

GAO

Report to the Subcommittee on
Oversight and Investigations,
Committee on Veterans' Affairs, House
of Representatives

September 2008

VETERANS HEALTH ADMINISTRATION

Improvements Needed in Design of Controls over Miscellaneous Obligations





Highlights of [GAO-08-976](#), a report to the Subcommittee on Oversight and Investigations, Committee on Veterans' Affairs, House of Representatives

VETERANS HEALTH ADMINISTRATION

Improvements Needed in Design of Controls over Miscellaneous Obligations

Why GAO Did This Study

The Veterans Health Administration (VHA) has been using miscellaneous obligations for over 60 years to record estimates of obligations to be incurred at a later time. The large percentage of procurements recorded as miscellaneous obligations in fiscal year 2007 raised questions about whether proper controls were in place over the authorization and use of billions of dollars.

GAO was asked to review (1) how VHA used miscellaneous obligations during fiscal year 2007, and (2) whether Department of Veterans Affairs (VA) policies and procedures were designed to provide adequate controls over their authorization and use. GAO obtained and analyzed available VHA data on miscellaneous obligations, reviewed VA policies and procedures, and reviewed a nongeneralizable sample of 42 miscellaneous obligations at three case study locations.

What GAO Recommends

GAO makes four recommendations to the Secretary of Veterans Affairs to modify its policies and procedures, in conjunction with VA's Office of General Counsel, to better ensure adequate oversight of miscellaneous obligations by contracting officials, segregation of duties throughout the process, and sufficient supporting documentation for miscellaneous obligations. VA concurred with the recommendations and identified specific actions it will take to implement them.

To view the full product, including the scope and methodology, click on [GAO-08-976](#). For more information, contact Kay L. Daly at (202) 512-9095 or dalykl@gao.gov.

What GAO Found

VHA recorded over \$6.9 billion of miscellaneous obligations for the procurement of mission-related goods and services in fiscal year 2007. According to VHA officials, miscellaneous obligations were used to facilitate payment for goods and services when the quantities and delivery dates are not known. According to VHA data, almost \$3.8 billion (55.1 percent) of VHA's miscellaneous obligations was for fee-based medical services for veterans and another \$1.4 billion (20.4 percent) was for drugs and medicines. The remainder funded, among other things, state homes for the care of disabled veterans, transportation of veterans to and from medical centers for treatment, and logistical support and facility maintenance for VHA medical centers nationwide.

GAO's *Standards for Internal Control in the Federal Government* states that agency management is responsible for developing detailed policies and procedures for internal control suitable for their agency's operations. However, VA policies and procedures were not designed to provide adequate controls over the authorization and use of miscellaneous obligations with respect to oversight by contracting officials, segregation of duties, and supporting documentation for the obligation of funds. Collectively, these control design flaws increase the risk of fraud, waste, and abuse (including employees converting government assets to their own use without detection). These control design flaws were confirmed in our case studies at VHA Medical centers in Pittsburgh, Pennsylvania; Cheyenne, Wyoming; and Kansas City, Missouri.

Summary of Control Design Deficiencies at Three Case Study Locations

Station	Number of obligations reviewed	No documented approval by contracting officials	Inadequate segregation of duties	Inadequate supporting documentation		
				Incomplete purpose description	Blank vendor field	Blank contract field
Pittsburgh	14	14	9	3	6	3
Cheyenne	11	11	11	1	6	4
Kansas City	17	17	10	4	8	9
Total	42	42	30	8	20	16

Source: GAO analysis of VHA data.

In May 2008, VHA issued revised guidance on required procedures for authorizing and using miscellaneous obligations. GAO reviewed the revised guidance and found that while it offered some improvement, it did not fully address the specific control design flaws GAO identified. Furthermore, according to VA officials, VA's policies governing miscellaneous obligations have not been subject to legal review by VA's Office of General Counsel. Such a review is essential to ensure that policies and procedures comply with applicable federal appropriations law and internal control standards.

Contents

Letter		1
	Results in Brief	3
	Background	5
	Miscellaneous Obligations Used Extensively for Mission-Related Activities in Fiscal Year 2007	10
	Deficiencies in Design of Controls over Miscellaneous Obligations Increase the Risk of Fraud, Waste, and Abuse	13
	Conclusions	23
	Recommendations for Executive Action	23
	Agency Comments and Our Evaluation	24
<hr/>		
Appendix I	Scope and Methodology	26
<hr/>		
Appendix II	Comments from the Department of Veterans Affairs	30
<hr/>		
Appendix III	Miscellaneous Obligations by VISN in Fiscal Year 2007	33
<hr/>		
Appendix IV	VHA Stations Ranked by Use of Miscellaneous Obligations	34
<hr/>		
Appendix V	GAO Contact and Staff Acknowledgments	38
<hr/>		
Tables		
	Table 1: Miscellaneous Obligations at VHA and VA for Fiscal Year 2007	10
	Table 2: Summary of Case Study Results	14
	Table 3: Case Study Analysis of Segregation of Duties	17

Figures

Figure 1: Veterans Integrated Service Networks (VISN)	6
Figure 2: VA's Miscellaneous Obligation Process	9
Figure 3: VHA Miscellaneous Obligations for Fiscal Year 2007	11

Abbreviations

BOC	budget object code
FAR	Federal Acquisition Regulation
FMS	Financial Management System
IFCAP	Integrated Funds Distribution, Control Point Activity, Accounting and Procurement
IPA	independent public accountant
OIG	Office of Inspector General
UPMC	University of Pittsburgh Medical Center
VA	Department of Veterans Affairs
VHA	Veterans Health Administration
VISN	Veterans Integrated Service Network
VISTA	Veterans Health Information System and Technology Architecture

This is a work of the U.S. government and is not subject to copyright protection in the United States. It may be reproduced and distributed in its entirety without further permission from GAO. However, because this work may contain copyrighted images or other material, permission from the copyright holder may be necessary if you wish to reproduce this material separately.



United States Government Accountability Office
Washington, DC 20548

September 11, 2008

The Honorable Harry E. Mitchell
Chairman
The Honorable Ginny Brown-Waite
Ranking Member
Subcommittee on Oversight and Investigations
Committee on Veterans' Affairs
House of Representatives

The Department of Veterans Affairs (VA) is responsible for providing a variety of services to veterans, including medical care, disability compensation, and vocational rehabilitation. The Veterans Health Administration (VHA), a component of VA, manages one of the largest health care systems in the United States, providing health care to veterans throughout the country. VHA officials briefed your Subcommittee staff in September 2007 about various financial reporting weaknesses in the agency and initiatives under way to address them. In the briefing, VHA officials disclosed that \$4.8 billion (56 percent) of the reported \$8.6 billion in procurements through the third quarter of fiscal year 2007 had been done using funds categorized as “miscellaneous obligations.” VHA officials said that they have been using miscellaneous obligations for over 60 years to record estimates of obligations¹ to be incurred at a later time.² According to VA policy,³ miscellaneous obligations can be used to record

¹An obligation is a definite commitment that creates a legal liability of the government for the payment of goods and services ordered or received, or a legal duty on the part of the United States that could mature into a legal liability by virtue of actions on the part of the other party beyond the control of the United States. Payment may be made immediately or in the future.

²A miscellaneous obligation can be used as a funds control document to commit (reserve) funds that will be obligated under a contract or other legal obligation at a later date. VA Office of Finance Directive, VA Controller Policy MP-4, Part V, Chapter 3, Section 3 A.01 states in pertinent part that “it will be noted that in many instances an estimated miscellaneous obligation (VA Form 4-1358) is authorized for use to record estimated monthly obligations to be incurred for activities which are to be specifically authorized during the month by the issuance of individual orders, authorization requests, etc. These documents will be identified by the issuing officer with the pertinent estimated obligation and will be posted by the accounting section to such estimated obligation.”

³VA Office of Finance Directives, VA Controller Policy *MP-4, Part V, Chapter 3, Section A, Paragraph 3A.02 – Estimated Miscellaneous Obligation or Change in Obligation (VA Form 4-1358)*.

estimated obligations to facilitate the procurement of a variety of goods and services, including fee-based medical and nursing services and beneficiary travel. In addition, VA's Office of Inspector General (OIG) issued a report in May 2007 on the alleged mismanagement of funds at the VA Boston Healthcare System.⁴ According to OIG officials, they obtained documents showing that a miscellaneous obligation for \$200,000 was requested, approved, and obligated by the same fiscal official, calling into question the adequacy of the segregation of duty controls over miscellaneous obligations. In light of these concerns, you requested that we review whether the design of VHA's internal controls over the use of miscellaneous obligations was adequate for fiscal year 2007.

In response to your request, we initiated a review to determine (1) how VHA used miscellaneous obligations during fiscal year 2007, and (2) whether VA's policies and procedures are designed to provide adequate controls over the authorization and use of miscellaneous obligations. Our review focused on the approximately \$6.9 billion of miscellaneous obligations that VHA made during fiscal year 2007, the most complete fiscal year for which data were available when we began our review. We discussed our preliminary findings at a hearing before the Subcommittee on July 31, 2008.⁵

To determine the purposes for which VHA used miscellaneous obligations during fiscal year 2007, we obtained and analyzed a copy of VHA's Integrated Funds Distribution, Control Point Activity, Accounting and Procurement (IFCAP) database of miscellaneous obligations. VA's Senior Procurement Executive stated that the IFCAP database provided the best available data on VHA miscellaneous obligations created in fiscal year 2007. We determined that the IFCAP data were sufficiently reliable for the purposes of our report based on (1) testing various required data elements, (2) performing walkthroughs of the system, and (3) tracing selected transactions from source documents to the database. We could not reconcile IFCAP miscellaneous obligations to VA's Financial Management System (FMS)—the VA accounting system of record used to generate VA financial statements and other reports—because FMS does

⁴Department of Veterans Affairs, Office of Inspector General, *Audit of Alleged Mismanagement of Government Funds at the VA Boston Healthcare System*, Report No. 06-00931-139 (Washington, D.C.: May 31, 2007).

⁵GAO, *Veterans Health Administration: Improvements Needed in Design of Controls over Miscellaneous Obligations*, [GAO-08-1056T](#) (Washington, D.C.: July 31, 2008).

not identify the method used to obligate funds for transactions (e.g., miscellaneous obligations, purchase card, purchase order).

