

Handwritten: 4, 114, 798

BY THE COMPTROLLER GENERAL

Report To The Congress

OF THE UNITED STATES

Weak Internal Controls Make Some Navy Activities Vulnerable To Fraud, Waste, And Abuse

Weaknesses in internal controls at the Naval Sea Systems Command, including two shipyards, and two other activities that provide services to the command make them vulnerable to fraudulent acts as well as nonintentional misuse of Federal funds.



114798

GAO believes that prevention is the key to combating fraud and abuse in Government, and that sound internal controls are the best means of prevention. The Navy should strengthen internal controls and minimize the vulnerability to fraud, waste, and abuse. This report is one of a series GAO is issuing on its vulnerability assessments of Federal agencies.



AFMD-81-30
APRIL 3, 1981

Handwritten: 016282

Request for copies of GAO reports should be sent to:

**U.S. General Accounting Office
Document Handling and Information
Services Facility
P.O. Box 6015
Gaithersburg, Md. 20760**

Telephone (202) 275-6241

The first five copies of individual reports are free of charge. Additional copies of bound audit reports are \$3.25 each. Additional copies of unbound report (i.e., letter reports) and most other publications are \$1.00 each. There will be a 25% discount on all orders for 100 or more copies mailed to a single address. Sales orders must be prepaid on a cash, check, or money order basis. Check should be made out to the "Superintendent of Documents".



COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON D.C. 20548

B-202279

To the President of the Senate and the
Speaker of the House of Representatives

This report summarizes the results of our review of selected Navy Department activities to assess their vulnerability to fraud, waste, and abuse. It describes weaknesses we found in fiscal and managerial controls over administrative activities at the Naval Sea Systems Command and two other activities that provide services to the command, and makes general and specific recommendations to the Secretary of the Navy.

This is one of a series of reports we will issue on the vulnerability of selected Federal agencies and programs to fraud and abuse. The review was undertaken by our Fraud Prevention Task Force which was established to respond to growing public concern over abuse and misuse of taxpayers' money.

Copies of this report are being sent to the Director of the Office of Management and Budget, the Secretary of Defense, and the Secretary of the Navy.

Milton J. Rowland

Acting Comptroller General
of the United States

D I G E S T

GAO believes the Navy activities it reviewed are vulnerable to fraud, waste, and abuse because their internal control systems are not functioning effectively. Although not aimed at finding fraud, waste, or abuse, GAO's review nonetheless disclosed unauthorized purchases, duplicate payments, \$5.8 million in receivables written off without adequate justification, and related problems--most of which could have been reduced significantly through better internal controls.

This report is one of a series GAO is issuing on its assessments of the vulnerability of Federal agencies to fraud, waste, and abuse. This assessment covers the Naval Sea Systems Command, including two shipyards, and two other activities which provide support services to the command. The purpose of our review was to determine whether the internal control systems of these activities adequately protect Federal funds and assets from fraud, waste, and abuse. As evidenced by a related GAO study to be issued in the near future, fraud does exist within the Navy. The study showed that from January 1, 1977, to March 31, 1979, the Navy had 17,799 reported cases of fraud and illegal acts--the largest number of any of 21 agencies included in that study.

Good internal controls are the most effective deterrent to fraud, embezzlement, and related illegal acts. Internal controls are adopted by an agency to safeguard assets, check the accuracy and reliability of accounting data, promote operational efficiency, and encourage adherence to prescribed management policies. These checks can detect errors and make fraud and related illegal acts more difficult. Each Federal agency is required to maintain adequate systems of internal control by the Budget and Accounting Procedures Act of 1950.

BETTER INTERNAL CONTROLS ARE NEEDED

GAO found inadequate controls over several functions at the Naval Sea Systems Command, two shipyards, and two activities that provide support services. As a result a significant portion of their funds may not be spent for purposes intended. Specific weaknesses noted included:

- AGC 60328
- DLG 03093
- Inadequate controls over payroll at the Navy Regional Finance Center and Norfolk and Charleston shipyards which could result in inaccuracies and irregularities. (See pp. 6-9.)
 - Inadequate controls over blank and negotiable U.S. Government checks at the Navy Regional Finance Center which allow misuse. (See pp. 9 and 10.)
 - Poor security over computer facilities and equipment at the Navy Regional Data Automation Center, Washington, D.C., and at Norfolk and Charleston shipyards, which provides opportunities to manipulate computer programs or files. (See pp. 11 and 12.)
 - Circumvention of procurement regulations at the Naval Sea Systems Command resulting in over \$122,000 spent for unauthorized purchases/leases. (See pp. 13-17.)
 - Insufficient review of payment requests and a lack of necessary checks of automated system disbursements at the Navy Regional Finance Center causing duplicate payments as high as \$1.2 million. (See p. 17.)
 - A 7-month, \$8 million backlog of accounts payable at the Charleston shipyard as of September 30, 1979, that had not been reconciled to supporting documentation to determine if only legitimate invoices were paid. (See pp. 18-20.)
 - Accounts receivable valued at about \$5.8 million at the Charleston shipyard written off the general ledger from fiscal 1978 through fiscal 1979, without adequate justification. (See p. 21.)
 - Lack of basic controls at the Naval Sea Systems Command over approving and processing employee travel claims, and at Personnel Support Activities which pay the claims. (See pp. 21-24.)

GAO believes that (1) a lack of emphasis on internal controls makes the activities reviewed vulnerable to fraud, waste, and abuse and (2) immediate corrective action is necessary to reduce the risk.

IMPROVEMENTS ARE NEEDED IN INTERNAL AUDIT

An agency's internal audit and review effort is critical for effective management and serves as an important element of internal control. Managers rely on auditors to provide assurance, through audits, that all agency tasks and functions are controlled and are carried out legally and correctly.

In analyzing the effectiveness of Navy audit efforts and of the actions taken to correct audit findings, GAO found that Navy internal audit reports do not always identify the underlying cause of audit findings and the reasons for noncompliance with regulations; too few staff members are assigned to internal auditing and review functions to review all activities at recommended intervals; and internal audit personnel do not participate in automated data processing planning. (See pp. 25-29.)

PROPOSED LEGISLATION

GAO believes that internal controls can be made more effective by strengthening existing law. The Congress is considering two bills that would require greater accountability by heads of Federal agencies for the effectiveness of their organizations' systems of internal financial control, thereby strengthening the accountability aspects of the Accounting and Auditing Act of 1950.

The Financial Integrity Act of 1981 (H.R. 350, 97th Cong.) would require agency heads to undertake annual evaluations of their organizations' internal control systems and report the results of such evaluations to the Congress and the President. The Federal Managers' Accountability Act of 1981 (H.R. 1526, 97th Cong.) would require (1) evaluations and reports on the adequacy of the systems of internal accounting and administrative control of each executive agency and (2) the head of each agency to include, with the request for appropriations, a statement certifying

*NARDAE
DC 93172*

that the request is based upon an accounting system that has been approved by the Comptroller General.

GAO would participate in the process by providing guidance for conducting the examinations and by reviewing the results. GAO believes both pieces of legislation would contribute to the development of adequate internal control systems in the Navy. Our experience is that internal control systems require a commitment from top management and consistent vigilance to be effective. Therefore we support legislation of this nature and believe it will definitely help bring about such commitment and vigilance.

CONCLUSIONS AND RECOMMENDATIONS

The Navy's insufficient emphasis on internal controls at the activities GAO reviewed indicates that other activities and shipyards also may be vulnerable to fraud, waste, and abuse. At most locations GAO visited, internal controls can be strengthened at little or no additional cost.

GAO recommends that the Secretary of the Navy more vigorously enforce requirements for adequate systems of internal control by:

- Emphasizing to managers at all levels the importance of controlling tasks and functions for which managers are responsible and accountable.
- Establishing a central internal control officer to oversee these controls and ensure that each command and major location establish its own officer to see that (1) improvements are made to correct the problems GAO found and (2) surveillance is constantly maintained to prevent their recurrence.
- Requiring proper segregation of payroll functions at the Navy Regional Finance Center so that no one person can handle all phases of a transaction. (See p. 7.)
- Improving other controls over payroll at the Naval Sea Systems Command headquarters and the shipyards, such as requiring (1) control totals to be predetermined when source documents are prepared, (2) personnel offices to be informed by the payroll staff of actions processed to

payroll files, and (3) frequent reconciliation of payroll and personnel files. (See pp. 6-9.)

- Directing all installations to assign an automated data processing security officer, implement a security training program, and restrict access to computer equipment, computer tapes, and system documentation. (See pp. 11 and 12.)
- Directing the Naval Sea Systems Command to implement procedures for (1) expediting the processing of requests for office equipment, (2) performing internal reviews of contract overhead charges to ensure that only authorized items are charged, (3) reviewing the contract and funding documents used in acquiring office equipment to ensure that charges are proper and accounted for, and (4) providing specific detailed guidelines on the use of funding documentation. (See pp. 13-17.)
- Ensuring that the Navy Regional Finance Center improves its review of payment requests and automated system edits by thoroughly examining documentation supporting expenditures before making payments, and by ensuring that the more sophisticated computerized system being designed (see p. 18) requires that an adequate number of invoice elements match to preclude duplicate payments. (See pp. 17 and 18.)
- Requiring the Charleston shipyard to match payments to supporting documentation and to properly classify accounts receivable so that they are collected promptly. (See p. 21.)
- Improving controls over travel at the Naval Sea Systems Command headquarters by (1) requiring appropriate officials to approve travel, (2) seeing that travel advances are liquidated promptly and that claims are properly reviewed, and (3) ensuring that managers receive reports containing the information they need for controlling and planning travel expenditures. (See pp. 21 and 23.)
- Requiring the Charleston shipyard to improve its control over travel by addressing the weaknesses identified in this report. (See pp. 23 and 24.)

--Making internal audits more effective by (1) reassessing staffing priorities to adequately emphasize internal auditing and reviewing functions at all levels of command in light of decreasing size and other factors that make Navy activities more vulnerable to fraud, waste, and abuse, (2) requiring internal audit participation in the design, development, and test phases of a new computer system to ensure that factors to enhance auditability, audit trails, security, and quality output are designed and developed into new systems, and (3) requiring internal audits to identify underlying causes of problems uncovered so that action can be taken to prevent recurrence. (See pp. 25-29.)

AGENCY COMMENTS AND GAO'S EVALUATION

The Department of Defense provided extensive comments on this report. It agreed with 7 of the 11 recommendations and has initiated or promised to take corrective action on 5 of these 7. It disagreed with the remaining four recommendations because it contends that existing controls are adequate. Apart from the recommendations, the Department expressed concern about the title (subsequently revised) and the failure of the report to place the findings in perspective to the size, mission, and resources administered by the Naval Sea Systems Command.

GAO has carefully evaluated the Department's lengthy comments and, where appropriate, has revised the body of the report to clarify specific points or to update information provided. However, GAO's basic position remains unchanged; namely, that a need exists for stronger internal controls, the recommendations are valid, and they should be implemented promptly. (See app. II.)

C o n t e n t s

| | | <u>Page</u> |
|---------|---|-------------|
| DIGEST | | i |
| CHAPTER | | |
| 1 | INTRODUCTION | 1 |
| | Description of vulnerability assessments | 1 |
| | Purpose and programs of Navy activities reviewed | 2 |
| | Objectives, scope, and methodology | 3 |
| 2 | CIVILIAN PAYROLL OPERATIONS NEED ADDITIONAL CONTROLS | 6 |
| | Better control is needed over computer processing of payroll data | 6 |
| | Payroll processing duties are not sufficiently separated | 7 |
| | Personnel offices are not informed of personnel actions processed to the master payroll files | 8 |
| | Payroll and personnel files are not routinely matched | 8 |
| | Additional controls are needed over blank and negotiable U.S. Government checks | 9 |
| 3 | ACCESS TO COMPUTER FACILITIES AND OPERATIONS SHOULD BE RESTRICTED | 11 |
| | Programmers should not have unrestricted access to the computer room nor operate computer equipment | 11 |
| | Computer operators should not have unsupervised access to system documentation | 11 |
| | Access to the tape library should be restricted | 12 |
| 4 | BETTER CONTROLS ARE NEEDED OVER PROCUREMENT, DISBURSEMENTS, AND RECEIPTS | 13 |
| | NAVSEA's contract/procurement system needs improvement | 14 |
| | Better NRFC control over disbursements would eliminate duplicate and erroneous payments to vendors | 17 |
| | Norfolk and Charleston shipyards need better controls over accounts payable | 18 |

| | | <u>Page</u> |
|---------|--|-------------|
| CHAPTER | | |
| | Charleston shipyard needs to improve its accounting for receivables | 21 |
| | Inadequate procedures and review allow abuse of Navy's travel system | 21 |
| 5 | MORE EFFECTIVE INTERNAL AUDITS ARE NEEDED | 25 |
| | The underlying causes of problems disclosed during audits should be developed and reported | 25 |
| | The Navy should consider allocating more resources to the internal audit and internal review functions | 27 |
| | Internal auditors should be involved in ADP planning | 28 |
| 6 | CONCLUSIONS, RECOMMENDATIONS, AND AGENCY COMMENTS | 30 |
| | Conclusions | 30 |
| | Recommendations | 31 |
| | Agency comments | 33 |

APPENDIX

| | | |
|----|---|----|
| I | Checklist of internal control weaknesses found during our vulnerability assessment of NAVSEA headquarters, NRFC, NARDAC, Norfolk and Charleston shipyards | 34 |
| II | Agency comments and our evaluation | 43 |

ABBREVIATIONS

| | |
|--------|--------------------------------------|
| ADP | automatic data processing |
| GAO | General Accounting Office |
| NARDAC | Navy Regional Data Automation Center |
| NAVSEA | Naval Sea Systems Command |
| NRFC | Navy Regional Finance Center |
| PSA | Personnel Support Activity |

CHAPTER 1

INTRODUCTION

The General Accounting Office created a Special Task Force for the Prevention of Fraud and Abuse in response to growing public concern about abuses and misuses of taxpayer money. This report, concerning selected Navy Department activities, is one of a series of reports we will issue on the basis of a new audit approach referred to as a vulnerability assessment.

DESCRIPTION OF VULNERABILITY ASSESSMENTS

Vulnerability assessments are designed to show the susceptibility of Government agency programs to fraud and other illegal acts by evaluating the adequacy of internal controls. In a broad sense, internal controls are all methods adopted by an agency to safeguard assets, check the accuracy and reliability of accounting data, promote operational efficiency, and encourage adherence to prescribed management policies. Management controls are the procedures used by operating groups, rather than financial and accounting groups, that are concerned with the decision processes leading to management's authorization of transactions. Internal and management controls are not necessarily mutually exclusive because the procedures and records used for management control may also be necessary for internal accounting control.

A good system of internal control can discourage and minimize fraud, waste, and abuse because of two important features--(1) the separation of duties within the system and (2) procedures that govern the authorization, preparation, review, and flow of all transactions through the system. Thus, to succeed in abusing Federal programs or in defrauding an organization having sound internal controls, it is usually necessary for an individual to have the help of others.

Supervisors must play an active role in reviewing operations to ensure that controls exist and are working properly. They cannot rely only on auditors to detect weaknesses or abuses of control systems because audits normally deal with only a small number of transactions that have already transpired.

Because of the importance of good financial management systems that rely heavily on good internal controls, we have issued several publications on this subject. One of the most important is the Policy and Procedures Manual for Guidance of Federal Agencies. This manual contains accounting principles and standards prescribed by the Comptroller General--principles and standards relating to the development, installation, and operation of that part of an agency's financial management system that concerns fiscal operations, and guidelines and principles for agencies' internal auditing efforts. Several other documents have been issued

concerning the necessity for a good financial management system. Inherent in these publications is the concept that financial management systems are only as good as the internal controls that govern actions and information affecting the systems.

Recognizing the need for strong internal controls over Government operations, the Congress enacted the Budget and Accounting Procedures Act of 1950, which, among other things, made the head of each executive agency responsible for establishing and maintaining adequate systems of accounting and internal control. More recently, the Congress passed legislation which established Inspectors General in many executive agencies and departments.

In a related GAO study to be issued soon, we found that fraud does exist within the Navy. The study showed that from January 1, 1977, to March 31, 1979, the Navy had 17,799 reported cases of fraud and illegal acts--the largest number of any of 21 agencies included in that study.

PURPOSE AND PROGRAMS OF NAVY ACTIVITIES REVIEWED

The Naval Sea Systems Command (NAVSEA), which is the largest activity of the Naval Material Command and incurred obligations of \$8 billion during fiscal 1980, is responsible for

- the research, development, procurement, logistic support, and other functions for ships and craft, shipboard weapon systems, air-launched mines and torpedos, shipboard components such as propulsion (including nuclear), power generating, sonar, search radar, and auxiliary equipment;
- procurement, technical guidance, and supervision of operations related to salvage of stranded and sunken ships and craft; and
- central technical authority for ship and nuclear power safety; explosives, propellants, and actuating components; and explosive safety and explosive ordinance disposal.

The Navy Regional Finance Center (NRFC), Washington, D.C., among other things processed payroll and other NAVSEA disbursements. In fiscal 1979 NRFC disbursed approximately \$2.3 billion to vendors in payment of equipment, materials, supplies, and services. Also in fiscal 1979, NRFC disbursed over \$779 million for military payrolls, civilian payrolls, and travel claims. NRFC uses two automated systems to process the payments: the Automated Payment Voucher and the Integrated Disbursing and Accounting systems.

There are six regional data processing centers called Navy Regional Data Automation Centers (NARDACs). One is located in the

Washington Navy Yard and the rest in field activities throughout the country. NARDACs are a component of the Naval Data Automation Command which administers and coordinates the Navy nontactical automated data processing (ADP) program. The program includes development of policy and procedures, approval of systems development, acquisition/utilization of automatic data processing equipment and service contracts, sponsoring of ADP technology, and career development and training of ADP personnel.

The chart on page 5 illustrates the relationship of the activities discussed in this report with other Navy organizations.

