

DOCUMENT RESUME

01969 - [A1252236]

[Centralized Subsystem for Paying Officers in the Commissioned Corps of the Public Health Service]. FGMSD-77-23; B-164031. May 3, 1977. 14 pp.

Report to Joseph Califano, Secretary, Department of Health, Education, and Welfare; by D. L. Scantlebury, Director, Financial and General Management Studies Div.

Issue Area: Personnel Management and Compensation (300).
Contact: Financial and General Management Studies Div.
Budget Function: General Government: Central Personnel Management (805).

Organization Concerned: Public Health Service.

Authority: (P.L. 90-207; 37 U.S.C. 313). (P.L. 93-274; 37 U.S.C. 313(e)). 6 GAO 7. 6 GAO 15. 6 GAO 9. 6 GAO 4.

The subsystem of the centralized payroll system for paying officers of the PHS Commissioned Corps was reviewed, and the adequacy of system controls that check whether paychecks are issued correctly and promptly to Corps officers were evaluated. The actions taken on recommendations in audit reports issued since 1969 on the centralized payroll operation were noted. Findings/Conclusions: HEW needs to improve its payroll system for the Corps to comply with standards established in the GAO Policy and Procedures Manual for Guidance of Federal Agencies. The internal controls over the Corps' payroll operations were inadequate because the operating procedures in the payroll manual were neither current nor complete; payroll data were processed without adequate controls to insure accuracy and completeness; and duties were not properly separated to reduce opportunities for fraudulent or irregular acts. Recommendations: The Secretary of HEW should provide adequate internal controls over operations; fully implement controls to prevent unauthorized payments under automatic check processing procedures; pay housing and other living allowances on the basis of current rates; collect debts due from Corps officers promptly; and evaluate the eligibility of officers to receive special retention bonuses on a case-by-case basis until appropriate eligibility criteria are established. (SC)

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

DIVISION OF FINANCIAL AND
GENERAL MANAGEMENT STUDIES

MAY 3 1977

B-164031

The Honorable
The Secretary of Health,
Education, and welfare

Dear Mr. Secretary:

This report is the third of a series on our review of the Department of Health, Education, and welfare's (HEW's) centralized payroll system. It presents our review of the subsystem for paying officers in the Commissioned Corps of the Public Health Service, one of the uniformed services of the United States. The review was made at HEW's Division of Central Payroll in Washington, D.C., and the Public Health Service's Claims Office and its Commissioned Personnel Operations Division, both in Rockville, Maryland.

The Corps' payroll amounted to about \$191 million in calendar year 1976 for approximately 7,800 active and inactive military officers. The Corps is organized along military lines, with its officers holding military rank and receiving pay similar to their counterparts in the Department of Defense. Many Corps officers are physicians and dentists who are assigned to public health facilities in the United States and U.S. health facilities in foreign countries.

Section 112(b) of the Budget and Accounting Procedures Act of 1950 provides for executive agencies' accounting systems to be approved by the Comptroller General. HEW's statement of principles and standards for its accounting systems was approved in April 1970. HEW plans to submit the centralized payroll system design for approval in June 1979.

As a part of our review, we evaluated the adequacy of system controls to make sure that paychecks were being issued correctly and promptly to Corps officers. We also examined actions by HEW on recommendations in audit reports issued since 1969 on the centralized payroll operation. The recommendations were made in reports by us, HEW's Audit Agency, and a special interagency payroll review panel convened by HEW.

As discussed in detail in the following sections of this report, HEW needs to improve its payroll system for the Corps to comply with standards established in our Policy and Procedures Manual for Guidance of Federal Agencies. We recommend that you:

- Provide adequate internal controls over payroll operations to help insure that only authorized and accurate payments are made.
- Fully implement controls to prevent unauthorized payments under automatic check processing procedures.
- Pay housing and other living allowances on the basis of current rates.
- Collect debts due from Corps officers promptly.
- Evaluate eligibility of officers to receive special retention bonuses on a case-by-case basis until appropriate eligibility criteria is established.

We are also recommending that you have the Assistant Secretary for Management and Budget and the Assistant Secretary for Health monitor the implementation of our recommendations.

NEED TO IMPROVE INTERNAL CONTROLS OVER PAYROLL OPERATIONS

HEW's internal controls over the Corps' payroll operation were inadequate because:

- The operating procedures in the payroll manual were neither current nor complete.
- Payroll data was processed without adequate controls to insure its accuracy and completeness.
- Duties were not properly separated to reduce opportunities for fraudulent or irregular acts.