To determine whether VA's policies and procedures are designed to provide adequate controls over the use of miscellaneous obligations, we compared VA policies and procedures governing the use of miscellaneous obligations with federal appropriations law and internal control standards, interviewed VHA officials in Denver, Colorado, and Washington, D.C., and conducted case studies at VHA medical centers in Cheyenne, Wyoming; Kansas City, Missouri; and Pittsburgh, Pennsylvania. As part of the case studies, we interviewed VHA financial management and procurement officials, and reviewed a nongeneralizable sample of miscellaneous obligations to provide more detailed data on the extent and nature of any control design deficiencies. We did not review VHA's procurement or service authorization processes. Appendix I contains a more detailed description of our scope and methodology. We conducted our audit work from November 2007 through July 2008 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Results in Brief

In fiscal year 2007, available information from the Integrated Funds Distribution, Control Point Activity, Accounting and Procurement (IFCAP) database show that VHA used miscellaneous obligations to record over \$6.9 billion against its appropriations for the procurement of mission-related goods and services. According to the IFCAP data, almost \$3.8 billion of this total (55.1 percent) was for fee-based medical and dental services for veterans and another \$1.4 billion (20.4 percent) was for drugs, medicines, and hospital supplies. The remainder covered, among other things, state homes for the care of disabled veterans, transportation of veterans to and from medical centers for treatment, and logistical support and facility maintenance for VHA medical centers nationwide. VHA officials said they used miscellaneous obligations to administratively reserve estimated funds required to facilitate the payments for goods and services for which specific quantities and time frames were uncertain. Another cited benefit was that miscellaneous obligations simplify the procurement process when no underlying contract or purchase order exists. For example, VHA centers used miscellaneous obligations to record estimated obligations for an umbrella agreement for fee-based medical

services; the umbrella agreement can then be used to fund the work performed by a number of different physicians. Nonetheless, without effectively designed mitigating controls, the use of miscellaneous obligations may also expose VHA to increased risk of fraud, waste, and abuse.

VA policies and procedures were not designed to provide adequate controls over the use of miscellaneous obligations with respect to oversight by contracting officials, segregation of duties, and supporting documentation for recording the obligation of funds. Specifically, although VA's September 29, 2006, policy required contracting officials to review miscellaneous obligations to help ensure the proper use of these obligations, the supporting procedures did not describe how these reviews should be carried out. Further, the design of the current control process did not include detailed procedures for conducting either an automated or manual review of miscellaneous obligations by contracting officials. With regard to segregation of duties, the miscellaneous obligation automated system and associated policies and procedures were not designed to prevent one person from performing multiple roles in the process of authorizing and executing miscellaneous obligations. Finally, with regard to documentation, we found that current guidance did not include detailed procedures on what was to be included in the purpose field of the miscellaneous obligation authorization document and did not require that the vendor name and contract number be included. These control design flaws were confirmed in our case studies at Pittsburgh, Cheyenne, and Kansas City. Such VHA-wide policy and procedure design flaws increase the risk of fraud, waste, and abuse at the 129 VHA stations using miscellaneous obligations in fiscal year 2007. New guidance for the use of miscellaneous obligations was issued in May 2008. This guidance, while it offered some improvement, did not fully address the three problem areas. Also, we understand that VA attorneys have not reviewed these policies to help ensure compliance with applicable appropriations law and other requirements.

We are making four recommendations to VA to establish policies and procedures that will improve overall control design to better ensure adequate oversight of miscellaneous obligations by contracting officials, segregation of duties during the authorization process, and supporting documentation for miscellaneous obligations. We received written comments on a draft of this report from the Deputy Secretary of Veterans Affairs, which are reprinted in appendix II. VA concurred with our recommendations and identified specific actions it plans to take to

implement these recommendations. VA also provided technical comments which we considered and incorporated as appropriate.

Background

VA is responsible for providing federal benefits to veterans. Headed by the Secretary of Veterans Affairs, VA operates nationwide programs for health care, financial assistance, and burial benefits. In fiscal year 2007, VA received appropriations of over \$77 billion, including over \$35 billion for health care and approximately \$41.4 billion for other benefits. The Congress appropriated more than \$87 billion for VA in fiscal year 2008.

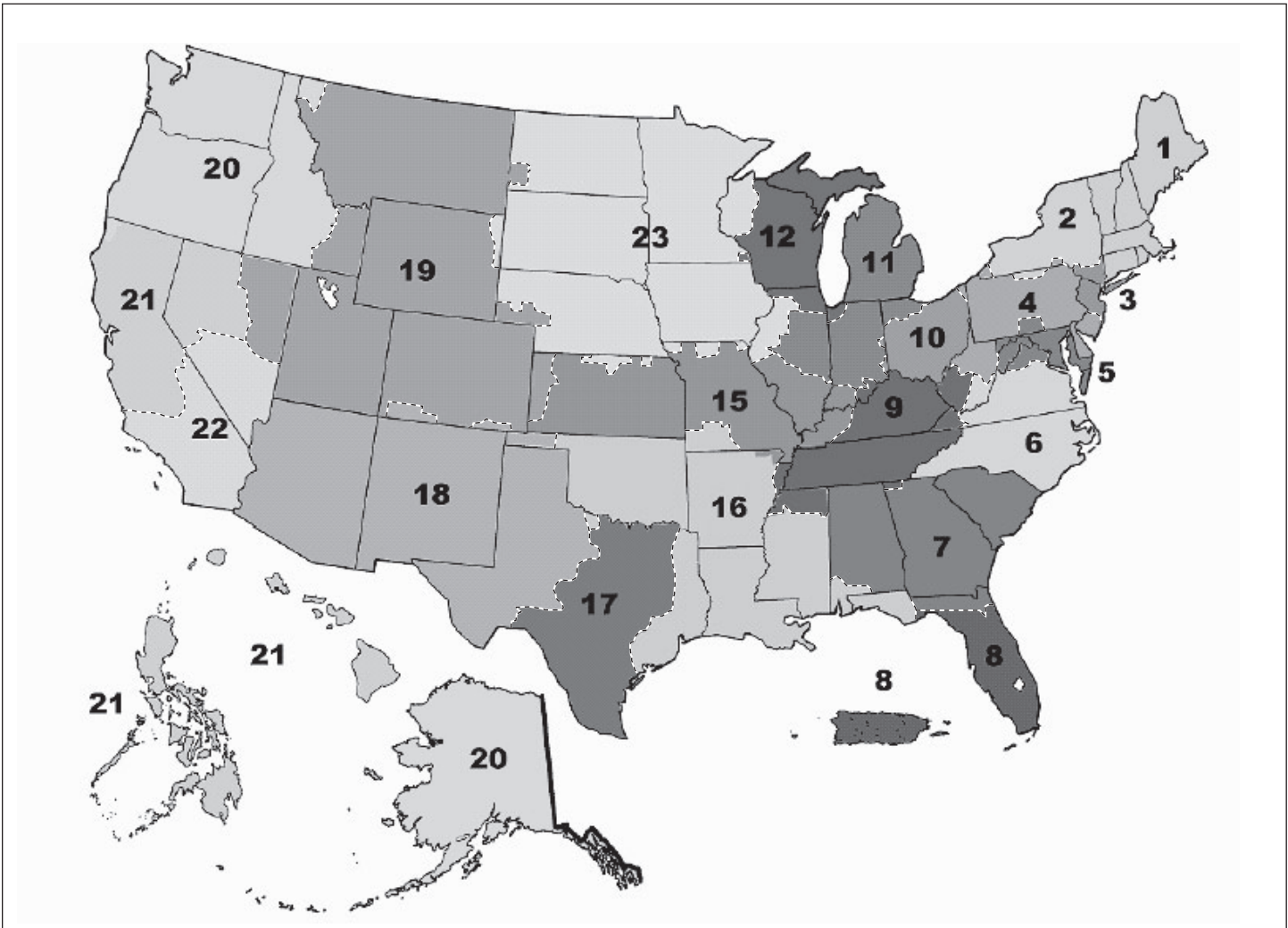
VHA is responsible for implementing the VA medical assistance programs. In fiscal year 2007, VHA operated more than 1,200 sites of care, including 155 medical centers, 135 nursing homes, 717 ambulatory care and community-based outpatient clinics, and 209 Readjustment Counseling Centers. VHA health care centers provide a broad range of primary care, specialized care, and related medical and social support services. The number of patients treated increased by 47.4 percent from 3.8 million in 2000 to nearly 5.6 million in 2007 due to an increased number of veterans eligible to receive care.

As shown in figure 1, VHA has organized its health care centers under 21 Veterans Integrated Service Networks (VISN),⁶ which oversee the operations of the various medical centers and treatment facilities within their assigned geographic areas.

During fiscal year 2007, these networks provided more medical services to a greater number of veterans than at any time during VA's long history.

⁶VISNs 13 and 14 were consolidated and designated VISN 23.

Figure 1: Veterans Integrated Service Networks (VISN)



- | | | |
|---|--|---|
| 1. VA New England Healthcare System | 8. VA Sunshine Healthcare Network | 17. VA Heart of Texas Health Care Network |
| 2. VA Healthcare Network Upstate New York | 9. VA Mid South Healthcare Network | 18. VA Southwest Health Care Network |
| 3. VA NY/NJ Veterans Healthcare Network | 10. VA Healthcare System of Ohio | 19. Rocky Mountain Network |
| 4. VA Stars & Stripes Healthcare Network | 11. Veterans in Partnership | 20. Northwest Network |
| 5. VA Capitol Health Care Network | 12. VA Great Lakes Health Care System | 21. Sierra Pacific Network |
| 6. VA Mid-Atlantic Health Care Network | 15. VA Heartland Network | 22. Desert Pacific Healthcare Network |
| 7. The Southeast Network | 16. South Central VA Health Care Network | 23. VA Midwest Health Care Network |

Source: U.S. Department of Veterans Affairs.

