



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

January 13, 2004

The Honorable Lane Evans  
Ranking Democratic Member  
Committee on Veterans Affairs  
House of Representatives

The Honorable Bob Filner  
Ranking Democratic Member  
Subcommittee on Coast Guard  
and Maritime Transportation  
Committee on Transportation and  
Infrastructure  
House of Representatives

The Honorable Corrine Brown  
House of Representatives

Subject: *U.S. Coast Guard National Pollution Funds Center:  
Improvements Are Needed in Internal Control Over Disbursements*

The Oil Spill Liability Trust Fund (Fund) is a \$1 billion fund that has two major components: the Emergency Fund and the Principal Fund. The Emergency Fund is used for paying for federal removal actions and the initiation of natural resource damage assessments by designated federal, state, or Indian tribe officials, resulting from oil spills or the substantial threat of oil spills to the waters or shorelines of the United States. The Principal Fund is used for paying certain claims for uncompensated removal costs and damages resulting from oil spills or the substantial threat of oil spills to the waters or shorelines of the United States. The Fund is administered by the National Pollution Funds Center (NPFC) of the U.S. Coast Guard (USCG).

In May 2002, at your request, we issued a legal opinion related to the uses and limitations of the Fund and concluded that the Fund is not available to pay employee salaries and other operating expenses.<sup>1</sup> The USCG reported that from fiscal years 1998 through 2002, \$32.8 million from the Fund was used to pay costs associated with processing claims, including salaries and other operating expenses. In April 2003, the USCG returned the \$32.8

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<sup>1</sup>These costs are to be paid out of an annual operating expense appropriation.

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million to the Fund. In light of our conclusion regarding the appropriate use of these funds, you asked that we review the control over disbursements from the Fund and assess the propriety of these disbursements.

On September 17, 2003, we briefed your offices on the results of our review of internal control over claim payments made from the Fund.<sup>2</sup> We provided a second briefing on December 3, 2003, related to our review of internal control over disbursements for operating expenses paid from the Principal Fund and removal costs paid from the Emergency Fund. This report summarizes the information provided during that second briefing. The enclosed briefing slides highlight the results of our work and the information provided.

We reviewed disbursements for operating expenses and removal costs to determine whether (1) the design of existing internal control provided reasonable assurance that improper payments would not occur or would be detected in the normal course of business, (2) they were made in accordance with established USCG and NPFC policies and procedures, and (3) they were made in accordance with the uses specified in the Oil Pollution Act of 1990 (OPA) and other federal laws and regulations, and represented a proper use of government funds. Also at your request, we are providing information about NPFC's payroll expenses and claim activity fluctuations for fiscal years 1998 through 2003. This information is included in appendix I of the attached slides.

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## Results in Brief

The USCG and NPFC have established a system of internal control over operating expenses and Emergency Fund disbursement processes. However, we found some weaknesses in the design and operation of internal control over operating expenses and disbursements from the Fund that increase the risk of improper payments. Weaknesses in the design of control included a lack of documented reconciliations of the amounts included in removal cost reports with those recorded in USCG's accounting system. We found additional internal control weaknesses in that

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<sup>2</sup>U.S. General Accounting Office, *U.S. Coast Guard National Pollution Funds Center: Claims Payment Process Was Functioning Effectively, but Additional Controls Are Needed to Reduce the Risk of Improper Payments*, GAO-04-114R (Washington, D.C.: Oct. 3, 2003).

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USCG/NPFC did not always follow established policies and procedures that are intended to help ensure the validity of disbursements.

Of the nonstatistical selection of 467 disbursements obtained through data mining<sup>3</sup> for fiscal years 1998 through 2002, we found that 33, or 7 percent of these disbursements, totaling \$43,425, lacked adequate supporting documentation. Of the 33 disbursements, 9 transactions lacked purchase receipts such as invoices, 10 additional transactions lacked purchase request forms, and 14 lacked both purchase receipts and purchase request forms. We also found that 25, or 5 percent of the 467 disbursements, totaling \$26,182, lacked proper approvals. Specifically, 3 transactions lacked proof of approval from supervisors, 18 additional transactions lacked proof of approval from fund certifying officers before purchases were made, and 4 lacked proof of approval from supervisors and fund certifying officers. Another 39 transactions totaling \$155,994 for payments to contractors and other government agencies, and reimbursements to employees and others lacked documentation of supervisory review and approval before payments were made. In addition, equipment purchases totaling \$62,700 were not recorded in the property tracking system.

We also used the nonstatistical selection of disbursements obtained through data mining to determine whether these disbursements complied with certain federal laws and regulations and represented a proper use of government funds. We found that (1) NPFC did not properly document their justification for using federal funds to reimburse \$14,481 in travel expenses for 11 nonfederal potential claimants to attend natural resource damage (NRD) seminars, (2) the USCG Finance Center (FINCEN) incurred a total \$24,546<sup>4</sup> in late payment fees and lost discounts, and (3) the validity of 17<sup>5</sup> disbursements tested totaling \$6,589 was questionable because adequate supporting documentation was missing. The weaknesses we

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<sup>3</sup>Data mining applies a search process to a dataset, analyzing for trends, relationships, and interesting associations. For instance, it can be used to efficiently query transaction data for characteristics that may indicate potentially improper activity.

<sup>4</sup>Of the 467 disbursement transactions, the USCG FINCEN incurred a total of \$8,868 in late payment fees and lost discounts. We extended our test beyond the 467 disbursements to include all late payment fees and lost discounts incurred during fiscal years 1998 through 2002. As a result, we found that NPFC incurred an additional \$15,678 for a total of \$24,546.

<sup>5</sup>As discussed earlier, 23 disbursements lacked adequate supporting documentation. Of the 23 disbursements, 17 were missing purchase receipts or invoices and were therefore questionable. Another 6 had partial supporting documentation and were not considered questionable.

