Office of Inspector General
Audit Report

Supplementary Report on Audit of Internal Control Systems Related to the Office of the Secretary of Transportation's Financial Statements for Fiscal Years 1994 and 1995

Report No: AD-OT-7-001
Date Issued: January 24, 1997

DEPARTMENT OF TRANSPORTATION
UNITED STATES OF AMERICA

Memorandum

U.S. Department of Transportation
Office of the Secretary of Transportation
Office of Inspector General

Subject: ACTION: Supplementary Report on Audit of Internal Control Systems Related to the Office of the Secretary of Transportation's Financial Statements for Fiscal Years 1994 and 1995
Report No: AD-OT-7-001

Date: January 24, 1997

From: Lawrence H. Weintrob
Assistant Inspector General for Auditing, JA-1

Reply To Attn Of: JA-20:X61496

To: Director, Office of Financial Management, B-30
Director, Transportation Administrative Services Center, SVC-1
Associate Administrator for Budget and Policy, TBP-1

I am providing the subject report for your information and use. It contains additional details on, and recommendations for correcting, internal control problems briefly summarized in our (i) August 18, 1995, report (Report Number AD-OT-5-008) presenting our disclaimer of opinion on the Office of the Secretary of Transportation's (OST) Statement of Financial Position as of September 30, 1994, and (ii) February 28, 1996, report (Report Number AD-OT-6-002) presenting our qualified opinion on OST's Statement of Financial Position as of September 30, 1995. In preparing this report, we considered comments by your staffs on our October 29, 1996, discussion draft report. At the November 21, 1996, exit conference, agreements were reached on the findings and recommendations and monetary amounts. It was also agreed that we would proceed directly to a final report. A synopsis of the report follows this memorandum.

This report contains six findings and six recommendations. In accordance with Department of Transportation Order 8000.1C, please provide within 60 days your written comments on the findings and recommendations including target dates for implementing the recommendations. We would also like comments on the "Other Issue" included in this report related to investing the Working Capital Fund cash balance.

I appreciate the cooperation and assistance extended to our auditors during these audits. If you or your staff have any questions on the report, please contact James Childers of my staff on 366-1974.

Attachment

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U.S. Department of Transportation

Office of Inspector General

Supplementary Report on Internal Control Systems Related to the Office of the Secretary of Transportation's Financial Statements for Fiscal Years 1994 and 1995

AD-OT-7-001 ***January 24, 1997***

Objectives

The internal control related objectives for our audits of the Office of the Secretary of Transportation's (OST) Financial Statements for Fiscal Years (FY) 1994 and 1995 were to determine whether OST and the Federal Transit Administration (FTA) (i) had in place an adequate internal accounting and administrative control structure that provided reasonable assurance of achieving internal control objectives and (ii) had adequate policies and procedures in place to provide reasonable assurance of achieving its internal accounting and administrative control objectives regarding the existence and completeness assertions for performance measures.

Conclusions

OST and FTA generally had adequate policies and procedures in place to provide reasonable assurance that the existence and completeness assertions for performance measures were met. However, four material internal control weaknesses and two non material reportable conditions impaired OST's internal control structure associated with the FY 1994 financial statement. The material weaknesses related to internal controls over, and/or operating procedures for: (i)ensuring Property and Equipment (P&E) accountability; (ii) supporting accounts payable balance; (iii) supporting accounts receivable net balance; and (iv) recording and reporting the Short Term Lending Program activity. The non material reportable conditions involved (i) recording and reporting Other Governmental Liabilities and (ii) establishing accrual procedures for donations. During the audits, OST and FTA took definitive actions that corrected one material weakness and one non material weakness. Regarding the remaining weaknesses, OST and FTA had not established adequate internal controls over (i)P&E accountability, (ii) accounts payable balance; (iii) accounts receivable net balance; and (iv) recording and reporting Other Governmental Liabilities.

SYNOPSIS

OST may be able to earn interest by investing a portion of its Working Capital Fund cash balance in U.S. Treasury securities.

Monetary Impact

We estimated the potential interest OST could earn from investing a portion of the Working Capital Fund cash to be about $2 million per year. While no specific savings were identified with the other recommendations, correcting the weaknesses will help ensure accuracy, timeliness, and reliability of financial information and efficiency of operations.