VA Policies and Procedures on the Use of Miscellaneous Obligations

VA has used “Estimated Miscellaneous Obligation or Change in Obligation” (VA Form 4-1358) to record estimated obligations for goods and services for over 60 years. According to VA policy,⁷ miscellaneous obligations can be used to record obligations against appropriations for the procurement of a variety of goods and services, including fee-based medical, dental, and nursing services; non-VA hospitalization; nursing home care; beneficiary travel; and rent and utilities. The policy states that miscellaneous obligations should be used as obligation control documents when a formal purchase order or authorization is not required, and when necessary to record estimated obligations to be incurred by the subsequent issue of purchase orders. The policy also states that the use of miscellaneous obligations should be kept to an absolute minimum, consistent with sound financial management policies on the control of funds, and should only be used in cases where there was a bona fide need for the goods and services being procured.

In September 2006, VA policy for miscellaneous obligations was revised in an attempt to minimize the use of miscellaneous obligations as an obligation control document.⁸ The revision states that miscellaneous obligations should not be used as obligation control documents unless the head contracting official for the station has determined that a purchase order⁹ or contract will not be required. However, the policy provides that fiscal staff can use miscellaneous obligations as a tracking mechanism for obligations of variable quantity contracts,¹⁰ as well as for public utilities. In January 2008, VA issued interim guidance on the use of miscellaneous

⁷VA Office of Finance Directives, *VA Controller Policy, MP-4, Part V, Chapter 3, Section A, Paragraph 3A.02 – Estimated Miscellaneous Obligation or Change in Obligation (VA Form 4-1358)*, www.va.gov accessed on December 12, 2007.

⁸VA Office of Finance Bulletin 06GA1.05, *Revision to MP-4, Part V, Chapter 3, Section A, Paragraph 3A.02 – Estimated Miscellaneous Obligation or Change in Obligation (VA Form 4-1358)* (Sept. 29, 2006).

⁹A purchase order is written authorization for a supplier to ship products to an agency at a specified price. Purchase orders may be supported by an underlying contract or function as the sole legally binding document.

¹⁰In variable quantity contracts, the quantity of goods to be furnished or services to be performed may vary. Variations may be at the option of VA or the contractor. Under variable quantity contracts, normally no amount is obligated at the time the contract is signed. The order, which comes after the contract, obligates VA for goods or services and the obligation must be recorded for the exact amount, or a reasonable estimate of the order.

obligations; however, the guidance did not apply to the fiscal year 2007 miscellaneous obligations we reviewed.¹¹

In recent years VHA has attempted to improve its oversight of miscellaneous obligations. For example, VHA's Clinical Logistics Group created the IFCAP system database in April 2006 to analyze the use of miscellaneous obligations agencywide. The database is updated monthly and contains information on the miscellaneous obligations created monthly by the 21 VISN offices and their associated stations. VHA officials are using the IFCAP database to (1) analyze the number and dollar amounts of procurements being done using contracts and purchase cards, and recorded using miscellaneous obligations, and (2) identify the types of goods and services recorded as miscellaneous obligations. Prior to the creation of the IFCAP database, such information on the use of miscellaneous obligations nationwide was not readily available to VHA upper-level management.

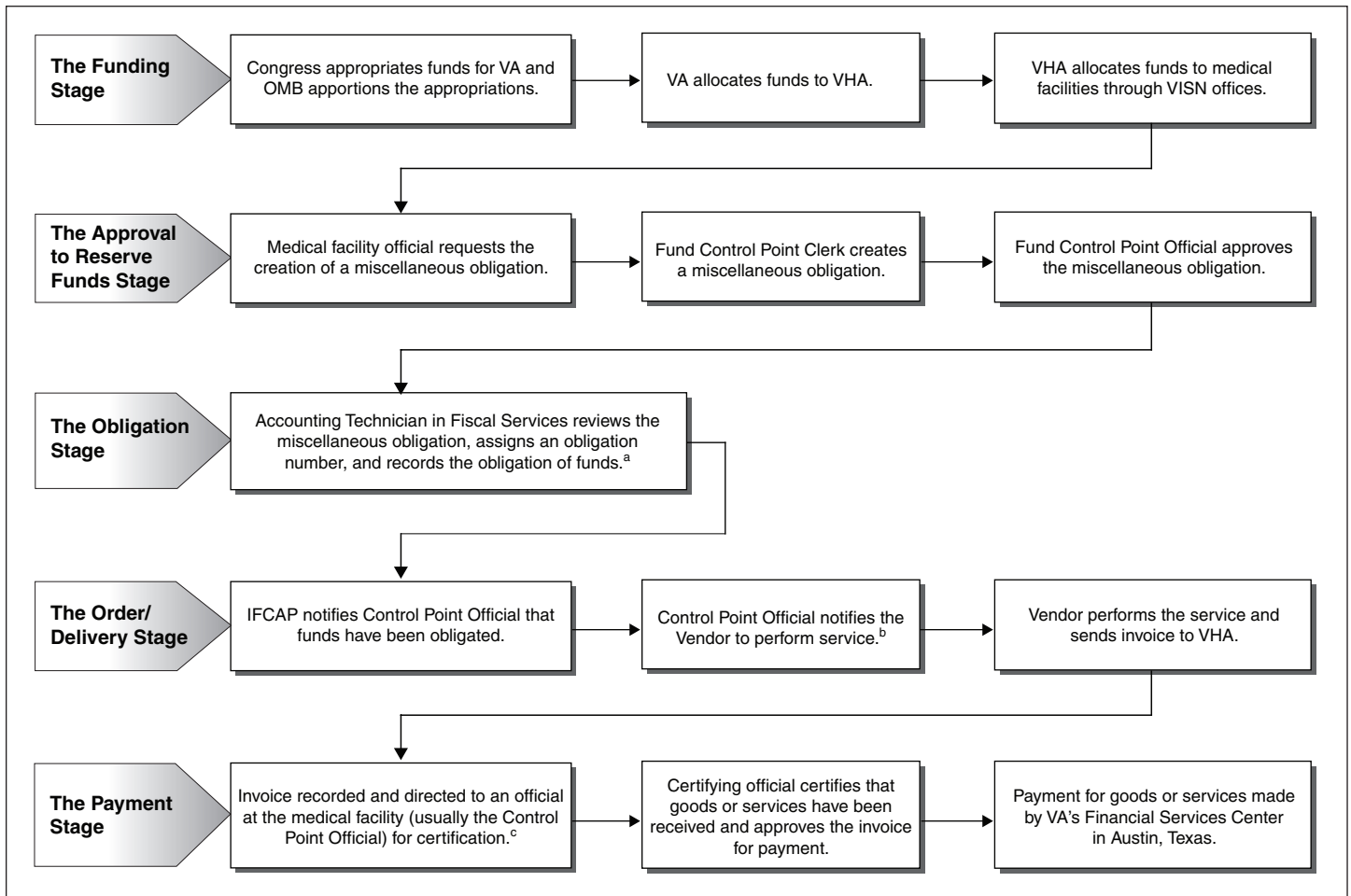
VHA's Current Miscellaneous Obligation Process

The creation and processing of miscellaneous obligations (VA Form 4-1358) is documented in IFCAP—a component of VA's Veterans Health Information System and Technology Architecture (VISTA). The miscellaneous obligation request passes through several stages illustrated in figure 2.¹²

¹¹Department of Veterans Affairs Memorandum, *Interim Guidance on Miscellaneous Obligations, VA Form 4-1358* (Jan. 30, 2008).

¹²Further details on processes in place are described in VA's *Integrated Funds Distribution Control Point Activity, Account and Procurement (IFCAP) PPM Accountable Officer User's Guide, Version 5.1* (May 2007).

Figure 2: VA's Miscellaneous Obligation Process



Source: GAO analysis of VA policy and procedures.

^aIn many transactions, the amount recorded reflects an administrative reservation of funds for which no obligations have yet been incurred.

^bOur review did not include the processes VHA officials may use to incur legal obligations, such as by issuing purchase orders or delivery orders.

^cA different payment process is followed for fee-based medical, dental and nursing services.

Miscellaneous Obligations Used Extensively for Mission-Related Activities in Fiscal Year 2007

The IFCAP database shows that in fiscal year 2007 nearly 132,000 miscellaneous obligations, with a total value of nearly \$9.8 billion, were created (see table 1). While VA's Central Office had \$2.9 billion in miscellaneous obligations during fiscal year 2007, our review focused on the \$6.9 billion in miscellaneous obligations used by VHA's 129 stations,¹³ located in every VISN throughout the country, for a variety of mission-related activities. (See app. III for a list of the uses of miscellaneous obligations by VISN, and app. IV for a list of the uses of miscellaneous obligations by station).

Table 1: Miscellaneous Obligations at VHA and VA for Fiscal Year 2007

(Dollars in billions)

VISN name	Number of miscellaneous obligations	Dollar amount of miscellaneous obligations	Percentage of total dollar value
VHA ^a	127,070	\$6.9	70%
VA's Central Office ^b	4,839	2.9	30%
Total	131,909	\$9.8	100%

Source: GAO analysis of IFCAP data.

^aIncludes miscellaneous obligations for VISNs 1-12 and 15-23 (VISNs 13 and 14 were consolidated and designated VISN 23).

^bVA's Central Office (VISN 0) is responsible for the administration of the Consolidated Mail Outpatient Pharmacy (CMOP) initiative that provides mail order prescriptions to veterans using automated distribution centers located throughout the country. In fiscal year 2007, VISN 0 obligated about \$2.08 billion in miscellaneous obligations for drugs, medicines, and other supplies, and almost \$800 million for various fee-based medical, dental, and other services.

