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GAO

Report to the Secretary of Veterans Affairs

August 1989

FINANCIAL MANAGEMENT

Opportunities for Improving VA's Internal Accounting Controls and Procedures

GAO/AFMD-89-35

GAO

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

Accounting and Financial
Management Division

B-226801

August 11, 1989

The Honorable Edward J. Derwinski
The Secretary of Veterans Affairs

Dear Mr. Secretary:

Our report to the Congress provided the results of our examination of the Veterans Administration's (which, in March 1989, became the Department of Veterans Affairs) consolidated financial statements for fiscal years 1987 and 1986 (GAO/AFMD-89-23, November 30, 1988). In that report, we discussed internal accounting control weaknesses that were material for the purpose of assessing whether the agency's consolidated financial statements were fairly stated. This report expands on some of those weaknesses but primarily describes other opportunities for improving internal accounting controls and procedures in the areas of financial reporting, medical care, veterans benefits, housing credit, and payroll.

This report contains recommendations to you. The head of a federal agency is required by 31 U.S.C. 720 to submit a written statement on actions taken on these recommendations to the Senate Committee on Governmental Affairs and the House Committee on Government Operations not later than 60 days after the date of the report and to the House and Senate Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of the report.

We are sending copies of this report to the Director of the Office of Management and Budget; the Secretary of the Treasury; and the Chairmen of the Senate Committee on Governmental Affairs, the House Committee on Government Operations, and the House and Senate Committees on Appropriations. Copies will also be made available to others upon request. Please contact me at (202) 275-9406 if you or your staff have any questions concerning this report. Other major contributors to this report are listed in appendix I.

Sincerely yours,

Dennis J. Duquette

Dennis J. Duquette
Director, Agency Financial Audits

Executive Summary

Purpose

The Department of Veterans Affairs (VA), with the third largest number of civilian federal employees in the federal government, carries out a diversity of programs to meet the health-care and financial needs of veterans and their dependents. These programs were carried out during fiscal year 1987 at a cost of about $31 billion. To properly manage and accurately account for these programs requires effective systems of accounting and internal controls.

GAO reviewed certain aspects of VA's internal accounting controls and procedures as part of its examination of the agency's financial statements for fiscal year 1987. This report describes VA's financial management environment and presents opportunities for improving certain internal accounting controls and financial management practices within the agency.

Background

In the health-care area, VA operates 172 medical centers and other medical facilities and procures other medical services from non-VA medical providers in order to treat eligible veterans and their dependents. The total cost of the VA health-care program for fiscal year 1987 was about $10.2 billion.

VA also administers financial programs which provide various benefits and assistance to veterans and their dependents, including compensation and pension payments, education assistance payments, housing credit assistance, life insurance, and burial benefits. The cost of providing these financial benefits during fiscal year 1987 amounted to about $20.8 billion. To manage and account for these programs, VA currently operates 42 financial management systems.

These programs are funded by (1) funds appropriated by the Congress (about 90 percent) and (2) fees received from housing credit assistance operations, premiums and interest income from life insurance operations, and reimbursements from medical care services (about 10 percent).

Results in Brief

VA has demonstrated a commitment to strengthen financial management and was one of the first federal agencies to prepare consolidated financial statements in accordance with generally accepted accounting principles for the federal government. VA has also implemented a project to develop a modern, automated, integrated, agencywide financial management system by 1992 and is in the process of redesigning its automated payroll system. However, GAO's financial audit disclosed weaknesses in internal controls which show that not only will the planned improvements need to be completed, but other improvements should be implemented as well.

Although the weaknesses in internal controls described in this report did not materially affect the fair presentation of VA's financial statements, GAO believes that correcting these weaknesses would prevent errors or irregularities that could result in misstatements of amounts reported by VA's financial accounting systems.

GAO also believes that VA management's continued involvement and commitment is essential for the success of these improvements, as well as for the implementation of the other needed improvements in VA's financial management systems.

The principal weaknesses GAO found were the

- lack of a financial reporting system that automates the financial statement consolidation process, including general ledger balances, adjusting and closing entries, and financial statements;
- lack of effective internal controls in the medical care, veterans benefits, and housing credit assistance areas that are intended to ensure proper recoveries of cost and accuracy of account balances; and
- inadequate automated payroll system controls for ensuring that all VA employees are paid correctly and on-time.

Principal Findings

Financial Reporting Improvements Are Needed

Although VA has made significant progress in preparing consolidated financial statements in accordance with generally accepted accounting principles for the federal government (Title 2 of GAO's Policy and Procedures Manual for Guidance of Federal Agencies), GAO's fiscal year 1987 financial audit disclosed that not all of the requirements are being met. Specifically, the financial statement consolidation process is not integrated with the underlying accounting systems, the general ledger balances do not provide the basis for the financial statements, and the consolidation and year-end closing procedures are not documented or adequately supported. (See chapter 2.)

Medical Care Internal Controls Not Implemented

Generally, GAO found that internal controls that were intended to ensure the proper recovery of cost and the accuracy of account balances in the medical care area, were not adequately implemented. These include controls such as reviews of year-end obligations, reconciliations of certain control and subsidiary accounts, and financial procedures for ensuring that transactions are recorded in the proper fiscal year. (See chapter 3.)

Internal Controls Lacking in Veterans Benefits and Other Areas

In the veterans benefits area, GAO found that internal controls are lacking in automated systems to ensure that compensation, pension, and education benefit payment data are processed completely and accurately. In addition, proper authorization is not obtained for releasing compensation, pension, and education benefit payments over threshold amounts. Federal government or VA requirements have not been met in certain areas, such as timely collection action on accounts receivable, the recognition and recording of all liabilities, and the prompt and accurate accumulation and reporting of obligational data on all appropriated funds. (See chapter 4.)

Although VA has improved certain principal controls in the housing credit assistance area, several weaknesses still exist. The remaining weaknesses include the lack of an established system for recognizing losses on guaranteed loans, the lack of reconciliation between the general ledger control account balances and the subsidiary ledger balances, and improper documentation and approval of some journal vouchers. (See chapter 5.)

In the area of payroll internal controls, GAO found that the current payroll system does not include effective controls for ensuring the implementation of proper pay changes for "special rate" and "special pay" employees. As a result, incorrect payments are made. Also, pay verifications and reconciliations that are intended to ensure that payroll data are correctly processed are not performed. (See chapter 6.)

Recommendations

GAO recommends that the Secretary of Veterans Affairs direct appropriate VA officials to develop a plan for implementing corrective action that addresses the internal control problems identified in the housing credit area.

Agency Comments

Responsible VA officials provided comments on this report. These comments are presented and evaluated in the "Agency Comments and Our

Evaluation" sections in chapters 2 through 6. VA generally agreed with GAO's findings and described its corrective action plans to address all of the weaknesses identified. GAO believes that the corrective action plans address the problems identified in all areas, except housing credit. GAO will review the adequacy of the implementation of VA's corrective actions during subsequent audits.

