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BILLIONS SPENT ON "MISCELLANEOUS" EXPENDITURES: INADEQUATE CONTROLS AT THE U.S. DEPARTMENT OF VETERANS AFFAIRS

HEARING

BEFORE THE

SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS

OF THE

COMMITTEE ON VETERANS' AFFAIRS
U.S. HOUSE OF REPRESENTATIVES

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BILLIONS SPENT ON "MISCELLANEOUS" EXPENDITURES: INADEQUATE CONTROLS AT THE U.S. DEPARTMENT OF VETERANS AFFAIRS

THURSDAY, JULY 31, 2008

U.S. HOUSE OF REPRESENTATIVES,
COMMITTEE ON VETERANS' AFFAIRS,
SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS,
Washington, DC.

The Subcommittee met, pursuant to notice, at 10:00 a.m., in Room 334, Cannon House Office Building, Hon. Harry E. Mitchell [Chairman of the Subcommittee] presiding.

Present: Representatives Mitchell, Space, Walz, Rodriguez, and Bilbray.

OPENING STATEMENT OF CHAIRMAN MITCHELL

Mr. MITCHELL. Good morning and welcome to the Subcommittee on Oversight and Investigations hearing on "Billions Spent on Miscellaneous Expenditures," also entitled "Inadequate Controls at the U.S. Department of Veterans Affairs" (VA). This is July 31st and this hearing will come to order.

We are here today to examine an issue of great importance. The Department of Veterans Affairs is the second largest in the Federal Government. It is authorized to spend billions of dollars of taxpayers' money every year to care for those who bravely stepped forward to defend our Nation.

We have an obligation to ensure that the VA uses these funds appropriately and they are not lost through waste, fraud, or abuse. We must also be sure that they use adequate internal financial controls and management.

Unfortunately, the VA does not have adequate internal controls. Worse yet, is this problem is not new. VA's auditors yearly have found material weaknesses in VA's financial management systems' functionality and in financial management oversight.

We will hear from the U.S. General Accountability Office (GAO) that the VA procured billions of dollars of goods and services by ways of "miscellaneous obligations" that should not have been procured this way. Improper use of miscellaneous obligations obscures how taxpayers' money is being spent.

In addition, goods and services that should have been procured competitively can be subverted using this process.

Even when miscellaneous obligations are properly used, GAO's review disclosed significant defects in VA's internal financial controls and reporting.

For example, VA employees often fail to describe the purpose of a miscellaneous obligation or used uncertain descriptions like "third quarter invoice," which would not adequately describe its purpose to an unbiased audit.

GAO's review also disclosed serious failures in a bedrock principle of financial management, the segregation of duties. It is elementary that the person authorized to sign the checks cannot be the same person that approves the expense. In 30 out of 42 transactions that GAO looked at, VA failed to ensure the proper segregation of duties.

Just a few years ago, VA spent $350 million on a failed attempt to create a modern electronic financial system. VA has embarked on redoing that project. But even if successful, it may be many years away from completion. We cannot wait.

Even with the imperfect financial and procurement systems it has, VA must ensure compliance with basic principles of financial control.

We look forward to hearing today from VA about how it is going to do this. But before I recognize the Ranking Republican Member for his remarks, I would like to swear in our witnesses.

[The prepared statement of Chairman Mitchell appears on p. 27.]

I ask that all witnesses stand from both panels and raise their right hand.

[Witnesses sworn.]

Mr. MITCHELL. Thank you.

Next I ask unanimous consent that the Honorable Robert J. Henke, Assistant Secretary for Management for the Department of Veterans Affairs, may submit a statement for the record. Hearing no objection, so ordered.

[The prepared statement of Hon. Henke appears on p. 46.]

I now recognize Mr. Brian Bilbray for his opening remarks.

OPENING STATEMENT OF HON. BRIAN P. BILBRAY

Mr. BILBRAY. Thank you, Mr. Chairman.

Mr. Chairman, I am honored to sit in today. The Ranking Member, Ms. Brown-Waite, she has apologized for not being able to be here, but you and she have been working in a way that I think that is commendable to not only this Committee but to the entire Congress and Nation.

A bipartisan effort here I think is something that the American people would like to see more of across all the Committees in Washington, DC. And so I want to commend you for that and with working with her on that.

Let me just say that I have to apologize to the witnesses today. I read this report and I look at the category of miscellaneous obligations and I hate to say it. I guess we are all products of our experience. And all at once, I go back to 1978 when I was a 27-year-old Mayor and the auditor came in and told me that there were no checks and balances on miscellaneous expenditures. And I had to followup that with a local district attorney.

Now, I do not think anybody today is saying that there is criminal activity going on just because there seems to be some real problems with the accounting process here, but when it comes to accounting, process does matter, reporting does matter, especially when we are talking about the expenditures of the taxpayers' hard-earned money that we have forced from them to send to Washington. And we have not only a right, we have a responsibility to make sure those funds are used appropriately and within the law.