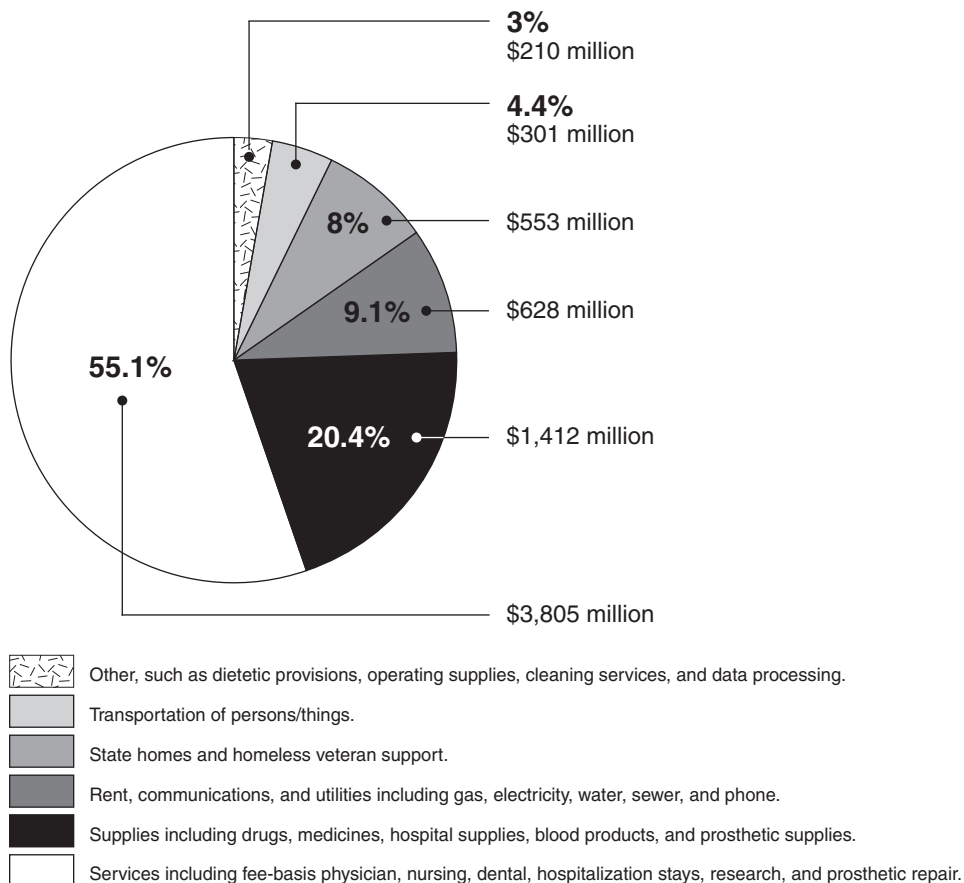
According to available VHA data, VHA used miscellaneous obligations to record estimated obligations of over \$6.9 billion for mission-related goods and services. As shown in figure 3, about \$3.8 billion (55.1 percent) was for fee-based medical and dental services for veterans, and another \$1.4 billion (20.4 percent) was for drugs, medicines, and hospital supplies. The remainder was for, among other things, state veterans homes,¹⁴ transportation of veterans to and from medical centers for treatment, and

¹³The IFCAP database included 129 VHA stations. A VHA station may include more than one medical center.

¹⁴State veterans homes are established by individual states and approved by VA for the care of disabled veterans. The homes include facilities for domiciliary nursing home care and adult day health care.

logistical support and facility maintenance for VHA medical centers nationwide.

Figure 3: VHA Miscellaneous Obligations for Fiscal Year 2007



Source: GAO analysis of VHA data.

According to VHA contracting and fiscal service officials, using miscellaneous obligations tends to reduce administrative workload and facilitates the payment for contracted goods and services, including drugs, medicines, and transportation, and for goods and services for which no preexisting contracts exist, such as fee-basis medical and dental services and utilities.

VHA officials stated that miscellaneous obligations facilitate the payment for contracted goods and services when the quantities and delivery dates are not known. A miscellaneous obligation can be created for an estimated

amount and then modified as specific quantities are needed or specific delivery dates are set. When a purchase order is created, however, the obligated amount cannot be changed without a modification of the purchase order. According to VHA officials, the need to prepare numerous modifications to purchase orders could place an undue burden on the limited contracting personnel available at individual centers and could also require additional work on the part of fiscal services personnel.

VHA officials stated that the use of miscellaneous obligations can simplify the procurement process when no preexisting contract or purchase order exists. For example, providing medical care on a fee-basis to veterans outside of VHA medical centers may involve the services of thousands of private physicians nationwide. Attempting to negotiate a separate agreement or contract with each of these individuals would be a difficult task for VHA's contracting staff. Under the policies and procedures in place during fiscal year 2007, VHA centers could use miscellaneous obligations as umbrella authorizations for fee-based medical services performed by a number of different physicians. In effect, in cases for which there is no preexisting contract, the miscellaneous obligation form becomes the record of an obligation.¹⁵ However, use of miscellaneous obligations may also increase the risk of fraud, waste, and abuse. Consequently, mitigating controls must be designed to help compensate for the lack of a negotiated contract. Absent contractual terms, one risk area is the authorized fee schedule for the medical services being provided. In this case, federal regulations call for payments to non-VA physicians for services associated with outpatient and inpatient care provided at non-VA facilities to be the lesser of the amount billed or the amount calculated using the formula developed by the Department of Health and Human Services under Medicare's participating physician fee schedule for the period in which the service is provided.¹⁶ However, we did not verify that VHA officials were properly following the fee schedule.

¹⁵In their comments on our draft report, VA officials said that this practice is consistent with 38 C.F.R. 17.52, which provides that infrequently used services, such as fee-basis services, may be initiated using individual authorizations. They said that individual authorizations for fee-basis care are not subject to procurement regulations, and that procurement regulations apply when the need for like medical services from the same medical provider is frequent enough to warrant the use of standard acquisition processes.

¹⁶38 C.F.R. 17.56.

Deficiencies in Design of Controls over Miscellaneous Obligations Increase the Risk of Fraud, Waste, and Abuse

VA policies and procedures were not designed to provide adequate controls over the use of miscellaneous obligations. According to our *Standards for Internal Control in the Federal Government*,¹⁷ agency management is responsible for developing detailed policies and procedures for internal control suitable for their agency's operations and ensuring that they provide for adequate monitoring by management, segregation of duties, and supporting documentation for the need to acquire specific goods in the quantities purchased. We identified control design flaws in each of these oversight areas, and we confirmed that these weaknesses existed at the three locations where we conducted case studies. Collectively, these control design flaws increase the risk of fraud, waste, and abuse (including employees converting government assets to their own use without detection). New guidance for the use of miscellaneous obligations was released in January 2008 and finalized in May 2008. We reviewed the new guidance and found that while it offered some improvement, it did not fully address the specific control design flaws we identified. Furthermore, VA officials told us that this guidance was not subject to any legal review. Such an analysis is essential to help ensure that the design of policies and procedures comply with all applicable federal appropriations law and internal control standards.

We reviewed 42 miscellaneous obligations at the three case study locations and developed illustrative, more detailed information on the extent and nature of these control design flaws. Table 2 summarizes the locations visited, the miscellaneous obligations reviewed at each location, and the extent and nature of control design deficiencies found.

¹⁷GAO, *Standards for Internal Control in the Federal Government*, [GAO/AIMD-00-21.3.1](#) (Washington, D.C.: November 1999).

Table 2: Summary of Case Study Results

Station	Number of obligations reviewed	Dollar value of obligations reviewed	No documented approval by contracting officials	Inadequate segregation of duties ^a	Inadequate supporting documentation		
					Incomplete purpose description ^b	Blank vendor field	Blank contract field ^c
Pittsburgh	14	\$6,694,853	14	9	3	6	3
Cheyenne	11	\$2,076,648	11	11	1	6	4
Kansas City ^d	17	\$27,274,395	17	10	4	8	9
Total	42	\$36,045,896	42	30	8	20	16

Source: GAO analysis of VHA data.

^aIn 30 of the 42 obligations we reviewed, one official performed two or more of the following functions: requesting, creating, approving, or obligating funds for the original miscellaneous obligations, or certifying delivery of goods and services and approving payment.

^bIn 8 of 42 instances, we could not determine the nature, timing, or the extent of the goods or services being procured from the description in the purpose field without reference to supporting invoices.

^cIn these instances, we confirmed that contracts existed, but no contract number was listed on the miscellaneous obligation document.

^dIncludes facilities located in Kansas City, Kansas; Wichita, Kansas; Columbia, Missouri; and eastern Kansas.

Inadequate Contracting Oversight of Miscellaneous Obligations

To help minimize the use of miscellaneous obligations, VA policy stated that miscellaneous obligations would not be used as obligation control documents unless the contracting authority for a station had determined that purchase orders or contracts would not be required. Furthermore, VA policy required review of miscellaneous obligations by contracting officials to help ensure proper use in accordance with federal acquisition regulations, but did not address the intended extent and nature of these reviews or how the reviews should be documented. Contracting officials were unable to electronically document their review of miscellaneous obligations and no manual documentation procedures had been developed. Our review of 42 miscellaneous obligations prepared at three VHA stations showed that contracting officers were at times familiar with specific miscellaneous obligations at their facilities, but that they had no documented approvals available for review. Furthermore, none of the three sites we visited had procedures in place to document review of the miscellaneous obligations by the appropriate contracting authorities.

Effective oversight and review by trained, qualified officials is a key factor in identifying a potential risk for fraud, waste, or abuse. Without control procedures to help ensure that contracting personnel review and approve miscellaneous obligations prior to their creation, VHA is at risk that

procurements will not have safeguards established through a contract approach. For example, in our case study at the VA Pittsburgh Medical Center, we found 12 miscellaneous obligations, totaling about \$673,000, used to pay for laboratory services provided by the University of Pittsburgh Medical Center (UPMC). The Chief of Acquisition and Materiel Management for the VA Pittsburgh Medical Center stated that she was not aware of the UPMC's laboratory testing service procurements and would review these testing services to determine whether a contract should be established for these procurements. Subsequently, she stated that VISN 4, which includes the VA Pittsburgh Medical Center, was going to revise procedures to procure laboratory testing services through purchase orders backed by reviewed and competitively awarded contracts, instead of funding them through miscellaneous obligations.

Another Pittsburgh miscellaneous obligation for about \$141,000 was used to fund the procurement of livers for transplant patients. Local officials said that there was a national contract for the services, and that livers were provided at a standardized price of \$21,800. However, officials could not provide us with a copy of the contract, nor documentation of the standardized pricing schedule. Therefore, we could not confirm that VHA was properly billed for these services or that the procurement was properly authorized.

Furthermore, in the absence of review by contracting officials, controls were not designed to prevent miscellaneous obligations from being used for unauthorized purposes, or for assets that could be readily converted to personal use. Our analysis of the IFCAP database for fiscal year 2007 identified 145 miscellaneous obligations for over \$30.2 million that appeared to be used in the procurement of such items as passenger vehicles; furniture and fixtures; office equipment; and medical, dental, and scientific equipment. Although VA's miscellaneous obligation policy did not address this issue, VA officials stated that acquisition of such assets should be done by contracting officials and not through miscellaneous obligations. Without adequate controls to review miscellaneous obligations and prevent them from being used for the acquisition of such assets, it is possible that VHA may be exposing the agency to unnecessary risks by using miscellaneous obligations to fund the acquisitions of goods or services that should have been obtained under contract with conventional controls built in.