OBJECTIVES, SCOPE, AND METHODOLOGY

Our objective was to determine the extent of NAVSEA's vulnerability to fraud, waste, and abuse (and that of other activities which provide service to NAVSEA) by evaluating the adequacy of internal and management controls exercised over its administrative activities and its shipyard activities. More specifically, we set out to identify internal accounting and/or management control weaknesses which, if corrected, would provide greater protection of Federal funds and assets from fraud and abuse. The approach used in conducting vulnerability assessments requires (1) a broad examination of an agency's operations using an internal control checklist and (2) the testing of a limited number of transactions sampled on a judgmental basis.

As part of our vulnerability assessment of NAVSEA we evaluated certain administrative functions which support the program, such as payroll, travel, and property management. In some instances, our review of these functions extended beyond the confines of NAVSEA and some of the examples of weaknesses found in these administrative areas do not relate directly to NAVSEA.

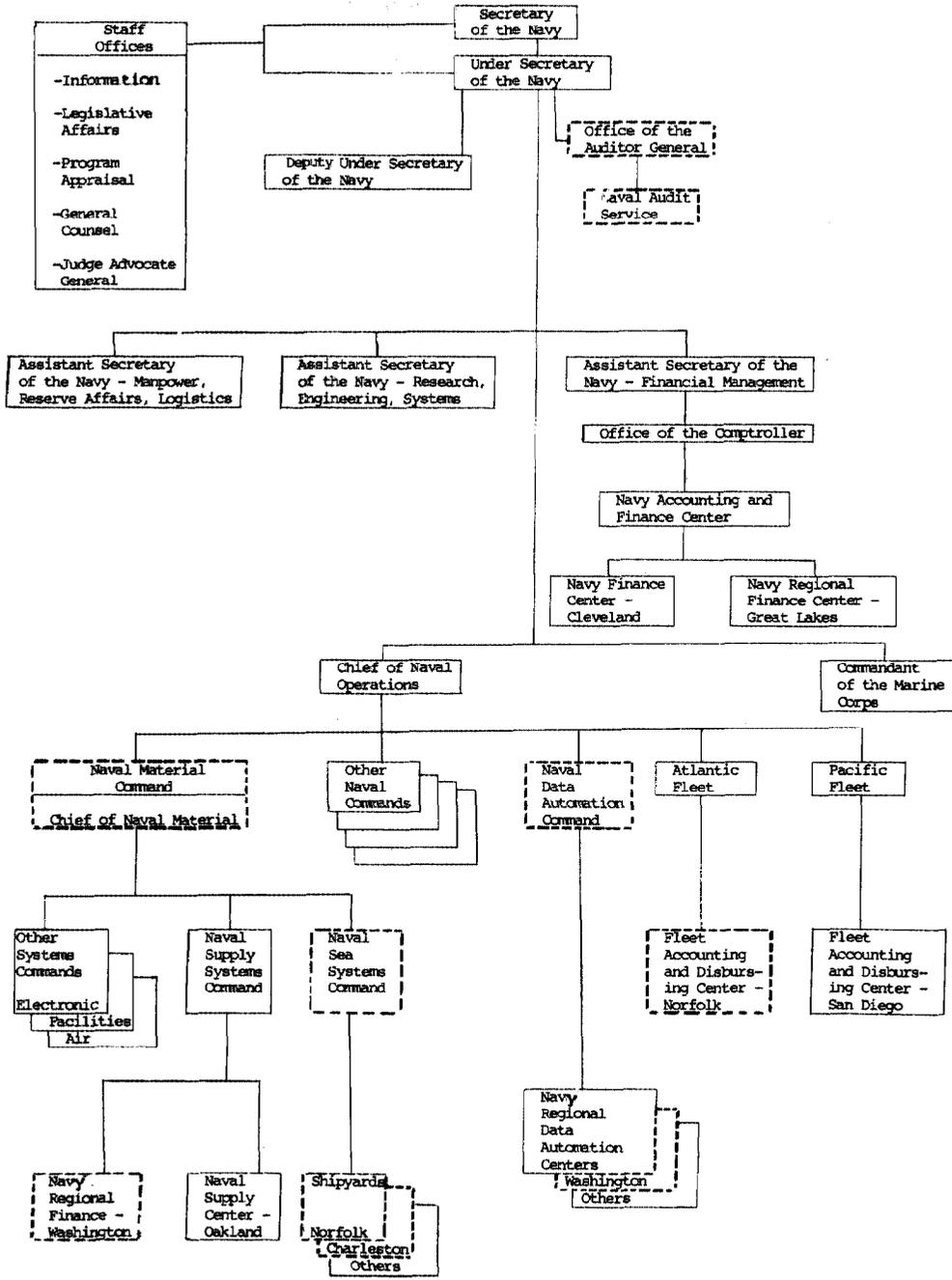
NAVSEA is the largest system command under the Naval Material Command. The two shipyards selected, Norfolk, Virginia, and Charleston, South Carolina, spent approximately \$597 million of the \$2 billion spent by NAVSEA's eight shipyards in fiscal 1979. As part of our review of internal controls, we reviewed NRFC, Washington, D.C., and the Fleet Accounting and Disbursing Center, Norfolk, Virginia, which process payroll and disbursements for NAVSEA. In addition, work was performed at the Personnel Support Activities at Washington and Charleston, which process travel vouchers for payment.

To evaluate computerized controls, we reviewed NARDACs at Washington and Norfolk. NARDACs, provide computerized processing and services for NRFC and the Norfolk shipyard. Since internal audit is an important element of internal controls, we also reviewed the Naval Audit Service.

At each location we administered our internal control questionnaire to agency officials and tested various transactions to

determine whether internal controls were in place and working properly. The questionnaire was based primarily on standards promulgated in GAO's Policy and Procedures Manual for Guidance of Federal Agencies. Specifically, we evaluated the controls over administrative activities which are those performed in support of the agency's basic mission, such as processing payroll or managing property assets. Many activities are performed daily while others, such as verification of physical inventories, require less frequent performance. We also evaluated controls performed by ADP equipment.

Department of the Navy Organizational Chart*



Audit Work Performed = - - - - -

*This organizational chart is drawn to highlight the organizations where we performed our audit work and to show the organizations' relationship to other Navy components at the time of our review. The chart is not all-inclusive and does not reflect organizational changes made after our review.

CHAPTER 2

CIVILIAN PAYROLL OPERATIONS

NEED ADDITIONAL CONTROLS

Civilian computerized payroll operations, with disbursements totaling \$264 million in fiscal 1979, lack some basic internal controls--making these operations vulnerable to fraud and abuse. We found inadequate controls over payroll data processed by computer, inadequate separation of duties among employees who process payroll, personnel offices not being informed of personnel actions and changes processed to the payroll files, payroll files not being routinely matched with personnel files, and inadequate controls over blank U.S. Government payroll checks. These weaknesses allow poor recordkeeping and accountability over payroll activities and provide opportunities to alter payroll disbursement.

GAO Policy and Procedures Manual for Guidance of Federal Agencies (6 GAO 12, 13) states that suitable control records and other control features over payroll operations should be maintained to provide positive evidence of the accuracy of such operations and to deter payroll irregularities. Further, the manual states that control procedures should be applied to documents such as personnel authorizations, time and attendance reports, and leave records, which affect the computation of earnings and amounts due. This ensures that the documents are properly taken into account in determining accounts payable and in processing payrolls. The following sections describe the weaknesses we found in NAVSEA civilian payroll operations.

BETTER CONTROL IS NEEDED OVER COMPUTER PROCESSING OF PAYROLL DATA

The automated payroll systems used by the Navy Regional Finance Center and the Charleston and Norfolk shipyards do not properly use record counts and predetermined control totals to help ensure complete and accurate processing of data. In many instances, these record counts and control totals are in the systems but are not properly used by the responsible Navy activities.

Record counts, representing the number of documents in the group being processed, ensure that all documents are processed. Record counts should be made when documents are prepared for processing and should accompany the documents through the processing cycle. By this method, each office receiving the documents for the next processing phase can compare the number of documents it should have received with the actual number counted, to see whether documents were added or lost. For example, timekeepers could count the number of certified time and attendance reports to be processed and enter them into the computer along with other data. The computer would automatically count the records transmitted and compare

the counts. If differences exist, the entire batch would be rejected (not processed) until corrected or until a warning message is printed to alert a clerk that data may have been added or lost.

At both the Charleston and Norfolk shipyards, time and attendance cards are entered into the automated system in groups called "batches." Each batch is given a control number but no record count or control totals are sent with the records. Only after entry into the system are a record count and control totals produced. Thus, there is no control to prevent the addition or deletion of a time and attendance record from the batch before entry into the system.

Control totals which ensure accurate processing of payroll information are not predetermined at the civilian personnel office when source documents are prepared. As a result, the system cannot detect whether documents are lost or processed erroneously. In addition, the control totals are developed and used by the payroll technicians who also enter the personnel actions. Our standards for Federal payroll systems provide that different individuals should maintain control records and prepare payrolls. Data may be incompletely or erroneously processed if these weaknesses are not corrected.

PAYROLL PROCESSING DUTIES
ARE NOT SUFFICIENTLY SEPARATED

Payroll processing duties performed in NRFC's civilian payroll department are not sufficiently divided among employees to provide the necessary checks and balances for ensuring accurate payroll disbursements. For example, payroll technicians process personnel actions as well as time and attendance data. Further, each technician reviews for accuracy the computer listings showing transactions he or she entered. The payroll technicians can therefore create or change master payroll records without independent review for validity or accuracy. Under these circumstances invalid payroll disbursements are quite possible.

GAO standards for Federal payroll systems provide that responsibility be appropriately separated to ensure that one employee does not handle all phases of a transaction. The division of responsibilities should provide internal checks on performance and minimize opportunities for carrying out unauthorized or otherwise irregular acts. More specifically, our standards state that individuals processing appointments, promotions, and assignments should not record and report attendance or be associated with payroll preparation.

As a result of our review, Navy officials said they will institute a procedure requiring an independent review of personnel actions entered into the computer by terminal operators. NRFC is also pursuing an automated means of entering personnel actions directly from the personnel office.

PERSONNEL OFFICES ARE NOT INFORMED
OF PERSONNEL ACTIONS PROCESSED
TO THE MASTER PAYROLL FILES

The personnel offices at NAVSEA and at the Charleston and Norfolk Naval Shipyards are not provided a listing of personnel actions processed to the master payroll files. As a result, the personnel offices do not always know whether authorized personnel actions are recorded on the master payroll files and therefore, as NAVSEA officials told us, they do not know whether inaccuracies exist in the payroll files. At the Norfolk shipyard, during our November 1979 visit, a report in the payroll department showed uncorrected errors dated as early as February and March 1979.

Departments initiating documents for computer processing should be provided with and use computer listings showing all transactions processed.

PAYROLL AND PERSONNEL FILES
ARE NOT ROUTINELY MATCHED

The master payroll files for NAVSEA and the Charleston and Norfolk shipyards are not routinely matched against master personnel files. 1/ As a result, there is no assurance that data contained on the separate master files are consistent. We found many discrepancies between the two files at the Norfolk shipyard. A routine and timely match of files would be a valuable tool and should be required and enforced to ensure that all authorized--and no unauthorized--personnel transactions are processed to the master payroll files.

At Norfolk we reviewed and compared 647 employee records contained in the personnel and payroll master files. We found 148 discrepancies (23 percent) as follows:

- 89 employees were on the payroll file but not on the personnel file.
- 27 within-grade step discrepancies existed between the two files.
- 16 grade discrepancies existed between the two files.
- 16 employees were on the personnel file but not on the payroll file.

We were informed that the two files have not been reconciled since May 1978 at either Charleston or Norfolk shipyards. NAVSEA

1/In this case, the Naval Automated Civilian Manpower Information System.

officials compared its payroll and personnel master files in mid-1978, but the discrepancies discovered were not reconciled. Another comparison was made in September 1979. However, this time the payroll file was about 2 months older than the personnel file and so the results were meaningless because recent personnel actions did not appear on the payroll file. These deficiencies have increased the risk that unauthorized and inaccurate payroll disbursements have been made when they could have been easily prevented.

ADDITIONAL CONTROLS ARE NEEDED OVER BLANK
AND NEGOTIABLE U.S. GOVERNMENT CHECKS

Controls by the NRFC disbursing office over blank U.S. Government checks do not adequately protect the checks from misuse, and no audit trail exists for determining how each blank check was used. According to officials of the U.S. Secret Service Forgery Division, some cases of forged and stolen checks have involved the Navy. We believe that the lack of controls over safeguarding and issuing checks has led to stolen and forged checks.

The NRFC disbursing office uses several logs to control the use of blank checks. However, log entries are sometimes not made or are made incorrectly. Also, the controls over canceling erroneous paychecks and the physical security provided over checks do not adequately protect against theft or loss. For example, the disbursing office logs each blank check, which then goes to the computer center for payroll processing and is signed by computer center personnel to support the transfer of checks. The audit trail showing check usage is broken, however, because blank checks not used during payroll processing are not always logged back into the disbursing office. We found this to be the case for 60 percent of the blank checks returned to the disbursing office. Disbursing office personnel stated that if they are busy when the checks are returned from payroll processing, they do not take time to log in the return. As a result, the loss of some checks may go undetected.

Another log is used to record blank checks substituted for erroneous paychecks that must be canceled. To determine whether the use of all checks had been recorded, we compared that log with the check inventory and found five checks which the log indicated had been issued, but which were still on hand. The disbursing officer said that if these checks had been lost or stolen during the interim, the loss would not have been detected.

A third log is used to record blank checks substituted for checks that payees claim they did not receive. Three blank checks were not listed on the inventory and comparison of this log with the check inventory showed that the three checks were also not recorded in the log. A search by the disbursing officer provided documents supporting the use of one of these checks. However, no supporting documents could be found that explained the use of the other two checks. The disbursing officer then contacted the

Department of the Treasury to determine if it could provide information on the two checks in question. Six weeks later, Treasury officials identified the payee on one check but could not identify the payee on the second check. This illustrates that the lack of an audit trail over blank checks increases the possibility of their theft or loss.

Compounding these problems is the fact that an NRFC clerk who initially receives erroneous checks to be canceled is also primarily involved in the cancellation. This means there is no adequate insurance that all erroneous paychecks received are, in fact, canceled. If a clerk selectively held out paychecks and supporting documents, there would be little chance of detection. We were advised by the Secret Service that similarly weak procedures permitted a dishonest clerk to steal and subsequently forge, over 7 months, 252 U.S. Treasury checks valued at \$55,000. The check cancellation procedures in that case (which involved a Navy disbursing office) were very similar to those in place at the NRFC disbursing office.

Subsequent to our review, the NRFC disbursing officer told us the procedure has been changed to involve an additional clerk in the initial steps of the check cancellation process. Now, one clerk receives the checks and the other clerk receives the documentation. A summary of the documentation is then logged in by one clerk and given to the other clerk for further processing with the checks. This prevents one dishonest clerk handling the checks, acting alone, from embezzling funds. Again, errors are more likely to be detected when duties are separated, and fraud is less likely to occur when it requires collusion.

CHAPTER 3

ACCESS TO COMPUTER FACILITIES AND OPERATIONS SHOULD BE RESTRICTED

Security at the Navy Regional Data Automation Center, Washington, D.C., and the Charleston and Norfolk shipyards is inadequate to prevent unauthorized access to computer operations and computer resources. Federal standards require that controls be established to restrict such access to authorized employees. In our opinion, controls are not adequate to prevent unauthorized changes or manipulation of computer programs or files, and so the risk of fraud, waste, or abuse is high.

PROGRAMMERS SHOULD NOT HAVE UNRESTRICTED ACCESS TO THE COMPUTER ROOM NOR OPERATE COMPUTER EQUIPMENT

Programmers were allowed unrestricted access to the computer rooms at Charleston, Norfolk, and NARDAC. Sound ADP control requires that programmers have restricted access to the computer room and that they not be allowed to operate computer equipment. These requirements exist because programmers have the technical ability to make changes to computer programs and data files without being readily detected. Although we found no evidence of programmers doing this during our audit, the failure to restrict access subjects the computer systems to unnecessary risk.

At the NARDAC center, for example, we observed a programmer operating the computer equipment during our tour of the facility. We were informed that the programmer was temporarily filling in as an operator because the regular operators were in a meeting. We also were informed that programmers sometimes operate computer equipment to test their programs on weekends, even though no operators are present. Officials explained that this avoids disrupting normal production operations.

Although we did not see programmers operating computers in Norfolk, the shipyard's instructions allow programmers unlimited access to the computer room. At Charleston, programmers were authorized to enter the computer room to deliver test programs and pick up test results. We advised management of the risks involved with this procedure and were informed at the completion of our audit that this procedure is now prohibited. The new procedure requires programmers who are submitting tests and awaiting results to remain in an area outside the locked computer room.

COMPUTER OPERATORS SHOULD NOT HAVE UNSUPERVISED ACCESS TO SYSTEM DOCUMENTATION

Computer operators at Charleston, Norfolk, and NARDAC have access to systems documentation. Sound ADP control requires that

system documentation be secured, and that computer operators not be allowed unsupervised access. When knowledge gained by computer operators from system documentation is coupled with their technical knowledge of computer operations, the risk of unauthorized changes to programs and data files is increased.

Written procedures specifying the controls necessary over system documentation did not exist at Charleston and Norfolk. Further, at Charleston we were told that computer operators can easily gain access to areas where system documentation is kept. At Norfolk we noted that computer operators are authorized unsupervised access to the combination safe where system documentation is stored. Furthermore, senior operators are provided with a key to the programmers' offices where elements of system documentation are sometimes kept.

At NARDAC we visited the programmers' work area after normal work hours and found the doors to the area open. We saw system documentation on desk tops and noticed that since there were no lockable file cabinets for storage, the system documentation is readily accessible to computer operators on the evening and night shifts.

Navy officials have informed us that new procedures have been implemented to limit and supervise computer operators' access to system documentation.

ACCESS TO THE TAPE LIBRARY SHOULD BE RESTRICTED

Access to the tape library is not adequately restricted at the three computer centers. Access restrictions are important to protect the files from unauthorized use, manipulation, or destruction.

At NARDAC the tape library door remains open--even during the evening and night shifts when a tape librarian is not on duty. The tape library actually serves as a passageway between the computer room and the output room, and therefore persons other than the librarian often enter the tape library. In addition, a computer listing identifying the tapes in the library remains on a desk in open view, even during hours when the librarian is not present.