And, frankly, I am really concerned. This is probably one of the oldest issues in accounting, miscellaneous expenditures growing to such a large degree that it may even equal—you know, one account says out of twelve, $9 billion may be under that category. That is absolutely terrifying for anyone who is an accountant to think the potential for abuse is huge when there is not an appropriate accounting process.

So, Mr. Chairman, I would like to introduce into the record my opening statement. I have paraphrased. But let me just say personally I am very honored to serve with you and to fill in for the Ranking Member. And hopefully working together, the American people will be served by your bipartisan leadership.

Thank you.

[The prepared statement of Congressman Bilbray appears on p. 27.]

Mr. MITCHELL. Thank you.

Mr. Space.

Mr. SPACE. Thank you, Mr. Chairman.

I will enter a written statement for the record.

[No statement was submitted.]

Mr. MITCHELL. Mr. Rodriguez.

OPENING STATEMENT OF HON. CIRO D. RODRIGUEZ

Mr. RODRIGUEZ. Thank you, Mr. Chairman, for conducting this hearing. And there is no doubt that we need to followup—especially now that we have allocated some $13 billion additional resources for the VA. As we do that, we have to make sure we hold ourselves as well as the VA accountable to ensure those resources are expended in the best interest of our veterans out there.

So I look forward to this testimony. Thank you very much.

Mr. MITCHELL. Thank you.

I ask unanimous consent that all Members have 5 legislative days to submit a statement for the record. Hearing no objection, so ordered.

At this time, I would like to recognize Ms. Kay Daly, Acting Director of Financial Management and Assurance from the U.S. Government Accountability Office (GAO).

Ms. Daly is accompanied by Mr. Glenn Slocum, who is the Assistant Director of Financial Management and Assurance for the U.S. Government Accountability Office.

I would like to ask our witness to stay within her 5 minutes for her opening statements. And your full written statement will be entered into the record.

Thank you.

Ms. Daly, just before you begin, I am interested in your name. I have a recent record that came from Ireland, which one of the

title songs is called Katie Daly. So I just thought, and it has become one of my favorites.

STATEMENT OF KAY L. DALY, ACTING DIRECTOR, FINANCIAL MANAGEMENT AND ASSURANCE, U.S. GOVERNMENT ACCOUNTABILITY OFFICE; ACCOMPANIED BY GLENN SLOCUM, ASSISTANT DIRECTOR, FINANCIAL MANAGEMENT AND ASSURANCE, U.S. GOVERNMENT ACCOUNTABILITY OFFICE

Ms. DALY. Well, Mr. Chairman, this is my married name, but let me assure you my husband and all of his family are very Irish, and have taken many trips back to Ireland. But thank you so much.

I appreciate the opportunity, Chairman Mitchell, Congressman Bilbray, Congressman Space, and Congressman Rodriguez for the opportunity to discuss the Veterans Health Administration's (VHA's) use of miscellaneous obligations.

Today I would like to talk about our preliminary observations on first how VA used miscellaneous obligations during fiscal year 2007 and then, second, whether VA's policies and procedures provide adequate controls over the use of miscellaneous obligations.

Now, on the first topic, VHA recorded over $6.9 billion in miscellaneous obligations during fiscal year 2007. These miscellaneous obligations were used for a variety of mission-related goods and services, things such as fee-based medical services, drugs, medicines, transportation of veterans to and from Medical Centers, and logistical support and supplies.

Now, on the second topic, the results of our audit work over the fiscal year 2007, miscellaneous obligations guidance found that VHA's policies and procedures did not provide adequate controls over the use of these transactions and without effectively designed controls, using miscellaneous obligations exposes VHA to increased risk of fraud, waste, and abuse.

Specifically, although the existing policies require contracting officials to review miscellaneous obligations, there was no guidance as to how such reviews should be carried out and documented.

With regard to segregation of duties, the policies and procedures for miscellaneous obligations did not prevent one individual from being able to perform multiple tasks in authorizing and executing the obligations.

Finally, regarding documentation, VA's guidance did not require that key pieces of information be included on the authorization form.

Now, collectively, these systemic control design flaws were identified in the case studies that we conducted at three different VHA locations.

[Chart shown.]

As shown in the table here, and I believe you have a copy available to you, there was a lack of documented oversight by contracting officials in all of the 42 case studies that we examined. We also found inadequate segregation of duties in 30 of the 42 cases.

Also, supporting documentation was not complete in many of the cases. For example, the purpose field lacked crucial descriptive information and in many cases, the vendor name and contract number were also not provided.

Now, VHA has recently issued new guidance on the use of miscellaneous obligations that does offer some improvements, but it did not fully address the specific control design flaws that we identified.