Inadequate Segregation of Duties

One tenet of an effectively designed control system is that key duties and responsibilities need to be divided or segregated among different people to reduce the risk of error or fraud.¹⁸ These controls should include separating the responsibilities for authorizing transactions, processing and recording them, reviewing the transactions, and accepting any acquired assets. The basic principle is that no one individual should be permitted to control all key aspects of a transaction or event, such as acquiring a good or service.

However, IFCAP control design allows a single official to perform multiple key roles in the process of creating and executing miscellaneous obligations, and VA policies and procedures do not specifically prohibit this practice. Control point officials are authorized to create, edit, and approve requests for miscellaneous obligations. In addition, these same individuals can certify the delivery of goods and services and approve payment. Such weak control design could enable a VHA employee to convert VHA assets to his or her own use, without detection (such as the personal property acquired through the use of miscellaneous obligations described in the previous section).

Our review of the previously mentioned 42 miscellaneous obligations at three case study locations indicated that controls in place at these locations were not designed to ensure sufficient segregation of duties for procurements. Specifically, as noted in table 3, we found inadequate segregation of key duties in 30 of the 42 obligations we reviewed. In these instances, controls were not designed to prevent one official from performing two or more of the following key functions: (1) requesting the miscellaneous obligation, (2) approving the miscellaneous obligation, (3) recording the obligation of funds, or (4) certifying delivery of goods and services and approving payment.

¹⁸GAO, *Standards for Internal Control in the Federal Government*, [GAO/AIMD-00-21.3.1](#) (Washington, D.C.: November 1999).

Table 3: Case Study Analysis of Segregation of Duties

Number of functions performed by agency officials^a	Obligations
One official performed two out of the four functions	15
One official performed three out of the four functions	13
One official performed all four functions	2
Subtotal--inadequate segregation of duties	30
Adequate segregation of duties--different officials performed each of the four functions	12
Total	42

Source: GAO analysis.

^aAgency officials performed various combinations of the following four functions: (1) requesting the miscellaneous obligation, (2) approving the miscellaneous obligation, (3) obligating funds, and (4) certifying receipt of goods and services and approving payment.

As noted in table 3, in 13 of the 42 obligations we examined, the same official performed three of the four functions. In 11 of these cases, the same official requested and approved the miscellaneous obligations, and then certified receipt of goods and services. For example, in one case in Pittsburgh, one official requested and approved a miscellaneous obligation of over \$140,000 for medical services and then certified receipt and approved payment for at least \$43,000 of those services. In another case in Cheyenne, we found one miscellaneous obligation for utilities where one official requested, approved, and certified receipt and approved payment of over \$103,000 in services.

In two instances in Cheyenne involving employee grievance settlements for about \$22,000, one official performed all four functions. While our review found that these obligations were for legitimate purposes, the fact that one official was able to perform multiple functions is indicative of an inherent control system flaw. One individual, controlling all of the key stages of the transaction, leaves VHA vulnerable to potential fraud, waste, or abuse because of the opportunity for the creation of inappropriate, perhaps fraudulent, transactions.

The VA OIG noted a similar problem in its review of the alleged mismanagement of funds at the VA Boston Healthcare System.¹⁹ According

¹⁹Department of Veterans Affairs, Office of Inspector General, *Audit of Alleged Mismanagement of Government Funds at the VA Boston Healthcare System*, Report No. 06-00931-139 (Washington, D.C.: May 31, 2007).

to OIG officials, they obtained documents showing that a miscellaneous obligation was used to obligate \$200,000, and was requested, approved, and obligated by the same fiscal official. The OIG officials said that this transaction called into question the adequacy of segregation of duty controls over funds obligated through miscellaneous obligations.

Similarly, a July 2007 report by an independent public accountant (IPA) also found, among other things, the segregation of duties for VA's miscellaneous obligation process was inadequate.²⁰ The report noted that control point officials at a VISN, VA's Central Office, and two medical centers had the ability to act as the requestor and approving official for the same transaction. This condition was observed at four of the six locations the IPA reviewed. The IPA recommended that the medical centers update their local policies to prevent control point officials from acting both as requestor and approving official on the same transaction. Similarly, in 23 of the 42 miscellaneous obligations we reviewed in our case studies, the same individual served as both the requestor and approving official for a miscellaneous obligation.²¹

Lack of Adequate Supporting Documentation

Another tenet of an effectively designed control system is that all transactions need to be clearly documented and all documentation and records should be properly managed and maintained.²² Adequate documentation is essential to support an effective funds control system; is crucial in helping to ensure that a procurement represents a bona fide need; and reduces the risk of fraud, waste, and abuse. When a legal obligation is recorded, it must be supported by adequate documentary evidence of the liability.²³ An agency should use its best estimate to reserve an amount for future obligation when the amount of the government's final liability is undefined. Further, the basis for the estimate and the computation must be documented. Although VA's form entitled "Estimated Miscellaneous Obligation or Change in Obligation" (VA Form 4-1358)

²⁰Grant Thornton, *Department of Veterans Affairs, OMB Circular A-123, Appendix A – Findings and Recommendations Report (Procurement Management)* (July 18, 2007).

²¹In 8 of the 23 cases, one official requested and approved a miscellaneous obligation. For the remaining 15 cases, one official performed those two tasks plus one or more other key tasks, such as recording the obligation of funds and certifying receipt of goods and services and approving payment.

²²GAO, *Standards for Internal Control in the Federal Government*, [GAO/AIMD-00-21.3.1](#) (Washington, D.C.: November 1999).

²³31 U.S.C. §1501(a).

includes three key fields—the purpose, vendor, and contract number fields—that provide crucial supporting documentation for the obligation, VA policies and procedures were not sufficiently detailed to specifically require this type of information needed to adequately document miscellaneous obligations. During the period covered by our review, VA did not have specific guidance as to what information should be included in the purpose field, including such essential data as the nature and extent of the transaction. Further, during our case studies, we found many instances where these fields on the miscellaneous obligation form were left blank or did not provide adequate information as a result of this control design flaw.

Specifically, in our case studies, we found that these control design flaws resulted in the purpose field on 8 of the 42 miscellaneous obligations having insufficient data to determine whether the miscellaneous obligation represented a bona fide need. In many instances, while the stated purposes may have been adequate for the requesters and approving officials in the using services, this level of documentation was not sufficient for an independent reviewer to determine from the purpose field what items were procured and whether the appropriate budget object code was charged. As a result of these deficiencies in the design of controls, in several cases we had to rely on invoices to determine the probable purpose of the miscellaneous obligation and whether it represented a bona fide need. For example, in Kansas City, we found one miscellaneous obligation for over \$1.3 million whose purpose was listed as "To obligate funds for the Oct 06 payment," while the associated invoices showed that the miscellaneous obligation was used to cover the services of medical resident staff. In another instance, we found a miscellaneous obligation for over \$53,000 whose purpose was listed as "October billing," while the associated invoices showed that the miscellaneous obligation was used for automated prescription services provided at the Kansas Soldiers Home in October 2007. In another case in Pittsburgh, we found a miscellaneous obligation for over \$45,000 whose purpose was listed as "LABCORP 5/1-5/31/07," while the associated invoices showed that the obligation was for laboratory testing services. Without procedures calling for more definitive descriptions of the purpose, we could not confirm that these miscellaneous obligations were for bona fide needs or that the invoices reflected a legitimate use of federal funds.

Although appropriation law provides that the basis for the amount obligated should be documented, we found deficient VA control design resulted in several miscellaneous obligations at one location with inadequate support for the recorded obligations.²⁴ For example, according to our analysis of the IFCAP database, 12 miscellaneous obligations, totaling almost \$1.3 million, were created using no-year funds²⁵ by the VA Pittsburgh Medical Center on September 28, 2007, to support the St. Clairsville community-based outpatient clinic. One miscellaneous obligation for \$106,400 covered March 2008 services, and another miscellaneous obligation for \$108,400 covered April 2008 clinic services. The purpose fields for the two miscellaneous obligations did not provide an explanation of how the estimates were calculated. When asked, medical center officials stated that the estimates were based on historical trends or calculations, but they did not provide any documentation to support the estimates. Furthermore, established control procedures did not require them to do so. In another instance, the VA Kansas City Medical Center obligated \$200,000 for “patient care services at the Kirksville community-based outpatient clinic from 10/01/06 to 12/31/06.” The purpose field did not provide an explanation of how the estimate was calculated.

Further, in the absence of explicit documentation requirements, data fields were left blank on a number of the miscellaneous obligations we examined. For example, the vendor field was left blank in 20 of the 42 miscellaneous obligations we reviewed. Current VA guidance states that the vendor field is to be left blank when multiple vendors exist since the IFCAP system allows only one vendor to be listed; however, we observed several cases where the field was left blank even when there was only one vendor. For example, in Kansas City we found obligations for electricity and natural gas where historically only one vendor had been used, but the vendor field was left blank. Similarly, in Kansas City another miscellaneous obligation was used in the procurement of \$8.6 million in services at the Warrensburg Veteran’s Home in Warrensburg, Missouri, but the vendor field was left blank. While payment was made to the vendor that invoiced VA in these instances, leaving the vendor field blank poses several problems for agency management, including establishing that the

²⁴GAO, *Principles of Federal Appropriations Law: Third Edition, Volume II*, [GAO-06-382SP](#) (Washington, D.C.: Feb. 1, 2006).

²⁵No-year funds are appropriations for which budget authority remains available for obligation for an indefinite period of time. A no-year appropriation is usually identified by language such as “to remain available until expended.”

vendor is appropriate for the purpose of the miscellaneous obligation and verifying that the correct, authorized vendor is paid.

We also found that the contract number field was left blank in 16 of the 42 miscellaneous obligations reviewed, even though supporting contracts did exist for these miscellaneous obligations. VA guidance did not require that the contract number be included in order to process the miscellaneous obligation. However, missing contract numbers make it difficult to determine whether VA is receiving the appropriate type and quantity of goods and services at the correct price.