The Norfolk and Charleston computer centers do not employ librarians. Instead, computer operators retrieve the computer tapes needed for processing. Furthermore, no log is kept to control the removal and return of tapes and the libraries remain unlocked during computer operations. Such virtually unlimited access to tape libraries and lack of controls over stored files increase the potential for unauthorized use, manipulation, or destruction of the files.

CHAPTER 4

BETTER CONTROLS ARE NEEDED OVER

PROCUREMENT, DISBURSEMENTS, AND RECEIPTS

In fiscal 1979, NAVSEA awarded over \$9 billion in contracts. During the same fiscal year, NRFC disbursed \$2.3 billion. We found that both NAVSEA headquarters and the Navy Regional Finance Center, Washington, D.C., were vulnerable to fraud, waste, and abuse as a result of (1) inadequate controls over procurement procedures at NAVSEA, (2) inadequate manual reviews and automated system edits of disbursements at NRFC, and (3) inadequate controls over authorizing, approving, processing, and paying employee travel orders and claims.

We noted that

- over \$122,000 was spent on unauthorized office equipment at NAVSEA,
- duplicate checks for as much as \$1.2 million have been issued,
- overpayments of up to \$425,000 have been made to vendors,
- there is not enough assurance that contract moneys are being spent for purposes intended, and
- travelers can abuse the travel system or incur unnecessary additional cost.

At the Charleston and Norfolk shipyards we found procedural and control weaknesses in accounts payable and accounts receivable. As a result of accounts payable weaknesses, duplicate payments are occurring and a 7-month backlog at Charleston of payables valued at over \$8 million had not been reconciled to supporting documentation. Insufficient controls over receivables resulted in about \$5.8 million at Charleston being written off the general ledger during fiscal 1978 and 1979 without an adequate review of underlying reasons. Also at Charleston, accounts receivable due from commercial sources, totaling \$288,000, were classified as receivable from U.S. Government sources. Without the proper classification of accounts receivable there is no assurance that all accounts receivable are collected promptly, if at all.

Travel activities at NAVSEA headquarters and the Charleston shipyard are susceptible to fraud, waste, and abuse because of inadequate controls over authorizing, approving, processing, and paying employee travel orders and claims. For example, we found that a large number of NAVSEA travel orders were requested and approved by the same official. Also, no meaningful reports exist for determining amounts of outstanding travel advances or whether advances were liquidated within 15 days after completion of a trip, as required by Navy regulations. As a result, employees

can keep travel advances indefinitely, persons may leave NAVSEA without liquidating their advances, and advances can be granted even when trips are not made. These deficiencies, described in more detail on the following pages, make the NAVSEA travel function vulnerable to illegal and wasteful acts.

To eliminate potential abuse of travel, NAVSEA should implement controls to ensure that only necessary travel is authorized and to provide for systematically approving, processing, validating, paying, and recording travel transactions. Reports generated from the system should provide management with tools for controlling and planning travel expenditures.

These conditions exist despite the Budget and Accounting Procedures Act of 1950, our Policy and Procedures Manual for Guidance of Federal Agencies, Navy internal audit reports which have pointed out internal control weaknesses, and written Navy procedures. We believe these conditions persist because top management at the activities reviewed have placed too little emphasis on enforcing the requirement for strong internal controls over these functions. The following sections describe in detail the weaknesses we found.

NAVSEA'S CONTRACT/PROCUREMENT SYSTEM NEEDS IMPROVEMENT

We found internal controls over procurement procedures were inadequate at NAVSEA headquarters. Funds were not only potentially vulnerable but in some cases had actually been misused. At the time of our review, NAVSEA headquarters personnel had circumvented the Navy's procurement system by purchasing or leasing 121 pieces of office equipment directly through field activities and contractors instead of through the Navy procurement branch as required by Navy regulations. The majority of these items were acquired by placing orders over the telephone without written justification. In addition, contract officers were charging the costs to incidental or overhead expenses, and the unauthorized pieces of equipment were not being entered into the inventory system. These conditions existed despite efforts by the Navy Audit Service, NAVSEA's Office of Internal Review, and NAVSEA's supply section to correct the problem.

Navy procurement directives state that managers of procuring activities should ensure that proper procedures exist and are implemented for procurement operations. Also, although existing instructions require that procurement requisitions be submitted to the Navy procurement branch for approval and processing, these procedures are being circumvented. Office equipment such as telecopiers, facsimile transmission machines, word processors, and office copying equipment is purchased or leased through Navy field activities and contractors without proper approval. Instead of sending requisitions to the procurement branch for approval and processing, project managers make purchases over the telephone for items that are not covered in the funding document.

As an example of the lack of procurement control we encountered at NAVSEA, a video cassette recording system costing approximately \$1,000 was delivered July 2, 1979, and in November 1980 was still at NAVSEA's receiving dock waiting to be picked up by the purchaser. ^{1/} This equipment had been obtained by circumventing the procurement system.

Through a self-initiated survey conducted in April 1978, the NAVSEA supply section and the Naval Audit Service found that personnel within NAVSEA had leased or purchased 84 pieces of office equipment directly through field activities or from private contractors without proper approval. Some of the equipment had been installed for as long as 4 years. Cost data was available as shown below for 14 of the items.

| <u>Source</u> | <u>Number of items</u> | <u>Cumulative purchase, lease, annual maintenance cost</u> |
|-------------------------------|------------------------|--|
| Furnished by contractors | 3 | \$ 44,317 |
| Furnished by field activities | <u>11</u> | <u>78,256</u> |
| Total | <u>14</u> | <u>\$122,573</u> |

Of the 84 items, including these 14, 21 were furnished by contractors and 63 were furnished by field activities. The 84 items of equipment uncovered by the survey at NAVSEA had increased to 121 at the time of our review.

Not only were the procurements and leases not authorized by the Navy procurement branch, many were not within the scope of the contracts under which they were purchased and paid. As of January 1979, the NAVSEA supply section discovered that 17 of the 21 equipment items that NAVSEA had obtained from contractors were not specified in the contracts under which they were furnished.

The reason given by NAVSEA officials for circumventing the procurement system was that the procurement branch was too slow in processing requisitions. The NAVSEA Office of Internal Review has recently completed a study of the unauthorized procurements and concludes, among other things, that the excessive procurement

^{1/}On Jan. 15, 1981, we were notified by letter that action has been taken to credit and debit this item to the proper funding accounts. Also, written justification and a signature for the receipt has been provided. Since our report was then in the final processing stages we were unable to verify these statements before publication.

lead times are a contributing factor. In our opinion, this does not justify eluding proper procedures. For routine items, officials must plan better to take into consideration the length of time required for processing, ordering, and shipping the material requested. We believe that management is at fault for not making sure that proper approvals are obtained.

In addition to circumventing proper procedures, Navy officials procured most unauthorized pieces of office equipment in NAVSEA by using funding authorities different from those normally used to procure or lease office equipment. This disguised the purchases and presented an inaccurate account of the money spent. The items purchased or leased were sometimes charged to the contract's incidental expenses or to overhead. When equipment was purchased or leased directly through field activities, the costs were sometimes charged to the Navy Industrial Fund (a revolving fund established by the Congress to provide working capital for naval industrial activities). Funding documents are not specific and projects are making telephone orders for office equipment not called for under the funding documents. Also, there is apparently no routine review of contract overhead charges.

Another effect of not following established procurement procedures is that the equipment purchased or leased has cost more than it should have. If NAVSEA personnel had followed the proper procedures by leasing or purchasing office equipment through the Federal Supply Schedule, instead of allowing contractors to provide the office equipment, they would have saved the Government money.

For example, a Navy audit of NAVSEA, covering office equipment procured or leased by circumventing the procurement system, disclosed that one contractor supplied seven pieces of office equipment (word processing and facsimile transmission equipment) under five contracts. The five contracts totaled \$9.7 million. We compared the costs charged for the word processors with the rates given on the Federal Supply Schedule and found that if NAVSEA had purchased these items of equipment through the Federal Supply Schedule it would have saved \$2,131. If the equipment had been leased for 24 months, it would have saved \$1,950 plus repair and maintenance costs. Although the savings in this example are relatively small, the potential for much higher savings exists, considering all the equipment that is purchased and leased outside normal procurement procedures.

The final adverse effect of circumventing procurement procedures is that the equipment bought is not entered into inventory records. GAO's Policy and Procedures Manual for Guidance of Federal Agencies (2 GAO 12.5) states that appropriate records must be kept of physical quantities of Government-owned property and its location. Without these records, the Government does not show ownership; inaccurate inventories lead to lack of control over assets and inaccurate budget requirement reports to the Congress.

We believe the deficiencies noted above resulted from excessive procurement lead time for obtaining office equipment. However, this does not justify eluding established procedures.

As a NAVSEA official stated, the equipment pointed out in this report includes only the items that have been detected. Additional office equipment and other items may have been procured in the same manner. Furthermore, the potential exists for fraudulent activities since the majority of this equipment was ordered over the telephone without written authority.

BETTER NRFC CONTROL OVER DISBURSEMENTS
WOULD ELIMINATE DUPLICATE AND ERRONEOUS
PAYMENTS TO VENDORS

NRFC has made both duplicate and erroneous payments because of insufficient review of payment requests and a lack of necessary automated system edits. In fiscal 1979, NRFC reported more than \$1.5 million in duplicate payments.

Our Policy and Procedures Manual for Guidance of Federal Agencies (7 GAO 24.1) states that the principal objectives of control over disbursements are to ensure that they are all legal, proper, correct, accurately recorded, and promptly reported. Additionally, the Manual (7 GAO 24.3) states that

"agencies should be particularly alert to the possibility of duplicating payments whenever * * * payments have been delayed for extended periods of time after due date and duplicate copies of invoices are received from vendors as follow up claims."

We found that NRFC did not have sufficient procedures to meet these objectives or to adequately alert them to all possible duplicate payments. Therefore, additional duplicate payments probably have occurred but have not been detected.

We reviewed the 17 largest known duplicate payments made by NRFC during fiscal 1979 (96 percent of the total dollar value of the known duplicate disbursements for that period) to determine what caused them. The following examples typify the weaknesses that cause duplicate checks to be issued.

The largest duplicate payment identified during fiscal 1979 was a \$1,209,190 appropriation transfer to the Department of the Air Force. It occurred because the Finance Center first paid a copy of the invoice submitted by the Air Force and later paid the original invoice. The original invoice was received and certified for payment, but then apparently misplaced, so the Air Force submitted a duplicate invoice 5 months later. This was paid. Then more than 7 months after payment, the original invoice was found and it too was paid--creating the duplicate payment. We saw that a record of the first payment had been placed in the appropriate

files, but the payment processing clerk did not adequately review the files before paying the year-old invoice.

Another six duplicate payments totaling \$51,000 resulted at least partly from inadequate review of duplicate invoices submitted by vendors. These invoices were certified for payment and then processed by an automated system which is supposed to compare and identify possible duplicate invoices. However, this computer system rejects an invoice as a duplicate only if procurement numbers, invoice numbers, invoice amounts, and invoice dates all match. If even one element differs from the others, the invoice will not be recognized as a duplicate and will be paid. For these six cases, the duplicate invoices contained different elements and therefore were not identified by the computer as being duplicates, even though they were.

Navy officials told us that four elements of the invoices must match, rather than two primary ones (procurement number and invoice number), because valid payments occasionally have the same procurement and invoice numbers. For example, vendors often separately bill the Navy for shipping charges by submitting duplicate invoices and changing the date and amount to be paid. According to these officials, a match of only the procurement number and invoice number would result in numerous rejections of valid invoices and therefore increase the workload because manual review would be necessary. However, as the number of invoice elements that must match increases, the number of duplicate invoices that will be detected by the automated system decreases. In our opinion, this deficiency contributes significantly to the issuance of duplicate checks. Navy officials informed us that a more sophisticated computerized system is being designed which, when implemented in 1982, should provide a more effective review of invoices.

Besides identifying duplicate payments, we found erroneous payments were made by NRFC. For example, one vendor was overpaid \$425,568.72. Although we did not conduct a detailed review of erroneous payments, as we did for duplicate payments, erroneous payments generally result from the same internal control weakness as do duplicate checks--insufficient review. We believe NRFC could significantly reduce the number of duplicate and erroneous payments by ensuring that all invoices are sufficiently reviewed and supported by appropriate documentation.

NORFOLK AND CHARLESTON SHIPYARDS
NEED BETTER CONTROLS OVER ACCOUNTS PAYABLE

At the time of our review, Norfolk's accounts payable unit did not have current written policies and procedures governing the review and approval of documents needed to support expenditures. Consequently, expenditures may not be properly reviewed before payments are made and the risk of erroneous payments is very high.

Specifically, voucher certifiers do not have a list of people and/or signatures of people authorized to sign for the receipt of goods and services. Instead, personal knowledge of employees who sign for goods is the only control. Without a list of employees authorized to receive goods, unauthorized persons can sign for material or a service. In commenting on our report, Navy officials stated that the accounts payable unit at Norfolk has established a list of personnel authorized to sign for the receipt of goods and services.

According to Norfolk officials, the accounts payable unit occasionally relies on telephone confirmation from either the supply unit or the user because receiving documents cannot be found. This practice could lead to the payment of material not actually received. Navy officials stated in their comments that the accounts payable unit occasionally confirms receipt of material by telephone and a certification is then obtained to affirm the telephone confirmation. They also stated that the voucher will not be accepted by the Fleet Accounting and Disbursing Office. However, we found that in one instance, a payment had been made without documented evidence of receipt.

Another weakness is that the comptroller department had no claims register or similar control mechanism for monitoring credit memos or checks due from suppliers. The same accounts payable clerk is responsible for (1) processing and certifying invoices for payment, (2) monitoring the receipt of credit memos and checks, and (3) making adjustments to the financial records. Without better mechanisms for accountability and separation of duties, the shipyard does not have adequate control over checks and credit memos due from suppliers. Navy officials stated in their comments that a claims register was implemented as a result of our review in November 1979. Regarding separation of duties, Navy officials stated that they have taken action to correct this problem.

No regular review of accounts payable files was performed to account for all documents. As of November 1979, 9 months had elapsed since the unit had determined if

- all items ordered have been received,
- all items received have been billed,
- all items billed have been paid, and
- all paid vouchers are complete and properly filed.

Because of the lack of accounting for documents, Norfolk officials have no assurance that all items ordered are received, billed, and paid.

The accounts payable unit at Charleston also lacks controls to prevent duplicate and erroneous payments. The unit relies

primarily on reviewing and matching payment documents after payments are made. As of September 30, 1979, the matching process had identified transactions where credit totaling \$273,000 was determined to be due the shipyard. Our analysis of 50 of these transactions, with credit of over \$59,000 pending, showed that 9 of the 50 (18 percent) were overpayments valued at \$2,000 and 8 of the 50 (16 percent) were duplicate payments valued at \$4,100. After our review, Navy officials stated they found that \$38,414 of the \$273,000 (14 percent) were erroneous payments and the rest were valid payments. Additional overpayments and duplicate payments may have been undetected because of a 7-month backlog of unmatched procurement documents. Navy officials stated in their comments that the 7-month backlog has been reduced to 2 months.

Accounts payable unit employees submit invoices for payment and supporting documentation to the Fleet Accounting and Disbursing Office in Norfolk, Virginia. Disbursing office clerks are supposed to review the documentation and certify the payment as authorized and correct. However, no one at Charleston's accounts payable unit reviews the billings sent to the Norfolk disbursing office to ensure that only valid invoices and documentation are sent. This has frequently allowed erroneous or duplicate invoices to be submitted and paid.

At the time of our review, payments exceeding \$8 million at Charleston had not been matched with supporting documentation. The comptroller explained that much of the current payment process was devised to provide prompt payment to the commercial vendors. However, because of the problems with erroneous and duplicate payments, Charleston plans to acquire local disbursing authority in October 1981. Billings will be paid locally instead of by the disbursing office in Norfolk. The accounts payable unit plans to review or audit billings before payment and to mechanize the document matching process. This should reduce the number of duplicate and erroneous payments.

The accounts payable unit also lacks effective procedures for settling or collecting credits and overpayments due from vendors. In some cases, settlement has taken up to 2 years because files have not been established or organized to ensure prompt followup action.

In reviewing the file for one \$50 overpayment which took 2 years to settle, we noted that only two letters requesting a refund were sent to the vendor--one in September 1977 and the other in April 1979. In another instance, a \$3,617 overpayment was made in July 1977, but not recovered until June 1979 because no file had been established that identified this case as unsettled. It was discovered by chance during a search for other procurement documents.

CHARLESTON SHIPYARD NEEDS TO IMPROVE
ITS ACCOUNTING FOR RECEIVABLES

At the Charleston shipyard, accounts receivable valued at about \$5.8 million were written off the general ledger during fiscal 1978 and 1979 without adequate justification. At the time of our review, shipyard officials were unable to explain why these receivables were written off. The shipyard comptroller agreed to make a comprehensive review of all writeoffs to determine why these situations occurred. Subsequently, Navy officials told us that the \$5.8 million was for material returned to the supply system for which the shipyard did not receive credit.

Also, Charleston accounting personnel have included accounts receivable due from other, nongovernmental sources in the amounts reported as due from Federal Government sources. Financial and operating statements for the quarter ending September 30, 1979, showed all receivables as due from Federal sources and none due from other sources. However, other financial records indicated that receivables of at least \$288,000 were due from commercial sources.

We have previously reported this problem at other shipyards and have recommended effective implementation of the shipyard accounting system design approved by the Comptroller General, which emphasizes properly classified accounts receivable on financial statements. Shipyard officials agreed that commercial accounts receivable should be segregated and that corrective action would be taken.

Our Policy and Procedures Manual for Guidance of Federal Agencies (2 GAO 12.4) states that under the accrual method of accounting, receivables representing amounts due from others should be accounted for as assets from the time the acts giving rise to such claims are completed until the claims are collected, converted into other resources, or determined to be uncollectible. Accounting for receivables is an important control over agency resources in that it results in a systematic record of amounts due, which is essential. Also, separate accounts for major categories of receivables should be maintained to facilitate clear and full disclosure of an agency's resources in its financial reports. This was not being done at the Charleston shipyard.