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identified in the design and operation of internal control over the disbursement processes, if left uncorrected, increase the Fund's vulnerability to future improper payments.

In addition, during fiscal year 2003, NPFC continued to improperly use the Fund to pay about \$645,000 in operating expenses and obligated another \$151,000 against the Fund. NPFC officials told us that they are in the process of transferring these transactions from the Fund into a newly established account created for recording NPFC operating expenses. As with the \$32.8 million previously returned, this transfer will not compensate the Fund for lost interest. NPFC's continued improper use of the Fund to pay for operating expenses is a violation of federal law. Not only does this practice expose the Fund to misuse, but we estimate that the Fund may have lost as much as \$1.6 million in interest<sup>6</sup> as a result.

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## Recommendations for Executive Action

To improve the design of internal control over disbursements from the Fund, we recommend that the Commandant of the U.S. Coast Guard direct the Director of the National Pollution Funds Center to establish policies and procedures to require that

- case officers document the reconciliation of removal costs reports to amounts paid in the accounting system, and
- case officers' supervisors document their review of these reconciliations.

To establish better compliance with U.S. Coast Guard/National Pollution Funds Center policies and procedures, we recommend that the Commandant of the U.S. Coast Guard direct the Director of the National Pollution Funds Center to

- reinforce documentation and approval requirements by instituting training for all relevant employees,
- institute monitoring techniques such as periodic spot checks to help ensure that such requirements are consistently followed, and

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<sup>6</sup>To calculate interest, we multiplied the average 6-month rate for U.S. Treasury bills (the rate at which the Fund earns interest) times the average operating expense balance for each fiscal year.

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- establish a mechanism to ensure that accountable assets are properly recorded in USCG's fixed assets system.

To enforce compliance with the Oil Pollution Act of 1990 and other federal laws and regulations and reduce the risk of improper payments, we recommend that the Commandant of the U.S. Coast Guard direct the Director of the National Pollution Funds Center to

- expedite actions needed to cease using the Fund to pay operating expenses as advised in our May 2002 legal opinion,
- record obligations against USCG's annual operating expense appropriation in order to ensure that adequate funds are available to reimburse the Fund for any unreimbursed or future use of the Fund to pay operating expenses,
- complete the transfer of all operating expenses that were improperly paid from the Fund in fiscal year 2003 to the new operating expense account,
- ensure proper justification exists for nonfederal travelers to be reimbursed to attend NRD seminars in advance of any such travel, and
- follow up on transactions that were missing purchase invoices to determine what was purchased and whether the items were for legitimate government needs.

We also recommend that the Commandant of the U.S. Coast Guard direct the Chief Financial Officer of the U.S. Coast Guard to

- reinforce documentation and approval requirements for disbursements from the Fund by instituting training for all relevant employees, and
- institute a monitoring system such as periodic spot checks to help ensure that such requirements are consistently followed.

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## Agency Comments

We obtained oral comments on a draft of our briefing slides from the Director of the U.S. Coast Guard National Pollution Funds Center and other officials. They agreed with our recommendations. The officials emphasized that at the time they initially began using the Fund to pay operating expenses, they had an opinion from the USCG Chief Counsel that

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this was a proper use of the Fund. As noted earlier, we concluded in May 2002 that the Fund is not available to pay NPFC operating expenses. The officials also emphasized that they now have electronic approvals that they believe provide better supervisory review and oversight. They provided technical and clarifying comments, which we incorporated as appropriate.

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## Scope and Methodology

To determine whether the design of existing internal control over operating expenses and Emergency Fund removal costs disbursement processes provide reasonable assurance that improper payments will not occur or will be detected in the normal course of business, we (1) reviewed USCG/NPFC's policies and procedures related to operating expenses and Emergency Fund removal costs disbursements, (2) considered the Comptroller General's *Standards for Internal Control in the Federal Government*,<sup>7</sup> (3) interviewed staff and officials in the USCG and the NPFC offices, and (4) performed walkthroughs of the operating expenses and Emergency Fund removal costs disbursement processes, and compared the results to USCG/NPFC's policies and procedures and the *Standards for Internal Control in the Federal Government*.

To determine whether disbursements were made in accordance with USCG/NPFC's policies and procedures, we (1) performed data mining of operating expenses paid from the Fund during fiscal years 1998 and 2002 to identify unusual transactions and patterns including personal use items, Internet purchases, training and travel, equipment purchases, employee reimbursements, contract payments other than removal costs, and late payment fees, and (2) used a nonstatistical selection of 467 disbursements obtained through data mining and tested for adequate documentation, proper approvals, and adequate safeguarding of assets.

We also used the nonstatistical selection of disbursements obtained through data mining to determine whether these disbursements were made in accordance with OPA and other federal laws and regulations and represent a proper use of government funds. Specifically, we reviewed OPA and federal laws and regulations to obtain an understanding of allowed costs, and reviewed purchase receipts or invoices to ensure that purchases were made for official government use and were allowed costs.

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<sup>7</sup>U.S. General Accounting Office, *Standards for Internal Control in the Federal Government*, GAO/AIMD-00-21.3.1 (Washington, D.C.: November 1999).

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We did not project our test results to the universe of NPFC disbursements in fiscal years 1998 through 2002.

To determine the fluctuations in payroll expenses and claims activity, we obtained data from the USCG and NPFC and identified significant fluctuations in payroll and claims activity for fiscal years 1998 through 2002, and obtained USCG/NPFC's explanations for these fluctuations. We did not verify the accuracy of the amounts included in NPFC's payroll and claim systems.

We requested comments on a draft of the enclosed briefing slides from the Commandant of the U.S. Coast Guard or his designee and have included any comments as appropriate in the letter and enclosed slides. We conducted our work from November 2002 through November 2003, in accordance with generally accepted government auditing standards.

