Department of
Veterans Affairs

Office of Inspector General

Management Letter:
Management Oversight of
Property, Plant, and Equipment
Financial Information

Report No.: 7AF-G10-085
Date: May 12, 1997

Office of Inspector General
Washington DC 20420

Department of Veterans Affairs

Memorandum

Date: May 12,1997

From: Director, Financial Statement Audit Operations Division (52CF)

Subj: Management Letter: Management Oversight of Property, Plant, and Equipment Financial Information, Report No. 7AF-G10-085

To: Deputy Assistant Secretary for Financial Management (047)
Chief Financial Officer, Veterans Health Administration (17)

1. As part of our audit of the Department of Veterans Affairs (VA) Fiscal Year (FY) 1996 Consolidated Financial Statements, we evaluated internal accounting controls over property, plant, and equipment (PP&E). We have separated our observations into three management letters with the objective of improving communication and providing suggestions to the management levels where it can be the most helpful. This management letter is an overview, and provides information and observations from our overall analysis of PP&E data in the general ledger and fixed asset subsystem, and actions by the Veterans Health Administration (VHA), Chief Financial Officer (CFO) to improve internal controls. Details of our audit work at medical centers are discussed in two separate management letters that address actions that are generally needed at medical facilities to improve internal controls over the accuracy of financial data for real property[1] and non-expendable equipment.[2]

2. Our prior financial statement audits[3] identified problems with the systems used to track PP&E and a number of errors in PP&E and related depreciation account balances. During FY 1996, we found that much progress has been made in improving the tracking of PP&E and correcting account balances. However, we found a number of significant errors and internal control weaknesses that could, if not corrected, result in future qualifications. Therefore, VHA and VA CFO staffs need to continue efforts to oversee PP&E accounting activities, provide additional guidance and training, and to analyze PP&E accounts and provide operating facilities the results when adjustments are needed. Details of our audit observations are discussed in the enclosure.

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[1] Management Letter "Accuracy of Real Property Financial Information," Report No. 7AF-G10-087.
[2] Management Letter: "Accuracy of Non-expendable Equipment Financial Information," Report No. 7AF-G10-086.
[3] Audits of VA's Consolidated Financial Statements for Fiscal Years 1995, Report No. 6AF-G10-043; 1994, Report No. 5AF-G10-052; 1993, Report No. 4AF-M02-083; and 1992, Report No. 3AF-M02-155.

Deputy Assistant Secretary for Financial Management (047)
Chief Financial Officer, Veterans Health Administration (17)

3. We appreciate the assistance provided to the audit staff. If you want to discuss the contents of this report or if you need additional information, please contact Mr. Garry Martin at (202) 565-9404 or me at (202) 565-7013.

For the Assistant Inspector General For Auditing

(Original Signed By:)
John E. Jonson
Director, Financial Statement Audit
Operations Division

Enclosure

cc: Veterans Health Administration, Director, Report Review and Analysis Service (105E)
Veterans Benefits Administration, Director, Office of Resource Management (24)
National Cemetery System, Director, Office of Operations Support (402)

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PURPOSE

As part of our audit of the Department of Veterans Affairs (VA) Fiscal Year (FY) 1996 Consolidated Financial Statements (CFS), we evaluated internal accounting controls over property, plant, and equipment (PP&E). The audit was conducted in accordance with generally accepted government auditing standards.

Our prior financial statement audits identified problems with the systems used to track PP&E and a number of errors in PP&E and related depreciation account balances. We found that much progress had been made in improving the tracking of PP&E and correcting account balances for FY 1996. For example, along with implementing the final phase of the Financial Management System (FMS) Fixed Asset Subsystem (subsidiary ledger), the Veterans Health Administration (VHA) Chief Financial Officer (CFO) staff:

- Worked with medical facilities to reconcile and adjust their general ledger PP&E accounts to the subsidiary ledger.
- Performed analytical reviews of general ledger accounts to identify and correct errors and irregular balances.
- Issued additional guidance and instructions.