Recommendations

The Office of Inspector General (OIG) is making a total of six recommendations to correct the three material internal control weaknesses and one reportable condition. Since OST and FTA actions taken during the audits corrected one material weakness and one reportable condition, no recommendations on these issues are necessary.

Management Position

At the exit conference, OST and FTA agreed with the findings, recommendations, and monetary amounts in our October 29, 1996, discussion draft report. It was also agreed that the OIG would issue this report and obtain written comments and target dates for implementing the recommendations.

Office of Inspector General Comments

We are awaiting management comments on this final report.

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I. INTRODUCTION

A. Background

The Office of the Secretary of Transportation (OST) provides leadership, professional guidance, broad oversight, and coordination in the development and implementation of policies, plans, and programs for the Department of Transportation (DOT). As such, OST serves as the catalyst for many of the Departmentwide initiatives that are undertaken in carrying out the mission of the Department.

OST's financial statements for Fiscal Years (FY) 1994 and 1995 covered only the activities which were subject to the provisions of the Chief Financial Officers (CFO) Act of 1990. These activities consisted of the Working Capital Fund (WCF), Small and Disadvantaged Business Loan Program (known as the Short Term Lending Program), Gifts and Bequests (G&B) Fund, and Payments to Air Carriers. The Payments to Air Carriers were not included in the statement for FY 1994 that was prepared by OST.

OST accounting personnel prepared the financial statement for FY 1994 and Federal Transit Administration (FTA) accounting personnel prepared the OST financial statement for FY 1995. After the audits were completed, the Transportation Administrative Services Center was formed which now provides the services for the WCF. OST reported total assets of $75.2 million on the Statement of Financial Position as of September 30, 1995, and $61.3 million as of September 30, 1994. In addition, revenues of $112.8 million were reported for FY 1995 and $84.1 million for FY 1994 on the Combined Statement of Operations. The primary reason for the increase in total assets and revenues between FYs 1994 and 1995 was the inclusion of Payments to Air Carriers which reported $7.3 million in assets and $26.7 million in revenues.

The largest fund represented on the OST financial statements is the WCF which was authorized in 1966. The basic principle of the WCF is to consolidate under one financing arrangement common services that would provide economies of scale and efficiency of operations while avoiding a duplication of effort. The WCF operates as a revolving fund in which goods and services are financed by charging current operating expenses back to the customers and funding asset acquisitions from equity available for reinvestment which was derived through the depreciation of capitalized goods. The WCF reflected $4.7 million of revenues exceeding expenses from operations for FY 1995 but a $414,000 shortfall of revenues for FY 1994.

OST and FTA are responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control mechanisms, policies, and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that transactions are properly recorded and accounted for to permit the preparation of reliable financial reports in accordance with applicable accounting policies and to maintain accountability over assets; funds, property, and other assets are safeguarded against loss from unauthorized use or disposition; transactions are executed in compliance with laws and regulations having a direct and material effect on the financial statement; and data supporting reported performance measures are properly recorded and accounted for to permit preparation of reliable and complete performance information.

B. Objectives, Scope, and Methodology

Our audits of OST's Financial Statements for FYs 1994 and 1995 were performed in response to the financial statement audit provisions of the CFO Act of 1990. The internal control-related objectives for these audits were to determine whether OST and FTA (i) had in place an adequate internal accounting and administrative control structure that provided reasonable assurance of achieving internal control objectives and (ii) had adequate policies and procedures in place to provide reasonable assurance of achieving its internal accounting and administrative control objectives regarding the existence and completeness assertions for performance measures. These audits were conducted in accordance with the Government Auditing Standards prescribed by the Comptroller General of the United States, and included selected audit steps and procedures prescribed in the General Accounting Office (GAO) and President's Council on Integrity and Efficiency Financial Statement Audit Manuals and Office of Management and Budget (OMB) Bulletin 93-06, Audit Requirements for Federal Financial Statements. The audit work was performed at OST and FTA Headquarters in Washington, D.C.