INADEQUATE PROCEDURES AND REVIEW
ALLOW ABUSE OF NAVY'S TRAVEL SYSTEM

A large percentage of NAVSEA employee travel orders were requested and approved by the same official. Our review of 47 travel orders over 8 months disclosed that 21 had the same person's signature as requester and approver. When appropriate supervisors do not approve travel, travel funds may be used unwisely.

Also, according to a travel clerk, during about 2 weeks, 80 trips were canceled after issuance of travel orders and advances. Navy officials explained in their comments that trip cancellations are normally batch processed by the administrative personnel which may account for the large number of trips in a short time. For comparison, they stated that in the fourth quarter of fiscal 1980, 261 trips were canceled out of 4,500 trips processed. According to the travel services supervisor, many travel orders that have been processed are canceled the same or the next day because the command changes its mind about the necessity of the trip. In our opinion, the large number of trips being canceled was a direct result of managers' failure to properly approve travel in advance. Apparently, the approving official learns about a trip after it has been arranged. If the official then disapproves the trip because he deems it unnecessary or funds are not available, the travel office staff must cancel the travel order, Government Transportation Request, airline tickets, and advance check. This could be avoided if NAVSEA management properly controlled and approved travel.

According to Navy travel regulations, employee travel advances should be liquidated within 15 days of completing a trip. There is little assurance that this regulation is being followed, since available reports make that impossible to determine. However, one travel advance was received in July 1977 and not liquidated until August 1979--2 years later.

To adequately manage advances and adhere to the 15-day requirement, managers need current, accurate information detailing each outstanding travel advance held by an employee. However, NAVSEA's only travel advance report contains only a numeric listing of travel transactions by obligation and amount and of advances which have aged 60 days. The report does not show these critical items: travelers' names, identification numbers, month and year of the advances, trip departure dates, number of days traveled, return dates, and a total dollar amount of outstanding advances.

An adequate system of internal control over travel should include review of employee travel claims to ensure that the claims agree with the actual trips and work schedules. According to GAO's interpretation of the Federal Travel Regulations (GAO Order 0300.1), after the traveler certifies and dates the voucher, the supervisor or other responsible official who knows the purpose of the travel shall sign the voucher before submitting it for payment. Our review of 47 NAVSEA travel transactions disclosed that employee claims were not reviewed before submission to the Personnel Support Activity, Washington, D.C., for processing and payment, although the Support Activity does review them to determine whether proper supporting documentation is included. In commenting on our report, Navy officials stated that review of travel vouchers before submission to the Support Activity would not be productive.

Our review of claims and discussions with voucher examiners at the Support Activity disclosed that many claims are questioned and sent back to employees because of insufficient supporting documentation. However, Navy travel regulations contain no provisions for denying payment by NRFC for unreasonable claims or for incomplete documentation and/or justification. This lack of sufficient procedures and review provides opportunities for travelers to abuse the Navy's travel system.

Charleston shipyard's Support Activity Command, separate from the shipyard, has paid shipyard personnel's travel claims without question when they contained information which should have raised questions. Additionally, travel section personnel at Charleston shipyard do not thoroughly review vouchers.

Our review of 25 travel orders and related claims at Charleston showed instances in which

- the traveler's claim did not match the actual trip and work schedule,
- delays enroute and stopovers were not necessary and were for the convenience of the traveler,
- authorization and use of Government-owned or rental cars was not justified, and
- claims were not justified for meals obtained after the traveler's return to Charleston--especially when vouchers indicate there was little time for such a meal before arriving home.

We believe these conditions existed because shipyard procedures do not require

- written justification for use of Government-owned or rental cars,
- consideration of advance reservations for Government quarters, airline travel, and cars, including rental cars, to achieve the most economical rates available,
- certification by the traveler's immediate supervisor or others with knowledge of the trip that the claim agrees with the actual trip and work schedule (Navy officials stated in their comments that review and approval of travel claims by supervisors would not be productive),
- determination by the travel section that claims are explained by statements in the voucher,
- notification by the travel section to the payroll section when travelers have used annual or sick leave or should have done so because of circumstances of the trip, and

--training of supervisors and travelers to cover travel regulations and economical travel practices.

Also, we believe these conditions existed because Personnel Support Activity procedures did not emphasize return of questionable vouchers to the shipyard travel section for clarification.

Navy officials stated in their comments that procedures have been initiated or are in place for the items noted above with the exception of the suggestion to require the traveler's immediate supervisor to certify that travel claims agree with the actual trip and work schedule.

CHAPTER 5

MORE EFFECTIVE INTERNAL AUDITS ARE NEEDED

Navy management does not benefit fully from effective internal audit because (1) audit reports often do not include the underlying causes of audit findings, (2) there are not enough audit resources, and (3) there is no internal audit involvement in ADP planning.

The Congress has recognized the need for effective internal auditing in numerous laws, particularly the National Security Act Amendments of 1949 and the Budget and Accounting Procedures Act of 1950. The latter act requires the head of each agency to establish and maintain systems of

"* * * internal control designed to provide * * * effective control over and accountability for all funds, property, and other assets for which the agency is responsible including internal audit."

In addition, our Policy and Procedures Manual for Guidance of Federal Agencies (3 GAO 34) states that internal auditing is essential to management's attaining its goals because it furnishes information, analyses, appraisals, and recommendations pertinent to management duties and objectives.

THE UNDERLYING CAUSES OF PROBLEMS DISCLOSED DURING AUDITS SHOULD BE DEVELOPED AND REPORTED

Audit regulations and standards require that recommendations be made for corrective action. Naval internal audit reports provide useful information to Navy management, but the 744 reports issued during fiscal 1977 and 1978 would be of greater use if the underlying causes of problems were developed and reported so that meaningful recommendations could be made to prevent their recurrence. Navy regulations require that audit reports identify underlying causes of deficiencies. However, although the Naval Audit Service reports often cite instances of personnel failing to follow specific regulations, the reports rarely cite the causes of the failure. When a problem's cause is not clearly identified, officials attempting correction may waste resources by treating symptoms rather than causes.

For example, a Naval Audit Service report 1/ stated that costs were incurred in excess of funds authorized, additional funds were not requested as necessary, and unneeded funds were not returned promptly. The report stated that these problems were caused by

1/C-35417, Dec. 23, 1977.

inadequate monitoring by the audited unit, the Naval Electronic Systems Command. However, the report did not address the underlying causes of the inadequate monitoring and what could be done to prevent its recurrence. In response to a recommendation for comprehensive validity reviews, the audited unit cited a June 1977 NAVCOMPT Notice 7600, which reported a lack of compliance with review requirements and suggested several ways to improve the review process. Although the Naval Audit Service agreed with the unit's comments, it neither pursued the underlying causes of inadequate monitoring for this particular unit nor made specific recommendations for improvement.

Another Naval Audit Service report 1/ identified a recurring problem with undistributed disbursements resulting from unmatched disbursements. No attempt was made to identify \$38.7 million that had accumulated in the appropriation. The report recommended that the Naval Facilities Engineering Command identify and match undistributed disbursements that had accumulated since inception (1948) and noted that a new Integrated Disbursing and Accounting System would eliminate the problem of unmatched disbursements.

The response was that no records were available to perform a reconciliation because Navy regulations require retention of disbursement registers for only 4 years. The command further stated that, since the \$38.7 million represented only 0.3 percent of the total program since inception, an extensive review was not warranted.

In our opinion, the Naval Facilities Engineering Command did not respond to--and the Naval Audit Service did not pursue--the basic underlying cause of the accumulation or what could have been done to prevent its recurrence. The report was also silent on the disposition of those disbursements that could not be matched. There is no reason to believe that the condition will be corrected unless the underlying causes are identified.

Naval Audit Service officials informed us that during oral discussions of audit findings, the underlying causes are covered and it is not deemed necessary to include lengthy discussions of causes in the report. They also stated that these two examples were not representative of all reports issued by them.

We agree that many of the Naval Audit Service reports do contain meaningful recommendations. However, without proper written documentation of the underlying cause in the report, the full benefits of the audit would not be obtained. The most important benefit lost would be a documented audit trail, thereby frustrating or preventing followup to see if the proper action was taken. Upper level managers may not understand the problem or the rationale

1/C-35927, Apr. 13, 1978.

for the corrective action taken. Other managers with similar problems may not see the relationship between the underlying cause and actions taken to correct it. Oral discussions also increase the probability that the underlying cause might be lost due to turnover of managers or audit personnel. New management personnel would not be able to determine if the corrective action taken alleviated the problem permanently, delayed its recurrence, or addressed the underlying cause at all.

Uncorrected system weaknesses could lead to fraud and abuse through unauthorized expenditures. The internal audit staff's failure to effectively identify and report the underlying causes of problems hinders and could prevent management from taking timely corrective action.

THE NAVY SHOULD CONSIDER ALLOCATING
MORE RESOURCES TO THE INTERNAL AUDIT
AND INTERNAL REVIEW FUNCTIONS

Our Policy and Procedures Manual for Guidance of Federal Agencies (3 GAO 34) states that the operations of an organization should be audited to determine whether its internal control system is functioning correctly. The Department of Defense has determined that a 2- and 4-year cycle is the most desirable frequency standard for its internal audit entities such as the Naval Audit Service.

Because of personnel ceiling restraints and increased workload, the Naval Audit Service has been unable to meet this standard. It has consolidated and reorganized some functions and adjusted its audit cycle to 3- to 5-year intervals. Even after adjusting to the longer audit cycle, the Naval Audit Service canceled or postponed 85 audits during fiscal 1978. Although this situation has been reported to Navy management, the Naval Audit Service has suffered funding and staffing cuts over the last 4 years; it now apparently lacks the resources to provide required coverage and meet the above standards.

The decreases in the Navy's size, which usually includes consolidation of key functions, makes effective internal audit and internal review functions at all levels even more critical. Therefore, the Navy may need to reassess the amount of resources it needs to effectively carry out the President's commitment to fight fraud, waste, and abuse in Government.

Internal audit and review coverage can provide additional necessary internal controls and timely information on problems before the functions of operating units become impaired. Once examined and appraised, this information often leads to lower costs, increased efficiency, and faster ways of getting things done.

By personal contact and firsthand observation of useful and effective policies and procedures, the Navy's internal audit organizations can bring to top management's attention those policies and procedures needing modification, explanation, and interpretation. However, without adequate resources to be effective and provide regular firsthand observations, the Navy cannot benefit from effective internal audits.

INTERNAL AUDITORS SHOULD BE INVOLVED IN ADP PLANNING

Except for the Naval Data Automation Command, none of the internal audit organizations we surveyed participated in the planning for ADP resources. ADP planning activities are usually approved by a steering committee. A representative of top management chairs the committee and membership includes senior management officials of the data processing department and representatives of departments that depend on computer processed information. An ADP steering committee usually

- approves agencywide policies for data processing systems,
- approves short and long range plans to develop and implement new computer systems,
- evaluates the need for new computer equipment, and
- ensures that new computer equipment is acquired expeditiously.

In a January 23, 1979, report we stressed the need for internal audit involvement in the design, development, and test phases of a new computer system. ^{1/} Internal auditor involvement is highly desirable to ensure that factors to enhance auditability, audit trails for security, and quality output are included in the design of new systems. Since technical controls usually are an integral part of the whole system and cannot easily be added at a later date, these early phases in the system's life cycle are the best time for incorporating control safeguards.

Within NAVSEA, neither the internal review function nor the ADP security function participated in the development or design phases of NAVSEA computer systems. Furthermore, at the time of our review neither of these functions had an accurate inventory of NAVSEA ADP systems or had developed adequate expertise to evaluate the integrity and security of computerized data.

Naval Audit Service officials informed us that, since our field work, standardized ADP audit programs have been developed

^{1/}"Automated Systems Security--Federal Agencies Should Strengthen Safeguards Over Personnel And Other Sensitive Data," LCD-78-123.

and steps have been taken to identify all Navy and Marine Corps computer systems requiring audit. As of September 30, 1980, this review had identified over 500 systems to be audited. Also, as of November 5, 1980, the Naval Audit Service has again initiated action to obtain representation on the Navy's ADP Steering Committee.

At a time of increasing reliance on computers and advancing ADP technology, internal audit and internal review are valuable resources that are not being used by management to safeguard the confidentiality and integrity of data in computer systems. This is of increasing concern as Naval operations are becoming more heavily committed to computers, with a proportionate increase in vulnerability. The Navy Auditor General should be a participating member of the Navy's ADP Steering Committee. All internal audit organizations should develop their ADP expertise to complement the systems being developed, and should participate in their command-level ADP steering committees.

CHAPTER 6

CONCLUSIONS, RECOMMENDATIONS, AND AGENCY COMMENTS

CONCLUSIONS

As pointed out in chapters 2 through 4 of this report, a need exists for improving internal controls at NAVSEA headquarters, NRFC, NARDAC, and the Norfolk and Charleston shipyards. Specifically, better internal controls are needed over payroll, computers, procurement, disbursements, receipts, and travel.

Additional controls are needed over the payroll operations at NRFC, NAVSEA headquarters, and the two shipyards. Payroll processing duties are not sufficiently divided among employees to provide adequate checks and balances; record counts and predetermined totals are not used effectively; personnel offices are not informed of what personnel transactions are posted to master payroll files; and payroll lists are not routinely compared with personnel lists to identify possible discrepancies.

Controls over security at the Charleston and Norfolk shipyards and NARDAC are inadequate to prevent unauthorized access to computer resources. Programmers are allowed unrestricted access to the computer rooms at Charleston, Norfolk, and NARDAC, and computer operators at these locations have access to systems documentation. Furthermore, access to the tape library is not adequately restricted at the three computer centers.

Additional controls are needed over procurements and disbursements by check at NAVSEA headquarters and NRFC. Internal controls over procurement procedures are inadequate at NAVSEA headquarters. NRFC has made both duplicate and erroneous payments because of insufficient review of payment requests and a lack of necessary automated system edits. Improvements are needed in review of travel plans, orders, advances, and claims. Finally, better controls are needed over accounts payable and receivable operations at the Charleston and Norfolk shipyards.

We believe these situations exist because management has not emphasized the need for good internal control systems. The lack of sound internal controls at the above locations makes them vulnerable to fraud, waste, and abuse.

Navy internal audit activities, as pointed out in chapter 5, are not achieving their full potential because audit findings often do not describe the underlying causes of problems, there are not enough audit resources, and internal auditors are not involved in ADP planning. Management does not always know what corrective action is needed to prevent problems from recurring and its operations are not reviewed often enough to minimize the risk of fraud, waste, and abuse. The Assistant Secretary of the Navy (Financial

Management) stated that "both audit and internal review are essential to Navy management." We agree and believe this statement is inconsistent with the decreasing emphasis in resources allocated to Navy internal audit organizations.

We also believe that internal controls can be made more effective by strengthening existing law. The Congress is considering two pieces of legislation which would require greater accountability by heads of Federal agencies for the effectiveness of their organizations' systems of internal financial control. The Financial Integrity Act of 1981 (H.R. 350, 97th Cong.) would require agency heads to undertake annual evaluations of their organizations' internal control systems and report the results of such evaluations to the Congress and the President.

The Federal Managers' Accountability Act of 1981 (H.R. 350, 97th Cong.) would require (1) evaluations and reports on the adequacy of the systems of internal accounting and administrative control of each executive agency and (2) the head of each agency to include, with the request for appropriations, a statement certifying that the request is based upon an accounting system that has been approved by the Comptroller General.

We would participate in the process by providing guidance for conducting the examinations and by reviewing the results. We believe both pieces of legislation would contribute to the development of improved internal control systems in the Navy Department. Our experience is that internal control systems require a commitment from top management and consistent vigilance to be effective. Therefore we support legislation of this nature and believe it will definitely help bring about such commitment and vigilance.

RECOMMENDATIONS

To reduce the vulnerability of the activities we have discussed in this report, we recommend that the Secretary of the Navy emphasize to all management levels the significance of good internal controls and the need for managers to make sure that tasks and functions for which they are responsible are adequately controlled to prevent, or at least reduce, the risk of intentional or accidental misuse or abuse of Federal funds. In addition, we recommend that the Secretary take the following actions:

- Establish a central internal control officer to oversee these controls and ensure that each command and major location establish its own officer to see that (1) improvements are made to correct the problems noted during our review and (2) surveillance is constantly maintained to prevent recurrence of these problems.
- Require proper segregation of payroll functions at NRFC so that no one person can handle all phases of a transaction.

✓--Improve other controls over payroll at NAVSEA headquarters and the shipyards, such as requiring (1) control totals to be determined when source documents are prepared, (2) personnel offices to be informed by the payroll staff of actions processed to payroll files, and (3) a routine, periodic reconciliation of payroll and personnel files.

✓--Direct all installations to assign an ADP security officer, implement a security training program, and restrict access to computer equipment, computer tapes, and system documentation.

✓--Direct NAVSEA to implement procedures for (1) expediting the processing of requests for office equipment, (2) performing internal reviews of contract overhead charges to ensure that only authorized items are charged, (3) reviewing the contract and funding documents used in acquiring office equipment to ensure that other charges are proper and are accounted for, and (4) providing specific detailed guidelines on the use of funding documentation.

✓--Ensure that NRFC improves its review of payment requests and automated system edits by thoroughly examining documentation supporting expenditures before making payments, and by ensuring that the more sophisticated computer system being designed (see p. 18) requires an adequate number of matching invoice elements to preclude duplicate payments.

✓--Require the Charleston shipyard to match payments to supporting documentation and to properly classify accounts receivable so that they are collected promptly.

--Improve controls over travel at NAVSEA headquarters by (1) requiring appropriate officials to approve travel, (2) seeing that travel advances are liquidated promptly and that claims are properly reviewed, and (3) ensuring that managers receive reports containing information needed for controlling and planning travel expenditures.

--Require the Charleston shipyard to improve its control over travel by addressing the weaknesses identified on page 23 of this report.