And without basic controls over the billions of dollars that VHA is spending in miscellaneous obligations, VA is at significant risk of fraud, waste, and abuse. Effectively designed internal controls act as the first line of defense for preventing and detecting fraud and help to ensure that an agency meets its missions and goals, complies with laws and regulations, and provides reliable financial information on its programs and operations.

To help VA improve the design of its controls, we will be issuing a related report in this area with specific recommendations for a number of actions that VA could take to implement effective controls in these areas.

So with that, Chairman Mitchell, Congressman Bilbray, Congressman Space, and Congressman Rodriguez, this will complete my prepared statement.

But I would like to thank you for holding this hearing today because it helps shine a light on the internal control weaknesses at VA and helps spur activity in this area.

So I thank you for doing that. And with that, I would be glad to take any questions you might have.

[The prepared statement of Ms. Daly appears on p. 28.]

Mr. MITCHELL. Thank you.

I have a couple questions. The VA's September 29th, 2006, policy required the review of miscellaneous obligations by contracting officials to ensure their proper use. VA's supporting procedures did not detail how such reviews should be carried out.

And the question is, what recommendation do you have for VA that could improve controls in this area?

Ms. DALY. Well, our draft report contains a recommendation that VA implement policies and procedures to improve contracting oversight in this area. And I think this is very important because contracting officials help ensure that the contracts will be in accordance with laws and regulations, important laws that have been passed to help ensure competition in the contracting processes, and that the Economy Act and the Federal Acquisition Regulations are followed.

And with that, I think it is also important to recognize that in their May guidance that VHA issued, they have now required that these reviews be documented. And I think that is an important first step. There will be additional steps needed. And I think the critical one is going to be that there is monitoring to ensure these contracting steps are taken.

Mr. MITCHELL. Thank you.

And regarding the area of segregation of duties, the miscellaneous obligation automated system and associated policies and procedures were not designed to prevent a single official from performing multiple roles in the process of authorizing and executing miscellaneous obligations.

What is the risk of fraud, waste, and abuse in the VA by one person performing multiple roles and approving and obligating funds?

Ms. DALY. Chairman Mitchell, I think this places VA at a significant risk for fraud, waste, and abuse. One of the key tenets of internal controls is that one person should not control all aspects of a transaction. To do so does place unnecessary risk on that transaction, that the funds would be subverted for purposes other than that intended by the Congress and that the taxpayers were hoping when they sent their funds to Washington.

I think it is important that VA continue to develop processes that will address this issue. In particular, we saw that control point officials, which are the key officials in the VA Medical Centers that are doing the transactions, typically have the authority to request a transaction and approve that transaction and also certify payment in the end.

Mr. MITCHELL. And one last question before my time expires. In its review of a limited number of transactions that you did, GAO did not find any clear examples of fraud or waste or abuse. Nonetheless, you are adamant that VA needs to take immediate action to remedy the control deficiencies that you identified.

Why is that your adamant position?

Ms. DALY. Well, again, Congressman Mitchell, I think it is a matter of risk that VA has assumed here that is more than is necessary. I think that these systems have grown up over time, but it is important that VA is now recognizing that things need to change. Taxpayer dollars are at risk by having a lax control environment. And so to implement new controls to address this will protect our taxpayer dollars.

Mr. MITCHELL. Thank you very much.

And, Mr. Bilbray.

Mr. BILBRAY. Ms. Daly, is it not true that without the segregated duties, there are no checks and balances in reality? One person can make the call and either do a great job or do a terrible job?

Ms. DALY. Well, Congressman Bilbray, I agree that it certainly increases the risk that an unscrupulous employee could use the funds for purposes other than that intended.

Mr. BILBRAY. In fact, historically I think that this kind of one person control has shown that it does not happen overnight. It happens to be something that is slipped into a little bit. It does not make any difference. No one is there to call him down on a little mistake or a little transgression. And slowly but surely the problem builds and grows until it becomes a horrendous problem.

My question is, do you have any idea how long this structure has existed?

Ms. DALY. Well, I cannot give you a definitive answer on that, Congressman Bilbray. You know, our focus was really just on the 2007 transactions, but VA officials have provided us information indicating that the system goes back to the 1940s. But it is not clear, so I could try to get back to you with that information.

Mr. BILBRAY. I mean, again, it is all our responsibilities to make sure the system serves the public and that means that sometimes individuals may make mistakes, but we should make sure that the system minimizes that potential.

Out of 42 reviews, 30 of them or only 12 of them had what you felt was segregated oversight.

Ms. DALY. Right.

Mr. BILBRAY. That is a pretty substantial number when you get down there. And I would have to say that even with my less than stellar academic achievement of the past, that is not a passing grade for the process.

Ms. DALY. Exactly.

Mr. BILBRAY. And so I appreciate it.

And, Mr. Chairman, I will yield back. I look forward to hearing more testimony.

Mr. MITCHELL. Thank you.

Mr. Space.

Mr. SPACE. Thank you, Mr. Chairman.