These actions helped to correct the system problems and the many errors identified in audits of VA's CFS in prior years, therefore we were able to attest to the reasonableness of FY 1996 year-end PP&E account balances without qualification. However, VHA and VA CFO staffs need to continue their oversight of PP&E accounting activities to help ensure that the improvements obtained during FY 1996 are not lost. Also, during our FY 1996 audit, we found a number of significant errors and internal control weaknesses that could, if not corrected, result in future qualifications. These errors continue to occur because staff at some facilities were unfamiliar with basic accounting principles and changes brought about by the implementation of the FMS Fixed Asset (FA) Subsystem and the Automated Engineering Management System/Medical Equipment Reporting System (AEMS/MERS).

BACKGROUND

Definition of PP&E. Property, Plant, and Equipment is divided into two basic groups. Real property, consisting of land, buildings, improvements and other structures; and, equipment, including computer programs. VA policies usually address real property and equipment separately, since fund sources and transaction processing is different.

Chief Financial Officers Act. The CFO Act of 1990 (Public Law 101-576) requires VA to issue annual reports on its CFS. The Act also requires that the financial statements be audited each year to help ensure financial data is accurate and reliable for use in making decisions and improving accountability.

VA Policies. VA policies state that the accounting system should provide for effective internal controls. The internal control structure should provide reasonable assurance that: (a) accounting operations and transactions are in accordance with applicable laws, regulations, and agency policies; (b) assets are safeguarded against waste, loss, and unauthorized use; and (c) assets, expenditures, and revenues applicable to agency operations are properly recorded and accounted for to permit accurate and reliable financial reports.

Financial Management System. FMS is a comprehensive, agency-wide system that supports a full range of financial activities. The system was designed to: (a) increase accounting controls; (b) enhance internal controls; (c) implement the Standard General Ledger; and (d) comply with the Joint Financial Management Improvement Program Core Financial Systems Requirements. In April 1995, facilities started installing the FMS FA Subsystem, Fixed Asset Package (FAP), for real property assets, however equipment was not added to the system until June 1996. The system computes depreciation and contains detailed data (e.g., acquisition cost and date, and useful life) for each asset. In June 1996, facilities implemented AEMS/MERS which is a centralized data base residing in FAP, which contains data on equipment (non-expendable property). AEMS/MERS was originally developed for Engineering Service which has now evolved into a shared package as part of the FMS FAP system to account for and track PP&E.

SCOPE

To assess the accuracy and reliability of financial information in VA's FY 1996 CFS, we evaluated the accuracy and reasonableness of PP&E and related depreciation expense year-end account balances and the adequacy of key internal accounting controls over real property and equipment. Specifically, we visited appropriate VA Central Office staff, and selected field facilities, sent questionnaires to field activities, and analyzed national financial data.

Central Office Visits. We interviewed appropriate staff assigned to the VHA CFO and the Office of Deputy Assistant Secretary for Financial Management. We discussed financial policies, oversight of financial information, and actions taken to correct accounting errors identified during prior CFS audits.

Medical Center Visits. We visited 45 VA Medical Centers (VAMCs) to evaluate internal accounting controls for PP&E (see page 8 for a list of activities visited). We reviewed account reconciliations, physical inventories of equipment, and accuracy of PP&E data in the general ledger and the FAP.

Questionnaires to Activities. As of September 30, 1996, VA activities had over 185,000 PP&E items totaling $16.9 billion and accumulated depreciation totaling $7.0 billion. We sent questionnaires to 170 VA activities to validate the accuracy of data recorded in the FAP for 895 randomly selected PP&E items. Questionnaires were sent to VAMCs, Regional Offices, cemeteries, and various support activities.

Analyses of Financial Information. We analyzed year-end PP&E (1) general ledger account balances to identify abnormal and irregular balances; and, (2) asset information recorded in the FAP. Additionally, we reviewed VHA CFO staff's fourth quarter, FY 1996 efforts to help VAMCs reconcile and correct PP&E general ledger and FAP balances.

RESULTS OF AUDIT TESTS

Continuing Efforts Are Needed to Refine Property, Plant, and Equipment Records

Our analyses and tests of fixed asset general ledger and FAP data, and reviews of account reconciliations activities at headquarters disclosed significant accounting errors and internal control weaknesses.

Analyses of FAP and General Ledger Information

FAP. Our analyses of data recorded in the FAP, as of September 30, 1996, disclosed a number of errors and/or indicators of problems. For example:

- Thirteen hundred and seventy-seven equipment items ($2.4 million) had values of under $5,000 each. None of these items should have been capitalized under VA capitalization policy which states that items under $5,000 should be expensed. As a result, the equipment account balance was overstated by $2.4 million. In addition, 237 other equipment items had no acquisition value.