Contents

Abbreviations

ADP	automated data processing
CALM	Centralized Accounting for Local Management
DPC	Data Processing Center
FIPS	Federal Information Processing Standard
FMFIA	Federal Managers' Financial Integrity Act
FMS	financial management system
GAAP	generally accepted accounting principles
GAO	General Accounting Office
IRS	Internal Revenue Service
OMB	Office of Management and Budget
PAID	Personnel Accounting and Integrated Data
VA	Department of Veterans Affairs
VAMC	Veterans Affairs medical center

Introduction

Background

The Department of Veterans Affairs (VA) is the third largest civilian employer in the federal government.[1] VA's overall mission is to meet the financial, educational, and health-care needs of veterans and their dependents. The magnitude of VA's programs is evident in the following services that it rendered in fiscal year 1987:

- treated nearly 1.4 million inpatients in 172 medical centers and various other VA medical facilities and treated nearly 94,000 additional inpatients in non-VA hospitals and extended-care homes, and processed about 19.8 million outpatient visits to VA clinics and 1.8 million visits under VA authorization to private physicians for a total overall cost of about $10 billion.
- provided about $14.4 billion in compensation and pension payments to nearly 3.8 million veterans and their survivors, $788 million for education assistance payments, and $108.2 million in burial benefits;
- guaranteed or insured over 479,000 home loans for veterans; and
- operated the fifth largest individual life insurance program in the United States—administering or supervising about $213 billion in life insurance for nearly 7.4 million insureds.

VA is headed by the Secretary of Veterans Affairs, who is supported by various staff offices and three operating departments in carrying out the agency's responsibilities and administering its various programs. The principal organizational units responsible for performing financial management and automated data processing (ADP) activities are two staff offices, the Office of Budget and Finance (Controller) and the Associate Deputy Administrator for Management, and the three operating departments—the Veterans Health Services and Research Administration (formerly Department of Medicine and Surgery), Veterans Benefits Administration (formerly Department of Veterans Benefits), and National Cemetery System (formerly Department of Memorial Affairs). (The preceding organizational changes became effective March 15, 1989.) The financial management activities include controlling and accounting for VA's resources. Also, the Federal Managers' Financial

[1] The Veterans Administration became the Department of Veterans Affairs in March 1989, and the title of the agency's head was changed from Administrator to Secretary of Veterans Affairs.

Integrity Act[2] requires that management assess its financial management systems for conformance with the Comptroller General's accounting principles, standards, and related requirements,[3] and the internal control standards[4] issued pursuant to the act.

Financial Management Structure

The Controller provides advice and guidance to the Secretary on administrative and financial management matters and directs and coordinates these activities in the VA departments. These activities include:

- formulating accounting policies and procedures for all VA operations;
- formulating and presenting VA's annual budget;
- controlling spending authority over appropriated funds;
- managing 14 of VA's 42 financial management systems;
- monitoring and recommending improvements to all financial operations; and
- operating finance centers in Austin, Texas, and Hines, Illinois, to provide financial services, such as paying vendor invoices and other payment vouchers, for all VA operations.

VA's operating departments and their organizational components and field offices (VA regional offices, medical centers, and life insurance offices) are responsible for managing the majority of VA's financial management systems (25 of 42) and carrying out all financial management activities at the operating level. These financial management activities include establishing and maintaining internal controls and initiating and processing most accounting transactions.

VA has categorized its 42 financial management systems into two types—administrative and program. These systems are used to (1) record and control appropriated funds and other accounting transactions, (2) record summary financial information on the financial results of program and administrative operations, (3) prepare financial reports for managers' use, and (4) prepare summary financial reports on the results

[2]The Federal Managers' Financial Integrity Act of 1982 (31 U.S.C. 3512(b) and (c)) gives agency management the primary responsibility for maintaining adequate systems of internal control and accounting. The act requires that agency heads report annually to the President and the Congress on the status of these systems, and it holds managers responsible for correcting identified deficiencies. In addition, the act covers all management controls—not just those dealing with accounting controls and financial reporting—including the entire network of policies, procedures, practices, and systems that managers use to do their jobs.

[3]GAO's Policy and Procedures Manual for Guidance of Federal Agencies, Title 2.

[4]Title 2, appendix II, "Internal Control Standards."

of program and administrative operations and the status of appropriated funds.

Objective, Scope, and Methodology

The objective of our audit was to report on the fair presentation of VA's consolidated financial statements for fiscal years 1987 and 1986. In planning our audit, we evaluated VA's internal controls to assess the level of control risk in order to determine the nature, timing, and extent of our tests of account balances. We reported the significant internal accounting and ADP control weaknesses in our report on internal controls which was included in our financial audit report on VA's consolidated financial statements for fiscal years 1987 and 1986.[5] This report describes other weaknesses in internal accounting controls and procedures which, although not as significant as those discussed in our report on internal controls, nevertheless merit corrective action to strengthen the controls.

In evaluating internal accounting controls, we identified the control techniques in place to achieve critical control objectives for medical care, veterans benefits, housing assistance, life insurance programs, financial reporting, payroll, and automated data processing. If operating effectively, these controls would help ensure (1) the reliable processing of data by VA's financial accounting systems and (2) VA's compliance with applicable laws and regulations.

Our work was performed at the following locations:

- VA headquarters in Washington, D.C.;
- 10 VA regional offices;
- 28 VA medical centers;
- the accounts receivable center in St. Paul, Minnesota;
- the insurance centers in Philadelphia, Pennsylvania, and St. Paul, Minnesota;
- the VA Finance Center in Austin, Texas; and
- the data processing centers (DPCs) in Philadelphia, Pennsylvania; Hines, Illinois; and Austin, Texas.

Our audit work was conducted from August 1987 to May 1988 and was performed in accordance with generally accepted government auditing standards. Responsible officials of the Department of Veterans Affairs

[5] Financial Audit: Veterans Administration's Financial Statements for Fiscal Years 1987 and 1986 (GAO/AFMD-89-23, November 30, 1988).

provided comments on a draft of this report. These comments are presented and evaluated in the "Agency Comments and Our Evaluation" sections of chapters 2 through 6.

To facilitate corrective action by VA within its financial and ADP management structures, we have classified the opportunities for improving internal accounting controls and procedures into the following areas:

- financial reporting (chapter 2),
- medical care (chapter 3),
- veterans benefits (chapter 4),
- housing credit (chapter 5), and
- payroll (chapter 6).

The internal accounting controls and procedures in two other areas were also evaluated during our fiscal year 1987 financial statement audit—life insurance and ADP general controls. We found that the principal, non-ADP control weakness which still needs to be improved in the life insurance area was reported in our management letter for fiscal year 1986—the need for written guidance on the preparation of combined financial statements.[6] The weaknesses in ADP general controls were described in our report on internal controls for fiscal year 1987 since they were considered material. Accordingly, these two areas are not included in this report.

[6] B-226801, dated November 18, 1987, to the Administrator of Veterans Affairs.

Financial Reporting Improvements Are Needed

Consolidated financial statements and other external reports should be a normal byproduct of an agency's financial management system. VA has not completed integrating its reporting process with the underlying financial management system, and we found that the amounts in external and internal reports did not always agree with the amounts in the accounting systems. Some of these differences resulted in adjustments to the fiscal year 1987 financial statements. Specifically we found that

- accounting balances, such as cash and accounts payable, shown in the accounting system did not agree with those reported to the Department of the Treasury and the Office of Management and Budget (OMB), and VA has not identified the reasons for these differences and
- VA did not adequately document the closing procedures for its fiscal year 1987 closing process.

