FY 1995 SSF revenue. Services provided by ASC include:

Telecommunications Services - The Telecommunications Improvement Project (TIP), which consolidates **all** telephone services provided to the Parklawn Complex and the NIH Campus into one **contract**, has yielded savings of up to one-third on rates charged by the telephone company thru use of a collective bargaining process.

Procurement and contract administration - In FY 1995 ASC processed over 16,000 procurement acquisitions **and administered** 342 contract actions. Processing these actions thru the newly implemented Federal Acquisition Computer Network has yielded over \$5.7 million in cost avoidance and savings to the Government.

Building & Infrastructure Management - ASC provides services for the 1 million square **foot Parklawn** Building as well as to numerous satellite buildings within the Parklawn complex. Services include building maintenance, renovation and repair, and implementation of enhanced safety and security measures. In FY 1995, ASC relocated its central receiving and surplus property operations to a state of the art warehouse facility. **Combining** advanced inventory management systems and proximity to major ground shipping routes, the facility provides customers with a level of service unmatched within civilian government agencies. ASC also manages operation of photocopy centers throughout the complex, operation of the Health Library, motor pool operations, parking management, and mail delivery and messenger services. Finally, ASC provides printing procurement & limited on-site printing.

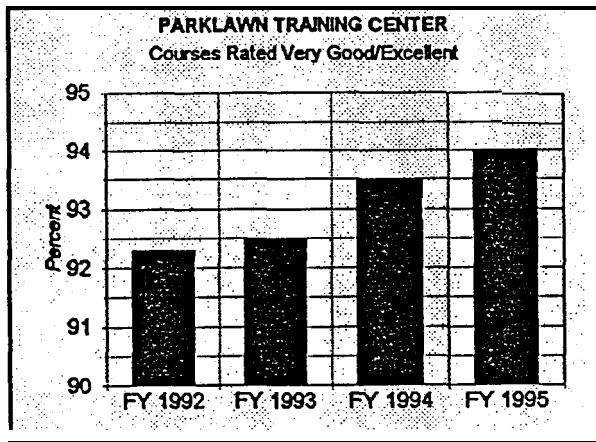
Public Health Reports

Public Health Reports provides **staffing** for the bimonthly publication **Public Health Reports** which was prepared within the Office of Public Affairs, OASH

Central Personnel Services

This OASH activity finances the staff which plans, conducts, and evaluates training programs in such areas as supervisory management **office** skills and procedures, and data technology. CPS generated 2% of SSF revenue in FY 1995. Training programs are demand oriented and restricted to the needs of customer organizations within the Parklawn Complex. During FY 1995, the **Parklawn Training Center**

conducted 625 classes with 94% of the participants rating the programs very good or excellent. Based on customer surveys, the quality of PTC course offerings has steadily improved as illustrated in the following graph



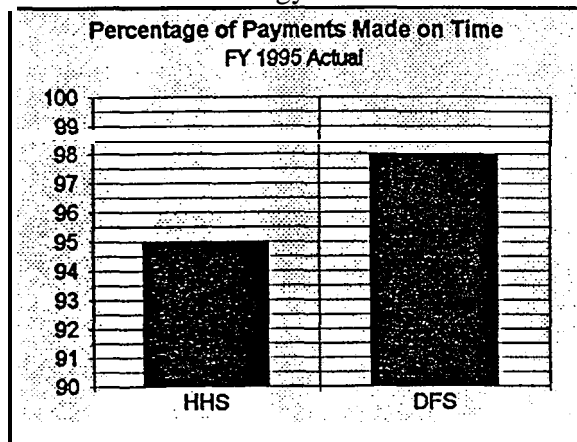
Division of Commissioned Personnel

The Division of Commissioned Personnel administers payroll and other personnel management programs for approximately 6,150 active duty, 6,400 inactive reserve, and 3,200 retired PHS Commissioned Officers. In FY 1995, this OASH activity accounted for 4.5% of SSF revenue.