- Fourteen Automatic Data Processing software assets ($191,000) had values of under $25,000 each. None of these items should have been capitalized under VA capitalization policy which states that software under $25,000 should be expensed. As a result, the equipment account balance was overstated by $191,000.

- Three thousand and sixty-one building items ($6.5 million) had acquisition values of less than $5,000 each, and 297 building items had no acquisition value. Although VA policy does not prohibit capitalizing building items under $5,000--this policy applies to equipment--we believe that consideration should be given to changing the policy to be consistent with the policy established for equipment.

- Four hundred and eighty-four building and equipment items ($7.7 million) were fully depreciated (book value was zero) but the designated useful life had not expired, indicating that some error had occurred, either in the system and/or how the entries for these items were processed. As a result, the assets were understated and depreciation expense and accumulated depreciation accounts were overstated. VA policies state that assets should be depreciated on a straight line basis over their useful lives.

- Twenty-six hundred and thirty-nine building and equipment items had a book value of $221.3 million, which should have been zero because their designated useful lives had expired, indicating that some error had occurred either in the system or in processing the accounting entries. As a result the assets were overstated and depreciation expense and accumulated depreciation accounts were understated.

- Two hundred and four building and equipment items ($3.5 million) had acquisition dates in the future, therefore depreciation was not started. As a result, the assets were overstated and depreciation expense and accumulated depreciation for these items were understated.

- No depreciation expense was calculated for 1,610 building and equipment items ($126.6 million) acquired before September 30, 1996, for which, depreciation should have started. As a result, the assets were overstated and the depreciation accounts were understated.

General Ledger Accounts. We analyzed FY 1996 year-end trial balance data for PP&E asset and accumulated depreciation accounts for all VA activities. We found normal debit accounts with credit ending balances and normal credit accounts with debit balances. These irregular account balances indicate that errors were made in recording and/or adjusting the transactions in these accounts.

- Debit Accounts with Credit Ending Balances -- Sixty-four activities had 92 accounts (buildings, equipment, etc.) with credit balances, at the end of FY 1996, which should have been debits. For these 92 accounts, the credit balances totaled $92.2 million, indicating an understatement of the assets by this amount or more.

- Credit Accounts with Debit Ending Balances -- Thirty-four activities had 46 accumulated depreciation accounts with debit balances at the end of FY 1996, which should have been credits. For these 34 accounts, the credit balances totaled $14.6 million, resulting in an overstatement of assets and an understatement of accumulated depreciation.

Need For Improved Reconciliations

Significant Adjustments. The FAP provided the VHA CFO staff the data they previously did not have to identify and correct the many reconciliation problems identified during prior audits[4] of VA's CFS. During the last quarter of FY 1996 the VHA CFO staff developed new reconciliation reports and worked with VAMCs to reconcile and adjust their general ledger and subsidiary record. Our 1996, audit showed that VAMCs made a number of significant adjustments to their general ledger accounts and/or FAP records to reduce reconciliation differences identified by the VHA CFO staff. We found that during the last quarter of FY 1996:

[4] See footnote 3.

- The general ledger asset accounts at 69 VAMCs or integrated sites were increased by 325.9 million, while at 90 they were decreased by $357.9 million, for a net decrease of $32 million.

- The subsidiary records or FAP at 112 VAMCs or integrated sites were increased by $641.6 million, while at 47 they were decreased by $97.1 million for a net increase of $544.5 million.

While we believe this was a valiant effort by the VHA CFO staff to correct these large differences, we also recognized that it was very difficult for medical facility staffs to perform the necessary research, during the last quarter of FY 1996, to correct errors that had developed over many years. During visits to 45 VAMCs we found that:

- Staff at 16 of the VAMCs did not complete one or more of the required monthly reconciliations of equipment and/or building accounts during the last quarter of FY 1996.

- Staff at 13 of the VAMCs had not completely reconciled data from the prior asset system to the new FAP.

- Staff at 23 of the VAMCs said that, due to lack of time for adequate research, they made unsupported adjustments to the equipment and/or building accounts, as the result of the reconciliation efforts by the VHA CFO staff. For example:

    - ♦ One facility reduced the fixed asset general ledger accounts by $44 million; however, documentation to support this adjustment was not available.