Operating procedures need to be formalized

Our Policy and Procedures Manual for Guidance of Federal Agencies (6 GAO 7) states:

"The publication of agency policies and procedures in manual form and the proper maintenance thereof are necessary to guide the individuals responsible for carrying out the day-to-day activities in a uniform and systematic manner. A properly prepared and currently maintained policy and procedures manual serves as a guide to which the actual operations may be compared to detect departures from prescribed requirements."

Central payroll needed to update its procedures manual for the Corps' payroll to comply with our standards. Specifically:

- The manual was dated August 1969 and numerous changes occurring since then have not been incorporated. For example, a form for 18 types of payroll actions was discontinued in 1974 but the manual did not show this change.
- Procedures for processing pay error notices were not included. We estimate that the Corps' payroll receives over 1,200 such notices annually.
- Guidance was not included for the circumstances under which paychecks could be processed outside the automated payroll system. We noted that, during a 2-month period, about 260 paychecks amounting to about \$1.4 million were processed outside the system.

We did not establish the extent to which the above conditions contributed to payroll errors. Generally, however, the absence of written procedures and guidance for payroll operations creates an environment where errors can occur and remain undetected for extended periods. Moreover, the condition complicates, and sometimes even precludes, identifying the causes of errors, because the correct way to process transactions is not documented. Furthermore, it negates the usefulness of the manual as an effective on-the-job training aid.

Greater control needed over documents affecting employees pay

Our Policy and Procedures Manual for Guidance of Federal Agencies (6 GAO 15) requires applying systematic procedures to control documents containing information entered

into a computerized system to calculate employees' pay. Such control procedures are necessary to reduce the potential for

- loss or addition of documents during processing and
- undetected errors or irregularities in data entered into the automated payroll system.

We noted that the Corps' payroll did not include record count controls (i.e., a comparison of the number of documents submitted for processing with the number actually processed). For example, Corps payroll used a private contractor to key-punch information from documents into machine-readable form and, although the documents were counted before being sent to the contractor, they were not counted when returned. As a result, there are no assurances that documents affecting employees' pay have not been lost or added during processing.

The Corps' payroll operator also did not use predetermined control totals, which normally supplement the control provided by record counts. In using this control, arithmetic totals are taken for selected data on input documents, such as hours worked and pay rates, before processing is started. During computer processing, corresponding totals are independently accumulated by the computer for comparison with the predetermined totals. If the totals are not equal, payroll officials (1) are immediately alerted that data was either not processed or processed incorrectly and (2) can take corrective action before erroneous payments are made.

Since 1957 we have instructed agencies to use predetermined control totals in automated payroll systems to control the accuracy of input for hours worked and rates of pay. Such controls would be particularly useful to detect instances where quantitative pay data is improperly recorded. For example, predetermined control totals could have readily detected instances in fiscal year 1976 where leave balances for commissioned officers were improperly recorded. Without the controls, this problem was not detected until employees complained about their recorded leave balances.

Predetermined control totals would be extremely useful for monitoring the accuracy of the services of the keypunch contractors. For example, contractors keypunch data to correct prior errors in pay records. Payroll clerks often use a special color to designate negative amounts on documents. According to central payroll officials, the contractor often does not record such amounts correctly and,

as a result, the original error is compounded. The use of predetermined control totals would detect such errors in time for central payroll to take corrective action to prevent resultant erroneous payments.

The effectiveness of a payroll system is dependent on using complete and accurate data. Because record counts and predetermined totals are sound methods of controlling data inputs, we believe HEW should include these controls in the Corps' payroll operation.

Need for separation of payroll duties

Our Policy and Procedures Manual for Guidance of Federal Agencies (6 GAO 9) states:

"The separation of duties relating to pay, leave, and allowances should assure that no one person performs all phases of a transaction from beginning to end without the intervention of some other person or persons who afford a cross-check. Such separation of duties provides a check on the accuracy of the work and substantially reduces the opportunity to commit fraudulent or other irregular acts."

The Corps' organization of its payroll operation did not provide adequate separation of duties. Payroll clerks processed changes to employees' pay based on data in personnel orders received from the Corps personnel office. Each clerk handled all orders for an assigned group of officers without verification or review by others. For example, when orders were received, the assigned payroll clerk:

- Determined pay, allowance, and withholding information needed for pay computation.
- Prepared source documents for keypunching the data into machine-readable form.
- Reviewed error messages from computer processing and prepared source documents to correct errors.
- Maintained records indicating whether the data on source documents, including those correcting errors, was processed correctly.

Allowing a payroll clerk to do all of the above steps would permit a payroll clerk to (1) add a fictitious employee

to the payroll, (2) process a lump sum leave payment differing from the entitled amount, or (3) pay employees allowances to which they are not entitled.