These conditions prevent VA's management and external users from receiving timely and accurate financial reports, as required by Title 2 and other federal regulations.

Consolidation Process Is Not Integrated With Accounting Systems

As we reported in our management letter for fiscal year 1986, VA manually prepares consolidated financial statements primarily with financial information produced by 42 financial management systems. The information is produced on an appropriation basis at the individual program activity level. VA's central office uses this information to produce various Treasury and OMB reports at the appropriation level. VA then incorporates components of some of these reports, such as the Treasury reports on financial position and operations (SF-220 and SF-221, respectively), into a worksheet for preparing the consolidated financial statements.

This process was improved during fiscal year 1987 through the use of a microcomputer spreadsheet. However, the most efficient and reliable method of preparing consolidated financial statements is the use of an automated, integrated accounting system. Such an integrated accounting system would not only lead to more accurate and timely financial reporting, but also to more consistent and reliable performance reporting. Furthermore, an integrated accounting system would improve financial auditing efficiency.

One of VA's 42 financial management systems is a general ledger system. This system consists only of individual general ledger accounts maintained by type of asset, liability, and expenditure, such as payroll expenses, administrative expenditures, and the mortgage loan and life insurance programs. However, there is no consolidated VA-wide general ledger which summarizes information on the overall status of appropriated funds, assets, and liabilities, and on the financial results of program and administrative operations. At present, to prepare annual financial reports on an organizational component or consolidated VA-wide basis, general ledger account balances have to be analyzed to resummarize information from an expenditure-type basis to an organizational-component basis.

Title 2 states that accounting systems must be designed and operated to provide the information which agency managers need to operate their programs efficiently and effectively. In our report, Managing the Cost of Government: Building an Effective Financial Management Structure (GAO/AFMD-85-35-A, February 1985), we discussed methods of program and organizational reporting "roll-ups" that would facilitate the preparation of program and consolidated financial reports and the comparison of budgeted and actual amounts.

We believe that this methodology would be effective for VA. Such a methodology would help VA ensure that its integrated financial management system (FMS) currently under development will meet all of the Title 2 requirements.

Differences in External Reports and General Ledger Are Not Reconciled

As indicated above, VA uses certain cash or appropriations data from its accounting systems to prepare required Treasury and OMB reports. When amounts on these Treasury and OMB reports differ from the accounting systems' final general ledger balances, the report amounts are used to prepare the consolidated financial statements. However, VA does not analyze differences between the Treasury and OMB reports and its general ledger as a part of the financial statement preparation process. Such an analysis would identify any needed adjustments and ensure that all internal and external financial reports are consistent and uniform.

Title 2 specifies that an agency's financial statements shall be the culmination of its systematic accounting process. Thus, the general ledger should provide the primary support for the financial information that is reported in VA's financial statements. However, we recognize that until VA implements its integrated FMS (currently scheduled to be implemented by 1992), this requirement can not be completely and effectively satisfied. But, we believe that VA can partially satisfy the requirement by using a microcomputer process for identifying differences between its general ledger accounts and financial statement amounts. For accounts with material differences, the microcomputer process could be used for analyzing and appropriately adjusting for these differences.

For example, our audit comparison of general ledger account balances to the financial statement balances disclosed differences in various account balances. Our analysis of a number of these accounts with major differences (e.g., cash with the U.S. Treasury) disclosed several needed adjustments which reduced the differences. For example, the financial statement showed that the account payable balance was about $1.9 million more than the general ledger balance of $440 million. Similarly, the accrued compensation and pension benefits balance of $34.9 million was understated by $699,000 in the general ledger.

Consolidation and Year-End Closing Procedures Are Not Documented

Adequate written guidelines for VA's financial statement consolidation process do not exist to aid those involved in the consolidation process. These guidelines are particularly critical because relatively few VA personnel are familiar with the process. In addition, VA's central office does not issue reminders to the VA regional offices and medical centers at the end of the fiscal year to inform them of many of the procedures that have to be done at year-end for proper closing of the year's accounting activities.

Problems associated with year-end closing procedures at VA include improper cut-off of receipts in the medical area, failure to conduct year-end reviews of obligations, and failure to reconcile control and subsidiary account balances, as discussed in the following chapters of this report. Also, other requirements, such as comparisons of account balances, need to be described in year-end closing procedures as previously discussed.

Title 2 states that comparability is a major qualitative factor that enables accounting information to be useful. To help ensure that the accounting information is comparable from one period to the next, a documented consolidation process with adequate guidelines is needed. In addition, the integrity of account balances is increased when all of the fiscal year's transactions are recorded in the appropriate period.

Conclusions

VA's improved procedures for preparing consolidated financial statements still do not satisfy Title 2 requirements in three significant areas.

Specifically, the overall VA financial statement consolidation process is not integrated with the underlying accounting systems, differences in amounts on required Treasury and OMB reports and general ledger account balances are not reconciled, and the consolidation and year-end closing procedures are not documented. These weaknesses did not affect our opinion on VA's fiscal year 1987 and 1986 financial statements; however, we believe that, in the aggregate, such weaknesses are detrimental to VA's efficient preparation of accurate and timely financial reports.

Agency Comments and Our Evaluation

We discussed these problems with agency officials who agreed that the existing procedures needed to be revised. They subsequently provided us with a description of the corrective action which has been implemented and includes the following.

- A process for ensuring that VA's new financial management system will provide consolidated financial information in accordance with the requirements of Title 2 has been established.
- The requirement for analyzing significant differences between Treasury and OMB report amounts and the general ledger balances and for recording adjustments, if necessary, is now included in the financial statement consolidation process.
- Formal year-end account closing and financial statement preparation procedures which include the following have been developed: (1) the requirement for notifying the affected VA offices of year-end closing procedures, including a schedule for the completion of each step of the year-end closing; cutoff dates, such as purchase orders and receipt documents; and a reminder of the requirement for reconciliation of accounts and year-end obligation reviews, (2) the identification of the trial balance composition of financial statement line items in addition to the Treasury/OMB report composition, and (3) a standardized form on which all consolidating journal entries are recorded, described, and approved, with the source or supporting documentation clearly indicated.

Based on a review of the stated procedures and discussions with agency officials, we believe that the corrective actions taken address the problems we identified. In subsequent audits, we will review the adequacy of the implementation of the corrective actions.

Internal Control Improvements Needed in the Medical Care Area

One of VA's major missions is to provide medical care to eligible veterans, and this function expended about $10 billion in fiscal year 1987. Because of the complex nature and diverse responsibilities of this activity, VA has established an elaborate system of internal controls over medical care. Our audit included a review of the significant accounting controls implemented at 28 VA medical centers (VAMCs) and disclosed that the internal controls were not always implemented or accomplished. The weaknesses we found included the following.