--Make internal audits more effective by (1) reassessing staffing priorities at all levels to adequately emphasize internal auditing in light of decreasing size and other factors which make Navy activities more vulnerable to fraud, waste, and abuse, (2) requiring internal audit participation in the design, development, and test phases of a new computer system to ensure that factors to enhance auditability, audit trails for security, and quality output are designed and developed into new systems, and (3) requiring internal auditors

to identify underlying causes of problems uncovered so that action can be taken to prevent recurrence.

AGENCY COMMENTS

The Department of Defense commented on matters presented in this report in a November 25, 1980, letter. Appendix II presents a detailed discussion of the Department's views as well as our evaluation of those views.

CHECKLIST OF INTERNAL CONTROL WEAKNESSES FOUND DURING
GAO'S VULNERABILITY ASSESSMENT OF NAVSEA HEADQUARTERS, NRFC,
NARDAC, NORFOLK AND CHARLESTON SHIPYARDS

| Internal control weaknesses | NAVSEA Headquarters | NRFC | NARDAC | Norfolk | Charleston |
|---|------------------------|------|--------|---------|------------|
| <u>Payroll</u> | | | | | |
| -Master payroll files not routinely matched with master personnel files | | X | | X | X |
| -Personnel offices not told when personnel actions are processed to the master payroll files | | X | | | |
| -Payroll and personnel files not reconciled in a timely manner | | | | X | X |
| -Record counts and predetermined control totals not used effectively to ensure complete and accurate processing of data | | X | | X | X |
| -Employee folders not maintained with supporting documents | | X | | | |
| -Departments which initiate documents not provided with computer listings showing what transactions were processed | | X | | | |
| -Transactions processed not independently reviewed | | X | | | |
| -Cumulative control totals not determined for total time and attendance information processed in a pay cycle | | X | | | |
| -Duties in processing personnel actions and time and attendance information not adequately separated | | X | | | |
| -Blank payroll checks not adequately safeguarded | | X | | | |

| Internal Control Weaknesses | NAVSEA Headquarters | NRFC | NARDAC | Norfolk | Charleston |
|---|---------------------|------|--------|---------|------------|
| -Adequate measures not provided to ensure that all erroneous paychecks received are canceled | | X | | | |
| -Inadequate physical security over checks in the disbursing office | | X | | | |
| -Pay records kept in insecure storage room | | X | | | |
| -Timekeeping and check distribution duties not adequately separated | * X | | | | X |
| <u>Purchasing</u> | | | | | |
| -Contract expenditures not charged to correct accounts | X | | | | |
| -No assurance of accountability of funds applied against contracts | X | | | | |
| -Proper procedures not followed by contracting officers and project managers in acquiring or leasing office equipment | * X | | | | |
| -Written receiving procedures not adequate to prevent deliveries of unauthorized purchases | * X | | | | |
| -Office equipment acquired without going through Federal supply contractors | * X | | | | |
| -Adequate training not provided for contract branch buyers | | | | X | |

*Navy officials stated these internal control weaknesses cited have been corrected or are in the process of being corrected.

| Internal Control Weaknesses | NAVSEA | | | | |
|---|--------------|------|--------|---------|------------|
| | Headquarters | NRFC | NARDAC | Norfolk | Charleston |
| -Duties involved in contracting tasks (receiving and depositing bids in a safe) not adequately separated | | | | X | |
| -Bids received not adequately safeguarded (no log or record) | | | | X | |
| <u>Administrative Purchases</u> | | | | | |
| -Lack of written procedures which outline receiving department responsibilities and separate those responsibilities in line with internal controls (preparing and submitting requisitions, certifying funds are available, preparing and sending receiving reports to the procurement branch) | * X | | | | |
| -Invoice processing functions not separated from requisitioning and procurement functions | X | | | | |
| -Receiving department not instructed to send copies of receiving reports directly to departments responsible for approving invoices, requisitioning, and procurement | * X | | | | |
| -No requirement for purchase requisitions to be approved and signed by the supply branch supervisor or by an official who does not approve invoices for payment | * X | | | | |
| -No signature file maintained of persons authorized to approve purchase orders and invoices for payment at NRFC and no verification of approving signatures against such a file before making payments | | X | | | |
| -No limit to number of persons authorized to approve purchase orders and invoices | | X | | | |

*Navy officials stated these internal control weaknesses cited have been corrected or are in the process of being corrected.

| Internal Control Weaknesses | NAVSEA Headquarters | NRFC | NARDAC | Norfolk | Charleston |
|---|---------------------|------|--------|---------|------------|
| -Signatures on invoices not checked for authenticity before payment | | X | | | |
| -Signature authority not limited | X | X | | | |
| -No procedures provided to prevent the mismanagement of funds, i.e., timely payment of invoices for discounts | | X | | | |
| -Access to purchase orders not restricted to persons authorized to approve invoices and purchase orders | * X | | | | |
| <u>Receiving, Storing, and Issuing Material</u> | | | | | |
| -Lack of written procedures within the supply department for receiving, storing, or issuing material | | | | X | |
| -Adequate security not provided within the receiving and storage functions | | | | X | |
| -Adequate procedures not provided for requisitioning office equipment | | | | X | |
| -No assurance that direct material inventory items will be delivered to their intended location | | | | X | |
| -Delivery section not making sure that delivery manifest documents are signed promptly and accounted for properly | | | | X | |
| -Stamping machine and blank manifest documents not properly secured | | | | X | |

*Navy officials stated these internal control weaknesses cited have been corrected or are in the process of being corrected.

| Internal Control Weaknesses | NAVSEA Headquarters | NRFC | NARDAC | Norfolk | Charleston |
|--|------------------------|------|--------|---------|------------|
| <u>Duplicate Checks</u> | | | | | |
| -Lack of adequate manual review and necessary system edits to preclude duplicate payments | | X | | | X |
| -Research files not adequately researched before payment of duplicate invoices | | X | | | |
| <u>Cash Receipts</u> | | | | | |
| -Procedures in the mailroom not developed and implemented to ensure that checks are properly received, controlled, and accounted for (i.e., logged in and reconciled against deposits) | | X | | X | |
| <u>Accounts Receivable</u> | | | | | |
| -Inadequate justification for accounts receivable writeoffs | | | | | X |
| -No proper record of accounts receivable from other sources | | | | | X |
| <u>Computer Security</u> | | | | | |
| -Unrestricted access to computer room | | | X | X | X |
| -Unrestricted access to system documentation | | | X | X | X |
| -Unrestricted access to tape library | | | X | X | X |
| -Proper control procedures not provided for programmers and computer operators | | | X | | |
| -Security training not provided for computer personnel | | | X | | |

| Internal Control Weaknesses | NAVSEA Headquarters | | | | Norfolk | Charleston |
|---|---------------------|--------|---|--|---------|------------|
| | NRFC | NARDAC | | | | |
| -Lack of procedures to ensure protection of computer equipment and continuous, undisrupted operations in NARDAC's computer room | | X | | | | |
| -Computer center operations not performed by persons independent from the security officer | | X | | | | |
| -Lack of adequate security to prevent unauthorized entry to computer room | | X | | | | |
| <u>Integrated Disbursing and Accounting System</u> | | | | | | |
| -No restriction on access to files within the new automated disbursing system | | | X | | | |
| -Unique passwords not maintained for each payment function so the user has access only to data necessary to perform his job | | | X | | | |
| -Unique user number not provided to each terminal user so the computer can check what the user is permitted to do | | | X | | | |

| Internal Control Weaknesses | NAVSEA Headquarters | NRFC | NARDAC | Norfolk | Charleston |
|---|------------------------|------|--------|---------|------------|
| -No policy to suppress the printing of passwords on hardcopy or on terminal display to avoid the possibility of casual observance | | X | | | |
| -Duties not separated and divided between two or more individuals so that one individual alone cannot generate a payment | | X | | | |
| -Each terminal not assigned a specific set of access categories in order to restrict the terminal to only those files it is intended to access | | X | | | |
| <u>ADP Audit</u> | | | | | |
| -Lack of adequate internal ADP audit capability | X | | X | | |
| -Lack of a comprehensive (Navy-wide) computer security program supported by complete operating instructions | X | | X | | |
| -ADP security functions not assigned to a staff level position so that they have sufficient visibility and authority to enforce security measures | X | | X | | |
| <u>Internal Audit</u> | | | | | |
| -Internal audit reports do not contain the underlying causes of problems which were developed and reported | X | | | | |
| -Too little internal audit resources to provide adequate audit coverage | X | | | | |
| -No participation in ADP steering committees | X | | X | | |

| Internal Control Weaknesses | NAVSEA | | | | |
|---|--------------|------|--------|---------|------------|
| | Headquarters | PSA* | NARDAC | Norfolk | Charleston |
| <u>Travel</u> | | | | | |
| -Travel vouchers not promptly sent to the travel section | | X | | X | |
| -Supervisors not adequately reviewing employees' claims (travel vouchers) before submission to PSA | X | | | | X |
| -Travelers not promptly paying excess travel advances (PSA travel services sent 1,592 of 9,526 excess advances in CY 1978 to the payroll department for collection--approximately 17 percent) | | X | | | |
| -Different signatures for the requesting official and approving officials not required on travel orders | X | | | | |
| -Meaningful reports not provided for determining travel advances outstanding and ensuring that advances outstanding are liquidated within 15 days of trip completion | X | | | X | |
| -Duties performed by travel clerks not properly separated (person processing travel orders is also signing travel advance checks) | X | | | | |
| -Use of check writing machine not restricted to a small number of persons | X | | | | |
| -Advance checks issued without proof of identification and without traveler signing for receipt to ensure accountability | X | | | | |
| -No systematic way of ensuring that travel vouchers are not submitted twice for payment | | X | | | |

*PSA: Personnel Support Activity, Washington, D.C.

| Internal Control Weaknesses | NAVSEA | | | | |
|---|--------------|-----|--------|---------|------------|
| | Headquarters | PSA | NARDAC | Norfolk | Charleston |
| -Travelers not providing to the travel services complete data, sufficient copies of orders or vouchers, enough supporting documents, and endorsements | | X | | | |
| -Appropriate information (signatures acknowledging receipt) not provided on travel orders to determine if an advance was actually received | X | | | | |
| <u>Office Equipment</u> | | | | | |
| -No provision for adequate separation of duties when office equipment is being acquired | | | | X | |
| <u>Accounts Payable</u> | | | | | |
| -Adequate written policies and procedures not provided within the accounts payable unit | | | | X | |
| -No assurance that proper documentation is obtained for the receipt of material | | | | X | |
| -No claims register for managing and monitoring of credit memos and checks due from suppliers | | | | X | |
| -Accounts payable files not reviewed to account for all related documents | | | | X | |
| -Payment documents not adequately reviewed and matched with receiving/inspection reports before payment | | | | | X |
| -Accounts payable documentation not reconciled | | | | | X |
| -Known pending credits not settled and known overpayments not collected | | | | | X |



DEPARTMENT OF THE NAVY
OFFICE OF THE COMPTROLLER
WASHINGTON, D.C. 20350

IN REPLY REFER TO

25 NOV 1980

Mr. D. L. Scantlebury
Director, Division of Financial and
General Management Studies
U. S. General Accounting Office
441 G Street, N. W.
Washington, D. C. 20548

Dear Mr. Scantlebury:

This is with regard to your letter of October 6, 1980 to the Secretary of the Navy concerning your report on "Weak Internal Controls Make the Naval Sea Systems Command Vulnerable to Fraud, Waste, and Abuse" (FGMSD-80-?, Assignment Code No. 911015, OSD Case #5545).

The Department of Defense comments to your report are attached.

Sincerely,


S. D. FROST
Acting

DGD Comments
on
GAO Draft Report of 6 October 1980
on
Weak Internal Controls Make the Naval Sea Systems
Command Vulnerable to Fraud, Waste, and Abuse
(OSD Case #5545)

I. GAO Findings and Recommendations.

GAO states that inadequate internal controls over several fiscal and managerial activities of the Navy make them vulnerable to fraudulent acts as well as nonintentional misuse of Federal funds. The GAO indicates that a need exists for improving internal controls at NAVSEA headquarters, NRFC, and the Norfolk and Charleston shipyards. Specifically, there is a need for (1) better internal controls over payroll, computers, procurement, disbursements, receipts, and travel and (2) actions to improve internal audits.

Payroll processing duties are not sufficiently divided among employees to provide adequate checks and balances; record counts and predetermined totals are not used effectively, personnel offices are not informed of what personnel transactions are posted to master payroll files; and payroll lists are not routinely compared with personnel lists to identify possible discrepancies.

Controls over security at the Charleston and Norfolk shipyards and NARDAC are inadequate to prevent unauthorized access to computer resources. Programmers were allowed unrestricted access to the computer rooms at Charleston, Norfolk, and NARDAC. Also, computer operators at the above locations have access to systems documentation. Furthermore, access to the tape library is not adequately restricted at the three computer centers.

Additional controls are needed over procurements and disbursements by check at NAVSEA headquarters and NRFC. Internal controls over procurement procedures were inadequate at NAVSEA headquarters. NRFC has made both duplicate and erroneous payments because of insufficient reviews of payment requests and a lack of necessary automated system edits. Also, improvements are needed in review of travel plans, orders, advances, and claims. Furthermore, better controls are needed over accounts payable and receivable operations at the Charleston and Norfolk shipyards.

GAO believes these situations exist because management has not emphasized the need for good internal control systems. The lack of sound internal controls at the above locations makes them vulnerable to fraud, waste, and abuse.

GAO also stated that Navy internal audit activities are not achieving their full potential because audit findings often do not describe the underlying causes of problems; there are not enough audit resources; and internal auditors are not involved in ADP planning. Management does not always know what corrective action needs to be taken to prevent problems from recurring and the frequency of reviews of its operations are not sufficient to assure that the risks of fraud, waste, and abuse are minimized. The Assistant Secretary of the Navy (Financial Management) stated that "both audit and internal review are essential to Navy management". However, GAO believes that this statement is not consistent with the decreasing emphasis in resources allocated to Navy internal audit organizations.

GAO made eleven recommendations to SECNAV (listed on pages 31-33 of the GAO report) which are discussed in the DOD comments below. ^{1/}

II. DOD Comments

General Comments:

1. The title of the report needs to be changed. As stated, the title does not afford the Congress and the general public a fair and objective evaluation of any response that can be offered. A better climate for report receptivity may be gained if subjective titling such as this is avoided. A more impartial title should be selected.

Additionally, the title cites only the Naval Sea Systems Command as the object of the report. Approximately 40% of the report concerns other commands which are not related to the command structure of the Naval Sea Systems Command. The Naval Regional Finance Center, the Naval Regional Data Automation Center, and the Naval Audit Service are organizational entities which report to other elements of the Naval establishment. The Naval Sea Systems Command cannot direct actions to these commands nor is it directly responsible for their actions. The inclusions of these elements in the report and the constant inference that all of the activities are at an equal level make the report extremely awkward and susceptible to large misinterpretations. During the OSD/Navy/GAO meeting on 30 October 1980, one title suggested to GAO was: "Assessing the Effectiveness of Internal Controls on Transactions Related to Some Navy Commands".

GAO COMMENT

The report's title has been changed and additional information has been included in chapter 1 to describe all of the activities included in the review.

^{1/} Page references have been changed to correspond to page numbers in the final report.

2. Throughout the report, the GAO makes continual reference to the GAO Policy and Procedures Manual as a standard guidance directive. NAVSEA financial and other policies/procedure directives are derived from higher Naval authority and Department of Defense documents. The constant reference to the GAO documents implies that NAVSEA systems and procedures should be directly attributed to the GAO publications. There is little indication that the NAVSEA directives in the functional areas under consideration were reviewed as a vital element of internal control system checks.

GAO COMMENT

According to the Budget and Accounting Procedures Act of 1950, the heads of executive agencies are responsible for establishing and maintaining adequate systems of accounting and internal controls. These systems must conform to the accounting principles, standards, and related requirements prescribed by the Comptroller General. The GAO Policy and Procedures Manual for Guidance of Federal Agencies sets forth these principles, standards, and requirements and was used as the primary source of criteria for this review.

However, Department of Defense, Department of the Navy, and NAVSEA policies and procedures also were examined and, in fact, the report specifically refers to these procedures in certain instances. We do not mean to imply that these policies and procedures do not exist. Rather, it is our contention that in numerous instances they were not adhered to.

3. The report, in general, does not present information in a manner that allows the reader to place various elements in perspective. The organizational size, the command mission, and the total resources administered by NAVSEA are not related to the areas where weaknesses are alleged. As examples, the sections of the report which deal with travel administration deficiencies and unauthorized procurements fail to show the relationship of weaknesses discovered to the significant total volume of business conducted in these areas.

GAO COMMENT

Chapter 1 of the report has been revised to include information on Navy activities, other than NAVSEA, included in the review. In addition, more information has been included in the sections on travel and procurement to place the deficiencies in perspective. However, the nature of a vulnerability assessment, as described in chapter 1, is to perform a broad examination of an agency's operations using an internal control checklist and the testing of a limited number of transactions.

The number of times a deficiency exists is not as relevant as the fact that it occurred--indicating a weakness in internal control which invites more of the same deficiencies. It is commonly accepted that prevention is the best way to combat fraud, waste, and abuse and that the key to prevention is sound internal controls.

4. The GAO should provide definitions of Fraud, Waste and Abuse in order to clarify the report. It is difficult to determine which category is being considered by the GAO in the various sections of the report. The Department of Defense has provided a set of definitions and standards for DOD reporting purposes in which the term "abuse" is no longer used. The GAO should provide a set of descriptions in order to have the terms consistent.

GAO COMMENT

The intent of the report is not to categorize the nature of the weaknesses identified but to show the areas in which the Navy activities need to strengthen internal controls to prevent these weaknesses from recurring. Therefore, no change has been made.

5. GAO did not conduct exit meetings with top level officials at each command they reviewed. Such meetings could have contributed to more accurate and complete findings in the GAO draft report and also affected the wording of the GAO recommendations therein.

GAO COMMENT

The above statement is not correct. Exit conferences were conducted with the shipyard commanders at Charleston and Norfolk. This fact is recognized in the agency's comments on page 54. We also met with top-level NRFC officials concerning our review of NRFC's payments to vendors. In addition, the staff met with top officials at NAVSEA and the Naval Material Command to discuss the contents of the checklist of internal control weaknesses (app. I). After the report was officially transmitted to the agency, we met informally with top-level officials of all activities included in the review to discuss the contents of the report.