Division of Fiscal Services

In FY 1995, this activity provided accounting and fiscal services for HRSA, IHS, SAMHSA, AHCPR, and OASH. DFS provides services including: the prompt recording and liquidation of accounting transactions; the reporting of accounting information for management uses (both internal and external); the providing of full accounting services related to debt management and claims collection activity; all types of disbursements, management

reviews, dispute resolution, and the provision of technical assistance to headquarters and field accounting activities relative to fiscal matters. With a budget of \$11 million, DFS generated more than 10 percent of the SSF revenue in 1995. DFS bills its customers based on a step-down cost allocation methodology.

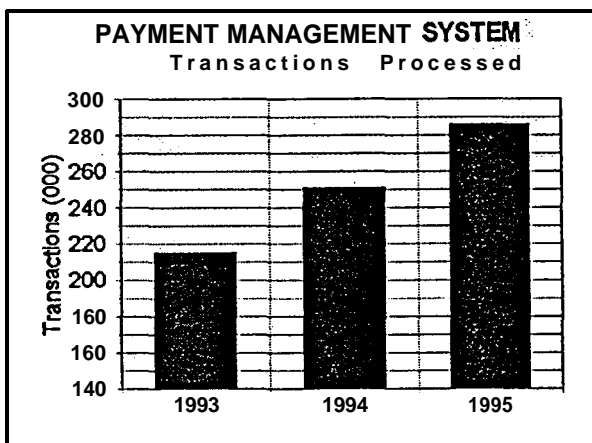
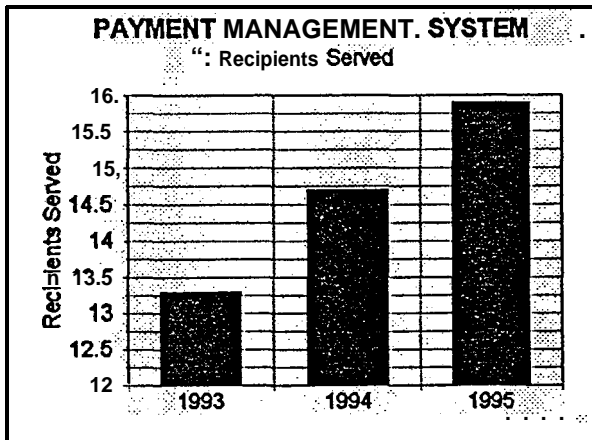


Despite the fact that the Division again paid more than \$1 billion worth of invoices in FY 1995, DFS continues to surpass the Departmental goal for the number of on-time payments, as outlined in the Prompt Payment Act. (see graph above). Due to recent enhancements in the accounting system, DFS saved tens of thousands of dollars through discounts for early payments.

Division of Payment Management

The Division of Payment Management operates the Payment Management System, the Department's central point for payments to grant and contract recipients. DPM serves HHS and a variety of other government organizations through operation of Electronic Funds Transfer systems such as SMARTLINK and CASHLINE that

of Electronic Funds Transfer systems such as SMARTLINK and CASHLINE that provide Direct Deposit-like electronic funds transfer to grantees and other recipients. Since 1993, DPM has experienced both a 20% increase in the number of recipients it serves and a 33% increase in the amount of transactions processed. (See graphs)



Supply Service Center

The HHS Supply Service Center (SSC), located in Perry Point, MD, is a full service medical supply activity that provides pharmaceutical & other medical supplies to DHHS agencies and other federal civilian

agencies worldwide. As an IHS activity, it accounted for 26% of FY 1995 SSF revenue. SSC supplies over 1,800 health care activities including the Peace Corps, U.S. AID, and State Department Embassies. The SSC is the only FDA licensed facility within the federal government that can repackage pharmaceuticals. Repackaging of pharmaceuticals allows the SSC to reduce costs to its customers by purchasing mass quantities of inventory at substantial discounts. SSC's Pharmacy Repacks provide an economical and time-saving alternative for small or remote locations that lack pharmacists on-site.

The greatest indicator of the depot's ability to meet its customer needs is the fill rate, the percentage of order lines filled completely compared to the number of lines accepted. In FY '95, the SSC maintained a 95% fill rate coupled with an average order turnaround time of 4 days (as opposed to 6 days in FY 94). Over the last five years, the number of backorders placed has dropped 71% while annual sales of the SSC have more than doubled. Although the SSC is not a mandatory supply source for any agency, the number and variety of its customers reflects the superior quality of its services as well as the competitive level of its prices.