Inadequate control requirements for supporting documentation and completing data fields concerning the purpose of the obligation, vendor information, and contract numbers can hinder oversight by senior VA management officials. The Deputy Assistant Secretary for Logistics and Acquisition²⁶ said that he and other VHA officials use the IFCAP database to monitor the extent and nature of miscellaneous obligations nationwide, including analyzing the number and dollar amounts of miscellaneous obligations and identifying the types of goods and services procured using miscellaneous obligations. He told us that he was concerned with the extent and nature of the use of miscellaneous obligations at VA, that he lacked adequate oversight or control over procurements made through miscellaneous obligations, and that he often did not know what was being bought or who it was being bought from. Our analysis of the IFCAP database found that over 88,000 (69 percent) of 127,070 miscellaneous obligations did not include vendor information, accounting for over \$5 billion of the \$6.9 billion in recorded miscellaneous obligations in fiscal year 2007. Similarly, the IFCAP database did not contain a description of what was purchased or information on the quantities purchased. As a result, important management information was not available to senior VA procurement officials.

²⁶This official acts as VA's Senior Procurement Executive and oversees the development and implementation of policies and procedures for departmentwide acquisition and logistics programs supporting all VA facilities.

Interim Guidance Does Not Address All Control Weaknesses

In January 2008, VHA issued interim guidance effective for all miscellaneous obligations created after January 30, 2008, concerning required procedures for using miscellaneous obligations.²⁷ The guidance provides that prior to creating a miscellaneous obligation, fiscal service staff are required to check with the contracting activity to ensure that a valid contract is associated with the miscellaneous obligation, except in specific, itemized cases. Under this guidance, the using service is to have the contracting activity determine (1) if a valid procurement authority exists, (2) if a procurement needs to be initiated, and (3) the appropriate method of obligation. Also, this guidance requires that a copy of the head contracting official's approval be kept with a copy of the miscellaneous obligation for future audit purposes. In addition, the guidance provides that the fiscal service may not create a miscellaneous obligation without appropriate information recorded in the purpose, vendor, and contract number fields on the document. The guidance specifically cites a number of invalid uses for miscellaneous obligations, including contract ambulance, lab tests, blood products, and construction, but did not always specify a procurement process to be used for these items.

In May 2008, VHA management finalized the interim guidance.²⁸ This guidance represents a step in the right direction. It includes a manual process for documenting contracting approval of miscellaneous obligations and specifically states that a miscellaneous obligation cannot be created if the purpose, vendor, and contract number fields are incomplete. However, the new guidance does not address the segregation of duties issues we and others have identified and does not establish an oversight mechanism to ensure that control procedures outlined are properly implemented.

In our view, VHA has missed an opportunity to obtain an important legal perspective on this matter. According to VA officials, these policies have not been subject to any legal review, which is essential in ensuring that the policies and procedures comply with federal funds control laws and regulations and any other relevant VA policies or procedures dealing with budgetary or procurement matters. For example, such a review would help ensure that the guidance adequately addresses Federal Acquisition

²⁷Department of Veterans Affairs Memorandum, *Interim Guidance on Miscellaneous Obligations*, VA Form 4-1358 (Jan. 30, 2008).

²⁸Department of Veterans Affairs, Memorandum, *Revised Guidance for Processing of Miscellaneous Obligations*, VA Form 4-1358 (May 18, 2008).

Regulation, requiring that no contract shall be entered into unless the contracting officer ensures that all requirements of law, executive orders, regulations, and all other applicable procedures, including clearances and approvals, have been met.²⁹ In addition, a legal review could help to ensure that this guidance (1) provides that all legal obligations of VA are supported by adequate documentation to meet the requirements of the recording statute 31 U.S.C. §1501(a) and (2) prevents any individual from committing the government for purchases of supplies, equipment, or services without being delegated contracting authority as a contracting officer, purchase card holder, or a designated representative of a contracting officer.³⁰ The absence of a legal review to determine the propriety of VA's miscellaneous obligations policies and procedures places VA at risk of not complying with important laws and regulations.

Conclusions

Without basic controls in place over billions of dollars in miscellaneous obligations, VA is at significant risk of fraud, waste, and abuse. Effectively designed internal controls serve as the first line of defense for preventing and detecting fraud, and they help ensure that an agency effectively and efficiently meets its missions, goals, and objectives; complies with laws and regulations; and is able to provide reliable financial and other information concerning its programs, operations, and activities. Although miscellaneous obligations can facilitate and streamline the procurement process, they require effectively designed mitigating controls to avoid impairing full accountability and transparency. In the absence of effectively designed key funds and acquisition controls, VA has limited assurance that its use of miscellaneous obligations is kept to a minimum, for bona fide needs, in the correct amounts, and to the correct vendors. Improved controls in the form of detailed policies and procedures, along with a management oversight mechanism, will be critical to reducing the government's risks from VA's use of miscellaneous obligations.

Recommendations for Executive Action

In order for VA to reduce the risks associated with the use of miscellaneous obligations, we recommend that the Secretary of Veterans Affairs, in conjunction with VA's Office of General Counsel, develop and implement policies and procedures consistent with federal appropriations law and internal control standards that

²⁹ 48 C.F.R. 1.602-1 (b).

³⁰ 48 C.F.R. 801.601 (b).

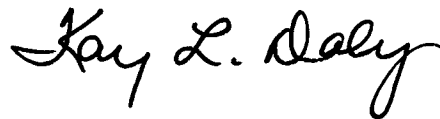
-
- establish a process for the review of miscellaneous obligations by contracting officials, including requiring appropriate documentation that the review has occurred;
 - segregate duties for (1) creating, approving, and recording miscellaneous obligations; (2) the certification and payment of invoices; and (3) the receipt of the resulting goods or services;
 - document the purposes, vendors, and contract numbers of miscellaneous obligations; and
 - establish an oversight mechanism to ensure that these control policies and procedures are fully and effectively implemented.

Agency Comments and Our Evaluation

We received written comments on a draft of this report from the Deputy Secretary of Veterans Affairs, which are reprinted in appendix II. VA concurred with our recommendations and identified specific actions it plans to take to implement these recommendations. For example, VA commented it plans to include electronic approval requirements of miscellaneous obligations by contracting officials in the financial component of its new accounting system. Also, VA commented it plans to address the segregation of duties issues identified in our report in an upcoming VA Office of Finance Bulletin, and that VA policy now requires documentation of the purpose, vendor, and contract number for all miscellaneous obligations. Finally, VA commented it plans to implement reporting and auditing processes to help ensure that the internal control procedures are properly implemented agencywide. If effectively implemented, these planned actions should enable VHA to substantially resolve the deficiencies pointed out in our report. VA also provided technical comments which we considered and incorporated as appropriate.

We are sending copies of this report to other interested congressional committees and to affected federal agencies. Copies of this report will also be made available to others upon request. In addition, this report is available at no charge on the GAO Web site at <http://www.gao.gov>.

If you or your staff have any questions regarding this report, please contact me at (202) 512-9095 or at dalykl@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made major contributions to this report are listed in appendix V.

A handwritten signature in black ink that reads "Kay L. Daly". The signature is written in a cursive, flowing style.

Kay L. Daly
Acting Director, Financial Management and Assurance

Appendix I: Scope and Methodology

In order to determine how VHA used miscellaneous obligations during fiscal year 2007, we obtained and analyzed a copy of VHA's Integrated Funds Distribution, Control Point Activity, Accounting and Procurement (IFCAP) database of miscellaneous obligations for that year. IFCAP is used to create miscellaneous obligations (VA Form 4-1358) at VA, and serves as a feeder system for VA's Financial Management System (FMS)—the department's financial reporting system of record. According to VA officials, FMS cannot be used to identify the universe of miscellaneous obligations at VHA in fiscal year 2007 because FMS does not identify the procurement method used for transactions (i.e., miscellaneous obligation, purchase card, purchase order). Furthermore, FMS does not capture the contract number, requester, approving official, and obligating official for obligations. However, according to senior agency officials, the IFCAP database is the most complete record of miscellaneous obligations available at VHA and can be used to provide an assessment of how miscellaneous obligations were used during fiscal year 2007.

IFCAP's data included information on the appropriation codes, vendors, budget object codes (BOC), date and amount of obligations, obligation numbers, approving officials, and VISN and VHA stations for VHA miscellaneous obligations. We converted the database to a spreadsheet format and sorted the data by VISN, station, and BOC to determine where and how miscellaneous obligations were used in fiscal year 2007 (See app. III and IV.)

To determine whether VHA's policies and procedures are designed to provide adequate controls over the use of miscellaneous obligations, we first reviewed VHA's policies and procedures governing the use of miscellaneous obligations at VA. Specifically, we reviewed the *VA Controller Policy, MP-4, Part V, Chapter 3, Section A, Paragraph 3A.02 – Estimated Miscellaneous Obligation or Change in Obligation (VA Form 4-1358)*; the VA Office of Finance Bulletin 06GA1.05, *Revision to MP-4, Part V, Chapter 3, Section A, Paragraph 3A.02 – Estimated Miscellaneous Obligation or Change in Obligation (VA Form 4-1358)*, dated September 29, 2006; VA *Interim Guidance on Miscellaneous Obligations, VA Form 1358*, dated January 30, 2008; VHA *Revised Guidance for Processing of Miscellaneous Obligations, VA Form 1358*, dated May 18, 2008; and other VA and VHA directives, policies, and procedures. We also used relevant sections of the Federal Acquisition Regulation (FAR); VA's Acquisition Regulation; appropriations law; and our *Standards for Internal Control in the Federal Government* in assessing the design of VA's policies and procedures. We met with VA and VHA officials in Washington, D.C., and coordinated with VHA's Office of

Inspector General staff to identify any previous audit findings relevant to our audit work. In addition, we interviewed representatives of VA's independent public accounting firm and reviewed copies of their reports.

In order to better understand the extent and nature of VA policy and procedure design deficiencies related to miscellaneous obligations, we conducted case studies at three VHA stations in Cheyenne, Wyoming; Kansas City, Missouri; and Pittsburgh, Pennsylvania.¹ The stations in Kansas City and Pittsburgh were selected because they had a high volume of miscellaneous obligation activity, and they were located in different regions of the country. We conducted field work at the Cheyenne, Wyoming, station during the design phase of our review to better understand the extent and nature of miscellaneous obligation control design deficiencies at a small medical center. Inclusion of the Cheyenne facility in our review increased the geographic diversity of our analysis and allowed us to compare the extent and nature of miscellaneous obligation design deficiencies at medical centers in the eastern, midwestern, and western portions of the United States.