    - ♦ Staff at another facility could not explain $13.7 million of adjustments to the real property accounts.

As a result of these issues, we believe that the VHA CFO staff should continue working with the medical facilities to help ensure that reconciliations are completed as required and proper and timely adjustments are made. Also, we believe VHA CFO needs to conduct a review of high-dollar value building and equipment items and have appropriate VAMCs research applicable documentation or make reasonable estimates to certify the accuracy of the asset amounts recorded in the general ledger, and the FAP.

Accuracy of Subsidiary Records

Sample Data. Our statistical sample of 895 PP&E items (416 building and 479 equipment items) disclosed a number of errors in the building and equipment subsidiary records (details are discussed in the other two management letters[5]). We sampled items that were 2 years old or less because supporting documents were not readily available at the VAMCs for older items. We believe that the untested items could also contain similar errors. Therefore, as indicated above, we believe that VHA CFO needs to conduct a review of high-dollar value building and equipment items; and have appropriate VAMCs research applicable documentation or make reasonable estimates to certify the accuracy of the asset amounts recorded in the general ledger and the FAP.

CONCLUSION

Much progress has been made in improving PP&E tracking systems and correcting fixed asset and related depreciation account balances, resulting in the removal of the prior year qualification. However, accounting errors still existed which, if not corrected, may result in a future qualification of VA's CFS. Accordingly, we encourage the VHA CFO to continue efforts to provide additional written instructions, and training to field staffs and emphasize the importance of financial reconciliations, physical inventories, and analytical reviews of fixed asset, general ledger, and FAP data. Specifically, we believe that actions are needed to:

- Continue management oversight of PP&E accounting activities.
- Continue to provide guidance, instructions, and training to field staff.
- Continue to emphasize and provide guidance to field activities on performing monthly reconciliations of general ledger and FAP totals.
- Continue to analyze national general ledger and FAP data to identify potential errors and irregularities.
- Report any errors or irregularities noted during oversight reviews to the appropriate VISN financial officer so that corrective action can be initiated.
- Initiate action to perform a special review of high-dollar value PP&E items. Have field staff research applicable documents or make a reasonable estimate to certify the accuracy of asset value and data recorded in the general ledger and the FAP.

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[5] See footnotes 1 and 2.

FACILITIES VISITED

VA Maryland Health Care System (512, 566, and 641)
VA Northern CA System of Clinics (612)
VA Puget Sound Health Care System (663/505)
VA South Texas Veterans Health System San Antonio/Kerville, TX (671/591)
VA Western New York Health Care System (528)
VAMC Albany, NY (500)
VAMC Atlanta, GA (508)
VAMC Augusta, GA (509)
VAMC Bay Pines, FL (516)
VAMC Bedford, MA (518)
VAMC Boston, MA (523)
VAMC Brockton, MA (525)
VAMC Bronx, NY (526)
VAMC Brooklyn, NY (527)
VAMC Chicago, IL (Lakeside) (535)
VAMC Chicago, IL (Westside) (537)
VAMC Dallas, TX (549)
VAMC Dublin, GA (557)
VAMC East Orange, NJ (561)
VAMC Hines, IL (578)
VAMC Houston, TX (580)
VAMC Kansas City, MO (589)
VAMC Lake City, FL (594)
VAMC Leavenworth, KS (686)
VAMC Loma Linda, CA (605)
VAMC Long Beach, CA (600)
VAMC Lyons, NJ (604)
VAMC Miami, FL (546)
VAMC New York, NY (630)
VAMC North Chicago, IL (556)
VAMC Northport, NY (632)
VAMC Palo Alto, CA (640)
VAMC Philadelphia, PA (642)
VAMC Portland, OR (648)
VAMC Richmond, VA (652)
VAMC San Diego, CA (664)
VAMC San Francisco, CA (662)
VAMC Sepulveda, CA (665)
VAMC St. Louis, MO (657)
VAMC Tampa, FL (673)
VAMC Washington, DC (688)
VAMC West Los Angeles, CA (691)
VAMC West Palm Beach, FL (548)
VAMC Wilmington, DE (460)
VAOPC Los Angeles, CA (752)