Specific Comments on the Digest:

Page i. 1st paragraph.

Comment: Statement that study was not aimed at finding fraud, waste, abuse... "Nevertheless disclosed..." infers that \$5.8 million in receivables fits one of the categories. As defined later, this item represents excess material returned to the supply system for credit over a period of two fiscal years.

GAO COMMENT

The statement has been revised to read "written off without adequate justification" because, at the time of our review, shipyard officials were unable to explain why these receivables were written off.

Page i. 2nd paragraph.

Comment: The relevance of this paragraph is not understood. The inference is that NAVSEA is guilty of fraud by association with the Navy. It is difficult to believe the GAO statistics cannot be broken down. This paragraph should be stricken.

GAO COMMENT

The purpose of the paragraph is to show that, although the identification of fraud cases was not a part of this review, a related study showed that fraud was a significant problem within the Navy. In fact, there were more reported fraud cases in the Navy than in any other agency.

The statistics were provided by the Navy, not by GAO. The purpose in this series of reviews by the GAO Fraud Task Force is to assist the various governmental agencies in preventing fraud, waste, and abuse of governmental funds. A more positive attitude by commands such as NAVSEA would greatly aid in attaining this objective.

Page ii. "Better Internal Controls Needed"

Comment: Statement that NAVSEA has "inadequate internal controls over several activities" infers that the items in the list that follows are all NAVSEA controllables. They are not, and the statement should be amended to state the items applicable to NAVSEA. Additionally, the statement "significant portion of its available funds may not be spent...etc." is not substantiated by evidence or proof in the report and should be stricken.

GAO COMMENT

The statement has been revised. The specific weaknesses are now identified with the specific location at which they were found.

However, we disagree that the report does not substantiate the stated potential for misspent funds. We found internal control weaknesses in every area we reviewed. Appendix I clearly shows the extent of vulnerability for each activity included in the review.

Page iii. "Improvements Needed in Internal Audit."

Comment: Statement should be added to clarify what activity is being cited. The Naval Audit Service relationship to NAVSEA should be detailed, as well as the reason this section is being included in a report on NAVSEA.

GAO COMMENT

No change has been made to the digest. However, the body has been revised to show the relationship of the Naval Audit Service and the Office of Internal Review to NAVSEA. We have also added an organizational chart to show the relationships of the activities included in our review. The draft report sent to the agency for comment contained our rationale for including a chapter on internal audit. As stated in our earlier draft, internal audits are part of, or should be part of, the agency's system of internal controls. Internal auditing is essential to management's attaining its goals because it furnishes information, analyses, appraisals, and recommendations pertinent to management duties and objectives.

We also discussed the findings of a Naval Audit Service survey on NAVSEA and other command procurement of office equipment in chapter 4. This discussion shows the importance of internal auditing in identifying weaknesses in internal controls and thereby in preventing fraud, waste, and abuse.

Page ii, last paragraph. "Lack of basic controls over approving, processing, and paying employee travel claims."

Comment: The travel claims function was transferred to the Personnel Support Activity, Washington, D.C., effective 1 October 1979. This information was available during the audit.

GAO COMMENT

This statement has been revised to read "Lack of basic controls at the Naval Sea Systems Command over approving and processing employee travel claims, and at Personnel Support Activities which pay the claims."

Page iv. "Conclusions and Recommendations."

Comment: Statement "...internal controls influence, etc...other activities may be vulnerable" infers again that NAVSEA has control of the 3 other commands reviewed. Additionally, the statement is an overgeneralization, draws an illogical conclusion and is not supported by evidence in the report.

GAO COMMENT

The statement has been revised to read "The Navy's insufficient emphasis on internal controls at the activities GAO reviewed..." We disagree that the statement is an overgeneralization, draws an illogical conclusion, and is not supported by evidence. The majority of internal control systems we reviewed are uniform for all Navy activities and were prescribed by the Department of the Navy. Therefore, if weaknesses in internal controls are found in one activity, those weaknesses may apply to all activities.

Recommendations in the Digest, as well as the specific weaknesses noted should be reviewed based on the specific comments that follow.

Specific Comments on Chapter 1, Introduction:

Page 1. 4th line "concerning NAVSEA...."

Comment: Sentence should be expanded to list all commands reviewed.

GAO COMMENT

The statement has been revised to say "selected Navy Department activities."

Page 2. "NAVSEA Command's Purpose."

Comment: This section should include a more comprehensive description of the NAVSEA organization including the number of employees, number and size of the field activities, size of headquarters plus a more accurate description of its financial resources.

GAO COMMENT

No change has been made because the agency has not given any reason for including this information. We do not think additional background information has any bearing on the internal control weaknesses identified.

Page 3. "Objectives, Scope."

Comment: The section which mentions NRFC and NARDAC should be expanded to explain their command relationships and total resources.

GAO COMMENT

The section on purpose and programs has been expanded to include this information and an organizational chart has been added to show the relationships of the activities reviewed. In addition, the Objectives, Scope, and Methodology section has been revised to show our rationale for selecting the activities for review.

Page 3. Paragraph 4.

Comment: The discussion concerning the evaluation of controls for program and administrative activities is not substantiated in the report. Program activities, as defined by GAO, for NAVSEA would involve an examination of the major shipbuilding and weapons acquisition programs. The report generally covers only the administrative aspects of NAVSEA. If the program activities were, in fact, reviewed, then a statement of the conditions found should be made. Otherwise the section should be rewritten to state that only administrative support activities were reviewed.

During discussions of the above finding at the OSD/Navy/GAO meeting on 30 October 1980, GAO indicated they would review their work papers to validate that controls over program activities were, in fact, reviewed.

GAO COMMENT

The term "program activities" has been deleted.

Specific Comments on GAO's Findings and Applicable Recommendations:1. Recommendation #1

To reduce the vulnerability of these activities, GAO recommends that the Secretary of the Navy emphasize to all management levels the significance of good internal controls and the need for managers to make sure that tasks and functions for which they are responsible are adequately controlled to prevent or at least reduce risks of either intentional or accidental misuse or abuse of Federal funds.

Comments:

Concur with intent; however, guidance currently contained in NAVCOMPT Manual, Vol. 1 - Comptrollership Organization and Responsibilities, SECNAVINST 7510.7A - Department of the Navy Audit Manual for Management, SECNAVINST 7510.8 - Internal Review in the Department of the Navy, and OPNAVINST 5040.7H - Naval Command Inspection Program, provide adequate guidance and emphasis to all management levels of the importance of internal controls to prevent waste through mismanagement or fraudulent or abusive practices. The collective guidance provided therein and as supplemented by implementing directives at Headquarters elements and individual commands provide the required emphasis to ensure that all activities are aware of the need for good internal controls.

GAO COMMENT

We have not said that written guidance did not exist. However, because of the numerous weaknesses found in internal controls over the areas we reviewed, we believe the guidance has not been followed. We believe the emphasis on the importance of internal controls must come from top management. If the head of an organization stresses the importance of such controls, managers at lower levels will perceive them in a similar light. More importantly, the managers must be held accountable for ensuring that existing internal control policies and procedures are properly implemented.

2. Recommendation #2

Establish an internal control officer to oversee these controls and assure that each Command and major location establish an officer to see that improvements are made to correct the problems noted during our review and that surveillance is constantly maintained to prevent recurrence of these problems.

Comments:

Do not concur. In our opinion there are adequate internal control officers within the various DON systems. The designation of an added official to oversee the existing controls would provide another management layer without providing an apparent improvement to productivity. The DON believes that there presently exists good internal control officials at every level of command. These officials, such as base commanders, internal review offices, are supported by audit, inspection and investigatory organizations - Naval Inspector General, Naval Audit Service, Naval Investigative Service. These are also buttressed by the GAO, the DAS, and the S&IS organizations, all of whom are involved in assuring that adequate internal control exist. The latest control system, currently being developed in DOD, is the "followup system" required by OMB and Congress. This system when implemented will provide for the followup of recommendations made by audit, inspection and investigation, by GAO, DAS, NAS, NIG, NIS, Navy Internal Review organizations. It is apparent that adequate control officials exist or will exist in the DON. Any additional layer of an internal control officer will be redundant.

GAO COMMENT

Despite the department's contention that there are adequate internal control officers within the various Navy systems, we found numerous weaknesses in internal controls which cause us to conclude that these officers are not at a sufficiently high organizational level. We believe that the underlying cause of the internal control weaknesses is the lack of commitment by top management of the Department and that a high-level internal control officer could focus efforts toward improvement.

3. Findings (Note: the below finding relates to Rec. #3, 4 & 7)

Page 6, "Better Control Needed Over Computer Processing."

Comment: The discussion on record counts and the inference that payroll data is not completely and accurately processed is not entirely accurate. At Charleston Naval Shipyard, the Payroll Section has a record count and an audit function on all personnel actions to ensure that the actions have been entered. Additionally, there are numerous controls in the shipyard pay system to ensure accurate processing of data. The Shipyard Management Information System payroll

application provides numerous control reports including: Daily Payroll Exception Report; Daily Payroll Control Report - Total (Hours and Dollars); Missing Timecard Listing; and the Daily Error Listing. In addition, each supervisor is responsible for reviewing the predetermined control totals maintained by the pay clerks to ensure the payroll is accurate.

GAO COMMENT

The statement on record counts and control totals has been revised to reflect that, in many instances, these record counts and control totals are in the system but are not properly used by the responsible Navy activities. We agree that shipyard management information systems do provide control reports. However, proper and timely use of these reports is necessary for the reports and the related system of internal controls to be effective. Also, the proper use of control totals and record counts indicates that they should be generated prior to entry on automated systems, not afterward.

Page 8. "Need to Match Payroll and Personnel Files."

Comment: The statements regarding the matching of payroll and personnel files are not entirely accurate. At the Norfolk Naval Shipyard, the Master Payroll File and the Personnel Automated Data System (PADS) file are matched weekly. The shipyard was unable to confirm the discrepancies cited by the auditors. Specific information as to the reported discrepancy was requested by the shipyard at the exit conference with the GAO personnel, but this information was not provided. At the time of the review, the reported finding was not discussed with or confirmed by knowledgeable shipyard officials. During the DOD/GAO meeting of 30 October 1980, GAO indicated they would review their work papers for validation of discrepancies and notes on whether they had provided Shipyard officials with information at the exit conference. At the Charleston Naval Shipyard, the Master Payroll File is normally matched to PADS files on an annual basis. At NAVSEA Headquarters, the need to match these records was noted in NAVSEA Internal Review Report 80-1 dated 29 January 1980 on timekeeping and overtime.

GAO COMMENT

The Personnel Automated Data System is not the official Navy personnel file. The Naval Automated Civilian Manpower information System (NACMIS) is, to our understanding, the official personnel file and for this proposed match, our facts, as stated in the draft report, were and are correct.

We reexamined the supporting papers for work at the shipyards and found that this information was provided to officials during the exit conference at the Norfolk Naval Shipyard. During our review at Charleston we found discrepancies, which we were able to reconcile, when we matched the NACMIS and the payroll files and discussed the need for periodic matches of the payroll file with NACMIS.

Recommendation #3

Require proper segregation of payroll functions at NRFC so that no one person handles all phases of a transaction.

Comment: Concur in principle. The following NAVCOMPT regulations provide sufficient division of duties to satisfy the intent of this recommendation:

a. NAVCOMPT Manual, Vol. 3, par. 033101 specifies that under no circumstances will payroll clerks be allowed to maintain their own individual pay accounts.

b. NAVCOMPT Manual, Vol. 4, par. 045012-2c(1) further states personnel designated to distribute pay checks should not participate in the preparation, approval, or certification of the payroll or the personnel action documents or in maintaining the payroll controls or earning records on the time and leave records.

NRFC Washington in practice does what the GAO recommends as a solution. Major rotations of payroll clerks are made annually to preclude long-range potential problems and as a training media. Most importantly, rotations take place routinely each pay period as a result of the peak work periods created by the payroll cycle whereby payroll clerks are assigned various portions of the total workload until payroll processing is completed. Thus, no one individual controls all phases of a transaction. As a matter of policy, the payroll clerk that updates the Payroll Master file does not process the biweekly Time and Attendance Report. Also, each activity payrolled is provided the Payroll for Personnel Services Report (NAVCOMPT Form 485) biweekly showing payroll transactions by employee - in effect providing for independent review for validity or accuracy. NAVMAT, upon request, is provided with a Payroll Master file for all Systems Commands for matching to their Master Personnel file. Further, payroll checks are distributed externally (payroll clerks never see the payroll checks) directly to the payrolled activities for review and verification of accuracy. Based on the above, NRFC, Washington payroll processing procedures meet the requirements of proper segregation of payroll functions. This position is further supported by the Naval Audit Service Capital Region Audit Report D38020, dated 4 June 1980, in which it is stated, "We concluded that the system did not vary in any material aspect from the approved system design and is in compliance with the principles, standards, and related requirements currently prescribed by the General Accounting Office Review Guide for Federal Agency Payroll System Design."

It is suggested this recommendation be withdrawn for reasons stated above.

GAO COMMENT

In a subsequent telephone conversation with NRFC's Executive Director we were told that the sentence in the second paragraph under b. above, "NRFC Washington in practice does what the GAO recommends as a solution" should have been changed to read "As a result of the GAO audit, NRFC will institute a procedure requiring an independent review of SF-50 (Notification of Personnel Action) data input by the ADP terminal operator." The official stated the change was too late to be incorporated in the Navy's official comments. Also, the official proposed that the following statements be added to this paragraph: "NRFC is pursuing the feasibility of obtaining SF-50 data through electronic ADP media. This data will be reviewed by payroll personnel prior to entering it into the payroll system."

Based upon the above information, the recommendation was not changed.

Recommendation #4

At NAVSEA Headquarters and the shipyards, improve other controls over payroll, such as requiring: (1) control totals to be determined when source documents are prepared; (2) personnel offices to be informed by the payroll staff of actions processed to payroll files; and (3) a routine periodic reconciliation of payroll and personnel files.

Comment: Do not concur. Adequate controls exist over payroll processing at the shipyards. Additional control totals are not required. Shipyard personnel offices are provided with the weekly payroll master file change register, and periodic reconciliation of payroll and personnel files is accomplished. The recommendation is no longer applicable to NAVSEA Headquarters. NAVSEA personnel and payroll functions are handled by separate activities that are not under NAVSEA cognizance.

GAO COMMENT

As stated above, our point is that controls did exist but were not being used effectively at NAVSEA or at the shipyards. As our recommendation states above "...improve other controls...", not implement new or additional controls. We are aware that shipyard payroll offices are provided weekly listings; however, "periodic reconciliations" were not being performed in a timely manner. In fact, we noted February and March 1979 errors on the payroll report during our November 1979 site visit to the Norfolk Shipyard.

We believe the recommendation is still applicable to NAVSEA because the ultimate responsibility for the accuracy of its payroll and personnel data rests with NAVSEA and its cognizant subordinate activities.

4. Findings (relate to Recommendation #5) page 11, para 2

"Programmers were allowed unrestricted access to the computer rooms at Charleston, Norfolk, and NARDAC. Sound ADP control requires that programmers have restricted access to the computer room and that they not be allowed to operate computer equipment. These requirements exist because programmers have the technical ability to make changes to computer programs and data files without being readily detected. Although we found no evidence of programmers doing this during our audit, the failure to restrict access subjects the computer systems to unnecessary risk."

"At the NARDAC center, for example, we observed a programmer operating the computer equipment during our tour of the facility. We were informed that the programmer was temporarily filling in as an operator because the regular operators were in a meeting. We also were informed that, even though no operators are present, programmers sometimes operate computer equipment on weekends to test their programs. Officials explained that this avoids disrupting normal production operations."

Comment: Concur that Programmers access must be restricted. However, system programming personnel are required to work on second and third shifts and on weekends in order to test and modify the executive system without disruption of production processing. Additionally, staffing with operations personnel and tape librarians would be an expensive overtime cost or would require rescheduling of shifts to provide coverage. Funding for overtime work is scarce and rescheduling shifts is impractical since the requirements for after hours work is sporadic.

The Navy realizes that more adequate security measures for the computer room are needed and this problem will be resolved when the NARDAC computer facility is moved to a consolidated site during the first or second quarter of calendar 81. The consolidated site will be staffed around the clock.

The Norfolk Naval Shipyard DPO Instruction 5530.1A which was in force at the time of the audit, authorizes unlimited access only for systems personnel who are computer software specialists. This restriction continues under the Norfolk Naval Shipyard current DPO Instruction 5530.1B. Application programmers are allowed in the computer room only on a problem situation basis. Access is controlled by cipher locks which are being changed to magnetic card key entry. NAVSEA letter 9941-PAH 5510/A Ser 2627 of 27 Oct 1980 to NAVSEASYS COM Shore Based detachments and others re-emphasizes the importance of enforcing current ADP Security Instructions.

GAO COMMENT

We believe that programming personnel with unrestricted access is an unwarranted risk--especially for systems programmers (as opposed to applications programmers). The Navy should provide additional measures to monitor, restrict, or reschedule programmers' access times in the computer room.

We have reexamined our working papers and the Instructions in question at the Norfolk Naval Shipyard. The Instruction 5530.1A authorizes access for all CODE 113 (programmers) with no distinction between application and systems programmers. We have not reviewed the current Instruction 5530.1B or the NAVSEA correspondence referred to above to determine if this situation has been remedied. Even so, we believe that unlimited access to the computer room by systems programmers constitutes an unacceptable risk.

Finding, page 11, para. 5

"Computer operators at Charleston, Norfolk, and NARDAC have access to systems documentation. Sound ADP control requires that system documentation be secured, and that computer operators not be allowed unsupervised access to the documentation. Knowledge gained by computer operators from system documentation coupled with their technical knowledge of computer operations increases the risk of their making unauthorized changes to programs and data files."

"Written procedures specifying the controls necessary over system documentation do not exist at Charleston and Norfolk. Further, at Charleston we were informed that computer operators can easily gain access to areas where system documentation is kept. At Norfolk, we noted that computer operators are authorized unsupervised access to the combination safe where system documentation is stored. Furthermore, senior operators are provided with a key to the programmers' offices which also have elements of the system documentation."