The work performed during our audit of the FY 1994 financial statement included obtaining an understanding of the significant internal control policies and procedures and assessing the level of control risk relevant to all significant activity cycles, classes of transactions, and/or account balances. For those significant internal control policies and procedures found to be properly designed and placed in operation, we performed sufficient tests to assess more fully whether the controls were effective and working as designed. Our evaluation of the controls for reported performance measures was limited to controls to ensure the existence and completeness of the information reported. Our objective was not to render an opinion on the overall internal accounting and administrative control structure. The categories of significant internal control structure policies and procedures subjected to testing during the audit are listed in exhibit A, along with an overview of test results.

The initial internal control work performed during our audit of the FY 1995 financial statement focused on determining whether or not the significant internal control policies and procedures identified in the prior year's audit had changed materially. Upon determining that no material changes had occurred, we limited further work to following up on the material weaknesses and reportable conditions identified in the FY 1994 financial statement audit.

At OST and FTA, some of the internal controls in the various activity cycles are dependent on automated information system processing. In accordance with Government Auditing Standards, our review of these controls must be performed by or under the supervision of an information systems control specialist. However, such a specialist was not available within the Office of Inspector General (OIG) to review these controls and these controls were thus not reviewed.

C. Prior Audit Coverage

Although OST had prepared a financial statement for each of the last four fiscal years, the statements for FYs 1994 and 1995 were the first subjected to audit under the provisions of the CFO Act. OIG Report Number AD-OT-5-008, dated August 18, 1995, presented our disclaimer of opinion on OST's Statement of Financial Position as of September 30, 1994, and briefly summarized the internal control problems that are discussed in more depth in this report. Report Number AD-OT-6-002, dated

February 28, 1996, presented our qualified opinion on OST's Statement of Financial Position as of September 30, 1995, and described our limited testing approach for the associated internal controls.

II. FINDINGS AND RECOMMENDATIONS

Based on the results of our tests, we concluded internal controls over performance measures provided reasonable assurance that the performance information reported in the financial statements for FYs 1994 and 1995 was reliable in terms of meeting the existence and completeness requirements. However, our internal control testing during the audit of OST's FY 1994 financial statement identified six deficiencies which we concluded should be considered reportable conditions under standards established by the GAO, the American Institute of Certified Public Accountants, and OMB Bulletin 93-06.[1] Furthermore, we concluded four of the six deficiencies should also be considered material weaknesses under the standards referenced above.[2] These deficiencies, discussed in detail in findings A to F below, permeated one of the four activity cycles and 9 of the 12 material accounts reviewed. (A tabular summary of our internal control test results, by activity cycle and material account reviewed, is provided in exhibit A.) During informal discussions of these issues with OST management officials, they generally concurred with each of the findings and acknowledged the need for appropriate corrective actions. Our limited internal control work during the audit of OST's FY 1995 financial statement did not identify any new material internal control weaknesses or non-material reportable conditions.

For reporting under the Federal Managers' Financial Integrity Act (FMFIA), material weaknesses are defined differently than for financial statement audit reporting purposes. An FMFIA material weakness is a specific instance of noncompliance with Section 2 of the FMFIA regarding program and/or administrative internal control systems. In addition, FMFIA provides for the identification and reporting of significant accounting system weaknesses as material nonconformances under Section 4. According to current departmental guidance for FMFIA implementation, both a material

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[1]Reportable conditions are matters coming to our attention involving significant deficiencies in the design or operation of the internal control structure which, in our judgment, could adversely affect the entity's ability to ensure the objectives of the internal control structure, as previously defined, are being achieved.

[2]For financial statement audit reporting purposes, a material weakness is a reportable condition where the design or operation of one or more specific internal control mechanisms does not reduce to a relatively low level the risk of material errors or irregularities occurring and not being detected within a reasonable time by employees in the normal course of performing their assigned functions.

FMFIA weakness and a material nonconformance must merit the attention of the Executive Office of the President or the relevant congressional oversight committee. In our view, none of the financial statement material weaknesses identified in this report meet the departmental criteria for reporting either as an FMFIA material weakness or material nonconformance.

Our consideration of the internal control structure would not necessarily identify all matters which should be considered reportable conditions. Accordingly, the six deficiencies our tests identified do not necessarily constitute all reportable conditions associated with the internal control structure established for OST's financial statements.