During the case studies, we met with senior medical center administrative, procurement, and financial management officials to discuss how VA policies and procedures were designed with regard to specific obligations, and assess the control environment design for using miscellaneous obligations at the local level. We discussed how miscellaneous obligations were used as part of the procurement process and the effect of new VHA guidance on medical center operations. We also reviewed the design of local policies and procedures for executing miscellaneous obligations and conducted walkthroughs of the processes.

To provide more detailed information on the extent and nature of the control design deficiencies we found at our case study locations, we identified a nongeneralizable sample of obligations for further review at each site. Through data mining techniques, we identified a total of 42 miscellaneous obligations for more detailed examination at our case study sites: 11 from Cheyenne, 17 from Kansas City, and 14 from Pittsburgh. We based our selection on the nature, dollar amount, date, and other identifying characteristics of the obligations. For each miscellaneous

¹We visited the Cheyenne VA Medical Center in Cheyenne, Wyoming; the Kansas City VA Medical Center in Kansas City, Missouri; and the VA Pittsburgh Healthcare System, H. John Heinz III Progressive Care Center, in Pittsburgh, Pennsylvania.

obligation selected, we accumulated information on the extent and nature of control design weaknesses in the areas of

- review and documentation by contracting officials;
- segregation of duties during the procurement process; and
- the purpose, timing, and documentation of obligations.

Concerning the adequacy of control design with respect to contracting review, we reviewed miscellaneous obligations for evidence of review by contracting officials and, for selected miscellaneous obligations, followed up with contracting officials to discuss contracts in place for miscellaneous obligations, whether review by contracting officials was needed, and when and how this review could occur and be documented.

Concerning the control design deficiencies with respect to segregation of duties, we reviewed miscellaneous obligation documents to determine which officials requested, approved, and obligated funds for the original miscellaneous obligations and then which officials certified delivery of goods and services and approved payment. We noted those instances where control design deficiencies permitted one official to perform multiple functions.

With respect to control design deficiencies relating to the supporting documentation for the miscellaneous obligations, we reviewed the purpose, vendor, and contract number fields for each obligation. For the purpose field, we assessed whether the required description was adequate to determine the nature, timing, and extent of the goods or services being procured and whether controls provided for an adequate explanation for any estimated miscellaneous obligation amounts. For the vendor and contract number fields, we assessed whether controls were designed to ensure entered information was complete, and we identified those instances where control deficiencies permitted fields to be left blank.

Because of time limitations, we did not review VHA's procurement or service authorization processes. In addition, in our case study approach, we were unable to analyze a sufficient number of obligations to allow us to generalize our conclusions to the sites visited, nor to the universe of VHA medical centers. The 42 obligations represented a total of approximately \$36.0 million; however, the results cannot be projected to the overall population of miscellaneous obligations in fiscal year 2007. While we found no examples of fraudulent or otherwise improper purchases made by VHA, our work was not specifically designed to identify such cases or estimate their full extent.

**Data Reliability
Assessment**

We assessed the reliability of the IFCAP data provided by (1) performing various tests on required data elements, (2) reviewing related policies and procedures, (3) performing walkthroughs of the system, (4) interviewing VA officials knowledgeable about the data, and (5) tracing selected transactions from source documents to the database. In addition, we verified that totals from the fiscal year 2007 IFCAP database agreed with a method of procurement compliance report provided by VA. We did not reconcile the IFCAP miscellaneous obligations reported to us to FMS—the VA system of record—and published VA financial statements because FMS does not identify the procurement method used for transactions (i.e., miscellaneous obligations, purchase card, purchase order). We determined that the data were sufficiently reliable for the purposes of our report and that the data can be used to provide an assessment of how miscellaneous obligations were used during fiscal year 2007.

We conducted this audit from November 2007 through July 2008 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. We requested comments on a draft of this report from the Secretary of Veterans Affairs or his designee. We received written comments from the Deputy Secretary of Veterans Affairs, which are reprinted in appendix II.

Appendix II: Comments from the Department of Veterans Affairs



THE DEPUTY SECRETARY OF VETERANS AFFAIRS
WASHINGTON

August 19, 2008

Ms. Kay Daly
Acting Director
Financial Management and Assurance
U. S. Government Accountability Office
441 G Street, NW
Washington, DC 20548

Dear Ms. Daly:

The Department of Veterans Affairs (VA) has reviewed the draft report, **VETERANS HEALTH ADMINISTRATION: Improvements Needed in Design of Controls over Miscellaneous Obligations** (GAO-08-976), and concurs with the recommendations.

The enclosures address GAO's recommendations and provide technical comments to the draft report. VA appreciates the opportunity to comment on the draft report.

Sincerely yours,

A handwritten signature in black ink, appearing to read "Gordon H. Mansfield".

Gordon H. Mansfield

Enclosures

Enclosure

Department of Veterans Affairs (VA) Comments to
Government Accountability Office (GAO) Draft Report
***VETERANS HEALTH ADMINISTRATION: Improvements Needed in Design
of Controls over Miscellaneous Obligations***
(GAO-08-976)

Recommendation 1: Establish a process for the review of miscellaneous obligations by contracting officials, including requiring appropriate documentation that the review has occurred.

Concur – The current process, as established by Veterans Health Administration (VHA) interim guidance, is for the contracting official's review and approval to be documented in an e-mail. This is strictly an interim process that will be used until the Integrated Funds Distribution, Control Point Activity, Accounting and Procurement (IFCAP) system can be changed to capture this information.

Requirements for an electronic approval process are included in the new Financial and Logistics Integrated Technology Enterprise (FLITE) and the Integrated Financial Accounting System (IFAS), the financial component of FLITE. IFAS requirements (finalized June 2008) include an electronic workflow to allow the system to route documents through predefined steps. IFAS requirements were created to specifically address the miscellaneous obligation process and include a gatekeeper who will review and direct the correct flow of the documents. The gatekeeper (an employee knowledgeable in procurement and workload distribution) will be responsible for ensuring the flow of purchasing documents to appropriate contracting/purchasing personnel.

Recommendation 2: Segregate duties for (1) creating, approving, and recording miscellaneous obligations, (2) the certification and payment of invoices, and (3) the receipt of the resulting goods or services.

Concur – The VA's Office of Finance Bulletin will address the issue of segregation of duties. This Bulletin is in the concurrence process and should be issued shortly.

IFAS will be a centralized system that also replaces the purchasing feature, currently performed by the IFCAP system. Access to IFAS will be managed at a central location; this will prevent individual stations from allowing users multiple accesses and will maintain the proper segregation of duties.

Enclosure

Department of Veterans Affairs (VA) Comments to
Government Accountability Office (GAO) Draft Report
**VETERANS HEALTH ADMINISTRATION: Improvements Needed in Design of
Controls over Miscellaneous Obligations**

(GAO-08-976)
(Continued)

Recommendation 3: Document the purpose, vendor, and contract number for miscellaneous obligations.

Concur - The interim VHA guidance requires that all VA Forms 1358, *Miscellaneous Obligation*, document the purpose, vendor, and if applicable, the contract number. These same requirements are included in the Department policy (VA Directive and Handbook) that has been issued.

The IFAS requirements state that the system must have the ability to edit and mandate specific fields to be completed before continuing to the next step. All three of these fields will be required.

However, there is no automated method for ensuring that the purpose, vendor, and contract number have been recorded on the 1358. VA will explore the feasibility of developing a patch that would allow VHA to capture these fields for reporting purposes.

Recommendation 4: Establish an oversight mechanism to ensure that these control policies and procedures are fully and effectively implemented

Concur - VHA has developed a monthly report that will track and trend the number and dollar amount of 1358s obligated in VHA by individual budget object code. This will enable VHA to determine whether the policy is being adhered to.

The IFAS project group (composed of subject matter experts from logistics, fiscal, and policy) has developed a policy on use of 1358s. The policy is under review before it is finalized, we will add guidance on segregation of duties and on the appropriate oversight procedures.

Another IFAS requirement is the ability to perform audits and statistical samples. This feature will allow VA to review and manage the use of miscellaneous obligations and oversee the audits.

Appendix III: Miscellaneous Obligations by VISN in Fiscal Year 2007

VISN ^a	VISN name	Number	Dollar amount	Percentage of total
1	VA New England Healthcare System	6,638	\$360,762,340	5.2%
2	VA Healthcare Network Upstate New York	2,910	160,799,144	2.3%
3	VA NY/NJ Veterans Healthcare Network	7,248	256,453,022	3.7%
4	VA Stars & Stripes Healthcare Network	12,321	328,355,399	4.8%
5	VA Capitol Health Care Network	2,024	185,679,821	2.7%
6	VA Mid-Atlantic Health Care Network	2,808	304,500,111	4.4%
7	The Southeast Network	4,548	440,137,101	6.4%
8	VA Sunshine Healthcare Network	9,985	496,497,019	7.2%
9	VA Mid South Healthcare Network	4,461	356,353,797	5.2%
10	VA Healthcare System of Ohio	5,093	247,515,982	3.6%
11	Veterans in Partnership	3,947	261,290,926	3.8%
12	VA Great Lakes Health Care System	4,284	293,466,391	4.2%
15	VA Heartland Network	5,941	300,314,177	4.3%
16	South Central VA Health Care Network	9,859	551,236,444	8.0%
17	VA Heart of Texas Health Care Network	2,388	292,273,251	4.2%
18	VA Southwest Health Care Network	6,308	346,135,243	5.0%
19	Rocky Mountain Network	3,332	220,514,581	3.2%
20	Northwest Network	9,370	360,007,803	5.2%
21	Sierra Pacific Network	11,262	403,378,623	5.8%
22	Desert Pacific Healthcare Network	1,906	388,244,689	5.6%
23	VA Midwest Health Care Network	10,437	354,911,219	5.1%
Total		127,070	\$6,908,827,084	100%

Source: GAO analysis of IFCAP database.

^aVISNs 13 and 14 were consolidated and designated as VISN 23.