- Written procedures, training programs, and supervisory reviews to improve controls over the cost recovery program were lacking in some of the VAMCs.
- Year-end obligation reviews which are required to ensure that outstanding obligations are reasonable and appropriate were not conducted by 10 VAMCs.
- VA had no assurance that control account balances for subsistence (perishable food items) payables were accurate because 22 VAMCs did not reconcile the control accounts with subsidiary records.
- Property accounting records did not accurately reflect the status of real property at 27 VAMCs because procedures had not been implemented to reconcile information contained in the property accounting system.
- Eleven VAMCs failed to make necessary adjustments in a timely manner after performing reconciliations to supply property records between the accounting system control accounts and the subsidiary system.
- Fourteen VAMCs failed to report to the IRS the write-off of receivables from individuals.
- Procedures to ensure that goods and services were recorded in the year of receipt were inadequately implemented.

Cost Recovery Programs Do Not Always Include Required Controls

We evaluated controls in three areas of medical care cost recovery: (1) persons who do not have qualifying military service, (2) qualified veterans who must pay part of their medical costs because their incomes exceed set limits, and (3) private insurance companies which provide medical insurance to qualified veterans. Of the 28 VAMCs we selected for review, we found that

- 10 VAMCs did not have written procedures for determining military service eligibility, 8 did not have written procedures for income tests, and 7 did not have written procedures for determining whether the patients had private medical insurance coverage;
- 12 VAMCs did not have formal training programs for instructing staff in medical care cost recovery procedures;

- 18 VAMCs did not conduct annual reviews of their medical care cost recovery program activities; and
- 10 VAMCs did not have routine supervisory reviews of the cost recovery determinations that were made by staff.

VA's policy and procedures manual requires each VAMC to establish a program for recovering medical care costs in appropriate cases. The VA manual requires that this program include several specific internal controls. These include

- procedural guidelines for employees whose duties include identifying collection cases and initiating bills,
- formalized training for staff in methods of identifying collection cases and initiating bills where applicable, and
- an annual systematic review to evaluate the program.

Title 2, appendix II, requires agencies to include systematic supervisory controls over each employee's work as an internal control. Supervisory controls are especially important in a cost recovery program because decisions in this area directly affect government cost.

During our fiscal year 1986 audit, we determined the need for stronger internal accounting controls to ensure that all medical services for which VA should be reimbursed were identified and billed to the appropriate party. Our review of 300 patient files at 10 VAMCs in fiscal year 1987 disclosed only 5 cases with unsupported eligibility determinations. We believe this improvement over our fiscal year 1986 findings is due, at least in part, to VA's increased use of the Decentralized Hospital Computer Program, which has incorporated several computer controls into the patient processing system. However, written procedures, training programs, and supervisory reviews remain necessary to ensure that VAMC personnel accurately identify and bill all appropriate recovery cases.

VAMCs Do Not Conduct Year-End Obligation Reviews

Title 7 of GAO's Policy and Procedures Manual for Guidance of Federal Agencies and 31 U.S.C. 1554 require that unliquidated obligation documents—those on which full payment has not been made—be reviewed at the end of each fiscal year. This review should (1) establish the validity of recorded obligations, (2) determine the continuing validity of older obligations, and (3) determine whether recently recorded obligations are valid. These reviews help ensure that, under 31 U.S.C. 1501(b), any statement of obligations submitted to the Congress includes only valid obligations. In addition, VA's policy and procedures manual requires a similar review of obligations.

We found that staff responsible for fiscal activities at 10 of the 28 VAMCs had not conducted or had not documented year-end obligation reviews. This review of unliquidated obligations is important because management and outside parties, such as the Congress, are provided with better information on VA's true liabilities and the amount of funds committed to specific programs.

VAMCs Do Not Reconcile Subsistence Payable Accounts

Of 28 centers we audited, 22 did not reconcile subsistence payable account balances (i.e., payables for perishable food purchases) with receiving reports and other documents evidencing indebtedness. The purpose of such reconciliations is to ensure the accuracy of the applicable general ledger control accounts and that goods and services were received. This deficiency may have occurred because in transferring disbursement responsibility for certain payables (including subsistence payables) from VA's Austin Finance Center to VAMCs, specific instructions to perform the reconciliations were not provided to the centers.

Title 2 and VA's policy and procedures manual require that accounts payable records be reconciled with receiving reports and other documents evidencing indebtedness.

Real Property Accounts Are Not Reconciled With Engineering Records

In our review of real property accounting records at 27 of the 28 VAMCs visited, we found that 20 of the VAMCs had not established procedures to reconcile these accounts with the information in engineering records and had not performed such reconciliations during fiscal year 1987. We identified several items of real property at four VAMCs which were still recorded in accounting records at the end of fiscal year 1987, although the items had been destroyed or the centers no longer owned them. At one VAMC, seven structures that were disposed of during fiscal year 1987 were still recorded in the accounting records at year-end for a book value of $337,615. We also identified buildings valued at several million dollars which were in use at the end of fiscal year 1987, but had not been recorded in the accounting records.

VA's policy and procedures manual requires that VAMC staff responsible for fiscal activities verify real property accounts with engineering records at the end of each fiscal year. This verification helps ensure that all VAMC real property, and only such property, is included in the financial statements.

Discrepancies in Property Records Are Not Promptly Corrected

We found that although reconciliations of supply property records between the Centralized Accounting for Local Management (CALM) system accounting records and subsidiary property records are usually performed, necessary adjustments to correct discrepancies are not always made in the month they are identified. Of the reconciliations we reviewed at 28 VAMCs, the accounting records for VA's nonexpendable property were not adjusted for reconciling items within the month at 11 VAMCs, and adjustments of subsidiary records in the supply department were not completed at 10 VAMCs. The property items that needed to be removed or added to the accounting and subsidiary supply records sometimes appeared on several monthly reconciliation listings before adjustments were made. Such delays resulted in $1.9 million in nonexpendable property items, which were received during fiscal year 1987, not being entered in CALM by year-end, as noted in our fiscal year 1987 report on internal accounting controls.

VA's policy and procedures manual requires VAMC staff responsible for fiscal and supply activities to periodically reconcile differences between CALM accounting records and the subsidiary property records, which are maintained by a separate computer system. VAMC personnel are required to compare reports from the two systems on nonexpendable equipment and warehoused supplies, identify any discrepancies, and properly enter adjusting transactions to the appropriate system.

Debt Write-Offs Are Not Reported to IRS

Of the 28 VAMCs at which we reviewed receivable activities, 14 did not report debt write-offs to the Internal Revenue Service (IRS) as income to the debtor. Generally, when a taxpayer is released from a debt, the amount of the debt represents taxable income to the taxpayer (26 U.S.C. 61(a)(12)). Office of Management and Budget (OMB) Circular A-129 establishes the policy that when a federal agency releases a taxpayer from a debt, the agency shall report any written-off amounts over $600 to IRS. At several VAMCs, fiscal personnel said they had not been informed of this policy.

Financial Transactions Are Not Recorded in the Proper Fiscal Year

VA's controls and procedures failed to adequately ensure that all financial transactions processed by VAMCs were properly recorded in the general ledger accounts in the fiscal year they occurred. Our statistical testing of October and November 1987 payment transactions disclosed goods valued at $434,126 that were received by VAMCs in fiscal year 1987 but were not recorded in that year's accounting records. Although the amounts involved were not considered material to VA's consolidated financial statements for fiscal year 1987, we believe that they are significant enough to warrant management's attention to correct the problem before future year-end closings.