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This report is available at no charge on our home page at <http://www.gao.gov>. If you have any questions about this report, please contact me at (202) 512-9508 or Rosa R. Harris, Assistant Director, Financial Management and Assurance, at (202) 512-9492. You may also reach us by e-mail at [calboml@gao.gov](mailto:calboml@gao.gov) or [harrisrr@gao.gov](mailto:harrisrr@gao.gov). Additional contributors to this assignment were Lisa Crye, Anh Dang, Tyshawn Davis, Christine Fant, Ryan D. Holden, Gabriella Kusz, Robert Preshlock, and Sandra S. Silzer.



Linda M. Calbom  
Director, Financial Management and Assurance

Enclosure

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# Enclosure



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## **U.S. Coast Guard National Pollution Funds Center**

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### **Improvements Are Needed in Internal Control Over Disbursements**

Briefing to the Staff of the Committees on Veterans Affairs and  
Transportation and Infrastructure, House of Representatives

December 3, 2003





## Table of Contents

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- Introduction and Objectives
- Results in Brief
- Background
- Overview of Effective Internal Control
- Internal Control Design
- Compliance with Policies and Procedures
- Propriety of Disbursements
- Conclusions
- Recommendations
- Agency Comments
- Scope and Methodology
- Appendix I: Payroll Expense and Claim Activity Fluctuations



## Introduction and Objectives

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- The Oil Spill Liability Trust Fund (Fund) is a \$1 billion fund which has two major components: the Emergency Fund and the Principal Fund.
  - The Emergency Fund is used for paying for federal removal actions and the initiation of natural resource damage assessments (NRDA) by designated federal, state, or Indian tribe officials, resulting from oil spills or the substantial threat of oil spills to the waters or shorelines of the United States.
  - The Principal Fund is used for paying certain claims for uncompensated removal costs and damages resulting from oil spills or the substantial threat of oil spills to the waters or shorelines of the United States.



## Introduction and Objectives ( cont.)

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- In May 2002, at your request, GAO addressed legal issues related to the uses and limitations of the Fund. We concluded that the Fund is not available to pay employee salaries and other operating expenses.<sup>1</sup>
- The U.S. Coast Guard (USCG) reported that from fiscal years 1998 through 2002, \$32.8 million from the Fund was used to pay costs associated with processing claims, including salaries and other operating expenses. In April 2003, the USCG returned the \$32.8 million to the Fund.
- In light of our conclusion, you asked that we review the control over disbursements from the Fund and assess the propriety of these disbursements.

<sup>1</sup>These costs are to be paid out of an annual operating expense appropriation.



## Introduction and Objectives (cont.)

- Specifically, we reviewed disbursements for operating expenses paid from the Principal Fund as well as removal costs paid from the Emergency Fund to determine whether
  - the design of existing internal controls provides reasonable assurance that improper payments will not occur or will be detected in the normal course of business,
  - they were made in accordance with established USCG and National Pollution Funds Center (NPFC) policies and procedures, and
  - these disbursements were made in accordance with the uses specified in the Oil Pollution Act of 1990 (OPA)<sup>2</sup> and federal laws and regulations, and represent a proper use of government funds.
- Also at your request, we are providing information about NPFC's payroll expense and claim activity fluctuations for fiscal years 1998 through 2003. This information is included in appendix I.

<sup>2</sup>Pub. L. No. 101-380, 104 Stat. 484 (1990).



## Introduction and Objectives (cont.)

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- This is our second briefing on the Fund. The first briefing covered the results of our work related to the review of claim payments made from the Fund. This second briefing covers the results of our review of disbursements for operating expenses paid from the Principal Fund and removal costs paid from the Emergency Fund.



Results in Brief

- The USCG and NPFC have established a system of internal control over operating expenses and Emergency Fund disbursement processes. However, we found some weaknesses in the design and operation of internal control over operating expenses and disbursements from the Fund that increase the risk of improper payments.
- Weaknesses in the design of control included a lack of documented reconciliations of the amounts included in removal cost reports and those recorded in USCG's accounting system.
- We found additional internal control weaknesses in that USCG/NPFC did not always follow established policies and procedures that are intended to help ensure the validity of disbursements.



Results in Brief (cont.)

- We obtained a nonstatistical selection of 467 disbursement transactions through data mining<sup>3</sup> for fiscal years 1998 through 2002. We found that
  - 33, or 7 percent of these transactions, totaling \$43,425 lacked adequate supporting documentation
    - 14 lacked both purchase receipts and purchase request forms;
    - 9 additional transactions lacked purchase receipts such as invoices; and
    - 10 additional transactions lacked purchase request forms.

<sup>3</sup>Data mining applies a search process to a dataset, analyzing for trends, relationships, and interesting associations. For instance, it can be used to efficiently query transaction data for characteristics that may indicate potentially improper activity.



Results in Brief (cont.)

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- 25, or 5 percent of these transactions, totaling \$26,182 lacked proper approvals
  - 4 lacked proof of approval from supervisors and fund certifying officers before purchases were made;
  - 3 additional transactions lacked proof of approval from supervisors before purchases were made; and
  - 18 additional transactions lacked proof of approval from the fund certifying officers before purchases were made.
- 39 transactions totaling \$155,994 for payments to contractors and other government agencies, and reimbursements to employees and others lacked documentation of supervisory review and approval before payments were made; and
- equipment purchases totaling \$62,700 were not recorded in the property tracking system.





Results in Brief (cont.)

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- We also used the nonstatistical selection of disbursements obtained through data mining to determine whether these disbursements complied with certain federal laws and regulations and represented a proper use of government funds. We found that
  - NPFC did not properly document their justification for using federal funds to reimburse \$14,481 in travel expenses for 11 nonfederal potential claimants to attend natural resource damage (NRD) seminars;
  - USCG Finance Center (FINCEN) incurred a total of \$8,868 in late payment fees and lost discounts;
    - We extended our tests beyond the 467 disbursements to include all late payment fees and lost discounts incurred during fiscal years 1998 through 2002. As a result, we found that NPFC incurred an additional \$15,678, for a total of \$24,546.