"At NARDAC, we visited the programmers' work area after normal work hours and found the doors to the work area open. After entering, we observed system documentation on desk tops and noticed that there were no lockable file cabinets for storing documentation. As a result, the system documentation is readily accessible to computer operators on the evening and night shifts."

Comment: Concur that computer operators have access to Systems documentation. User and operations documentation must be readily available for use during normal shift hours. Frequent and convenient access to the documentation is required in the normal course of operating the systems. However, the documentation should be secured at the close of business each day to preclude unauthorized use by personnel working during off duty hours. Procedures for securing documentation will be implemented as soon as locking containers can be procured.

Do not concur that computer operators have unsupervised access to systems documentation at the Norfolk or Charleston Naval Shipyards.

At the Norfolk Naval Shipyard, system documentation is retained in computer specialists offices which are locked when no one is in the work area. Back-up documentation is stored in the safe. Computer operators have only supervised access to the safe and to the computer specialists offices. These procedures are documented in Norfolk Naval Shipyard DPO Instruction 5330.1B.

At Charleston, unsupervised access to system documentation is restricted to employees who are responsible for the documentation. System documentation is maintained in the offices of analysts and programmers which are locked during non-work hours. In the one branch that is not located in a lockable area, since it contains the fire exit passageway, documentation is kept locked in cabinets. Computer operators do not have unsupervised access to system documentation.

GAO COMMENT

At both the Norfolk and Charleston Naval Shipyards, the senior computer operators have a key to the areas where documentation is located. At the Charleston Shipyard, as many as ten keys have been issued which would provide access to the computer area, one of which is located on the computer console available to anyone. Controlling the number of keys and knowing who has them does not in any way control how or when the keys are used. As stated previously, we did not have available for review the current DPO Instruction 5330.1B at the Norfolk Shipyard but the instruction in force at the time of our onsite visit (DPO Instruction 5530.1A enclosure 3) authorized GS-7 computer operators and above access (with no restrictions noted) to the data bank safe.

Finding, page 12, para. 5, 6, 7

"Access to the tape library is not adequately restricted at the three computer centers. Access restrictions are important to protect the files from unauthorized use, manipulation, or destruction."

"At NARDAC, the tape library door remains open, even during the evening and night shifts when a tape librarian is not on duty. The tape library actually serves as a passageway between the computer room and output room, and therefore others besides the tape librarian often enter the tape library. In addition, a computer listing identifying the tapes in the library remains on a desk in open view, even during hours when the librarian is not present."

"The Norfolk and Charleston computer centers do not employ librarians. Instead, computer operators retrieve the computer tapes needed for processing. Furthermore, no log is kept to control the removal and return of tapes and their libraries remain unlocked during computer operations."

Comment: Concur in principle. The NARDAC tape library at the Crystal Mall facility is located between the computer room and the production control desk. Production control (input/output control) personnel share tape librarian duties during regular work hours as required in their position descriptions. After regular working hours, operations and programming personnel occasionally are required to pull their own tapes since the tape librarian is only on duty during the prime shift. It is not possible to anticipate all tape requirements in advance of a production run or test session because of unexpected read/write errors encountered during processing.

The Crystal Mall facility is scheduled to move to the consolidated site during the first or second quarters of calendar 81. Tape librarian services will be provided at the new site.

For the Norfolk and Charleston Naval Shipyards, NAVSEA does not concur that access to the tape library is not adequately restricted.

At Norfolk, the tape library room adjoins the computer room and is subject to the same limited access as the computer room.

At Charleston, unsupervised access to the tape library is restricted to computer operators and supervisors. Tapes and disks are filed in a room connected to the computer room and this room is subject to the same limited access as the computer room. Back-ups are kept in fireproof safes in a locked room. The presence of two to four operators on each shift is considered an adequate deterrent to malfeasance by a computer operator. The cost of staffing the tape library three shifts a day, seven days a week, is considered prohibitive.

GAO COMMENT

The purpose of restricted access to the tape library is to prevent unauthorized use, manipulation, or destruction of files. The risks associated with unlimited, unsupervised access increases proportionately with the familiarity the person(s) has (have) with the system. The machine operator instruction books (e.g., run books) provide them with a high degree of familiarity with not only the applications for which they are responsible but also other operator applications. The problems noted in the previous section regarding access to documentation coupled with unlimited tape library access constitutes a potentially serious breach of internal control.

Thus, the situation at both the Norfolk and Charleston shipyards constitutes a potentially serious breach of internal control and may be even more serious at Charleston where several keys which provide access to the computer area are available to programming personnel.

Recommendation #5

Direct all installations to assign an ADP security officer, implement a security training program, and restrict access to computer equipment, computer tapes, and system documentation.

Comment: Concur with intent of Recommendation. A DON ADP Security Program was established on 2 April 1979 by issuance of OPNAV Instruction 5239.1. The Instruction addresses the requirement for an ADP Security officer and provides guidance concerning access to computer facilities. ADP Security training is currently provided by DODCI. OPNAV Instruction 5239.1 has been implemented at all levels of command.

NAVSEAINST 5510.13 designates SEA 994 as the NAVSEA ADP Security Officer and directs that each of the NAVSEA shore activities appoint an ADP Security Officer. Each of the NAVSEA shore activities has appointed an ADP Security Officer. This Instruction and NAVMATINST 5510.17 and OPNAVINST 5239.1 require restricted access to computer equipment, computer tapes and system documentation. The need for training is recognized. Due to the limited DOD training capacity, funds have been budgeted by NAVSEA for assistance from outside organizations. As stated previously, NAVSEA considers that adequate restrictions exist on access to computer equipment, computer tapes, and system documentation at the Naval Shipyards in question.

GAO COMMENT

Our review indicates that the Navy has not effectively implemented corrective action. For example, NAVSEAINST 5510.13 "implemented" as of April 3, 1978, directed that each of the NAVSEA shore activities appoint an ADP security officer. Other related instructions OPNAVINST 5510.131, NAVMATINST 5510.17, and SECNAVINST 5211.5A had been in effect for almost a year. Yet, as of June 1979, the Norfolk Shipyard had not appointed a fulltime ADP security officer even though an ADP security team of the NAVSEA Inspector General had informed them of this deficiency in June 1978.

Security inspections conducted by the NAVSEA Inspector General during calendar years 1978 and 1979 indicated that several other NAVSEA shore activities had not complied with the aforementioned "implemented" instructions.

Our review also disclosed that OPNAVINST 5239.1, dated April 2, 1979, was issued as a stopgap measure and was to be superseded by NAVDACINST 5510.1 (draft), dated September 26, 1979. This had not been accomplished as of October 1980. Our review of OPNAVINST 5239.1 disclosed that it is basically a compendium of DOD instructions of 1972-1973 versions with 1978 updates and a 1977 National Bureau of Standards interim report on risk assessment. However we do not believe the Navy's ADP security program will be adequate until an instruction is issued.

5. Findings (relate to Recommendation #6), page 14, NAVSEA Contract/Procurement.

Comment: The amount of coverage given to the unauthorized procurement of office equipment is considered excessive and if not placed in proper perspective conveys the impression that major procurement actions are included in this description. The GAO report is also silent on the efforts of NAVSEA to deal with this problem. It should be noted that the 121 equipment items provided to the GAO are a part of the 10,000 item inventory of serialized office equipment.

GAO COMMENT

We believe the coverage is not excessive because circumvention of procurement procedures has been going on for several years. We revised the report to state that the majority of the office equipment was obtained by placing orders over the telephone without written justification. The potential exists for major procurement actions to be included. We revised the report to show the current situation at NAVSEA. Our information indicates that the 121 equipment items are not part of the 10,000 item inventory of serialized office equipment.

Finding, Page 14, Procurement.

Comment: The inclusion of NAVAIR and NAVELEX items in this discussion is not understood. The total cost of \$250,000, which includes the NAVAIR and NAVELEX items, is shown on page 15 as a total cost to NAVSEA only.

The GAO has not examined the underlying cause of the unauthorized procurement problem. The NAVSEA Office of Internal Review has recently completed a study of the unauthorized procurements and concludes among other things, that the excessive procurement lead times are a direct contributing factor. Additionally, the priority system which the GAO describes in this paragraph is not known to the NAVSEA Procurement Section.

GAO COMMENT

We initially wanted to show the extent of the procurement abuse but NAVSEA officials requested that we talk only in terms of NAVSEA. Therefore, we have deleted the NAVAIR and NAVELEX items. The total cost of \$250,000 has been revised to \$122,573 to reflect NAVSEA items only. We have added that the majority of the items were acquired by placing orders over the telephone without written justification. Also, we deleted the discussion on the priority system because a NAVSEA internal review official stated that their review of unauthorized equipment purchases or leases indicated that the average procurement lead times for procuring or leasing office equipment were from 150 to 170 days.

Finding, Page 16, Procurement

Comment: The reference to the \$9.7 million contracts should be rephrased to avoid the confusion that this is the cost of the equipment in question. During the DOD/GAO meeting, GAO agreed this paragraph was unclear and would review notes for possible rewording.

GAO COMMENT

The statement has been revised to read "The five contracts totaled \$9.7 million."

Finding, Page 16, Paragraph 2 - Reference to the item that equipment costs were sometimes charged to the Navy Industrial Fund.

Comment: The Navy Industrial Fund provides working capital for all Navy industrial activities not just naval shipyards. This parenthetical explanation of the Navy Industrial Fund appears to infer that naval shipyards were the field activities purchasing equipment for Headquarters so that procurement procedures could be circumvented. The definition of the Navy, not naval, Industrial Fund should be changed to read "(a revolving fund established by the Congress to provide working capital for naval industrial activities)".

GAO COMMENT

The statement has been revised to read, "a revolving fund... for naval industrial activities."

Finding, Page 18 - Conclusion by GAO that insufficient review of the activities of contracting offices and project managers has resulted in the unauthorized procurements.

Comment: This conclusion, which results in Recommendation #6, page 32, reveals a misunderstanding of the manner in which the unauthorized purchases took place.

GAO COMMENT

The conclusion has been revised to include NAVSEA's comment that the unauthorized commitments resulted from excessive procurement lead time for obtaining office equipment. However the potential still exists for fraudulent activities because the majority of these equipment items were ordered by telephone without written justification or authority.

Recommendation #6

Require an independent review of proposed procurements by someone other than the contracting officers and project managers to preclude unauthorized purchases and purchases not within the scope of Navy contracts.

Comment: Do not concur. This recommendation is based on a misunderstanding of the manner in which the unauthorized purchases took place. The inference is that the contracting officers and project managers are placing funding documents for the specific equipment with contractors or field activities and that an additional check will eliminate the problem. This is inaccurate and results in a recommendation that will not provide a solution. During the DOD/GAO meeting, discussion of Recommendation #6 and related findings indicated that a differently worded recommendation might be more helpful in resolving any problem. A better recommendation, it was discussed, might be to emphasize the need to expedite the system for procurement of office equipment.

GAO COMMENT

The recommendation has been reworded to take into account the need for expediting the process for procurement of office equipment. We are also recommending that NAVSEA (1) perform internal reviews of contract overhead charges to ensure that only authorized items are charged, (2) review the contract and funding documents used in acquiring the office equipment to ensure that other charges are proper and are accounted for and (3) provide specific detailed guidance on the use of funding documentation.

6. Findings (Recommendation #7)

Finding, Page 36 - "Failure to maintain a signature file for persons authorized to approve purchase orders and invoices for payment at NRFC and verify approving signatures against this file before making payments."

Comment: The Comptroller of the Navy does not require that this activity maintain a signature file of persons authorized to approve purchase orders and invoices for payment. NRFC maintains that the designation and maintenance of a signature file of persons authorized to execute a contract/purchase order or to certify an invoice is the responsibility of the procuring or certifying activity.

GAO COMMENT

We found that NRFC pays invoices, accompanied by a purchase order, based upon the invoice being certified that goods or services have been received. NRFC does not check the signatures on these documents for authenticity. We believe that, if signature authority is limited to several officials within each organization the NRFC supports, the persons paying the invoices would become familiar with the authorized signatures. Because NRFC does not check signatures, there is no guarantee that payments are supported by purchase orders and invoices that are approved by authorizing persons.

Finding, Page 38

"Cash Receipts. Failure to develop and implement procedures to insure that checks are properly received, controlled, and accounted for (i.e., checks in a log and reconciling it against deposits)."

Comments: All checks and pertinent documentation received by this command are forwarded to the Disbursing Officer. A record of receipt is made (receipt number, check number, payee, payer, bank ID No. and amount) and a copy of the record plus any documentation that may have been received with checks are forwarded to the NRFC action Department. The action Department sends Fiscal Control proper collection documents within 24 hours of receipt. These documents are matched with checks. An adding machine tape is made of the collection vouchers and checks. The tapes are compared by overall totals and the deposit ticket is typed. Deposit ticket numbers and date of deposit are listed on the record of receipt (log). Deposit tickets and checks are given to another clerk to mail. This clerk verifies the checks to tape before mailing. The vouchers are processed through the Financial Processing System for reporting to the applicable accounting activity.

GAO COMMENT

We have added the word "mailroom" to the statement. The point we are making is that there were no procedures within NRFC's mailroom to assure receipts are properly received and logged in before sending them to the fiscal department. The person in the mailroom should record each receipt in a log and transmit the log and the receipts to the fiscal department where all receipts should be accounted for. Checks (especially returned checks payable to vendors) could easily be misplaced or taken for personal gain.

GAO Recommendation #7 (Page 32)

See that NRFC improves its review of payment request and automated system edits by thoroughly examining documentation supporting expenditures before it makes payments and ensuring that the more sophisticated computer system being designed (see page 18) contains an adequate number of invoice elements which must match to preclude duplicate payments.

Comments: Concur. The present manual audits have produced duplicate payments. However, the Automated Public Voucher and IDA systems were designed to preclude duplicate payments by validating the following data elements against a prior payment file: PIIN and invoice number, invoice date and gross amount. As a regular step in the audit procedures, invoices against contracts/orders on which folders are maintained are checked against the item controls to determine if previously paid. In addition, NRFC receives numerous old invoices and duplicate invoices on which no contract folders are maintained. These are manually reviewed from a computer printout which stores a year's records and microfiche records that contain information back to 1977. In addition, NRFC retains approximately two years payment listings for research purposes. If no record of payment is located, the invoice is stamped "No Record of Prev. Pymt", initialed by the researcher and processed for payment. In addition, the Examination Department has the option of questioning any invoices in this area that are not stamped. NRFC pays approximately 180,000 invoices per year and of this amount approximately 100 are found to be duplicate payments. The duplicate payments in most cases, were caused by human error when manual audits of invoices were required.

The new more sophisticated payment certification system, being designed for implementation in 1981, will provide a more effective automated review of invoices and will eliminate many of the manual audits now required. The new payment certification system will replace the current Automated Public Voucher and interim IDA systems. The system will integrate the contract files with the accounting record and provide total control over potential duplicate payments. In addition to previously identified duplicate payment data element validations, the obligation record and contract line item will be used to provide a complete analysis of all payments being processed. GAO participated in the functional design of the IDA payment certification system and informally approved the method of detecting duplicate payments.

GAO COMMENT

Our information indicates that the IDA system will be implemented in 1981. Duplicate payments should be reduced when IDA is fully operational. Because the agency concurs with our recommendation, we made no change.

7. Findings (Recommendation #8)

Finding, Page 18, Paragraph 5 - Failure to have adequate written policies and procedures within accounts payable unit at Norfolk.

Comment: General policies and procedures are covered by the Navy Industrial Fund Handbook, NAVSO P-1242, the Navy Comptroller Manuals and the Navy Supply Manual. Detailed policies and procedures are covered in the Management Information Systems manuals and the individual position descriptions. Norfolk Naval Shipyard's accounts payable unit has established a list of personnel authorized to sign for the receipt of goods and services.

GAO COMMENT

We revised our statement to read, "Norfolk's accounts payable unit did not have current ..." We found that voucher certifiers did not have a list of people and/or signatures of people authorized to sign for receipt of goods and services. As a result of our review, the accounts payable unit established a list of personnel authorized to sign for the receipt of goods and services.

Finding, Page 19 - Failure to assure proper documentation is obtained for the receipt of material.

Comment: While it is true that the accounts payable unit occasionally confirms receipt of material by telephone, a certification is then obtained to affirm the telephone confirmation. Vouchers are submitted to the Fleet Accounting and Disbursing Center, Atlantic (FAADCLANT), for payment which verifies that all proper documentation is enclosed prior to paying the vendor's bills. The voucher will not be accepted by FAADCLANT for payment without a copy of the purchase order/contract and a certified copy of the vendor's invoice. Receiving and inspection documents are reviewed and maintained by the accounts payable unit, except for unusual circumstances such as parcel post receipts which are delivered directly to the ordering agent. During the DOD/GAO meeting, GAO indicated they would look at this finding again since the explanation of telephone follow-up was brought out.

GAO COMMENT

As stated above, the accounts payable unit occasionally confirms receipt of material by telephone and a certification is then obtained to affirm the telephone confirmation. However, the statement that the voucher will not be accepted by the Fleet Accounting and Disbursing Office is not correct. Our review showed that this situation can and did happen.

Finding, Page 19 - Failure to have a claims register for management and monitoring of credit memos and checks due from suppliers (Norfolk).

Comment: A formal claims register has been in use since November 1979. The second sentence of this paragraph appears to be misplaced. If intent is to show that a check is needed because only one person is responsible, it should be so stated.

GAO COMMENT

The claims register was implemented in November 1979, as a result of our review. The sentence referred to indicates that only one person is responsible for (1) processing and certifying invoices for payment, (2) monitoring the receipt of credit memos and checks, and (3) making adjustments to the financial records. However, we did revise the next sentence to read "Without better mechanisms for accountability and separation of duties, the shipyard does not have adequate control over checks and credit memos due from suppliers."

Finding, Pages 20 - Failure to adequately review and match payment documents and receiving/inspection reports before payment.