Ms. Daly, how are you today? Thank you for joining us and providing your testimony and the work that you have prepared in advance.

When was this audit conducted? What were the dates?

Ms. DALY. We started our work in approximately November of 2007 and are continuing to wrap it up now. Our draft report is over at VA for comment and we hope to have it fully issued in September of this year.

Mr. SPACE. What was the impetus or genesis of the audit? Why was it done?

Ms. DALY. Well, the start of the audit was the staff at VA came over and briefed the Committee here and informed them about the use of miscellaneous obligations. Therefore, the Chairman and Ranking Minority Member asked that GAO conduct a study into this area.

Mr. SPACE. Right. And when was the last audit conducted by the GAO of the VHA miscellaneous expenditure system?

Ms. DALY. Congressman, I am not sure that it has ever been done before to tell you the truth. I am not aware of any prior studies in this area.

Mr. SPACE. Okay. And when were your reports or findings delivered to the VHA?

Ms. DALY. We provided a copy of our report July 17th, I believe.

Mr. SPACE. Okay. And your audit was confined to the VHA, not the entire Veterans Administration, other departments; is that correct?

Ms. DALY. That is correct.

Mr. SPACE. Do you have any kind of estimation or idea as to the nature of whether these miscellaneous expenditure auditing deficiencies exist in other departments within the VA?

Ms. DALY. Well, Congressman, I am sorry, but I cannot speak to that simply because our review focused just on what was happening at VHA.

Mr. SPACE. I understand from your testimony and from the report that the VHA has taken steps, but it appears to me that you are not satisfied with them.

Ms. DALY. Well, I think that is close to a fair approximation of our assessment of their steps to date. You know, they have taken important first steps in that they issued new guidance that address some of the issues that we have brought out regarding contracting reviews over these transactions. They now are requiring that a review be—they have always required that a review be performed, but from what we saw, it was not being performed.

Mr. SPACE. And the principal problem would be the failure to fully address the need for segregation and oversight?

Ms. DALY. That is correct. There is still a need for those issues to be addressed and I am looking forward to seeing how VA plans to address those. Their May 2008 guidance did not fully address that issue, so we think that is an important area to still be covered.

Mr. SPACE. I guess I am curious as to where we go from here and your recommendations on what this Subcommittee can do to ensure that those deficiencies are corrected in a timely fashion.

Ms. DALY. Well, as always, the Congress provides an important oversight function to help ensure that agencies do what they promise they are going to do. And we stand ready to help you in that endeavor in any way you would like.

Mr. SPACE. Is there a follow-up audit scheduled? Do you intend to look at this again in 6 months, 9 months, a year?

Ms. DALY. Well, we would leave that to the Committee's discretion. We would be glad to followup if you would like us to.

Mr. SPACE. Thank you very much.

Ms. DALY. You are welcome.

Mr. SPACE. I yield back.

Mr. MITCHELL. Thank you.

Mr. Rodriguez.

Mr. RODRIGUEZ. Thank you, Mr. Chairman.

Let me ask you, in followup on the questions that have been asked, what do you recommend that we do to make sure we stay on top of it knowing full well that there is a large amount of resources going to the agency.

I also know that sometimes externally it is difficult for them to move because if they have been doing this for some time on their own, you almost need an external group to come in.

What are some of the recommendations that your agency can come up with that would allow those of us who are not accountants to exert our oversight responsibility?

Ms. DALY. Congressman Rodriguez, I think it is important first for VA to implement a monitoring mechanism internally to make sure that the new policy and guidance, that it has come out with on contracting oversight and the documentation requirements to monitor that and ensure that those steps are indeed taken. You know, it is one thing to issue a policy. It is something else entirely to make sure it is implemented.

So a good step will be to ensure that those things are being covered internally. Secondly, I think the oversight by the Congress is an important tool to be used to help ensure that the agency is taking the actions that it has agreed to take. And we stand ready to help you in that area.

Mr. RODRIGUEZ. Okay. Let me ask that question again.

Ms. DALY. Okay.

Mr. RODRIGUEZ. Not being an accountant, not being an economist, you see a situation such as that. You are saying to allow them to come forward with recommendations.

Are there some specific items? Do they allow an opportunity for whistle blowing, for example? Have you had any opportunity to be able to get people there to talk to you about the possibility that

fraud has existed or waste has existed as a result of just having one individual overseeing an operation versus being more open?

Ms. DALY. Congressman Rodriguez, we have not had any whistle blower complaints related to this on GAO's hotline. We do have a hotline where anyone can call in and give us tips on issues just like you talked about. I think the Inspector General (IG) of VA also has a similar hotline where people can call in whether they are VA employees or not.

Mr. RODRIGUEZ. And have you had access to those?

Ms. DALY. We have not accessed those ourselves, sir, as part of this study.

Mr. RODRIGUEZ. Okay. And what does it take for you to have to get access to that?