Results in Brief (cont.)

- The validity of 17<sup>4</sup> disbursements tested totaling \$6,589 was questionable because supporting documentation was missing.
- In addition, during fiscal year 2003, NPFC continued to improperly use the Fund to pay about \$645,000 in operating expenses and obligated another \$151,000 against the Fund. NPFC officials told us that they are in the process of transferring these transactions from the Fund into a newly established account created for recording NPFC operating expenses.
  - As with the \$32.8 million previously returned to the Fund, this transfer will not compensate for lost interest. We estimate that total lost interest on the improper use of the Fund could be as much as \$1.6 million as of September 30, 2003.<sup>5</sup>

<sup>4</sup>As discussed earlier, 23 disbursements lacked adequate supporting documentation. Of the 23 disbursements, 17 were missing any form of purchase receipts or invoices and were therefore questionable. Another 6 had partial supporting documentation and were not considered questionable.

<sup>5</sup>To calculate interest, we multiplied the average 6-month maturity rate for U.S. Treasury bills (the rate at which the Fund earns interest) times the average operating expense balance for each fiscal year.



Results in Brief (cont.)

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- We are making several recommendations intended to improve the design of internal controls over the operating expense and Emergency Fund disbursement processes and to establish better compliance with policies and procedures and federal laws and regulations.
- USCG/NPFC officials agreed with our recommendations. They emphasized that at the time they initially began using the Fund to pay operating expenses, they had an opinion from the USCG Chief Counsel that this was a proper use of the Fund. As noted earlier, GAO concluded in May 2002 that the Fund is not directly available to pay NPFC operating expenses.

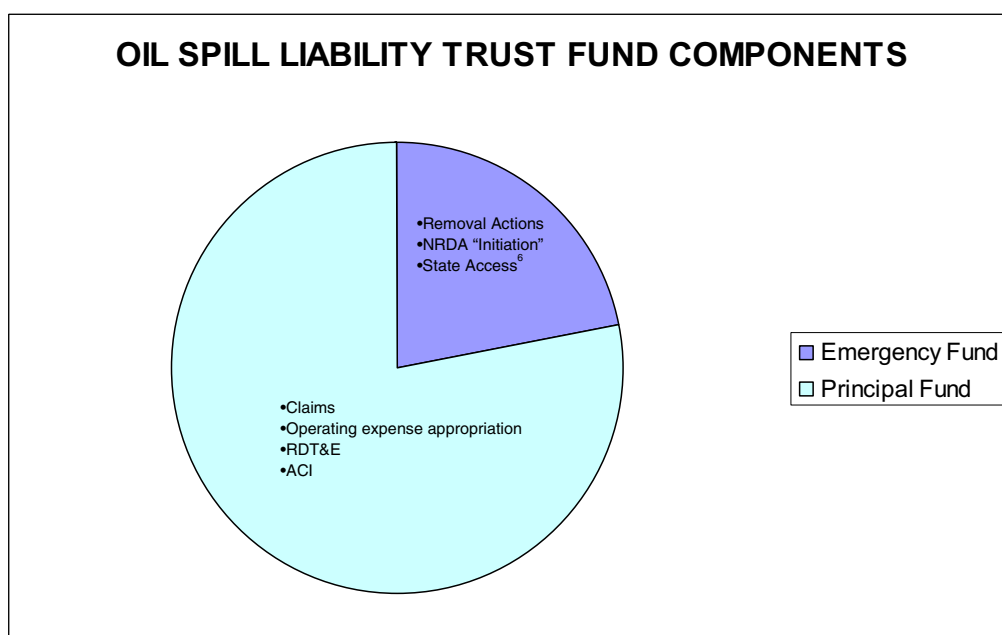


## Background

- OPA authorized the Fund to pay claims for certain costs resulting from oil spills or the substantial threat of oil spills. The act also
  - authorized the President to make up to \$50 million available from the Fund each year without further appropriation to pay for emergency removal costs and initiation of natural resource damage assessments (NRDA) resulting from oil spills,
  - authorized an appropriation from the Fund of not more than \$25 million each year for operating expenses incurred by the USCG to implement the act, and
  - provided authorization for the appropriation of funds for other uses such as research, development, testing, and evaluation (RDT&E); and acquisition, construction, and improvements (ACI).



Background (cont.)



Source: NPFC Year in Review Report for Fiscal Years 2001 and 2002

<sup>6</sup>State Access is a process through which states can directly receive federal funds for immediate removal costs in response to an actual or substantial threat of a discharge of oil.



Background (cont.)

- Administration of the Fund was delegated to the USCG by Executive Order and in February 1991, NPFC was commissioned to perform this function as an independent headquarters unit reporting directly to the Coast Guard Chief of Staff.
- NPFC administers and manages uses of the Fund by
  - making funds available for immediate federal oil removal activities and the initiation of natural resource damage assessments,
  - paying claims for losses or damages associated with an oil spill, and
  - recovering costs from responsible parties.



Background (cont.)

- During fiscal years 1998 through 2002, about \$32.8 million in disbursements were improperly paid from the Fund for operating expenses.<sup>7</sup> These expenses should have been paid from USCG's annual operating expense appropriation.
- Some of the operating expenses paid from the Fund included employee salaries, lease payments, travel expenses, training costs, office supplies, equipment, furniture, health club membership fees, and reimbursement of travel expenses for job interviewees.
- After our inquiries about the corrective actions taken to address the problem discussed in our May 2002 legal opinion, the USCG returned the \$32.8 million to the Fund in April 2003.<sup>8</sup>

<sup>7</sup>According to USCG/NPFC officials, at the time they had an opinion from the USCG Chief Counsel which found that the Fund was available to pay operating expenses.