Conclusions and recommendations

A large automated payroll system primarily relies on its internal control features to insure that entitled employees are paid accurately and promptly. Central payroll's system of control, however, cannot be relied upon because it lacks adequate controls over payroll documents and proper separation of duties. As a result, the potential exists that unauthorized or inaccurate payments could be made and not detected. Furthermore, because the system has not been adequately documented, it is difficult to determine the correct procedures and methods for performing payroll operations.

Therefore, we recommend that you instruct the Director, Division of Central Payroll, to:

- Develop clear and comprehensive procedures to cover all payroll activities and incorporate such procedures into the payroll manual.
- Use record counts and predetermined control totals to help insure that documents are processed completely and accurately.
- Reassign payroll duties so that one employee is not responsible for both (1) initiating payroll data input and (2) reviewing and handling the records related to such transactions.

Agency comments

Central payroll officials agreed with our findings and indicated that they would implement our recommendations, except the one related to predetermined control totals. The Director, Division of Central Payroll, said that additional internal review might serve his division's control requirements better.

We recognize the advantages of internal reviews, but believe that predetermined control totals are a more economical method of disclosing errors in quantitative data. Further, the predetermined control totals would alert officials to errors soon after they occur, while internal reviews

would not alert management as quickly. Therefore, we believe that additional internal reviews are not an adequate substitute for using predetermined control totals that we are proposing.

NEED TO FULLY IMPLEMENT CONTROLS
OVER AUTOMATIC PAYCHECK PROCESSING

At the beginning of our review, the Corps was using an exception-type system to pay its officers. Paychecks were automatically issued to each active officer for a full month's pay, and special actions were required to keep such checks from being issued to officers not entitled to pay. The Corps had devised controls to alert payroll personnel when the special action was required. The controls, however, were not fully implemented at the completion of our review and, as a result, paychecks could have been issued to officers not entitled to pay.

In our prior report on HEW's payroll system (B-164031, Jan. 17, 1969), we discussed the disadvantages of using an exception-type payroll system. The report discussed the system's potential to issue checks to employees not entitled to pay. Examples of overpayments attributable to the system were discussed, including cases where five inactive Corps officers received paychecks for periods when they were not entitled to pay. The paychecks, amounting to \$7,411, were cashed by the officers.

We suggested that HEW abandon the exception-type system and adopt a system requiring positive input as a basis for issuing paychecks. In responding to our report, HEW agreed and said that the system would be changed to require a time and attendance report as the basis for issuing paychecks. This requirement for issuing paychecks was also incorporated into chapter 29 of the Corps' personnel manual.

In our latest review, however, we noted that monthly checks were still being issued automatically to Corps officers. HEW officials said the payroll system was changed to require positive inputs from time and attendance reports before paychecks could be issued, but that the Corps, like other military services, did not always have timekeepers at duty stations, especially those in remote locations. Time and attendance reports were said to be frequently late, which would have resulted in late deliveries of paychecks to officers. According to HEW officials, they decided to bypass the control requiring positive inputs

from time and attendance reports and to issue checks automatically.

There are circumstances, particularly in the military services, where difficulty in obtaining positive time and attendance reports dictates use of exception-type pay systems. When this happens, we encourage the military services to adopt controls alerting officials to instances where paychecks were processed for personnel not entitled to pay. During our review, HEW officials said such controls were being implemented in the Corps' payroll operations. As explained by them, a principal feature of the controls was to match listings of officers to receive checks against listings of active-duty officers maintained by the Corps. HEW officials said the new controls identified officers not entitled to paychecks and stopped delivery of checks when appropriate.

We did not examine the new controls because their implementation began after our fieldwork was completed. We noted, however, that HEW had not

- documented the new control procedures in the Corps' payroll manual,
- designated the individuals responsible for control procedures, or
- established procedures for communicating nonentitlement information between payroll and personnel.

Conclusions and recommendations

HEW should formalize the controls it developed to establish whether commissioned officers are entitled to the paychecks prepared for them each pay period, providing the controls are adequate for the intended purpose. This would document that portion of the payroll system and would insure that personnel were familiar with the various control procedures they are responsible for.

Therefore, we recommend that you instruct the Director, Division of Central Payroll, in coordination with the Director, Commissioned Personnel Operations Division, to:

- Make sure procedures are adequate to prevent Corps officers from receiving paychecks to which they are not entitled, and if so, incorporate these procedures into the manual.

--Assign responsibility for the control procedures to appropriate personnel and monitor performance as necessary to insure that payments are made only to entitled commissioned officers.