The $434,126 total value of improperly recorded payments represented about 12.4 percent of the $3.5 million total value of items sampled. Our sample was taken from a universe of items valued at $39 million. The improper recordings we identified involved nine transactions which originated at seven VAMCs—one each at six VAMCs and three at a single VAMC.

The improper recording of the payment transactions occurred because the VAMCs in question did not enter transaction documents in the computer system in a timely manner. Such improper recordings caused understatements in the VAMCs' operating expenses and accounts payable and overstatements in the equity account, undelivered orders.

Title 2 requires that goods or services be recognized as an asset or an expense and that the related payable be established in the period in which the goods or services are received. In addition, OMB's Financial Management and Accounting Objectives (M-85-10, March 15, 1985) specify that financial data should be recorded as soon as practicable after a transaction has occurred. Also, a basic concept of generally accepted accounting principles is that revenues should be matched with the associated expenses in the same accounting period.

Conclusions

The internal controls used to control the billions of dollars VA expends in the medical care area need to be improved. In some cases, such as review of obligation balances and reconciling control accounts to subsidiary records, VA's procedures were adequate, but they were not properly implemented. In other cases, such as reporting debt write-offs to IRS, VA had not developed adequate controls to ensure that VA's financial management responsibility was fulfilled. The weaknesses identified during our review will require VA to develop and implement a comprehensive plan for correcting the problems identified.

Agency Comments and Our Evaluation

We discussed these problems with agency officials who agreed that the existing procedures needed to be revised. They provided us with a corrective action plan which addressed needed improvements in internal controls in the following areas.

- Implementation of VA-required manual controls in the cost recovery programs at each VA medical center.
- Staff analysis and documentation of obligation documents near the end of each fiscal year.
- Reconciliation of accounts payable records to related documents on a monthly basis, with specific emphasis on the need to complete all reconciliations by year-end.
- Reconciliation of real property accounts with engineering records at the end of each fiscal year.
- Completion of the required monthly reconciliation between the accounting and supply records, including finalizing any necessary adjustment transactions, and completion at year-end of all reconciliations and any necessary adjustments.
- Reporting of debt write-offs, as necessary, to the IRS.
- Processing of all accounting transactions on a monthly basis, with special emphasis on the need to process all transactions by year-end.

Based on a review of the stated procedures and discussions with agency officials, we believe that the corrective action plan appropriately addresses the problems we identified. Accordingly, we are not including any recommendations on these issues in this report. In subsequent audits, we will review the adequacy of the implementation of this plan.

Internal Control Improvements Needed in the Veterans Benefits Area

Expenses for veterans benefits during fiscal year 1987 exceeded $15 billion and covered such diverse areas as disability compensation, pensions, and educational assistance. Our review of the accounting controls utilized to control this area disclosed the following weaknesses:

- numerous internal control deficiencies in the ADP systems utilized to account for and control benefit payments, including inadequate system documentation and not implementing proper fund control procedures, and
- inconsistent implementation of a policy to ensure that benefit checks which exceed specified dollar values are manually verified before issuance.

Other problem areas we identified in the internal controls over the veterans benefits programs included untimely action on collection of accounts receivable, failure to properly recognize liabilities incurred, inadequate fund control procedures, lack of written procedures for initiating and authorizing many of the accounting processes, and failure to implement an effective quality assurance program.

Deficiencies in the Compensation and Pension and Education Benefits Systems

Data processing system and VA regional office deficiencies that we described in our management letter for fiscal year 1986 continued to exist through 1987 for the compensation and pension benefit payment and accounting system. In addition, our 1987 work found similar deficiencies in the systems used to pay and account for education benefits.

As we previously reported for fiscal year 1986, automated and manual claims processing procedures and controls used to authorize, pay, and account for compensation and pension benefits do not provide sufficient assurance that compensation and pension system master records were properly updated, or that payments were made in the proper amount. The following are examples of the weaknesses which we identified in our fiscal year 1986 management letter which were still uncorrected at the time of our fiscal year 1987 audit.

- Data processing control reports designed to ensure that transactions were properly processed by reconciling control files to the master file were out-of-balance. We first reported this problem to VA in 1976.[1]
- Transaction counts could not always be reconciled among computer programs because programs used different methods to count records. These

[1] Letter report to the Administrator of Veterans Affairs (GAO/MWD-76-90, February 6, 1976).

counts could help ensure that all claims data submitted by regional offices were processed, unauthorized claims data were neither added nor created during processing, and rejected transactions were properly reentered or otherwise processed.

- Comparisons of authorized payment information (input) to processed payment information (output) were not performed or were incorrectly performed in 10 of 17 regional offices reviewed for fiscal year 1986. For fiscal year 1987, the reviews were not performed or were improperly performed at 4 of the 10 regional offices we visited.
- The compensation and pension system did not provide documentation to verify benefit payment vouchers generated after the master file had been updated for the month. These payments, referred to as irregular payments, totaled $133 million in fiscal year 1986 and $188 million in fiscal year 1987.

Education Systems

In addition to the previously reported weaknesses in the compensation and pension benefit systems, we also reported that VA's computer systems for paying and accounting for educational benefits under various education programs do not meet internal control standards for ensuring accurate and proper master-record updates and subsequent payments.

The system which pays and accounts for educational benefits allowed under Chapters 34 and 35 of Title 38 of the United States Code provides limited assurance that master records are correctly updated when transactions are processed or that benefit payments actually reflect amounts that should be paid. Based on documentation for this system, which was published in 1966, there are two key control reports for this system. One report was designed to verify that all transactions are accurately processed, and the other report was intended to verify that payment vouchers properly reflect the results of master-record updating. However, although the control report covering the accuracy of transactions processed indicated that all transactions were not processed for the 2-month period we examined, VA staff had not intervened to reconcile the variance. Amounts on the second control report (which was intended to verify the accuracy of each month's benefit payment vouchers) are not used in certifying the vouchers for payment. The Chief of the Finance Division at the Hines, Illinois, Data Processing Center, informed us that "control points" have not been used to ensure the accuracy of education system vouchers since at least 1973.

Despite official certification that vouchers are correct and proper for payment, our tests at the Hines DPC did not disclose any evidence that the amounts of benefit payments authorized on education system vouchers were checked against anything to ensure the accuracy of the vouchers. According to the Hines DPC Finance Division Chief, his staff only made sure that sufficient funds were available and that the vouchers were properly recorded in the accounting journal.

Federal Information Processing Standards Publication (FIPS Pub) 73 states that maintaining data integrity is a major objective for a benefit payment computer system. FIPS Pub 73 identifies control techniques that can be used to achieve data integrity. One of these controls is the reconciliation of control files to the master file, as was envisioned by VA's 1966 system documentation. Also, Title 2 states that data processing controls should provide reasonable assurance that all transactions have been completely and correctly processed.

In addition, federal fiscal procedures as contained in Title 7 of GAO's Policy and Procedures Manual for Guidance of Federal Agencies requires, in general, that vouchers be audited prior to payment in order to (1) verify the accuracy of data on the vouchers, (2) ascertain that the vouchers and supporting documents are properly authorized, and (3) determine that the transactions are legal. But, in the case of VA's education vouchers, only the last objective of the preaudit process is achieved, thus, increasing the risk of improper payments.