<sup>8</sup>USCG/NPFC officials stated that they will continue to review the accuracy of this reimbursed amount and may adjust it accordingly.



Background (cont.)

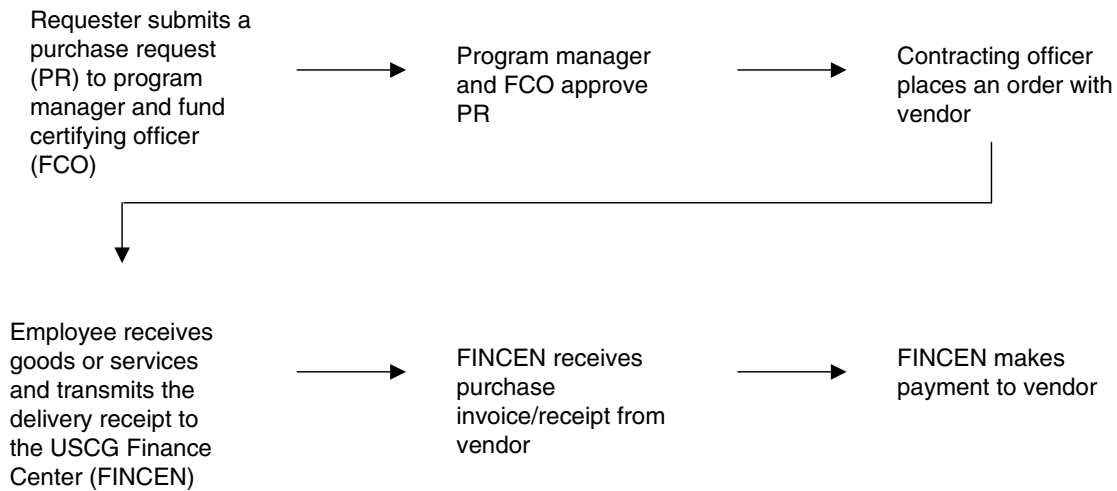
- During fiscal years 1998 through 2002, NPFC reported about 32,523 disbursements totaling \$319.7 million. Of this amount, about \$41.1 million in operating expenses were reported.
- The following diagram illustrates NPFC's operating expense disbursement process.





## Background (cont.)

### Operating Expense Disbursement Process



Source: Walk-through interview with NPFC officials.



## Overview of Effective Internal Control

As discussed in GAO's *Standards for Internal Control in the Federal Government*,<sup>9</sup>

- internal control—a major part of managing an organization—is a continuous, built-in component of operations that provides reasonable, but not absolute, assurance of meeting agency objectives,
- internal control consists of the plans, methods, and procedures used to meet the agency's missions, goals, and objectives, and
- internal control should be designed to provide reasonable assurance regarding prevention or prompt detection of unauthorized acquisition, use, or disposition of an agency's assets.

<sup>9</sup>*Standards for Internal Control in the Federal Government*, GAO/AIMD-00-21.3.1, which was prepared to fulfill our statutory requirement under the Federal Managers' Financial Integrity Act, provides an overall framework for establishing and maintaining internal control and for identifying and addressing major performance and management challenges and areas at greatest risk of fraud, waste, abuse, and mismanagement.



## Internal Control Design

We identified weaknesses in the design of internal control over disbursements from the Emergency Fund that made the Fund more vulnerable to improper payments.

**Control weakness:** The case files for Emergency Fund disbursements did not always include documented reconciliations of the amounts included in removal cost reports submitted by federal on-scene coordinators (FOSC)<sup>10</sup> and those recorded in USCG's accounting system. NPFC officials told us that case officers reconcile cost reports to the disbursements recorded in the accounting system. However, NPFC's policies and procedures do not require that these reconciliations be documented.

- *Standards for Internal Control in the Federal Government* states that internal control activities such as reconciliation and maintenance of related records provide evidence that these activities were executed and appropriately documented.

<sup>10</sup>FOSCs are USCG employees who are responsible for determining removal costs for an oil spill incident during oil spill response. FOSCs are physically stationed in USCG field locations.



## Internal Control Design (cont.)

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- Without consistently documented reconciliations, information is not always readily available to support the accuracy of amounts recorded for oil spill removal costs and proper supervisory review is impeded.



## Compliance with Policies and Procedures

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- Additional internal control weaknesses existed in that USCG/NPFC did not always follow established policies and procedures that are intended to help ensure the validity of disbursements.
  - Through data mining, we obtained a nonstatistical selection of 467 disbursements totaling \$2.5 million and performed tests for
    - adequate documentation,
    - proper approvals, and
    - adequate safeguarding of assets.
- *Standards for Internal Control in the Federal Government* states that (1) all transactions need to be clearly documented, and the documentation should be readily available for examination, (2) controls should be established to ensure that all transactions are authorized, and (3) physical controls should be established to secure and safeguard vulnerable assets.



## Compliance with Policies & Procedures (cont.)

### Documentation

- Of the 467 transactions tested, at least 33<sup>11</sup> (16 for NPFC and 17 for USCG field offices), or 7 percent of these transactions, totaling \$43,425 lacked adequate supporting documentation.<sup>12</sup> Specifically, 14 lacked purchase receipts such as invoices and purchase requests, 9 additional transactions lacked purchase receipts, and 10 additional transactions lacked supporting purchase request forms.
  - USCG/NPFC policies and procedures require that supporting documentation such as purchase receipts and purchase request forms be maintained in the files.
  - Without proper documentation, USCG/NPFC officials do not have an adequate basis for determining the validity of transactions they are approving.

<sup>11</sup>There were another 91 transactions totaling \$222,953 with transaction dates beyond NPFC's 3-year records retention policy. Supporting documentation for these transactions had been destroyed.