Ms. DALY. I think it would just be a matter of making certain inquiries to the people who do have responsibility over those hotlines.

Mr. RODRIGUEZ. Because a lot of times the best source is the people themselves. They will tell you what is wrong, you know. Sometimes there might be just complaints and gripes, those kind of things. But a lot of times, that might be a way of getting a good handle on it.

What kind of time table are we talking about that, you are allowing the system to have in order to come back and try to correct itself because you are talking about almost two-thirds of the system having some serious problems when you talk about 12 out of 40; is that correct?

Ms. DALY. That is correct, sir, that there are some serious problems with their controls. And I think an organization as large as VA and VHA in particular that we focused on in this review will take some time to be fixed, but I think it is important that VA move quickly in this area to mitigate its risk.

Mr. RODRIGUEZ. What do you mean by quickly?

Ms. DALY. Well, it is going to——

Mr. RODRIGUEZ. What is appropriate?

Ms. DALY. That is a difficult question to answer, sir, because it is going to vary depending upon the circumstances.

I think the policy guidance is something that could be done much more quickly than making sure that it is fully implemented throughout VA, which is the critical step. You know, you can issue guidance, but having it implemented is the challenging part.

Mr. RODRIGUEZ. What kind of report should we ask for from you that would allow us to get a better grip on this issue so that we can make sure we hold the system accountable in being responsive to the constituency?

Ms. DALY. Well, I would be glad to work with you and any other Members of the Committee in crafting such a request for our services and that we could be doing that as soon as the hearing is over.

Mr. RODRIGUEZ. Okay. And, once again, any indication of somewhat of a time table that gives us an opportunity to oversee this situation, that we should expect something by when?

Ms. DALY. Like I said, that is challenging. I would think that certain things could be done more quickly than others. I would probably ask VA what they think might be a reasonable time table and then make an assessment from there.

Mr. RODRIGUEZ. Okay. Thank you.

Ms. DALY. You are welcome. Thank you.

Mr. MITCHELL. Thank you.

Mr. BILBRAY. Mr. Chairman, just a followup on Mr. Rodriguez.

Mr. MITCHELL. Yes.

Mr. BILBRAY. I think one of the things we know, though, is so much with this is unlike a lot of other problems we may have with operations going awry. The whistle blower usually does not help on this because no one knows.

It is much like the case I had in my city and that DC just had where money was going in, but nobody was checking, so there was no way for another party to know what was going on because the system was not there.

Now, Ms. Daly, is it not true, though, that when we go to segregating the services, it is not enough just to go to two people checking out, that you really want to go to three so you almost square the check and that the security of three is mega times over what a two-person check off point?

So is that not one of those things that we should be aiming for in an appropriate system?

Ms. DALY. Well, Congressman Bilbray, I think you made an important point there. Of course, the gold standard in a four-step process that we have here would be all four steps being segregated. But there are certainly mitigating controls that you can put in place to make sure that things are being done to the standards that really provide the safety for these funds that are needed.

Mr. BILBRAY. And getting back to exactly what Mr. Rodriguez was saying, what can we do now, and what can this Administration do, and this Committee do working with the Administration to make sure that in January we have a system that is accountable to the taxpayers?

Ms. DALY. Well, I think continuing to provide oversight in this area is an exceptionally important point. It often takes a series of steps in order to ensure that steps are taken by agencies to move them forward.

I am very impressed that they are planning to do some monitoring activities over this internally, but with the Congress continuing to provide oversight, continuing to ask them to move forward, continuing to provide accountability from these officials will be a critical step too.

Mr. BILBRAY. But we need to have a minimum standard they modify to be able—the procedure that is appropriate in modern day accounting, not 1940 models.

Thank you very much.

Ms. DALY. Thank you.

Mr. MITCHELL. Thank you.

Mr. Walz.

Mr. WALZ. No questions, Mr. Chairman.

Mr. MITCHELL. Well, thank you very much. I appreciate it. And hopefully we will be working together much longer than this short period of time we have had so far. So thank you.

Ms. DALY. Thank you.

Mr. MITCHELL. I would like to welcome panel number two to the witness table.

At this time, I would like to recognize Mr. Edward Murray, Deputy Assistant Secretary for Finance and the Deputy Chief Financial Officer for the Department of Veterans Affairs.

Mr. Murray is accompanied by Mr. Frederick Downs, Jr., Chief Prosthetics and Clinical Logistics Officer for the Veterans Health Administration; Mr. W. Paul Kearns, Chief Financial Officer (CFO) for the Veterans Health Administration; Mr. Jan Frye, Deputy Assistant Secretary for Acquisition and Logistics and Senior Procurement Executive for the Department of Veterans Affairs; and Ms. Phillipa Anderson, Assistant General Counsel for the Department of Veterans Affairs.

And I would like to recognize Mr. Murray for up to 5 minutes.