When authorizing payments, regional office staff is responsible for determining the legality of individual payments. The education system, however, provides no means of ensuring the accuracy of the aggregate payment both as to the total number of checks or the total dollar amount of the payment vouchers.

As stated in our fiscal year 1986 management letter, VA is in the process of modernizing the compensation and pension benefit system. This modernization project also includes the education system. However, this project is not expected to be completed until mid-1990 or later.

Payment Verification Process Is Not Always Followed

As one means of helping to ensure payment integrity, VA has a policy that requires the Hines DPC Finance Division to obtain authorization from the applicable VA regional office before releasing compensation, pension, and education payments over certain thresholds. These thresholds range from $750 to $5,000, depending on the benefit program involved. Our tests found that regional offices generally followed the required procedures when the Hines DPC Finance Division requested authorization of such pending payments. However, our work at the Hines DPC found that at least 343 payment checks, issued through the compensation and pension system between July and September 1987, were released without apparent regional office authorization. Further work at two regional offices, relating to payment checks scheduled to be issued by the Hines DPC during September 1987, disclosed that the regional offices had not received timely notification of all of these payments and consequently could not authorize release of the payments.

VA's policy and procedures manual requires the prerelease authorization of the large checks and specifies the procedures to be followed. However, these procedures do not require supervisory review at the Hines DPC of large-check release authorization. Title 2 requires that qualified and continuous supervision be provided to ensure that internal control objectives are achieved.

The responsible Hines DPC Finance Division official attributed the release of the apparently unauthorized checks to a temporary employee who was unfamiliar with the requirements. We believe, however, that the lack of adequate supervisory review over the process, including reviewing the log of check-release authorizations received, contributed to the problem. Also, control over the process was vested in a single individual who was not fully qualified.

Release of checks that have not received regional office authorization could result in erroneous payments. These payments would then have to be set up as accounts receivable and recovered.

Other Opportunities to Improve Internal Accounting Controls

In addition to problems and deficiencies that could impact payment validity and accuracy, our tests disclosed other areas where VA needs to improve accounting and financial management controls over veterans benefit programs. These areas include accounts receivable collection, liability recognition, fund control, documentation of procedures, and implementation of a quality assurance program.

Accounts Receivable—Collection and Reporting

For 1986, we reported that 8 of 17 VA regional offices did not take or document timely collection action on all receivables we reviewed, and not all regional offices properly reconciled subsidiary accounts receivable listings to collection records or reported the results of this reconciliation to the VA central office. Our tests during the 1987 audit showed similar results; of the 10 regional offices we reviewed, 6 did not take and/or document timely collection action on all receivables that we tested. Additionally, four regional offices did not completely reconcile the year-end subsidiary accounts receivable listing to memorandum records, and three regional offices did not report all accounts receivable information to the central office correctly.

Under both the Federal Claims Collection Standards[2] and VA procedures, timely and effective action should be taken on accounts receivable. The appropriate action varies with the nature of the receivable and can range from writing off low-value receivables with little likelihood of collection, to having the Department of Justice file suit for collection. To help ensure that appropriate action is taken, VA requires regional offices to reconcile DPC-generated subsidiary accounts receivable listings to locally maintained collection records. The results of this quarterly reconciliation are to be reported to VA's central office.

VA has taken some actions to improve the situation. Subsequent to fiscal year 1987, VA completed centralizing collection responsibility for certain benefit-related loans, and it plans to centralize collection responsibility for benefit receivables due from the heirs of deceased debtors. We are evaluating these actions during our fiscal year 1988 audit.

Recognition of Liabilities

In our fiscal year 1986 management letter, we reported that VA did not compute or record all liabilities for compensation and pension programs. Under an agreement with OMB, VA did not record (1) the estimated liability attributable to the reinstatement of suspended benefit payments or (2) the liability resulting from the accumulation of amounts accrued from returned benefit checks or the accumulation of monthly benefit amounts that do not meet VA's check-issuance threshold. However, this practice is not in accordance with generally accepted accounting principles for federal agencies. We estimated these contingent liabilities to total $19.4 million in 1986 and $16.6 million in 1987.

Title 2 requires that contingent liabilities be recorded and reported if available information indicates a liability probably has been incurred and the amount can be reasonably estimated. Since VA has adequate information to estimate the impact of these contingent liabilities, it should reflect this amount in its financial statements. As of September 30, 1988, VA had not taken action on our prior suggestion that

[2]These standards were issued by the Department of Justice and the General Accounting Office on March 9, 1984, under the Debt Collection Act and are found at 4 C.F.R. 101.1-105.5.

it compute and record these liabilities in the compensation and pension benefit payment and accounting system.

Benefit Accounting Systems Lack Fund Control

Benefit accounting systems for three of VA's benefit appropriations do not contain all necessary accounts for effective and accurate fund control. In one system used to pay benefits for a job training program, we found that year-end accounts payable were overstated by $14 million because the accounting system expensed undelivered orders (obligations that had not yet become due) instead of properly showing them as undelivered orders in the equity account. The other two benefit payment accounting systems also lacked this capability to properly record undelivered orders. VA corrected the identified overstatement, for financial statement purposes, after we brought it to management's attention.

Title 31, Chapter 35 of the United States Code, OMB Circular A-127, and Title 2 procedures require that agencies have effective fund control and accounting systems. The procedures also require that the accounting systems accumulate and report obligational data promptly and accurately. However, by not properly showing the amount of undelivered orders, VA did not comply with these requirements.

Written Financial Procedures

Contrary to Title 2 and OMB Circular A-127, the Hines DPC Finance Division lacks current written procedures for initiating and authorizing many of the functions it performs and the transactions it initiates. For example, no current written procedures exist to describe the processes used to certify payment vouchers in the compensation and pension system and to send these vouchers to Treasury for payment. These vouchers totaled over $14 billion in fiscal year 1987. In addition, the Hines DPC Finance Division lacks formal written procedures for verifying and releasing large checks; preparing and reconciling Treasury reports; preparing and processing journal vouchers; and preparing, authorizing, and controlling documents authorizing direct modification to accounting records (i.e., VA's "fixit" transactions). Preparation of and adherence to procedures covering direct record modifications is especially important since these transactions, unlike journal vouchers, do not always leave a usable audit trail in the accounting system. For example, VA used a direct record modification to remove $22 million in compensation and pension costs from the accounting records in September 1987. The revised accounting journal gave no overt indication that costs were removed.

Federal internal control standards require that internal control systems and all transactions and other significant events be clearly documented, with the documentation readily available for examination. For example, OMB's financial management and accounting objectives in Circular A-127 and federal accounting system standards in Title 2 mandate that (1) both manual and automated components of an accounting system be documented to reflect how the system actually operates and (2) all accounting systems include adequate audit trails.