<sup>12</sup>According to USCG/NPFC officials, documentation for field transactions should have been maintained by USCG field employees.



## Compliance with Policies & Procedures (cont.)

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### Approvals

- Of the 467 transactions tested, we found that 25, (19 for NPFC and 6 for USCG field offices) or 5 percent totaling \$26,182 lacked proper approvals before purchases were made as required by USCG/NPFC policies and procedures.<sup>13</sup> Specifically, 4 lacked proof of approval from supervisors and fund certifying officers, 3 additional transactions lacked proof of approval from supervisors, and 18 additional transactions lacked proof of approval from the fund certifying officers.
- We also found that 39 NPFC transactions for payments to contractors and other government agencies, and reimbursements to employees and others totaling \$155,994, lacked documentation of supervisory review and approval before payments were made as required by NPFC policies and procedures.
- The lack of adequate approvals increases the risk of improper or erroneous purchases and payments.

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<sup>13</sup>According to USCG/NPFC officials, purchases made by USCG field office personnel should have been approved by USCG supervisors.



## Compliance with Policies & Procedures (cont.)

### Safeguarding Assets

- The NPFC property officer did not always record equipment purchases in the Accountable Item Management System (AIM),<sup>14</sup> nor did NPFC management review the inventory listing to ensure that all property was properly recorded in AIM. Of the 20 equipment purchases tested, 3 were only partially recorded in AIM. The components not recorded totaled approximately \$62,700.
- Without a complete record of accountable assets, NPFC cannot readily track the location of its equipment and has increased exposure to loss or theft of equipment.

<sup>14</sup>AIM was the USCG automated system used for tracking property during the timeframe for our review. In May 2003, AIM was incorporated into the USCG oracle financials fixed assets system.





## Propriety of Disbursements

We also used our nonstatistical selection of 467 transactions to test whether they were in compliance with certain federal laws and regulations and represented a proper use of government funds. We found that overall improper use of the Fund was continuing. In addition, we identified several instances of improper payments, wasteful spending, and questionable disbursements.

**Improper Use of the Fund:** In fiscal year 2003, NPFC continued to improperly pay operating expenses totaling \$645,358 from the Fund and obligated operating expenses totaling \$150,651 against the Fund.

- Although NPFC officials understand, based on our May 2002 legal opinion, that the Fund is not available to pay NPFC operating expenses, they stated that they have continued to do so because in order to stop the expenses from being charged to the Fund, modifications to accounting data on source documents for contracts and leases are needed. These modifications are in process but have taken longer than anticipated.



## Propriety of Disbursements (cont.)

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- NPFC officials explained that they are in the process of transferring these expenses from the Fund into a newly established account that was created in March 2003 to be used for recording NPFC operating expenses. The transfer was delayed due to USCG's conversion to a new accounting system.
- As with the \$32.8 million previously returned to the Fund, the transfer will not compensate for lost interest. We estimate that the total lost interest on the improper use of the Fund could be as much as \$1.6 million as of September 30, 2003.



## Propriety of Disbursements (cont.)

**Improper Payment:** NPFC did not properly document their justification for using federal funds to reimburse \$14,481 in travel expenses to 11 nonfederal potential claimants who traveled to NPFC to attend NRD seminars. The documented justification for the seminar stated that the purpose of the training was to reach out to people who could most benefit from the opportunities and services provided by the Fund.

- Appropriated funds may not be used to pay the costs of nonfederal individuals to attend training unless they are providing a direct benefit to the government.<sup>15</sup>
- According to NPFC officials, they view this as a documentation issue since they believe the individuals did in fact provide a direct benefit to the government through their participation in the seminars because of their expertise in the topics being discussed.

<sup>15</sup>See 31 U.S.C. 1345; see also 5 U.S.C. 5703, which allows an agency to use invitational travel to pay the costs of nonfederal individuals to attend meetings if the attendees are providing a direct service to the government.



## Propriety of Disbursements (cont.)

**Wasteful Spending:** The transactions we selected for testing included \$8,868 in late payment fees and lost discounts during fiscal years 1998 through 2002. According to USCG officials, this occurred primarily because contract officers did not provide payment approval forms to FINCEN in time for it to make timely payments.

- We extended our tests beyond the 467 disbursements to include all late payment fees and lost discounts incurred during fiscal years 1998 through 2002, and found that the Fund incurred an additional \$15,678 for a total of \$24,546.
- USCG officials told us that they changed their procedures for contract payments in fiscal year 2000. Since that time, invoices have been sent directly to contracting officers with automated online approval available through FINCEN's Workflow Image Network System (WINS). This procedure allows payables personnel at FINCEN to expedite payments, take advantage of discounts, and avoid late payment penalties.



## Propriety of Disbursements (cont.)

**Questionable Disbursements:** We identified several transactions that were missing purchase receipts.<sup>16</sup> Because USCG/NPFC could not provide purchase receipts for 17 of the 467 transactions tested, we could not determine whether these transactions were valid.

- Without key purchase documentation, neither we nor USCG/NPFC officials could determine what was actually purchased, the number of items purchased, the cost of the items purchased, or if there was a legitimate government need for the items.

<sup>16</sup>As discussed earlier, 23 disbursements lacked adequate supporting documentation. Of the 23 disbursements, 17 were missing any form of purchase receipts or invoices and were therefore questionable. Another 6 had partial supporting documentation and were not considered questionable.



## Conclusions

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The USCG NPFC has established a system of internal control over its operating expenses and Emergency Fund disbursement processes. However, weaknesses in the design and operation of internal control over the disbursement processes, if left uncorrected, increase the Fund's vulnerability to future improper payments.

In addition, NPFC's continued improper use of the Fund to pay for operating expenses is a violation of federal law. Not only does this practice expose the Fund to misuse, but we calculated that the Fund may have lost as much as \$1.6 million in interest during fiscal years 1998 through 2002 as a result.