Comment: The accounts payable internal control procedure is based on manual matching of the invoice to the procurement document and signed receipt document. The total \$273,000 referred to did not represent erroneous payments by the FAADC for the shipyard. The majority of items were properly chargeable to the shipyard. One item for \$145,200 included in the \$273,000 total represented payment by FAADC against a document issued by the shipyard that had been certified for payment by the Navy Plant Representative at the contractor's plant vice the shipyard. During the DOD/GAO meeting, it was pointed out that out of the \$273,000 referred to in the finding, only \$38,414 was attributable to erroneous payments. GAO agreed to review their notes on the findings.

All aspects of the paying unit are matched by Accounts Payable Unit prior to sending the documents for payment. FAADCLANT again audits the paying unit prior to issuing a check. The Accounts Payable Unit retains a signature file of those employees authorized to sign receipt documents. Frequent changes in assignment of duties in Accounts Payable also reduces the possibility of establishing a conflict of interest.

Original comments made by GAO in Charleston indicated that they had sampled 50 aged commercial MIT items valued at \$59,000 which included 9 overpayments valued at about \$2,000 and 8 duplicate payments valued at \$4,100. The current GAO draft implies that of \$273,000, all are erroneous payments. GAO's sample did not find that.

GAO COMMENT

We revised the statement to read "As of September 30, 1979, the matching process had identified transactions where credit totaling \$273,000 was determined to be due the shipyard. Our analysis of 50 of these transactions, with credit of over \$59,000 pending, showed that 9 of the 50 (18 percent) were overpayments valued at \$2,000 and 8 of the 50 (16 percent) were duplicate payments valued at \$4,000. After our review, Navy officials stated they found that \$38,414 of the \$273,000 (14 percent) were erroneous payments and the rest were valid payments.

Finding, Page 20, Paragraph 3 - Failure to reconcile accounts payable documentation.

Comment: The review of supporting payment documentation as addressed in this paragraph is not a reconciliation process but rather a matching to liquidate the established accounts payable. Prior to forwarding a bill for payment to the FAADC, the Charleston Naval Shipyard reconciles the bill with the procurement document, and with the receipt document. The \$8 million reconciliation backlog addressed deals with the matching of the commercial billing card (indicating FAADC payment) to the shipyard's financial record cards for liquidation. One of the many benefits to be derived from the implementation of the Integrated Disbursing and Accounting Program will be the elimination of erroneous and duplicate payments. However, this benefit is not the primary reason for implementing IDA.

GAO COMMENT

We revised this statement to read "At the time of our review, payments exceeding \$8 million at Charleston had not been matched with supporting documentation."

Finding, Page 21, Paragraph 1 - Failure to determine adequate justification for accounts receivable write-offs.

Comment: The finding as written does not accurately portray the situation -- The \$5.8M is the total financial adjustments in these two fiscal years resulting from the difference between value of material returned to the system for credit and the amount of credit received. The shipyard accepts the supply system's determination of credit or no credit. A local review was conducted in December 1979 of turn-ins for a six month period. The reason the credit was not given varied from excess stockage position in the Supply Center to lack of system needs. The Shipyard Comptroller performs a comprehensive review for all accounts receivables write-offs. However, in the case of the \$5.8 million write-off, it represents material returned to the supply system for which credit was not given. There is no subsequent review required for material returned for which credit is not processed by the supply system. During the DOD/GAO meeting, GAO agreed to review their work papers on this finding.

GAO COMMENT

The statement has not been changed because, at the time of our review, shipyard officials were unable to explain why these receivables were written off. However, we did include Navy's subsequent explanation that the \$5.8 million was for material returned to the supply system for which the shipyard did not receive credit.

Finding, Page 21, Paragraph 2 - Failure to record accounts receivable from other sources properly.

Comment: The detail financial records at naval shipyards properly classify account receivables between system, commercial and other. However, the individual account balances were added together for presentation in the Financial Operating statements. This combining of account totals in no way provides for misstatement of asset value and are a minor category at naval shipyards.

GAO COMMENT

The GAO Policy and Procedures Manual (2 GAO 12.4(3)) requires that separate accounts for major categories of receivables be maintained to facilitate clear and full disclosure of an agency's resources in its financial reports.

Recommendation #8

Require the Charleston shipyard to reconcile accounts payable to supporting documentation and to properly classify accounts receivable so that they are collected promptly.

Comment: Do not concur. Charleston Naval Shipyard reconciles accounts payable to supporting documentation (vendor's bill, procurement document and proof of receipt) prior to forwarding the bill for payment. The process addressed by the auditors deals with liquidation of the accounts payable by matching to the billing card vice a reconciliation process, and the recommendation should be reworded to that effect.

The accounts receivable are properly classified on the shipyard's detail financial records as system, commercial and other. However, the individual account balances were added together for presentation in the Financial Operating Statements.

GAO COMMENT

We have revised the first part of the recommendation to read "Require the Charleston shipyard to match payments to supporting documentation and to ..." The individual account balances should be shown separately on the Financial Operating Statements.

8. Findings (Recommendations #9 and #10)Finding, Page 21 - Travel

Comment: An additional paragraph should be added to show the extent of travel both in NAVSEA Headquarters and at the naval shipyards. The examination of 47 travel transactions out of 25,000 at NAVSEAHqs should be placed in perspective.

The GAO should state whether this was a statistical sample or a judgment sample. If this was a probability sample, then the statistical parameters should be stated. Additionally, the information on the 80 trip cancellations should be expanded. Trip cancellations are normally batch processed by the administrative personnel which may account for the large number of trips in a short time frame. For comparison, in the Fourth Quarter FY 80, 261 trips were cancelled out of 4,500 trips processed.

Additionally, the comments regarding NAVSEA Headquarters and the shipyard travel should be separated for clarity.

NAVSEA has begun the development of a travel management system which is expected to become operational about March of 1981. Among many expected outputs of this system is the ability to monitor the liquidation of travel advances and the ability to provide officials charged with travel management responsibility information necessary for controlling, planning, and making decisions regarding travel requirements and expenditures.

NAVSEA does not concur with the section of the recommendation regarding travel claims. NAVSEA has no plans to review travel claims. Assuming that a traveler will be reimbursed only for those things reviewed and approved in the travel order, the necessity of duplicating the review of claims performed by the Personnel Support Detachment prior to payment is questioned. NAVSEA is not staffed for this function and performing it would lengthen the already unacceptable period of time it takes for a traveler to be paid for a travel claim.

GAO COMMENT

The approach used in conducting this vulnerability assessment required a broad examination of an agency's operations using an internal control checklist and the testing of a limited number of transactions as discussed in detail in chapter 1. The 47 travel transactions were sampled on a judgmental basis.

We revised the statement to read that Navy officials explained that trip cancellations are normally batch processed by the administrative personnel which may account for the large number of trips in a short time. For comparison, they stated that in the fourth quarter of fiscal 1980, 261 trips were canceled out of 4,500 trips processed.

According to GAO's interpretation of the Federal Travel Regulations, GAO Order 0300.1, chapter 6, part 2, after the traveler certifies and dates the voucher, the supervisor or other responsible official who knows the purpose of the travel shall sign the voucher before submitting it for payment.

Finding, Page 22 - Shipyard procedures should require the traveler's immediate supervisor or others with knowledge of the trip to certify that the claim agrees with the actual trip and work schedule.

Comment: Review and approval of travel claims by supervisors would not be productive. The supervisor is in no position to verify actual time on the job and must rely on time sheets kept at the TAD site. The supervisor is in a poorer position to validate charges on a claim than administrative personnel already charged to review and adjudicate claims. The supervisors review would only be an administrative burden and would not serve any useful purpose.

GAO COMMENT

According to GAO's interpretation of the Federal Travel Regulations, GAO Order 0300.1, chapter 6, part 2, after the traveler certifies and dates the voucher, the supervisor or other responsible official who knows the purpose of the travel shall sign the voucher before submitting it for payment.

Finding. Shipyard procedures should require the travel section to determine that claims are explained by statements in the voucher.

Comment: Travelers are presently required to explain on the travel voucher areas such as layovers, delays in route, or other questionable items.

GAO COMMENT

Our review of 25 travel orders at Charleston shipyard showed instances in which the traveler's claims did not match the actual trip and work schedules and claims were not justified for meals obtained after the traveler's return to Charleston--especially when vouchers indicate there was little time for such a meal before arriving home.

Finding. Shipyard procedures should require the Charleston travel section to notify the payroll section when travelers have used annual or sick leave or should have done so because of circumstances of the trip.

Comment. Use of annual or sick leave is noted and proper documentation forwarded to the payroll section relative to constructive travel only. The Charleston Naval Shipyard has adequate timekeeping procedures (CHSYDINST p7410.1F) to assign each employee's supervisor the responsibility of accurately reporting the employees time while on TAD. Subsequent adjustments are processed to the Comptroller by the employees supervisor for any sick or annual leave used that was not previously reported.

GAO COMMENT

Our review of 25 travel orders at Charleston shipyard showed instances in which delays enroute and stopovers were not necessary and were for the convenience of the traveler.

Finding. Shipyard procedures should require that training be provided to supervisors and travelers on travel regulations and economical travel practices.

Comment: Changes to existing travel regulations occur daily by messages, memorandas, notices, or other published means. Pertinent areas of concern to the individual traveler are issued in a shipyard travel bulletin on a quarterly basis or sooner if deemed appropriate. The bulletin is issued to all shipyard personnel. In addition, all personnel are advised to contact the travel section on any questionable travel issue so that latest information may be given on any matter. This method of transmitting travel information and regulations is considered to be appropriate to the situation.

GAO COMMENT

We believe more emphasis should be placed on training of supervisors and travelers to cover travel regulations and economical travel practices.

Finding, Page 24 - Shipyard procedures should require personnel support command personnel to return questionable vouchers to the travel section for clarification.

Comment: The Personnel Support Activity Detachment is a separate naval activity. Neither NAVSEA nor NAVSHIPYD have the authority to direct their action.

GAO COMMENT

We have revised this statement to read "Also, we believe these conditions existed because Personnel Support Activity procedures did not emphasize..."

Recommendation #9 - Improve controls over travel at NAVSEA Headquarters by requiring appropriate officials to approve travel, seeing that travel advances are liquidated promptly and that claims are properly reviewed; and assuring managers receive reports containing information for controlling, planning, and making decisions about travel expenditures.

Comment: Concur in part. NAVSEAINST 4650.1A, currently being updated, will specify who may approve travel orders. It provides that travel plans must be approved by an officer of flag rank and that signature authority may be delegated to no lower than Division Directors for individual trips that are consistent with the previously approved plan. NAVSEA believes that this policy will provide adequate controls while providing a realistic means of accommodating the volume of travel orders.

GAO COMMENT

We believe these procedures, if implemented, will improve the control of travel funds.

Recommendation #10 - Require the Charleston Shipyard to improve its control over travel by addressing the weaknesses identified in this report.

Comment: Concur for the majority of the procedures noted in the report. Procedures have been initiated or are in place for the items noted with the exception of the suggestion to require the traveler's immediate supervisor to certify that travel claims agree with the actual trip and work schedule. The review and approval of travel claims by supervisors would not be productive. The supervisor is in no position to verify actual time on the job and must rely on time sheets kept at the TAD site. Administrative personnel, already charged to review and adjudicate claims, are in a better position than the supervisor to validate charges on a claim.

GAO COMMENT

As stated before, we believe after the traveler certifies and dates the voucher, the supervisor or other responsible official who knows the purpose of the travel should sign the voucher before submitting it for payment.

9. Finding (relates to Recommendation #11)

Comment: The Naval Audit Service takes exception to wording on page 29 which discusses "Prior Report and Action Taken." As worded, we do not know whether GAO's comments are meant to condemn us or to praise us. We interpret the paragraph to mean that deficiencies identified in a prior GAO report (Report No. FGMSD-78-5) have not been corrected. It is the position of the Naval Audit Service, and verbally agreed to by GAO during Audit FGMSD-78-5, that the matter of military within the organization is resolved. Military have been removed from positions of making policy for the Naval Audit Service, and no need exists in this instant report for GAO to raise the issue unless specific recommendations are being made. Regarding the comment about non-appropriated fund audits, GAO also advised in the cited audit that less effort be devoted to that area. As a result, the House Appropriations Committee reduced Naval Audit Service funds for FY 1978 by \$1 million and we incurred a loss of associated manpower. Here again, any comment by GAO regarding this issue needs to be deleted from this report. In a similar manner, GAO's comments on followup procedures are also open to interpretation and too need to be deleted from the draft report. As an alternative, if the GAO wishes in this report to point out that the intent of Audit FGMSD-78-5 was not to criticize the effort devoted to audit of non-appropriated funds, but merely to point out that by reducing the effort more time could be devoted to other types of audit, and the Congressional action was inappropriate and should be reversed, we would not object.

GAO COMMENT

We have deleted the report's section which referred to "prior Reports and Actions Taken". We cannot comment on the congressional action taken because we are not cognizant of all factors involved in the decision to reduce Naval Audit Service funds for FY 1978. However, our intent in GAO report FGMSD-78-5 was to have the Naval Audit Service devote more effort to other types of audits.

Recommendation #11(a) - Make internal audits more effective by re-assessing staffing priorities to adequately emphasize internal auditing in light of decreasing size and other factors which make Navy activities more vulnerable to fraud, waste, and abuse.

Comment: The Navy concurs with the recommendation as subsequently explained by GAO. That is, more personnel are needed to effectively perform the audit mission. Accordingly, we believe that GAO needs to revise the recommendation wording to preclude any misinterpretation. Throughout the Navy, staffing shortages exist and continued reductions directed by Congress and OMB prevent readily apparent solutions. Increased staffing of the Naval Audit Service staff would permit a broader approach toward the audit of internal controls and increase the visible deterrent for prevention of fraud and waste. The Navy Department will consider the GAO recommendation in our continuing efforts to justify requirements for additional resources.

The Navy Department considers that the many positive actions taken in response to previous GAO recommendations have provided significant attention to making audits more effective. The most significant of these actions changed the reporting level of the Auditor General of the Navy from the ASTSECNAV FM to the Under Secretary of the Navy. This change alone has provided top level management attention to audit matters in our continuing efforts to combat waste and abuse.

GAO COMMENT

We have revised our report to include assessing staffing priorities at all levels and not just the Naval Audit Service. Since the Navy concurs with our recommendation no other changes were made.

Recommendation #11(b) - Make internal audits more effective by requiring internal audit participation in the design, development, and test phases of a new computer system to ensure that factors to enhance auditability, audit trails for security, and quality output are designed and developed into new systems.

Comment: Concur with the recommendation and NAVAUDSVC will continue to respond to Navy and Marine Corps requirements to review objectively the efforts of ADP design teams. Toward that objective, and prior to this draft report, standardized audit programs were developed for auditing computer systems, and steps were taken to identify all Navy and Marine Corps computer systems requiring audit. As of 30 September 1980 review had identified over 500 systems to be provided audit attention. The largest restraint in audit of this area is lack of personnel. About seven percent of our audit effort is directed toward auditing in the ADP environment, with primary emphasis on systems development audits. These audits are conducted to assess the reliability of the system and to ensure ADP systems contain adequate internal controls for prevention and detection of fraud, waste, and abuse.

GAO COMMENT

No change is necessary because the Navy concurs.

Recommendation #11(c) - Make internal audits more effective by requiring internal audits to identify underlying causes of problems uncovered so that action can be taken to prevent recurrence.

Comment: Concur with the recommendation. However, we do not believe the two FY 1977 audit reports cited by GAO are representative of all reports issued during FYs-1977 and 1978. The majority of audit reports do contain meaningful recommendations. Often, it is inappropriate for audit recommendations to be precise since there are several alternative courses of action that could alleviate or correct the problem, and it is a management prerogative to select the specific. Also, it should be understood that during oral discussions of audit findings, the underlying causes are covered and it is not deemed necessary to include lengthy discussions of this in the report when there is agreement between auditor and management - as to the nature of the corrective action to be taken. Nevertheless, we will continue to ensure audit reports identify the underlying causes of problems.

GAO COMMENT

We have revised the report to reflect that these two audit reports are not representative of all reports issued during that time frame. We also have included in the report the rationale for our belief that underlying causes should be included in the body of Naval Audit Service reports. Briefly, we believe that including the underlying causes in the report documents the fact that the cause was identified. In the event managers or auditors involved in the discussions are no longer available, the cause will have been noted for use by new managers or for followup audits. Another benefit is that other managers of similar organizations in the Navy would be able to determine if their organizations are affected by similar problems with the same underlying cause or causes. This does not prevent managers at different installations from taking different, equally effective corrective actions.

10. Conclusions, Page 30, Paragraph 5

Comment: The comment that all the weaknesses noted in the report are as a result of the lack of management emphasis appears to be a simplistic view of underlying causes. It infers that adequate internal control mechanisms in organization, procedures, and checks/balances are in place and satisfactory.

GAO COMMENT

We do not believe the statement is a simplistic view of underlying causes. If management does not take an active role in the implementation of internal controls and ensure that controls are in place and are working, management has not done its part in preventing fraud, waste, and abuse. Furthermore, if management does not take the initiative, the weaknesses noted in this report will probably occur elsewhere within the Navy.

11. Appendix I, Pages 34-42

Comments: Appendix I, which is a checklist of weak internal controls, is difficult to follow in relation to the basic report; particularly, as it relates to the findings and recommendations. In addition, in the area of travel, why has NRFC, Washington been included as having internal control weaknesses when it was widely promulgated that the travel functions were transferred to the Personnel Support Activity, Washington, D.C. on 1 October 1979. On-site auditing was not concluded until December 1979. Due to the confusing nature of the checklist as related to the findings and ultimate recommendations, it is recommended that Appendix I be removed from the final GAO report.

GAO COMMENT

We have changed the heading NRFC to PSA (Personnel Support Activity) for the weaknesses related to travel. The checklist represents all weaknesses found during our review. Some of the weaknesses appearing in the checklist do not appear in the report's body. Therefore, we think including appendix I will be useful to the reader to show the results of our review.

(911015)

AN EQUAL OPPORTUNITY EMPLOYER

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

**OFFICIAL BUSINESS
PENALTY FOR PRIVATE USE, \$300**

**POSTAGE AND FEES PAID
U. S. GENERAL ACCOUNTING OFFICE**



THIRD CLASS