STATEMENT OF EDWARD J. MURRAY, DEPUTY ASSISTANT SECRETARY FOR FINANCE, DEPUTY CHIEF FINANCIAL OFFICER, OFFICE OF MANAGEMENT, PRESENTING STATEMENT OF HON. ROBERT J. HENKE, ASSISTANT SECRETARY FOR MANAGEMENT, U.S. DEPARTMENT OF VETERANS AFFAIRS; ACCOMPANIED BY FREDERICK DOWNS JR., CHIEF PROSTHETICS AND CLINICAL LOGISTICS OFFICER, VETERANS HEALTH ADMINISTRATION, U.S. DEPARTMENT OF VETERANS AFFAIRS; W. PAUL KEARNS III, CHIEF FINANCIAL OFFICER, VETERANS HEALTH ADMINISTRATION, U.S. DEPARTMENT OF VETERANS AFFAIRS; JAN R. FRYE, DEPUTY ASSISTANT SECRETARY FOR ACQUISITION AND LOGISTICS, OFFICE OF MANAGEMENT, U.S. DEPARTMENT OF VETERANS AFFAIRS; AND PHILLIPA ANDERSON, ASSISTANT GENERAL COUNSEL, OFFICE OF GENERAL COUNSEL, U.S. DEPARTMENT OF VETERANS AFFAIRS

Mr. MURRAY. Mr. Chairman and Members of this Subcommittee, good morning. Thank you for the opportunity to discuss the draft Government Accountability Office report entitled, "Veterans Health Administration Improvements Needed and Design of Control Over Miscellaneous Obligations."

I am Edward Murray, VA's Deputy Assistant Secretary for Finance. I also serve as VA's Deputy Chief Financial Officer. I am here on behalf of Robert Henke, VA's Assistant Secretary for Management, who was not available to appear today.

I am accompanied by Mr. Frederick Downs, Chief Prosthetic and Clinical Logistics Officer in the Veterans Health Administration; Mr. Paul Kearns, Chief Financial Officer, Veterans Health Administration; Mr. Jan Frye, Deputy Assistant Secretary for Acquisition and Logistics and VA's Senior Procurement Executive; and Ms. Phillipa Anderson, Assistant General Counsel.

I have Mr. Henke's written statement which I would like to submit for the record.

I appreciate the opportunity to discuss the draft GAO report. Although in the draft report GAO found that VA policies and procedures were not adequately designed, it is important to note that GAO identified no incidents of waste, fraud, or abuse.

Our leadership is committed to improving the guidance, oversight, and business processes associated with the use of miscellaneous obligations and the delivery of service to our Nation's veterans.

This week, your staff met with me and VA staff to observe the steps VA is taking to reduce any vulnerability. VA agrees with all four of GAO's recommendations and we are prepared to discuss the various initiatives planned or underway to reduce the use of miscellaneous obligations and associated internal control risks.

We are issuing additional Departmental policy and guidance that will improve accountability of the miscellaneous obligations process. We have reports that enable us to track the improvements.

Interim guidance was issued in January 2008 and was further refined in May 2008 by the Veterans Health Administration because the Veterans Health Administration is the predominant user of this method of financial obligation.

The Office of General Counsel has reviewed the interim guidance and has determined that the new guidelines coupled with existing VA accounting policy meet legal recording requirements.

New requirements for miscellaneous obligations will be routed for review by the appropriate contracting official and this review will be documented and included in the record for the obligation.

The interim process will be used until a system change can be made to accomplish this electronically in the Integrated Funds Distribution Control Point Activity Accounting and Procurement system, referred to as IFCAP.

In addition, we are developing requirements for a patch to IFCAP mandating population of the purpose, vendor, and contract number fields. Until this patch is installed, data must be entered manually.

Miscellaneous obligations forms are used for both procurement and nonprocurement expenditure obligations. If the miscellaneous obligation is for goods or services not required to follow formal procurement procedures, which are nonprocurement items, such as fee-basis medical or dental services, authorizations for individual patients are tracked in the FeeBasis software system.

This process includes the appropriate approval requirements by the requesting service approving official. To ensure appropriate segregation of duties, a fiscal office employee approves payment of invoices. Receipt of medical or dental services is documented by either an industry standard billing abstract document or clinical information from the non-VA provider.

If the miscellaneous obligation is for one of the procurement items approved to be documented by use of a miscellaneous obligation, such as nursing homes, separate software programs in the Veterans Health Information Systems Technology Architecture track individual expenditures and show the appropriate approval by the requesting service approving official and fiscal office employees.

The contracting officers technical representative verifies that goods and services were received for the individual contracts. Contracting officers perform all procurement duties related to award of the contract.

To ensure that policies and procedures are being implemented and monitored, VHA now tracks and trends the number and dollar amounts of funds obligated using miscellaneous obligations by Budget Object Code every month. This process enables VHA to determine whether its facilities are adhering to VA and VHA policy.