## Recommendations

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To improve the design of internal control over disbursements from the Fund, we recommend that the Commandant of the USCG direct the Director of NPFC to

- establish policies and procedures to require that (1) case officers document the reconciliation of removal costs reports to amounts paid in the accounting system and (2) their supervisors document their review of these reconciliations.



## Recommendations (cont.)

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To establish better compliance with USCG/NPFC policies and procedures, we recommend that the Commandant of the USCG direct the Director of NPFC to

- reinforce documentation and approval requirements by instituting training for all relevant employees;
- institute a monitoring system such as periodic spot checks to help ensure that such requirements are consistently followed; and
- establish a mechanism to ensure that accountable assets are properly recorded in USCG's fixed assets system.





## Recommendations (cont.)

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To enforce compliance with OPA and other federal laws and regulations and reduce the risk of improper payments, we recommend that the Commandant of the USCG direct the Director of NPFC to

- expedite actions needed to cease using the Fund to pay operating expenses as we advised in our May 2002 legal opinion;
- in the interim, for any unreimbursed or future use of the Fund to pay operating expenses, record obligations against USCG's annual operating expense appropriation in order to ensure that adequate funds are available to reimburse the Fund;
- complete the transfer of all operating expenses that were improperly paid from the Fund in fiscal year 2003 to the new operating expense account;



## Recommendations (cont.)

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- ensure proper justification is documented for nonfederal travelers to be reimbursed to attend NRD seminars; and
- follow up on transactions that were missing purchase invoices to determine what was purchased and whether the items were for legitimate government needs.



Recommendations (cont.)

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We also recommend that the Commandant of the USCG direct the Chief Financial Officer of the USCG to

- reinforce documentation and approval requirements for disbursements from the Fund by instituting training for all relevant employees; and
- institute a monitoring system such as periodic spot checks to help ensure that such requirements are consistently followed.



## Agency Comments

- USCG/NPFC officials agreed with our recommendations. They emphasized that at the time they initially began using the Fund to pay operating expenses, they had an opinion from the USCG Chief Counsel that this was a proper use of the Fund. As noted earlier, GAO concluded in May 2002 that the Fund is not available to pay NPFC operating expenses.
- USCG/NPFC officials also emphasized that they now have electronic approvals which they believe provide better supervisory review and oversight.
- USCG/NPFC provided technical and clarifying comments, which we incorporated as appropriate.



## Scope and Methodology

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To determine whether the design of existing internal control over operating expenses and Emergency Fund removal costs disbursement processes provide reasonable assurance that improper payments will not occur or will be detected in the normal course of business, we

- reviewed USCG/NPFC's policies and procedures related to operating expenses and Emergency Fund removal costs disbursements,
- considered *Standards for Internal Control in the Federal Government*,
- interviewed staff and officials in the USCG and NPFC offices, and
- performed walkthroughs of the operating expenses and Emergency Fund removal costs disbursement processes, and compared the results to NPFC's policies and procedures and the *Standards for Internal Control in the Federal Government*.



## Scope and Methodology (cont.)

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To determine whether disbursements were made in accordance with USCG/NPFC's policies and procedures, we

- performed data mining of operating expenses paid from the Fund during fiscal years 1998 through 2002 to identify unusual transactions and patterns including personal use items, Internet purchases, training and travel, equipment purchases, employee reimbursements, contract payments other than removal costs, and late payment fees;
- used a nonstatistical selection of 467 disbursements obtained through data mining and tested for adequate documentation, proper approvals, and adequate safeguarding of assets.



## Scope and Methodology (cont.)

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- To test for adequate documentation, we looked for supporting purchase receipts, purchase request forms, contracts, delivery reports, and inventory documents, if applicable.
- To test for proper approvals, we reviewed transactions for evidence of proper approvals from supervisors and fund certifying officers prior to the purchase and for evidence of proper approvals prior to payment.
- To test for adequate safeguarding of assets, we reviewed NPFC's inventory report for equipment purchases and compared it to purchase receipts to ensure that the equipment was properly recorded in the AIM system.



## Scope and Methodology (cont.)

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We also used the nonstatistical selection of disbursements obtained through data mining to determine whether disbursements were made in accordance with OPA and other federal laws and regulations and represent a proper use of government funds. Specifically, we

- reviewed OPA and federal laws and regulations to obtain an understanding of allowable costs, and
- reviewed purchase receipts or invoices to ensure that purchases were made for official government use and were for allowable costs.

We did not project our test results to the universe of NPFC disbursements in fiscal years 1998 through 2002.





## Scope and Methodology (cont.)

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To determine the fluctuations in payroll expenses and claims activity we

- obtained data from NPFC and USCG and identified significant fluctuations in payroll and claims activity for fiscal years 1998 through 2003, and
- obtained USCG/NPFC's explanations for these fluctuations.
- We did not verify the accuracy of the amounts included in USCG/NPFC's payroll or claims systems.



## Scope and Methodology (cont.)

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- We requested oral comments on a draft of these briefing slides from USCG/NPFC officials that were incorporated as appropriate.
- We conducted our work from November 2002 through November 2003, in accordance with generally accepted government auditing standards.



## Appendix I Payroll Expense Fluctuations

- USCG and NPFC also provided the following data on NPFC's payroll expenses for fiscal years 1998 through 2003.<sup>17</sup> The following table depicts the changes in payroll expenses for these years.

Fiscal Year	Amount	Change	
		Dollars	Percentage
1998	5,451,471	-	-
1999	6,003,953	552,482	10.1%
2000	7,066,690	1,062,737	17.7%
2001	7,944,824	878,134	12.4%
2002	8,736,055	791,231	10.0%
2003	9,367,615	631,560	7.2%
Total Increase since 1998		3,916,144	71.8%

Source: NPFC and USCG data for fiscal years 1998 through 2003.

