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[Controls and Accountability for Checks Returned to Treasury's Disbursing Centers]. FGMSD-76-56; B-112924. March 1, 1977. 9 pp.

Report to Secretary, Department of the Treasury; by D. L. Scantlebury, Director, Financial and General Management Studies Div.

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Authority: Budget and Accounting Procedures Act of 1950. Treasury Fiscal Requirements Manual, ch. 7000. 4 Treasury F.R.M. 7030.10. 2 GAO 12.2. Treasury's Division of Disbursement Procedures Manual, part V, sec. 5110.

A review was conducted of the Department of the Treasury's controls over checks on hand that were returned as undelivered or were withdrawn from delivery after preparation. Findings/Conclusions: During fiscal year 1976, seven Treasury disbursing centers were holding about 53,000 negotiable checks (about $17.7 million) without adequate safeguards. About 41,000 of these undelivered checks were at least 6 months old. Because Treasury did not cancel the checks immediately, Federal agencies have been precluded from making timely adjustments to their accounting records. Several weaknesses were noted in internal controls over the processing of returned checks: mail containing checks was not always opened in the presence of other employees as required; checks not under accounting control were placed in open desks accessible to anyone; and uncancelled checks were processed without adequate controls. Treasury's problems in controlling returned checks could be minimized if such checks were cancelled shortly after receipt. Recommendations: The Secretary of the Treasury should: provide for cancellation of returned checks upon receipt by Treasury, and notify Federal agencies when their returned checks are cancelled; and improve controls over returned and withdrawn checks that are still negotiable by adequately separating duties of employees processing checks, restricting access to checks to those who have a need to handle them, and maintaining proper accountability over the checks. (RRS)

00286

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

DIVISION OF FINANCIAL AND GENERAL MANAGEMENT STUDIES

B-112924

MAR 1 1977

The Honorable
The Secretary of the Treasury

Dear Mr. Secretary:

This report presents the results of our review of the Department of the Treasury's controls over checks on hand that (1) were returned by the Postal Service and Federal agencies as undelivered or (2) were withdrawn from delivery after preparation by the Treasury.

The Budget and Accounting Procedures Act of 1950 requires heads of Federal agencies 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. As part of our responsibilities for reviewing financial management systems under the act, we reviewed Treasury's controls over returned and withdrawn checks.

Our review was made primarily at Treasury's eight disbursing centers. We examined Treasury's practices and procedures for controlling, safeguarding, and processing both returned and withdrawn checks; observed and tested procedures used to account for these checks; and talked to responsible officials.

We are recommending corrective measures needed to properly control, account for, and safeguard returned and withdrawn checks held by Treasury.

## NEED FOR CANCELLATION OF CHECKS RETURNED AS UNDELIVERABLE

At the time of our visits during fiscal year 1976, seven Treasury disbursing centers were holding about 53,000 negotiable checks--amounting to an estimated $17.7 million--without adequate safeguards. To prevent loss or theft of negotiable checks, we believe they should be immediately canceled.

These negotiable checks had been returned by the Postal Service and Federal agencies as undeliverable. About 41,000 of them were at least 6 months old. The checks were located in seven disbursing centers as follows:

| Disbursing center | Uncanceled checks on hand at date of GAO visit | |
|---|---|---|
| | Number | Amount |
| Austin | 1,374 | $ 379,400 |
| Birmingham | a/25,342 | a/1,320,800 |
| Chicago | 13,992 | 1,537,500 |
| Denver | 1,061 | 553,400 |
| Kansas City | 1,198 | 11,778,900 |
| San Francisco | 639 | 573,300 |
| Washington, D.C. | b/9,652 | b/1,550,900 |
| Total | c/53,258 | $17,694,200 |

a/Estimated by disbursing center--actual inventory not available or taken.

b/Estimate based on statistical sample by GAO--figures are the low end of the range.

c/About 78 percent of these checks were at least 6 months old.

Approximately 4,000 to 5,000 checks were on hand at the Philadephia Disbursing Center, but an estimate of their value was not available.

According to Treasury officials an unusally high volume of checks was returned in fiscal year 1976. They said this situation was related to issuing special checks to about 31 million individuals, as required by the Tax Reduction Act of 1975, and resulted from many incorrect mailing addresses furnished by Federal agencies. Treasury officials indicated that a more representative volume of checks would be those on hand as of January 1977; however, the stated quantity at that time amounted to around 15,000 checks worth over $14.8 million.

According to a Treasury report dated September 17, 1975, about 4.7 million checks were returned during fiscal year 1975. Only about 300,000 checks (6.4 percent) were remailed by Treasury disbursing centers. The other 4.4 million checks were canceled or held awaiting disposition instructions from Federal agencies. Currently less than

2 percent of all returned checks are remailed, according to Treasury officials.