Agency comments

Central payroll officials generally agreed with our findings.

NEED TO USE CURRENT RATES FOR HOUSING AND OTHER LIVING ALLOWANCES

The Corps paid its officers housing and cost-of-living allowances totaling about \$900,000 in calendar year 1976. Our Policy and Procedures Manual for Guidance of Federal Agencies (6 GAO 4) states that payroll systems should promptly pay allowances to all entitled employees, but HEW did not have procedures to promptly pay revised amounts for housing and cost-of-living. As a result, some officers entitled to the allowances have complained about receiving incorrect payments.

HEW pays the allowances to about 235 officers stationed in certain foreign countries, Alaska and Hawaii, and U.S. possessions where living expenses and housing costs are greater than those in the continental United States. The allowances are based on rates set by the Per Diem Travel and Transportation Allowance Committee, composed of officials of the military services, including the Corps. Separate rates are set for each location where allowances are paid, and such rates are revised periodically to consider changes in living expenses and housing costs.

The committee notifies personnel offices of the military services whenever it adjusts allowance rates. HEW's central payroll receives copies of the notifications which specify the date Federal agencies should start to pay the new rates. The revised rates are eventually published by the committee in the Joint Travel Regulations, but these regulations are often not changed to include the revised rates until over a month after effective dates of revisions.

Central payroll did not use the revised rates for pay purposes until after receiving the Joint Travel Regulations that contained the revised rates. Sometimes central payroll did not receive the revised regulations until 2 months after they were published, resulting in officers being underpaid

for allowances for periods ranging up to 3 months after rates were officially changed. Further, in the event of reductions in the allowance rates, overpayments to employees would have resulted. Such a long delay in paying revised allowances has been an inconvenience to officers entitled to them and has required additional effort to retroactively adjust pay over long periods.

Central payroll's manual did not have instructions for allowances to be paid on the basis of rates in the committee's initial notifications. Central payroll officials explained that, since they had not been instructed as to the purpose of the committee's notifications, they simply disregarded them.

Conclusion and recommendations

The Per Diem Travel and Transportation Committee's initial notifications provide HEW's central payroll with current information on rates authorized for paying housing and cost-of-living allowances. Because of this, we believe the rates in the notification should be used to pay such allowances and recommend that you instruct the Director, Division of Central Payroll, to:

- Make allowance payments based on the initial notification of a rate change.
- Revise the payroll manual to provide specific guidance on use of rates in initial notifications for pay purposes.

Agency comments

Central payroll officials agreed with our findings.

NEED TO BILL OFFICERS CORRECTLY FOR AMOUNTS OWED HEW

Physicians and dentists in the Corps may receive Government-subsidized training and bonus pay ^{1/} primarily as a recruiting and retention incentive. As a condition for such benefits, they must sign agreements to remain on

^{1/}The bonuses are paid under the variable incentive and continuation pay programs. For a more detailed discussion of these programs, see pages 12 and 13.

active duty for specified periods and to repay a portion of the training subsidy or bonus pay if they leave active duty before the time agreed upon. Between June 1975 and October 1976, the amount owed by inactive commissioned officers for repayment of subsidies and bonus pay increased from about \$64,000 to about \$357,000. We believe central payroll's failure to follow established HEW procedures for handling debts of inactive officers contributed considerably to this increase.

The U.S. Public Health Service Claims Office is responsible for collecting inactive officers' indebtedness. HEW procedures provide for their debts to be offset by any pay due the officers at the time they leave active duty, including amounts for accrued salaries, allowances, and leave. Under these procedures, central payroll should notify the claims office of the amounts to be offset. However, central payroll did not provide the claims office with such information on inactive officers who were indebted to HEW.

We analyzed claims and pay records for 18 inactive officers indebted to HEW. Our analysis disclosed that:

- 14 of the inactive officers were billed erroneously. The officers were asked to pay a total of \$17,670 which primarily represented the amount of recruiting and retention bonus they were required to repay. These officers, however, had accrued annual leave worth \$7,066 for which they had not been paid, and therefore, they should have been billed for only \$10,604.
- 6 officers paid the amounts erroneously billed, resulting in overpayments of \$2,869 to HEW. The overpayments had not been refunded 1 year later.
- 6 officers made no payments on the amounts erroneously billed and were later sent corrected bills.
- 2 officers failed to respond to the erroneous billings, and 1 year later they had not been sent corrected bills.

We believe the billing errors were caused because payroll clerks had not been instructed to include accrued annual leave in the amounts reported to the claims office. Also, the payroll clerks' supervisor had not reviewed

information furnished to the claims office and central payroll's procedures manual did not have instructions for reporting the indebtedness information.