Note: The annual change amount equals the difference between the current year and the prior year expenses. The annual change percentage equals the current year dollar variance divided by the prior year amount.

<sup>17</sup> Payroll expenses represent pay, benefits, and entitlements.



Appendix I  
Payroll Expense Fluctuations (cont.)

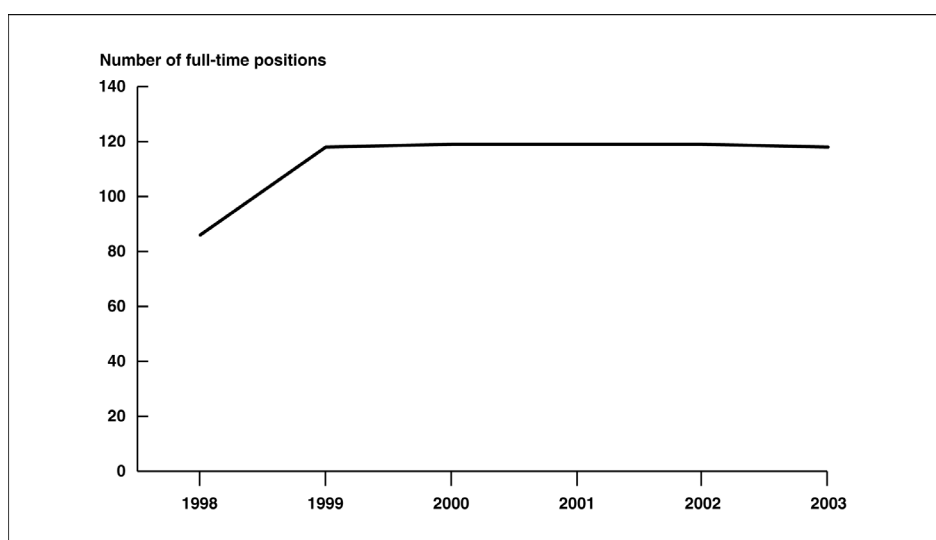
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- Payroll expenses increased by more than 70 percent over the 5 year period ended September 30, 2003.
  - USCG/NPFC officials told us that NPFC hired 26 new employees in fiscal year 1999, a 30 percent increase, and 1 new employee in fiscal year 2000 to assist with the implementation of the then newly acquired NRD claim adjudication program and to support substantial workload requirements of NPFC's existing claim adjudication backlog.
  - USCG/NPFC officials also told us annual increases in payroll from fiscal years 2000 through 2003 were due primarily to increases in national pay raises, housing allowances for military employees, health care and retirement costs, and within grade increases or promotions.



## Appendix I Payroll Expense Fluctuations (cont.)

### NPFC Full-Time Positions for Fiscal Years 1998 through 2003



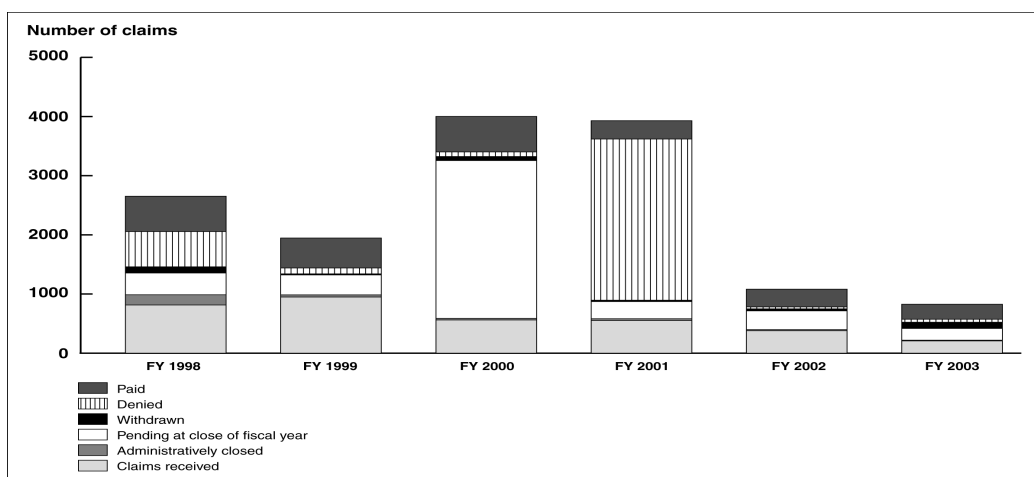
Source: NPFC data.

- According to NPFC officials, the number of full-time positions has remained constant since fiscal year 2000 because current staffing levels are required to keep pace with the ongoing claims workload and to adjudicate increasingly complex claims.



## Appendix I Claim Activity Fluctuations (cont.)

- The following figure depicts the fluctuations in the number of claims received and processed during fiscal years 1998 through 2003.



Source: NPFC data.

Note: Claims processed include those claims that were administratively closed, pending, withdrawn, denied, and paid and a number of claims that were received prior to fiscal year 1998 but processed during fiscal years 1998 through 2003. Claims pending in fiscal year 2000 includes claims received prior to fiscal year 1998.



Appendix I  
Claim Activity Fluctuations (cont.)

- NPFC officials provided the following explanations for the fluctuations in claims received and processed during fiscal years 1998 through 2003.
  - During fiscal years 1998 through 2001, there was a backlog of claims received because NPFC did not have enough claims adjudicators to process the claims.
  - In fiscal year 2000, the total number of pending claims increased because NPFC reopened about 1,900 NRD claims that had been administratively closed prior to fiscal year 1998.
  - In fiscal year 2001, NPFC reviewed a large number of NRD claims that did not meet OPA's criteria for valid claims resulting in an increase in denials during this time.
  - By fiscal year 2001, the number of backlogged claims decreased because NPFC hired more employees between fiscal years 1999 and 2000 to process the claims.

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