Because Treasury did not cancel checks immediately, Federal agencies have been precluded from making timely adjustments to their accounting records. Also, the returned checks held by Treasury could have been lost or stolen without detection because (1) the checks were not under proper accounting control and (2) access to them within the disbursing centers was not effectively restricted.

Treasury checks returned as undeliverable may still be payable to the payee or the payee's estate. The Treasury Fiscal Requirements Manual (ch. 7000), therefore, permits check cancellations to be authorized only by GAO or the agencies or offices certifying vouchers against which the checks were issued. This regulation also permits retaining uncanceled returned checks, pending disposition instructions from the agencies.

If agencies do not furnish disposition instructions for a check within a specified time, Treasury must cancel it. Generally the time limit is 6 months after date of issue.

Some Federal agencies have entered into agreements with Treasury to have returned checks canceled immediately upon receipt. For example, the Internal Revenue Service has arranged for immediate cancellation of returned tax refund checks although these checks may be held for 6 months.

We believe that Treasury could greatly reduce the possibility of errors and irregularities involving checks returned by Federal agencies and the Postal Service if all Federal agencies used automatic check cancellation procedures. These procedures are provided for in the Treasury Fiscal Requirements Manual (4 TFRM 7030.10), which allows an exception to procedures for handling and processing undeliverable checks as follows:

> "Administrative agencies operating 'Automatic Check Cancellation Procedures,' developed jointly with Treasury disbursing centers and offices, are exempt from the provisions of this section, since checks are immediately cancelled and processed on SF 1098, [Schedule of Cancelled Checks] as prescribed in ITFRM 4-7020."

## IMPROVEMENTS NEEDED IN INTERNAL CONTROLS OVER RETURNED CHECKS

During visits to the disbursing centers, we observed several weaknesses in internal controls over the processing of returned checks.

According to Treasury's Division of Disbursement Procedures Manual (part V, sec. 5110), all incoming mail containing or suspected of containing checks must be opened in the presence of another employee. Checks returned by Federal agencies to the wrong disbursing center are transmitted directly to the appropriate disbursing center. Mutilated checks are sent through a conditioning machine. A progress card is prepared for control purposes to accompany the checks during processing. These checks are sorted by major payment classes, coded as to reason for return, and lotted into groups of convenient size.

Treasury prepares and forwards returned check notices to the appropriate agency to request disposition instructions for all uncanceled checks. The checks are then forwarded to the returned check custodian for safekeeping in safes and vaults, where they are filed in sequence and interfiled daily. When authorized by Federal agencies, Treasury cancels the checks and advises the agency of the action on listings or magnetic tapes.

GAO's Policy and Procedures Manual for Guidance of Federal Agencies (2 GAO 12.2) states that Federal agencies should adopt procedures to account for and help provide effective control over cash resources. Such procedures should result in:

--Complete, honest, and accurate accounting for cash receipts, disbursements, and balances on hand or otherwise available for use.

--Compliance with all applicable requirements imposed externally for handling cash resources, including requirements of law and related regulations.

--Minimizing the possibility of errors and the misuse or other irregularity involving cash resources, and providing for the disclosure of errors or losses.

At the disbursing centers, we observed that Treasury's procedures for controlling and safeguarding returned checks were not always followed. Specifically:

--Mail containing or suspected of containing checks was not always opened in the presence of another employee as required.

--Checks not under accounting control were placed in open desks accessible to anyone during the processing operations.

--Uncanceled checks were processed without proper control, precluding adequate accountability. For example, at one disbursing center, no investigation was made when discrepancies existed between the number of checks processed and the number that should have been processed.

--At smaller disbursing centers, one person was responsible for the entire returned check processing cycle instead of dividing duties among officials and employees to separately handle and keep records of cash transactions.

--Two of the disbursing centers were not canceling checks held past the maximum retention periods.

We also believe there are weaknesses in Treasury's inventory procedures for controlling returned checks. As allowed by Treasury's Procedures Manual, the disbursing centers were not counting returned checks until after they were processed through a conditioning machine if mutilated, coded as to reason for return, and sorted by major classes of payment. This count was made primarily to develop workload data rather than control check inventory while processing.

The internal controls needed to correct the weaknesses noted above would be reduced if Treasury used automatic check cancellation procedures for all returned checks.

## IMPROVED CONTROLS NEEDED TO SAFEGUARD SOCIAL SECURITY CHECKS WITHDRAWN FROM DELIVERY

Each month the Social Security Administration (SSA) asks Treasury to prepare checks in advance of the issue date because of the large volume of payments to social security recipients. During the month, some checks are withdrawn before the mailing date at the request of SSA.