Although these weaknesses should be corrected, the potential impact of each individual weakness on the Department's consolidated financial statement would be immaterial for FY 1996. The following listing shows, for each of our six findings, whether corrective actions are pending and the potential impact on the departmental financial statement.

Findings	Action Pending on Recommendations	Potential Adverse Impact on Departmental Financial Statement
Material Weaknesses		
A	Yes	Minor
B	Yes	Minor
C	Yes	Minor
D	No	None
Reportable Conditions		
E	Yes	Minor
F	No	None

As presented below, our findings are grouped by category and significance. The more significant internal controls-related problem areas--those meeting the above definition of a financial statement "material weakness"--are grouped together and presented first.

The remaining internal controls-related issues are then discussed as "Reportable Conditions." Finally, a brief discussion is presented under "Other Issue" on the concept of OST earning interest by investing a portion of the WCF cash balance deposited with the U.S. Treasury.

Material Weaknesses

Finding A. Property & Equipment (P&E) Accounting Records Were Not Adequately Supported

WCF internal controls for P&E did not ensure the accounting records reflecting the $12 million net book value on the FY 1994 Combining Statement of Financial Position were adequately supported by subsidiary property records. The financial statement showed equipment, computer software, and leasehold improvements with an acquisition value of $35.9 million. During the audit, OST's accounting office requested the program offices to verify the P&E on hand as of September 30, 1994. After referring to their property records, the program offices reported an acquisition value of $35.4 million for P&E--a difference of $500,000. Although an effort was made to reconcile the accounting records to the corresponding property records, the reconciliation had not been completed by the end of our audit field work. As a result, we were unable to confirm the WCF P&E reported on the FY 1994 Combining Statement of Financial Position.

During FY 1995, substantial efforts were made to reconcile P&E accounting records to the corresponding property records in response to the FY 1994 audit finding. However, this identified material internal control weakness was not fully corrected, so the beginning P&E inventory balance as of October 1, 1994, could not be validated. Furthermore, records supporting the disposal of $12.6 million worth of P&E were generally not available. The lack of a beginning inventory balance and documents to support the disposal of the $12.6 million in P&E prevented us from applying other auditing procedures to determine whether the ending balance reported for P&E was fairly presented on the Combining Statement of Financial Position as of September 30, 1995.

Discussion

Guidance on accountability and control of P&E exists at several different levels within the Federal Government. Under the authority of the Budget and Accounting Act of 1950 and FMFIA, GAO issued "Standards For Internal Control in the Federal Government," which are to be followed by executive agencies. According to specific standards contained in this document, "transactions and other significant events are to be promptly recorded and properly classified" and "periodic comparison shall be made of the resources with recorded accountability to determine whether the two agree." Further, OMB Circular A-127 Financial Management Systems, dated July 23, 1993, paragraph 6 ("Policy") states: "Financial Management . . . requires accountability of financial and program managers for . . . control over the Federal Government's financial resources and protection of Federal assets." DOT has also issued several orders which discuss the financial and administrative management and control of in use real and personal property. DOT Orders 2700.12, <u>Financial Management Control of Property</u> and 4410.4 <u>Equipment Management and Control Handbook</u> provide this guidance.

Our audit of OST's FY 1994 financial statement disclosed the breakdown of internal controls over P&E occurred because accounting and program officials did not (i) take a complete physical inventory of all equipment, computer software, and leasehold improvements as required by DOT Order 4410.4, (ii) reconcile all property records and reports to general ledger accounts as required by DOT Order 2700.12, (iii) correctly record acquisition costs of P&E, and (iv) report fully depreciated assets on the fixed asset module at nominal values but instead reported acquisition dollar values for the assets. Additionally, guidance in DOT Orders 2700.12 and 4410.4 on retaining cost documentation supporting capitalized personal property records was inconsistent and inadequate. As a result, we were unable to confirm the P&E reported on the financial statement.