Conclusions and recommendations

The procedures HEW established to compute amounts owed by inactive officers are basically sound. These procedures provide for offsetting accrued pay, allowances, and leave against debts of inactive officers. If followed, we believe they would result in accurate billings and, thus, insure more timely collections. Therefore, we recommend that you instruct the Director, Division of Central Payroll, to:

- Insure that payroll clerks are adequately supervised and instructed on proper procedures for reporting indebtedness information to the claims office and include these procedures in central payroll's manual.
- Review indebtedness information already reported to the claims office and make revisions as necessary.

Agency comments

HEW officials generally agreed with our recommendations and said that existing differences between reported and actual amounts owed by commissioned officers would be resolved.

NEED TO EVALUATE BASIS FOR PROVIDING CERTAIN DOCTORS AND DENTISTS WITH BONUS PAY

Physicians and dentists can be paid bonuses for remaining in the Corps, provided they are in a critically short speciality that has been so designated by the Secretary of HEW. A critical shortage is defined as a category in which the supply of qualified personnel is, or is projected to be, inadequate. We reported in August 1976 that the Secretary had not designated such specialities and we recommended that action be taken to do so. Although action had not been completed on our recommendations, HEW started paying bonuses to over 150 additional physicians and dentists between August 1976 and January 1977, without any apparent determination that they were serving in a critical speciality.

In calendar year 1976 HEW paid approximately \$23 million in bonuses to about 2,000 Corps physicians and dentists, including the 150 additional doctors and dentists. The

bonuses are authorized under two programs intended to enhance recruitment and retention of physicians and dentists--the continuation pay program authorized by Public Law 90-207 (37 U.S.C. 311) and the variable incentive program authorized by Public Law 93-274 (37 U.S.C. 313 (e)). The latter program was authorized as a replacement for the continuation program; thus, the medical officers are not entitled to receive pay under both programs simultaneously.

The need for the Secretary of HEW to designate the critically short specialities was discussed in our report dated August 30, 1976, "Recruiting and Retaining Federal Physicians and Dentists: Problems, Progress, and Actions Needed for the Future (HRD-76-162)." We pointed out that authorizing legislation and HEW's regulations required the Secretary to designate specialities which are critically short in the Commissioned Corps.

In the 1976 report, we also pointed out a bonus becomes an income supplement under HEW's practice of paying it to all physicians and dentists, rather than as incentive pay to recruit and retain those in critically short specialities. As HEW's practice appeared contrary to congressional intent, we recommended that the Secretary of HEW identify and adequately document the critical specialities of physicians and dentists to receive bonuses under the two income-increasing programs. We also recommended that legislative authority be sought for payments of bonuses to physicians and dentists in noncritical specialities if the Secretary decides that such payments would be needed and desirable.

As of January 1977, HEW had not completed action on these recommendations but was continuing to pay the bonus to physicians and dentists that met other eligibility requirements under the programs, such as being in a specified grade and having completed a specified amount of service. As a result, over 150 additional physicians and dentists started receiving continuation and variable incentive pay between August 1976 and January 1977 without regard to the requirement that they serve in a critical speciality.

Conclusions and recommendations

We recognize that, before action can be completed on our previous recommendation to identify and document specialities critical to the Corps' operations, decisions will be required on granting bonus pay to additional physicians and dentists to retain them. We believe that new bonus payments should be minimized and done only on a

case-by-case basis, applying criteria for critical speciality categories that are fully consistent with the bonus programs' authorizing legislation. This apparently was not done in the cases where continuation and variable incentive pay was awarded from August 1976 to January 1977.

We believe that HEW should minimize the awarding of bonus pay until it has fully met the legal requirements for designating the dental and medical specialities that are critical to the Corps' operations. Therefore, we recommend that you:

- Insure that our prior recommendation for identifying and documenting critical specialities is completed as soon as possible.
- Until action on our prior recommendation is completed, award additional bonus pay only where absolutely necessary to retain medical and dental personnel, and document on a case-by-case basis the reasons for considering an individual to have a critical speciality.

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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 Committee on Government Operations and the Senate Committee on Governmental Affairs 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 above Committees; the Director, Division of Central Payroll; and the Assistant Inspector General for Audit. We are also sending a copy to Congressman Mario Biaggi by agreement, because of his interest in HEW's payroll system.

We wish to express our appreciation for the courtesies and cooperation extended to our representatives. We would appreciate your comments and advice on any actions taken or planned on the matters discussed in this report.

Sincerely yours,


D. L. Scantlebury
Director