In addition, VA established the Office of Business Oversight (OBO) in 2004 to realign and consolidate existing review organizations and functions and to have oversight and compliance responsibilities at the Departmental level. OBO will review miscellaneous obligations during their field reviews with special emphasis on adherence to control policies and procedures.

VA is taking meaningful steps to resolve the current challenges concerning the use of miscellaneous obligations. VA remains committed to improving its processes and we are confident that our challenges can be overcome for the benefit of the veterans we serve as well as the taxpayers. At the end of the day, this is not about systems. It is about veterans.

This concludes my statement, Mr. Chairman. I will be happy to answer any questions that you or the other Members of the Subcommittee may have. Thank you.

[The prepared statement of Hon. Henke appears on p. 46.]

Mr. MITCHELL. Thank you.

Let me just give you a little story about my background. I was a high school teacher and at the same time, I served as Mayor of our city. And I always found it interesting. Early in the morning as a teacher, I would go into the teacher's lounge and go through the mailbox and find a statement coming from the superintendent, but I was a classroom teacher, or from the school board. And I would say, if the superintendent or the school board would ever come down here and be in the classroom, they would not make these kinds of statements.

And then in the afternoon, I went to the Mayor's Office and I thought I really had a handle on things. And I would say, and I am sure there were many people in the city say, you know, if the Mayor would ever get out of his third floor office and come down here, he would not make those kinds of statements.

What I am asking you is you can make all the statements you want here and you can put in all the reforms you want, but the question is, how do you know that these are going to be implemented where it really counts?

The people that were in these particular stations, Pittsburgh, Cheyenne, Kansas City, this was just three of what the GAO went to do. How are you going to know that it is just not going to be dismissed by the people who say, well, here comes another Directive from Washington? Let us just keep doing what we have always done. They will never come down here. How do we know what we are asking you to do is going to be implemented?

Mr. MURRAY. Starting with fiscal year 2009, the Office of Business Oversight, which works directly for the Chief Financial Officer, is going to review 70 to 80 stations. They are going to visit these field facilities and are going to put a special review emphasis in this particular area to see that we do have segregation of duties and that these miscellaneous obligation transactions are being handled appropriately. So that is going to happen at the beginning of the fiscal year.

Mr. MITCHELL. You know, I looked at the resumes of all of you that are here as a backup for your support. And you all had many years in the financial situations in different departments.

And my question is, did you come into this situation that we find in the VHA, did you not find these and other—what is being recommended are standard financial procedures, checks and balances. And from what I understand, every year Deloitte would come in and they would give an audit and every year, they showed some weaknesses in your accounting and nothing has been done.

With all your experience, do these kinds of things happen in departments you are in? Did this not flag something to you that we should be doing something different than what has been going on?

Mr. MURRAY. I believe that we are doing some things differently. In fact, Grant Thornton also in July 2007 noted some segregation of duty and other deficiencies with the use of 13 miscellaneous documents.

One of the things we have done is strengthen our policy. We are in the process of issuing Departmental level policy that requires evidence of contracting review. One of the areas I am working with the Chief Information Officer (CIO) and VHA on is that we need to make changes in the system I referred to as IFCAP.

We have to make changes such that the system enforces the control that the contracting officer does, in fact, review every 1358 or miscellaneous obligation document. And we will work closely with VHA and our CIO to prioritize changes to the IFCAP system to ensure that there is a contracting officer review.

Mr. MITCHELL. I assume that in all the agencies you have worked for, all of you, and the years of service, this is the first time this type of thing has ever happened. I just cannot believe that. I think that with your experience, somebody should have found this out before a GAO report.

One of the things that is good, and you mentioned this, that there was no fraud, waste, or abuse that has occurred, but that is not because of the system. And we do not know if we checked all of them. And it is a credit to those who are working there.

But the important thing is, as Mr. Bilbray said, this opens up the opportunity for that. And it did not take much. Just read what happened recently in the DC municipal government with the people who, and it is why whistleblowers do not work, all of the stuff that was going on in that particular situation, this can happen. And what we are doing is if there is fraud, abuse, or waste or not, as you have said, this shortchanges the services that we ought to be giving to the people this agency is designed to serve. That is the bad part.

Thank you.

Mr. Bilbray.

Mr. BILBRAY. Thank you, Mr. Chairman.

First of all, I think we need to clarify that this appears to be a situation that has been around a long time. And I guess all of us should sort of approach this, that being notified that the beautiful home you bought that was built in the 1940s that looked so great when you walked in has a foundation that has major problems.

And so if we can all approach this with the fact that this is a common problem, we are not here to point fingers at any individual, but we are willing to say this is a problem that predates all of us technically.

But now the problem seems to be the lack of a definitive approach to solving the problem, of how we are going through and restructuring the foundation of the VA so that it has a sound fiscal structure with some kind of accountable process.