Our audit of OST's FY 1995 financial statement disclosed that substantial efforts were made to reconcile P&E accounting records to the corresponding property records. The FY 1995 accounting records showed $26.2 million acquisition value in equipment, computer software, and leasehold improvements. We selected 50 items, with a total acquisition value of $10.9 million, to trace from the accounting records to the corresponding property records and finally to a physical inventory of the items. We accepted 44 items in the sample. The remaining six items, valued at only $54,000 had recording and reporting problems and could not be located, but were considered immaterial because they were below our materiality threshold of $184,000.

As part of OST's reconciliation during FY 1995, $12.6 million of P&E was deleted from the accounting records. Records supporting the disposal of this P&E generally were not available. The lack of support for the disposal of the $12.6 million in P&E prevented us from applying other auditing procedures to determine whether the ending balance reported for P&E was fairly presented as of September 30, 1995.

Recommendations

We recommend that OST and FTA accounting officials:

1. Prepare periodic reconciliations of accounting records to property records and promptly investigate and followup on significant differences found to exist in the accounts.

2. Advise accounting personnel of the requirements for retaining cost data for P&E.

3. Modify existing DOT orders to require retention of all cost data supporting capitalized property items for at least 2 years after the date of disposal.

Finding B. Accounts Payable Were Not Substantiated

Internal control procedures were not adequate to assure that $15.8 million in WCF accounts payable reported on the Combining Statement of Financial Position as of September 30, 1994, was adequately supported. The OIG sent confirmation letters to 17 vendors for 23 accounts payable balances totaling $2.5 million. Seven of the vendors replied on eight of the accounts payable balances, collectively valued at $372,000. Of these seven vendors, four stated that $152,000 in accounts payable were not owed. In addition, accounts payable other than those identified through our confirmation letters were not supported. For example, the accounting records contained one account payable for $86,000 when a liability no longer existed. Despite OST efforts to assure the validity of accounts payable, we were unable to confirm, through audit testing, the amount reported for WCF Accounts Payable, Net on the FY 1994 Combining Statement of Financial Position.

During FY 1995, accounting personnel conducted an extensive review of accounts payable resulting in downward adjustments of $2 million to the $15.8 million that had been reported on the FY 1994 Combining Statement of Financial Position. In conducting the FY 1995 audit, we also identified two other accounts payable totaling $409,400 that were not valid payables. OST accounting personnel were informed and took prompt action to correct the FY 1995 Combining Statement of Financial Position.

Discussion

As previously stated, transactions and other significant events are to be promptly recorded and properly classified and periodic comparison shall be made of the resources with recorded accountability to determine whether the two agree. Federal Financial Management System Requirements-1 (FFMSR-1) requires that the core financial system must ensure transactions are controlled properly to provide reasonable assurance that the recording, processing, and reporting of financial data are properly performed and that the completeness and accuracy of authorized transactions are ensured.

Formal internal control procedures requiring periodic reviews of accounts payable to determine the validity of the recorded obligations have not been established. We determined that accounts payable were overstated because of the process of establishing accruals in anticipation of a bill from a vendor, and leaving the accruals in the accounts payable records for extended periods of time when goods or services had not been received. As a result of our audit of the FY 1994 financial statement, OST and FTA conducted an extensive review of accounts payable resulting in a downward adjustment of $2 million to the $15.8 million that had been reported on the FY 1994 statement. Although this review was effective, OST and FTA need to establish formal internal control procedures to require periodic reviews of accounts payable.

Recommendation

We recommend that OST and FTA accounting officials develop and implement formal internal control procedures to require periodic reviews of accounts payable to ensure their validity.

Finding C. Accounts Receivable, Net, Could Not Be Readily Verified

WCF internal controls for Intragovernmental Accounts Receivable, Net, as reported on the FY 1994 Combining Statement of Financial Position, did not ensure that $473,000 in credits to accounts receivable could be verified. These credits were netted against about $2.5 million in debits, producing a balance for WCF Accounts Receivable, Net, of about $2 million (the amount reported on the Combining Statement of Financial Position). OST recognized that the continuing need to process accounts receivable credits was a problem because of the extensive time required to allocate cost to customers compared to the time available to promptly pay the bill. Although the OIG received confirmation letters on the sample accounts receivable, we were unable to confirm net accounts receivable because of the $473,000 in unsupported credits. OST's Accounts Receivable Aging Report as of September 30, 1995, showed $496,000 of credits to accounts receivable, an increase of $23,000, in the WCF Summary Billing Account since September 30, 1994.