Treasury's Division of Disbursement Manual (part V, sec. 5240) permits these checks to be held by Treasury until the check issuance date, when the checks are canceled. At two of the disbursing centers, from July 1975 though February 1976 about 1 million SSA checks, amounting to about $240 million, had been prepared in advance of the issuance date and later withdrawn from delivery. The withdrawn checks are usually held from the time SSA requests withdrawal until the check issuance date, usually at the beginning of the following month. These checks are held until the issuance date for accountability purposes, but they do not have to remain negotiable.

Two of the disbursing centers issued SSA checks but did not keep a detailed inventory of the checks on hand other than a total count. A list was not made until the checks were to be canceled. These checks, which were preprinted, predated, and negotiable, were stored in open trays, accessible to anyone allowed in the area.

We believe that Treasury could greatly reduce the potential for misuse of these checks by canceling them as soon as practical after they are withdrawn.

## CONCLUSIONS AND RECOMMENDATIONS

Treasury needs to strengthen its present controls over undeliverable checks to minimize the possibility of errors and irregularities. Present procedures do not provide for adequate control over the inventory of returned checks while they are in processing, and the established control procedures are not always followed.

Treasury's problems in controlling returned checks could be minimized if such checks were canceled shortly after receipt. By agreement, Treasury automatically cancels returned checks that were issued for some Federal agencies shortly after receipt and credits the agency's appropriation or fund account. Since less than 2 percent of all returned checks are currently being remailed, we believe the automatic cancellation procedures should be extended to returned checks issued for all Federal agencies. The 2 percent of checks usually remailed could be reissued under newly approved payment vouchers.

SSA checks withdrawn from delivery should be rendered nonnegotiable when withdrawn, rather than at the beginning of each month when they are canceled and credited back to the SSA Trust Fund cash account. The automatic cancellation of returned checks and timely defacing of withdrawn checks would eliminate a need for retention and custody of negotiable checks and thus reduce the need for extensive improvements in control.

We recommend, therefore, that you instruct the Commissioner of Treasury's Bureau of Government Financial Operations to:

--Change the Treasury Fiscal Requirements Manual (ch. 7000) to provide for cancellation of returned checks upon receipt by Treasury and to continue notifying Federal agencies when their returned checks are canceled. Treasury should advise all Federal agencies of this change.

--Require the Division of Disbursement to render SSA checks withdrawn from delivery nonnegotiable as soon as practical after they are withdrawn.

--Make sure that the Division of Disbursement improves controls over returned and withdrawn checks that are still negotiable by (1) adequately separating duties of employees processing checks, (2) restricting access to checks to those who have a need to handle them, and (3) maintaining proper accountability over the checks. Treasury should study the costs of improved controls needed for each disbursing center and the benefits derived to determine the extent that controls should be implemented.

## AGENCY COMMENTS AND OUR EVALUATION

Treasury officials agreed that cancellation of returned checks upon receipt by Treasury disbursing centers would be beneficial. They said, however, that some Federal agencies might not agree to immediate cancellation because there might be substantial delays in reissuing checks due the payees. They also said all returned checks should not be automatically canceled because sometimes unique situations develop in which it would be beneficial to hold the returned checks for a while. As an example they cited returned checks for small amounts that are likely to be remailed, such as the $50 checks issued under the Tax Reduction Act of 1975.

We recognize the desirability of holding some checks for a while after they are returned but believe this could be authorized on an exception basis. Moreover, in view of the small number of checks being remailed, few checks would need to be held for remailing.

Treasury officials agreed with our recommendation related to SSA checks that are withdrawn, and they have instructed the disbursing centers to render the checks nonnegotiable as soon as they verify that the correct check has been withdrawn.

Treasury officials also generally agreed to act on our recommendations to correct weaknesses in controls over uncanceled checks. But, they opposed changes to procedures controlling inventories of returned checks that would require counts of checks as soon as they are received by the disbursing centers. They believed that much time would be lost attempting to investigate the differences between the counts of checks received and actually processed. We believe the time required to investigate differences would be substantial only if personnel are careless in counting and handling returned checks. If they are, the count we are suggesting is needed to reveal the extent of the problem and to provide safeguards against checks being lost or stolen.

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As you know, section 236 of the Legislative Reorganization Act of 1970 requires the head of a Federal agency to submit a written statement on actions taken on our recommendations to the House and Senate Committees on Government Operations not later than 60 days after the date of the report and to the House and Senate Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of the report.

We are sending copies of this report to the Senate and House Committees on Appropriations and Government Operations; the Director, Office of Management and Budget; the Commissioner, Treasury's Bureau of Government Financial Operations; and Treasury's Office of Audit.

We appreciate the courtesies and cooperation extended our representatives. We would like to receive your comments and advice on any action taken or planned on the matters discussed in this report.

Sincerely yours,

D. L. Scantlebury

D. L. Scantlebury
Director