Quality Assurance Program for Financial Systems

The VA Hines DPC Finance Division does not have, and is not required by VA to have, a quality assurance program. The Hines DPC Finance Division performs most of the fiscal and accounting activity associated with (1) VA's compensation, pension, and education appropriations and (2) its own administrative operations. As discussed throughout this chapter, our testing at the Hines DPC found numerous problems in programmatic accounting and fiscal operations, from lack of documented procedures to release of unverified large benefit payments. An effective quality assurance program at the Hines DPC Finance Division might have prevented, or led to the identification and correction of, these problems.

VA's policy and procedures manual establishes a systematic quality assessment process for hospitals and regional offices. The process provides a mechanism to help management analyze and evaluate accounting records and financial procedures and evaluate the quality of work being performed within fiscal operations. These reviews may also serve to inform management of internal control problems that require reporting and follow-up under the Federal Managers' Financial Integrity Act (FMFIA) of 1982.

However, the manual does not require that this systematic self-assessment process be performed at the Hines DPC Finance Division. The Hines DPC Finance Division Chief recognized the desirability of performing such reviews, but stated he currently lacked sufficient staff to do so.

Conclusions

VA has not developed basic controls in its automated system for veterans benefits to help ensure that payment transactions are properly processed. In addition, VA needs to develop controls to ensure that its existing procedures are adequately implemented. For example, it needs to ensure that large benefit payments are verified before issuance and that effective collection and reporting actions are taken on accounts receivable. Although adequate implementation of its existing procedures will address several deficiencies, VA needs to develop procedures in other areas, such as the initiation and authorization of certain financial functions. VA will also need to review its practice of recording liabilities associated with benefit payments to ensure that its procedures are consistent with generally accepted accounting principles for federal agencies.

Agency Comments and Our Evaluation

We discussed these problems with agency officials who agreed that the existing procedures needed to be revised. They provided us with a corrective action plan for improving internal controls in the following areas.

- The development of a means to compare the total number of data submitted from regional offices to the total number processed at the DPC, and a process to ensure that the modernized systems, including the education systems, have an effective and well-documented means of ensuring that beneficiary master records are properly updated and beneficiaries are paid the proper amount.
- Adequate supervisory review of the large-check release process to ensure only specifically authorized checks are issued.
- Presentation of action plans (in the next annual report under FMFIA and the next 5-year financial management system plan) to correct the benefit payment system problems and deficiencies.
- Proper and timely collection action on all receivables, and reconciliation of regional office records and reporting of the results of the regional office receivable management efforts to VA's central office.
- Implementation of the manual processes for computing and recording contingent liabilities at year-end.
- Proper accounting for obligations that have been incurred but are not yet due. In addition, the capability of all new or modified benefit payment accounting systems, such as a redesigned compensation and pension system, to account for all types of fund control transactions.
- Documentation of key processes and practices followed in performing financial management activities and maintaining the accounting records.
- Establishment of a generic review program for facilities that are not under either the Veterans Health Services and Research Administration or the Veterans Benefits Administration.

Based on a review of the stated procedures and discussions with agency officials, we believe that the corrective action plan appropriately addresses the problems we identified. Accordingly, we are not including any recommendations on this area in this report. In subsequent audits, we will review the adequacy of the implementation of this plan.

Internal Control Improvements Are Still Needed in the Housing Credit Assistance Area

VA's housing credit assistance program guarantees and holds home mortgages of about $146 billion and $1.2 billion, respectively, as of September 30, 1987. Adequate internal controls are needed in this area to provide management and external users adequate information on the cost associated with the program which is necessary to effectively manage this important area. Our review disclosed that VA has not implemented a system to effectively determine the losses associated with its housing credit program, which can cause program costs to be materially misstated. In addition, VA needs to improve its process for (1) reconciling subsidiary account balances to those shown in the general ledger and (2) ensuring that journal vouchers are properly supported and approved by supervisory personnel.

System for Determining a Provision for Loan Losses Is Lacking

Although VA adjusted its financial statements for fiscal years 1986 and 1987 to establish an adequate provision for the losses associated with its housing credit assistance program, it did not institute a system to annually adjust the provision for program losses on a consistent basis. Without a consistent mechanism to recognize such losses, VA's financial statements could be misstated. Equally important, such an accrual-based methodology would provide management and the Congress with important information on the costs of this program.

The analysis needed to determine the provision for loan losses requires both historic and current information from several sources. Because of the extensive data required to perform the analysis and the lack of an integrated ADP system to provide the data, the analysis is very time-consuming. We therefore suggested in our fiscal year 1986 management letter that the Administrator of Veterans Affairs direct the Controller to incorporate a process for this analysis into the housing credit automated systems where possible and, in the interim, to establish procedures to ensure a consistent, accrual-based analysis of program costs.

VA did not take action on our suggestions during fiscal year 1987. Accordingly, we assisted VA in estimating the loan losses for fiscal year 1987 by using a computer spreadsheet which we developed for this purpose. We provided our computer spreadsheet to VA along with instructions for its use in determining the loss provision for future fiscal years, until the process can be incorporated into VA's automated systems.

General Ledger Accounts Are Not Reconciled to Subsidiary Systems

Similar to our findings during our fiscal year 1986 examination, our 1987 work disclosed that for 10 of the VA regions we visited, the general ledger control accounts were not reconciled to the subsidiary systems. In addition, discrepancies between the control accounts and the subsidiary records were not resolved in a timely manner. For example, in one VA regional office, the claims receivable account for the housing credit assistance program had not been reconciled since the late 1970s. The difference as of December 1987 was over $1 million. In addition, because the regional office was unable to resolve this difference, it stopped posting receivables to the general ledger for about 5 months. This led to the general ledger's failing to reflect an estimated $8.8 million in claims receivables for fiscal year 1987.

During our 1987 examination, we also found instances where the VA central office did not properly perform required reconciliations of various control and subsidiary accounts. For example, central office personnel were unaware of a programming flaw in the subsidiary accounting system which details loan sales, by VA regional office, because they had not performed a reconciliation between this report and the general ledger. When we performed this reconciliation, we found that the subsidiary system report contained a $100 million mathematical error.

General ledger reconciliations are an important internal control technique in ensuring the integrity of data contained in VA's financial accounting system and must be consistently and properly performed. In the absence of properly performed reconciliations, an agency cannot be assured that all transactions are appropriately recorded in the accounting records. Adequate reconciliation procedures, at a minimum, should include the identification, investigation, and resolution of all differences and, where warranted, making appropriate adjustments to either the subsidiary records or the general ledger account balances. Also, it is important that these reconciliations be properly documented and performed promptly.

VA has taken some positive steps to emphasize the importance of account reconciliation in its regional offices by publicizing the issue in newsletters and training seminars. However, as previously stated, general ledger reconciliations are an important internal control technique in ensuring the integrity of data contained in VA's financial accounting systems, and action needs to be taken to ensure this requirement is accomplished.

Journal Vouchers Lack Adequate Documentation and Authorization

During both our 1986 and 1987 examinations, while performing control testing at VA regional offices, we noted several instances where journal vouchers relating to housing credit assistance transactions were prepared without adequate documentation. Furthermore, many of the vouchers either were not signed by a reviewing official or were prepared and authorized by the same individual. For example, during our 1987 review in one VA regional office, the proper authorizing signatures for preparation and/or approval were missing in 8 of the 10 journal vouchers we tested.