We also found during the FY 1995 audit that the Departmental Accounting Financial Information System (DAFIS) Open Document File (ODF) showed $93 million in Accounts Receivable for the WCF for FY 1995. OST contended these were not valid receivables and existed only because of a unique DAFIS problem that required OST and FTA accounting to enter a receivable into the ODF to get the transaction into the accounts receivable module. In addition, OST and FTA accounting had used this process to accumulate total reimbursement billings to each Operating Administration.

To determine the validity of OST's contention that these $93 million in the ODF were invalid receivables, we selected a random sample of 44 items from a total of 485 items in the universe. Our random selection was prepared using a discovery sampling technique considered appropriate under the circumstances.

According to supporting documents, all 44 items were found to have been paid in FY 1994 or FY 1995, and therefore, were no longer valid accounts receivable. Based on our sample results, we concluded the entire $93 million were invalid receivables. However, accounting personnel should research each receivable, to the extent practical, before removing these receivables from the ODF.

Discussion

FFMSR-1 states that in order to support the Receivable Management process, the core financial system must: (i) maintain detailed information by account sufficient to provide adequate audit trails and to support billing and research activities, (ii) update each account when billing documents are generated and collections are received, and (iii) maintain individual receivables and references to appropriate supporting documentation. OMB Circular A-127, Appendix X, parts 5 and 6e, states the head of each agency is responsible for ensuring that the agency's financial management system records and reports financial management data "to provide for full financial disclosure and accountability in accordance with appropriate budget and accounting principles and standards."

Statement of Federal Financial Accounting Concepts (SFFAC) Number 1, Objectives of Federal Financial Reporting, states that financial reporting should be reliable. That is, the information presented should be verifiable, comprehensive, and free from bias and should faithfully represent what it purports to represent. As discussed in SFFAC Number 2, Entity and Display, financial statements represent the principal means of communicating accounting information about an entity's resources, obligations and revenues to those outside the entity. GAO's Standards For Internal Controls require that executive agencies (i) ensure transactions and other significant events are promptly recorded and properly classified, and (ii) conduct periodic comparisons of resources and obligations with recorded accountability to determine whether they agree.

OST personnel stated the $496,000 represented the net charges of all the bills that have been processed against the WCF Summary Billing Account since the implementation of the WCF Cost and Billing System in 1991. We were able to obtain sufficient support for the FY 1995 credits of $23,000. Because OST staff accountants informed us that the documentation supporting the credits was not readily available and retrieving the information would be very time consuming we did not substantiate this amount during the FY 1994 audit.

The credits to accounts receivable were caused by DAFIS. Accounting Services Division personnel said DAFIS does not always match the payments received (credits) from Operating Administrations to the original charges (debits) in the accounts receivable file. Based on how the system currently works, net monthly charges that are posted to the WCF Summary Billing Account are automatically assigned a bill number, and an account receivable is established. Because there is a different bill number each month, bills are not offset against each other and the balance accumulates month after month. Thus, the debits and credits are shown separately in the accounts receivable files. As of March 4, 1996, DAFIS had not been changed to solve this problem.

Recommendation

We recommend that OST and FTA accounting officials implement interim corrective actions to remove (a) unsupported credits of $473,000 in accounts receivable that were posted to the WCF Summary Billing Account in FYs 1991 through 1994, and (b) invalid accounts receivable of $93 million in the DAFIS Open Document File.

Finding D. <u>Accounting Procedures Were Not Established</u>

Our FY 1994 audit found OST had not established accounting procedures for recording and reporting Short Term Lending Program (STLP) financial activity. Funds borrowed from the U.S. Treasury were not properly identified in the accounting records as a liability, and funds on loan were recorded and reported on the STLP portion of the draft Combining Statements as expenses instead of Credit Program Receivables and Related Foreclosed Property. Also, while an allowance for bad debts had been established, it was not reported on the draft Combining Statement of Financial Position. As a result, the STLP portion of the draft Combining Statement of Financial Position understated assets and liabilities and overstated net position while the STLP portion of the draft Combining Statement of Operations overstated expenses. OST initiated action to establish appropriate accounting procedures for FY 1995 and corrected the STLP portion of the FY 1994 Combining Statements of Financial Position and Operations. The adjustments OST identified to correct the STLP portion of the Combining Statements of Financial Position and Operations totaled about $14.8 million, but we could not verify the adjustments for accuracy because the pertinent details were not provided until after our audit work had been completed.