Appendix IV: VHA Stations Ranked by Use of Miscellaneous Obligations

Rank	Station	Facility number	VISN	Number	Amount
1	Omaha	636	23	6,832	\$158,912,717
2	North Florida/South Georgia VHA	573	8	4,131	145,875,702
3	Kansas City, Missouri	589	15	3,603	171,613,075
4	Pittsburgh HCS-University Dr	646	4	3,567	69,880,889
5	VA New York Harbor HCS – NY CA	630	3	3,280	85,275,329
6	San Francisco	662	21	3,200	89,361,982
7	N. California HCS-Martinez	612	21	3,166	88,567,989
8	Upstate New York HCS	528	2	2,910	160,799,144
9	Philadelphia	642	4	2,536	77,015,657
10	VA Boston HCS-Boston Division	523	1	2,351	102,803,146
11	St. Louis-John Cochran	657	15	2,338	128,701,102
12	Seattle, Washington	663	20	2,030	110,264,551
13	G. V. (Sonny) Montgomery VAMC	586	16	1,964	84,782,426
14	VAMC Bronx	526	3	1,743	37,336,434
15	Northern Arizona HCS	649	18	1,706	30,897,276
16	Miami	546	8	1,686	64,028,264
17	Middle Tennessee HCS	626	9	1,644	102,901,107
18	Cleveland-Wade Park	541	10	1,642	119,323,832
19	Portland	648	20	1,602	88,110,706
20	VA Palo Alto HCS-Palo Alto	640	21	1,498	100,993,614
21	Clarksburg	540	4	1,470	25,244,100
22	Amarillo HCS	504	18	1,453	32,694,257
23	Central California HCS (Fresno)	570	21	1,403	30,528,159
24	Fayetteville AR	564	16	1,386	42,468,351
25	Boise	531	20	1,385	35,371,800
26	New Orleans	629	16	1,369	57,125,143
27	VA New Jersey HCS	561	3	1,366	65,538,526
28	W Palm Beach	548	8	1,318	56,059,142
29	Dayton	552	10	1,306	43,574,791
30	Fort Meade	568	23	1,284	28,139,258
31	Bay Pines	516	8	1,128	76,081,613
32	Lebanon	595	4	1,105	29,330,151
33	Alaska HCS	463	20	1,090	55,377,371
34	Togus	402	1	1,085	52,777,782
35	Baltimore	512	5	1,060	92,856,732
36	Chillicothe	538	10	1,037	16,704,890

**Appendix IV: VHA Stations Ranked by Use of
Miscellaneous Obligations**

Rank	Station	Facility number	VISN	Number	Amount
37	Oklahoma City	635	16	1,020	80,419,697
38	Roseburg HCS	653	20	996	21,172,773
39	Lexington-Leestown	596	9	987	48,090,092
40	Milwaukee WI	695	12	974	59,113,209
41	Walla Walla	687	20	964	13,199,190
42	Dallas VAMC	549	17	942	100,556,097
43	Fargo	437	23	937	26,988,919
44	Wilmington	460	4	923	24,534,375
45	Providence	650	1	900	31,961,444
46	Pacific Islands HCS (Honolulu)	459	21	894	57,759,481
47	Southern Oregon Rehabilitation	692	20	883	11,294,874
48	Phoenix	644	18	879	84,069,252
49	Columbia SC	544	7	870	70,594,890
50	Wilkes Barre	693	4	861	26,987,646
51	Houston	580	16	855	67,739,913
52	Augusta	509	7	846	53,390,674
53	Tampa	673	8	838	116,270,986
54	Alexandria	502	16	830	25,417,175
55	Gulf Coast HCS	520	16	823	46,044,544
56	Hines	578	12	813	72,402,760
57	Eastern Colorado HCS	554	19	803	82,599,599
58	Salt Lake City HCS	660	19	803	68,390,644
59	San Antonio VAMC	671	17	801	113,175,496
60	Butler	529	4	792	15,272,087
61	West Haven	689	1	731	80,337,724
62	Ann Arbor HCS	506	11	715	50,017,830
63	N. Indiana HCS-Marion	610	11	706	33,501,439
64	Coatesville	542	4	702	17,933,344
65	Chicago HCS	537	12	700	53,085,848
66	El Paso HCS	756	18	699	24,242,716
67	Madison WI	607	12	696	46,845,867
68	VA Sierra Nevada HCS	654	21	691	31,948,186
69	Huntington	581	9	690	32,256,564
70	Greater Los Angeles HCS	691	22	670	113,284,821
71	Detroit (John D. Dingell)	553	11	667	41,810,942
72	New Mexico HCS	501	18	666	84,082,667
73	Tuscaloosa	679	7	650	20,128,372

**Appendix IV: VHA Stations Ranked by Use of
Miscellaneous Obligations**

Rank	Station	Facility number	VISN	Number	Amount
74	Temple VAMC	674	17	645	78,541,658
75	Indianapolis	583	11	645	54,906,324
76	Muskogee	623	16	645	39,781,639
77	Montana HCS	436	19	645	32,278,047
78	Durham	558	6	639	61,960,744
79	Sheridan	666	19	629	12,501,607
80	Manchester	608	1	606	27,003,396
81	White River Jct	405	1	580	28,279,283
82	S. Arizona HCS	678	18	578	69,574,532
83	Columbus	757	10	570	25,461,020
84	Central AR. Veterans HCS LR	598	16	564	70,779,560
85	Washington	688	5	563	65,013,443
86	Illiana HCS (Danville)	550	11	543	19,659,628
87	Cincinnati	539	10	538	42,451,450
88	Minneapolis	618	23	534	93,816,762
89	Mountain Home	621	9	517	57,849,934
90	Orlando	675	8	505	9,342,539
91	San Diego HCS	664	22	503	76,890,097
92	Decatur	508	7	494	103,798,914
93	Richmond	652	6	490	50,242,036
94	Montgomery	619	7	488	33,582,736
95	Birmingham	521	7	481	75,609,201
96	Iron Mountain MI	585	12	459	16,882,679
97	St. Cloud	656	23	456	17,539,831
98	Louisville	603	9	438	51,080,527
99	W.G. (Bill) Hefner Salisbury V	659	6	438	50,753,235
100	VAMC Northport	632	3	433	45,155,858
101	VA Hudson Valley HCS-Montrose	620	3	426	23,146,875
102	Spokane	668	20	420	25,216,539
103	Manila	358	21	410	4,219,213
104	Charleston	534	7	407	44,239,266
105	Overton Brooks VAMC	667	16	403	36,677,997
106	Martinsburg	613	5	401	27,809,646
107	Sioux Falls	438	23	394	29,513,732
108	San Juan	672	8	379	28,838,772
109	North Chicago IL	556	12	353	31,553,133
110	Battle Creek	515	11	337	43,990,975

**Appendix IV: VHA Stations Ranked by Use of
Miscellaneous Obligations**

Rank	Station	Facility number	VISN	Number	Amount
111	Saginaw	655	11	334	17,403,788
112	West Texas HCS	519	18	327	20,574,543
113	Salem	658	6	326	30,946,603
114	Dublin	557	7	312	38,793,048
115	Loma Linda VAMC	605	22	298	64,213,454
116	Tomah	676	12	289	13,582,895
117	Beckley	517	6	274	11,949,194
118	Cheyenne	442	19	250	13,484,935
119	Fayetteville NC	565	6	243	42,688,173
120	Southern Nevada HCS	593	22	236	95,628,301
121	Bedford	518	1	229	13,576,881
122	Asheville-Oteen	637	6	203	28,266,374
123	Grand Junction	575	19	202	11,259,749
124	Long Beach HCS	600	22	199	38,228,015
125	Hampton	590	6	195	27,693,752
126	Erie	562	4	191	15,333,253
127	Memphis	614	9	185	64,175,573
128	James E. Van Zandt VA (Altoona)	503	4	174	26,823,897
129	Northampton	631	1	156	24,022,684
	Total			127,070	\$6,908,827,084

Source: GAO analysis of IFCAP database.

Appendix V: GAO Contact and Staff Acknowledgments

GAO Contact

Kay Daly, (202) 512-9095 or dalykl@gao.gov.

Acknowledgments

In addition to the contact named above, Glenn Slocum (Assistant Director), Richard Cambosos, Debra Cottrell, Francine DelVecchio, Daniel Egan, W. Stephen Lowrey, Robert Sharpe, and George Warnock made key contributions to this report.

GAO's Mission

The Government Accountability Office, the audit, evaluation, and investigative arm of Congress, exists to support Congress in meeting its constitutional responsibilities and to help improve the performance and accountability of the federal government for the American people. GAO examines the use of public funds; evaluates federal programs and policies; and provides analyses, recommendations, and other assistance to help Congress make informed oversight, policy, and funding decisions. GAO's commitment to good government is reflected in its core values of accountability, integrity, and reliability.

Obtaining Copies of GAO Reports and Testimony

The fastest and easiest way to obtain copies of GAO documents at no cost is through GAO's Web site (www.gao.gov). Each weekday, GAO posts newly released reports, testimony, and correspondence on its Web site. To have GAO e-mail you a list of newly posted products every afternoon, go to www.gao.gov and select "E-mail Updates."

Order by Mail or Phone

The first copy of each printed report is free. Additional copies are \$2 each. A check or money order should be made out to the Superintendent of Documents. GAO also accepts VISA and Mastercard. Orders for 100 or more copies mailed to a single address are discounted 25 percent. Orders should be sent to:

U.S. Government Accountability Office
441 G Street NW, Room LM
Washington, DC 20548

To order by Phone: Voice: (202) 512-6000
TDD: (202) 512-2537
Fax: (202) 512-6061

To Report Fraud, Waste, and Abuse in Federal Programs

Contact:

Web site: www.gao.gov/fraudnet/fraudnet.htm

E-mail: fraudnet@gao.gov

Automated answering system: (800) 424-5454 or (202) 512-7470

Congressional Relations

Ralph Dawn, Managing Director, dawnr@gao.gov, (202) 512-4400
U.S. Government Accountability Office, 441 G Street NW, Room 7125
Washington, DC 20548

Public Affairs

Chuck Young, Managing Director, youngc1@gao.gov, (202) 512-4800
U.S. Government Accountability Office, 441 G Street NW, Room 7149
Washington, DC 20548