Title 2 requires that complete and accurate documentation be maintained for transactions and for other significant events. VA's policy and procedures manual further requires that journal vouchers be authorized by an individual not directly involved in their preparation.

VA's accounting manual for the housing credit assistance program also states that journal vouchers will be approved by the Chief, Accounting Section, in each regional office. Officials from one regional office have interpreted this manual reference to mean that no approval is needed when the Chief, Accounting Section, initiates the journal voucher. We believe that approval is required by an individual not directly involved in preparation of a voucher, even when it is initiated by the Chief, Accounting Section. Without adequate documentation and appropriate review, VA increases its risk of errors or irregularities occurring and going undetected in the recording of the housing credit assistance transactions.

Conclusions

Internal and external users, such as OMB and the Congress, need accurate, consistent, and timely information on the costs associated with VA's housing programs. At the current time, VA has not developed an adequate system to provide the necessary information. VA also needs to ensure that adequate separation of duties is maintained over journal vouchers which are prepared by senior officials.

Recommendations

We recommend that the Secretary of Veterans Affairs direct the Chief Benefits Director and the Controller to develop a plan for implementing corrective action on the internal control problems that our audit disclosed in the housing credit area. VA's requirements for reconciliation of account balances and documentation and proper authorization of accounting transactions are excellent internal control techniques for ensuring the integrity of data contained in VA's financial accounting system. Accordingly, the plan for corrective action should include procedures for ensuring compliance with agency policies and procedures. In addition, the Controller should clarify the policy regarding approval of journal vouchers to require an individual not directly involved in voucher preparation to approve vouchers initiated by the Chief, Accounting Section.

Agency Comments and Our Evaluation

We discussed these problems with agency officials who advised us that the Veterans Benefits Administration conducts detailed surveys of field-station fiscal functions in order to ensure compliance with both technical processing procedures and agency fiscal policies. However, as shown by our audit, the requirements for reconciliation of accounts balances and performance of other agency policies are not always accomplished. Accordingly, we believe our recommendation is appropriate for the problems described.

Also, agency officials agreed that there should be separation of duties between voucher preparation and approval. They indicated that appropriate action would be taken to ensure that vouchers are approved by an individual at a higher level than the individual who prepared the voucher.

Payroll Internal Control Improvements Are Needed

VA relies on the Personnel Accounting and Integrated Data (PAID) system to ensure that all employees are paid correctly and on-time. According to VA, however, this system is over 20 years old, uses outdated technology, requires excessive manual intervention, and has tendencies towards errors. Accordingly, VA is in the process of modernizing and redesigning the system. We identified two types of pay transactions where there is a tendency for errors because manual intervention is required with the current automated system in order to properly process the transactions. The two types of pay transactions are within-grade increases for special-rate employees and special pay for physicians and dentists. We also found that several locations did not perform the required verifications and reconciliations of information entered in the payroll system.

Errors in Certain Pay Transactions

VA had about 6,000 special-rate employees as of January 3, 1988. Special rates are established to aid in recruiting and retaining employees in areas where personnel shortages exist. VA's PAID system only recognizes "general schedule" pay rates and the system must be manually adjusted to account for special rates. For example, at one medical center that we visited, our test of payroll transactions included one special-rate employee who had received a within-grade increase during the pay period tested. The PAID system automatically computed the dollar amount of the employee's new pay using the general service pay rates. When the medical center failed to manually adjust the salary rate to reflect this employee's special-rate status, the employee's pay was understated by $36.40 per pay period. The underpayments amounted to $436.95 before corrective action was taken as a result of our identification of the incorrect pay transaction. A VA personnel official told us that in order to pay a special-rate employee, special codes must be entered into the employee's file, instructing the PAID system to bypass normal system controls because one of the system's controls requires that the salary amount be compatible with the general schedule pay rates. Thus, for special-rate employees, manual pay adjustments must be made, and the many PAID edits designed to control the processing of VA's payroll are not utilized.

A similar problem exists in VA's calculation of special incentive pay for physicians and dentists, which also must be performed manually. A September 18, 1985, report by VA's Inspector General disclosed that overpayments of about $180,900 could be attributed to errors in calculating special pay for physicians and dentists. This issue was also discussed in a March 31, 1988, Inspector General report. These overpayments were largely caused by VA medical centers not properly reducing physician and dentist special pay once they reach certain prescribed levels. The Inspector General also found that other problems, such as mathematical errors, were the result of VA's reliance on manual pay calculations. During our review, we were shown examples of overpayments at the Boston medical center which were made as a result of this problem. These overpayments to dentists ranged from $371 to $1,134 and were discovered 9 to 16 months after they first occurred by the medical center's review of selected pay and deduction items. VA is entitled to reimbursement for such overpayments. However, under federal claims standards, federal employees may request waiver of the requirement to pay back overpayments resulting from administrative errors. Thus, depending on the decision made on each waiver request, VA may not obtain reimbursement for these overpayments.

Verification Requirements Are Not Followed

The PAID system generates several reports which VA medical centers and regional offices (VA stations) are required to verify or reconcile to ensure the accuracy of VA's payroll records and payroll data processing. We found the following problems in the payroll verification and reconciliation process at the 37 VAMCs and regional offices we visited during our fiscal year 1987 audit.

- Five stations did not reconcile the total time and attendance reports that were transmitted from the stations with the number received at the Austin DPC.
- Six stations did not reconcile out-of-balance reports, which indicate whether personnel actions are transmitted correctly.
- Six stations did not reconcile differences between PAID and the VA "station trial balance" system.
- Sixteen stations did not completely reconcile the semiannual verification of selected pay and deduction items.
- Seven stations did not completely verify the monthly listings of employee accessions and separations.

Title 6 of GAO's Policy and Procedures Manual for Guidance of Federal Agencies requires that suitable controls be incorporated in payroll systems to provide effective checks to ensure that payroll data are correctly processed. Examples of such controls outlined in Titles 2 and 6 include: (1) reconciliations between general ledger balances and subsidiary accounts, (2) data communication controls, (3) record counts, and (4) verifications of file data.

Conclusions

The most efficient method of improving the accuracy of pay of special-rate and physician and dentist employees is to include the proper processing requirements and controls in VA's automated payroll system. Accordingly, the necessary automated system changes should be considered during the design phase of VA's payroll system redesign and modernization project. In the interim, each VA station needs to initiate action to verify the salary rates of all of the special-rate and physician and dentist employees. In addition, each VA station needs to implement controls to ensure that all required payroll reconciliations and computer report verifications are accomplished.

Agency Comments and Our Evaluation

We discussed these problems with agency officials who provided us with the corrective actions taken with respect to the problems described in this chapter. Based on our discussions with agency officials, we believe that the corrective actions taken address the problems we identified. Specifically, agency officials advised us that the PAID project to automate special pay calculations was scheduled for phased implementation to begin in June 1989, with complete implementation by September 30, 1989. In addition, all special salary rate schedules were automated in the PAID system on October 1, 1988, allowing for normal PAID processing of pay rates and within-grade increases. Accordingly, we are not including any recommendations in this report. In subsequent audits, we will review the adequacy of the implementation of these corrective actions.

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