In conducting the FY 1995 audit, we determined that the funds on loan as of September 30, 1994, and in the FY 1995 draft Combining Statement of Financial Position should have been separately recorded and reported as Other Cash on Hand and Credit Program Receivables instead of one lump sum of Credit Program Receivables. This distinction was necessary to properly reflect that STLP had $5,006,152 in participating banks which had not been loaned to borrowers. Since STLP could withdraw these funds, leaving this account as a receivable was improper. We advised FTA accounting officials of our determination on February 9, 1996, and corrective actions were taken to properly show Other Cash on Hand ($5,006,152) and Credit Program Receivables ($3,142,597) on the final FY 1995 Combining Statement of Financial Position.

<u>Discussion</u>

FFMSR-1 requires that agencies' core financial systems in order to support the Financial Reporting process must: (i) use financial data that can be traced directly to Standard General Ledger accounts to produce reports providing financial information, (ii) maintain accounting data to permit reporting in accordance with accounting standards recommended by the Federal Accounting Standards Advisory Board and issued by the

Director of OMB, and reporting requirements issued by the Director of OMB and the Secretary of the Treasury, and (iii) report events and transactions according to the accounting classification structure and within a given accounting period. OMB Bulletin No. 94-01 requires agencies to disclose each category of accounts receivable, present gross amounts due, allowance for estimated uncollectible amounts, methodology used to estimate the allowance for estimated uncollectible accounts, and the net amount due. The problem concerning the STLP financial reporting was corrected during the FY 1995 audit.

Recommendation

Since this problem was corrected during our audit work, no recommendations are necessary.

Reportable Conditions

Finding E. Other Governmental Liabilities Were Not Reported

OST did not ensure the proper recording and reporting of the WCF portion of the Federal Employees' Compensation Act liability. This item, estimated at $533,500 (based on Department of Labor actuarial projections), had not been recorded in the accounting records, and thus was omitted from the WCF portion of the draft FY 1994 Combining Statement of Financial Position. Further, a description of the methodology used to estimate the actuarial liability was not included in a note to the financial statement. As a result, Other Governmental Liabilities were understated on the WCF portion of the draft Combining Statement of Financial Position, and the notes to the financial statement were incomplete. OST agreed to make a note disclosure of this liability for the FY 1994 financial statement and develop accounting procedures to ensure proper recording of the liability in future years. Our FY 1995 audit found that the actuarial liability ($213,700) was disclosed in the notes to the financial statement; however, the actuarial liability was again omitted from the Combining Statement of Financial Position.

Discussion

OMB's memorandum of February 25, 1994, to Chief Financial Officers of executive departments and agencies subject to the CFO Act, discussed the need to display the actuarial liability for workers compensation benefits as a liability in the financial statement. OMB also noted in its memorandum that for general funds and revolving and trust funds without sufficient unobligated balances to cover the actuarial liability, the portion of the liability not covered by budgetary resources should be so classified. The OST Director of Financial Management also issued departmental guidance dated October 24, 1994, that discussed the need to include the actuarial liability in the FY 1994 financial statement. The memorandum also provided the Financial Statement Module general ledger adjustments required to properly reflect the actuarial liability on the Statement of Financial Position and the Statement of Operations and Changes in Net Position.

OST accounting officials stated the $533,500 actuarial liability was not recorded in the accounting records nor reported in the draft Combining Statement of Financial Position because departmental guidance for the preparation of the FY 1994 financial statement, which discussed the need to report the actuarial liability, was not issued until October 24, 1994, after the close of FY 1994. Although the actuarial liability was disclosed as a note to the FY 1995 financial statement, it was not properly included as a liability on the Combining Statement of Financial Position because accounting personnel followed the same procedures as used for the FY 1994 statement.

Recommendation

We recommend that OST and FTA accounting officials implement procedures to ensure compliance with OMB and departmental guidance on the reporting of the actuarial liability on financial statements.

Finding F. Accrual Procedures Were Not Followed

OST did not follow accrual procedures designed to ensure proper recording and reporting of accounts payable, net position, income, and expenses for two Gift and Bequest (G&B) Fund donations totaling $18,000. The donated amounts included $4,000 which was in excess of the total needed to reimburse specific costs. This $4,000 in excess funds was recorded in a net position account instead of in a liability account as unearned income to be returned to the U.S. Treasury. Also, income and expenses of about $6,000 were recorded in the wrong year. As a result, the G&B Fund portion of the draft FY 1994 Combining Statement of Financial Position understated Intragovernmental Liabilities by $4,000 and overstated Net Position (Cumulative Results of Operations) by $4,000. In addition, the G&B Fund portion of the draft Combining Statement of Operations overstated income, program expenses, and net position by $9,000, $6,000, and $3,000, respectively. Corrective action was verified during the audit of the FY 1995 financial statement.

Discussion

As commented on in SFFAC Number 2, Entity and Display, financial statements represent the principal means of communicating accounting information about an entity's resources, obligations, revenues, etc. to those outside the entity. SFFAC Number 1 states that financial reporting should be reliable; that is, the information presented should be verifiable, comprehensive, and free from bias and should faithfully represent what it purports to represent. GAO's Standards For Internal Controls requires that executive agencies (i) ensure transactions and other significant events are promptly recorded and properly classified and (ii) conduct periodic comparisons of resources and obligations with recorded accountability to determine whether they agree.

The accrual problems were corrected during our audit work. The final Principal Statements for FY 1994 were revised and we verified that corrective actions were taken during our audit of the FY 1995 financial statement.

Recommendation

Since the problems were corrected during our audit work, no recommendations are necessary.

Other Issue

Investment of WCF Balance

OST does not earn interest on the WCF cash balance deposited with the U.S. Treasury. OST may be able to earn interest by investing a portion of this cash balance in U.S. Treasury securities. OST management was not aware of the interest-earning potential of its Working Capital Fund cash balance. At an assumed interest rate of 6.25 percent, the average $32 million fund balance for the last 2 years could have earned OST interest of about $2 million each year had it been invested.

In our view, OST management officials should consider seeking congressional approval and legislative authority, as required, to permit the WCF to earn interest on its cash balance.

INTERNAL CONTROL TEST RESULTS FOR ACTIVITY CYCLES & MATERIAL ACCOUNTS REVIEWED

Cycle/Account Description	Controls Adequate*	Reportable Condition	Report Reference
ACTIVITY CYCLES			
Fund Authority	x		
Reconciliation of Fund Balance with Treasur	x		
Procurement**	x		
Property Management		x	Finding A
ASSET ACCOUNTS			
Financial Resources:			
Fund Balance With Treasury		x	Finding D
Accounts Receivable		x	Finding C
Advances Receivable		x	Finding D
Credit Program Receivables		x	Finding D
Cash and Other Monetary Assets	x		
Non-Financial Resources:			
Property and Equipment:		x	Finding A
LIABILITY ACCOUNTS			
Funded Liabilities:			
Accounts Payable		x	Findings B and F
Accrued Entitlement Benefits		x	Finding E
Accrued Payroll and Benefits	x		
Accrued Leave	x		
Debt		x	Finding D
NET POSITION ACCOUNTS			
Invested Capital		x	Findings A, B, D, and E

* Our consideration of the internal control structure would not necessarily identify all matters which shoul considered reportable conditions.

** Limited to a review of procurement integrity

Exhibit B

AUDIT TEAM MEMBERS

The following is a listing of the audit team members who participated in the audits of the OST financial statements for FYs 1994 and 1995.

James Childers, CPA, CGFM	Program Director
Richard W. Sucher	Project Manager
Hilbert Turner	Project Manager
Dorothy Jefferson, CPA, CGFM	Auditor-in-Charge
William Anhalt	Auditor
Zena L. Huen, CGFM	Auditor
Alfred Oandasan, CGFM	Auditor
Natasha Watts	Auditor