Mr. Murray, you were saying that you are relieved that there was no fraud detected. Do you think 42 reviews out of 131,000 expenditures is a reasonable and confidence building review process?

Mr. MURRAY. No, I do not.

Mr. BILBRAY. Okay.

Mr. MURRAY. I do not know that it was statistically generated, but I would say probably not.

Mr. BILBRAY. Okay. I think we have just got to say let us not say, hey, nothing has been found because in reality, you scratched the surface and found enough evidence to say, wow, you know, the potential for it is so huge.

So let us not even talk about how nothing happened. Let us assume just by the nature of the system that there is so much happening and has happened since 1940 that none of us know about and we will probably never know about it.

So let us just accept there is a horrendous problem that predates our taking the responsibility. This was raised in 2003 and 2004 as a concern. Now we would like to raise it up to a major concern if not a fiscal crisis of confidence that we need to address.

And, you know, Mr. Frye, do you feel that you have adequate information on monitoring the use of these funds?

Mr. FRYE. Well, let me put it in context. With the use of 1358s, the acquisition professionals do not get involved if these are fee-basis transactions. In other words, these do not fall under the Federal Acquisition Regulation headline.

What my concern is——

Mr. BILBRAY. Do you know where miscellaneous is going? Do you know why it was going?

Mr. FRYE. I know where, if it is fee basis, I know where it is going, yes. Do I review the information on a monthly basis as to where fee basis is going, no, I do not.

Mr. BILBRAY. Yes. Who would review it or who reviews it today to see if it is appropriate?

Mr. FRYE. The VHA reviews on a monthly basis reports that they generate on the use of miscellaneous obligations out in Veterans Health Administration.

Mr. BILBRAY. How do they review it when the fact is that you end up with, you know, so much of the reporting left blank or not describing exactly what the expenditure was for?

I mean, the reporting process looks like it has just got gaping holes. You review something and you get how much money was spent, but there are whole sections in here that do not—people did not bother to say, you know, why it was done and for what reason and what the justification.

So how do you review justification if even the auditors are pointing out that the reporting sheets are not being filled out?

Mr. FRYE. Well, I would agree with you. If the forms are not filled out properly, it makes it very difficult to review it on the face of the form.

Mr. BILBRAY. Mr. Murray, my question is, there are appropriate accounting procedures and systems that the 21st century world has accepted for a long time. This is not rocket science. This is, you know, something that is just like a minimum standard for anybody that handles any funds, let alone public funds.

Are you going to have those processes online and ready to go so that we can sort of repair this foundation this year, so that 3 years from now, 5 years from now, we are not back here doing what we are doing today after being warned about this back in 2003 and 2004? Are we going to have multi review? Are we going to have at least three people being able to review any expenditure so that there is some accountability in here? Are we going to have that online ready for the next fiscal year?

Mr. MURRAY. I will work with the Veterans Health Administration staff to ensure we segregate those duties. And hopefully we will give Mr. Downs an opportunity to talk about some of what he is doing in terms of oversight and what he is proposing to do to ensure that the purpose of contract fields are filled. It is unfortunate that the IFCAP system is very archaic and to actually review the separations of duty, you have to basically touch that field facility or that Medical Center.

We do not get to work with the modern tools that industry has. We have a lot of confidence, Mr. Henke and I, that if we can get FLITE going we will have work flow, separation of duties, and audit tools embedded in our next generation financial management system.

To a great degree, we are hamstrung with the environment we have in terms of system tools. Nonetheless, Mr. Downs has a very ambitious way to do good oversight of miscellaneous obligations if he would have an opportunity to discuss it.

Mr. BILBRAY. Thank you, Mr. Chairman. I look forward to hearing from Mr. Downs whenever appropriate.

Mr. MITCHELL. Thank you.

Mr. Space.

Mr. SPACE. Thank you, Mr. Chairman.

I find myself agreeing with, I think, the implication just registered by my colleague, Mr. Bilbray, that one would have to be a fool to think that a system so full of potential for abuse has not, in fact, been abused and fraud, waste, or abuse has not occurred.

But I also think that the sampling is sufficiently large to make clear that these systemic problems are of a profound nature. And while I still find it somewhat difficult to believe that this situation has never been examined, looked at, or perhaps even considered up until the last couple of years, I am curious, and perhaps you know this and maybe you do not, upwards of $6 billion fell through this miscellaneous expenditure provision.

Do you have any knowledge of what that number would have looked like, say, 4 years ago?

Mr. MURRAY. I will have to get back to you with that number.

Mr. SPACE. Yeah. While you are at it, I would like to see what that number is for the last 20 years, each and every year.

[The following information was subsequently received from the VA:]

HVAC O&I Colloquy on Miscellaneous Obligations

During the July 31, 2008 House Veterans' Affairs Oversight and Investigations Subcommittee hearing on the topic of miscellaneous obligations, Congressman Space requested detailed historical information on the use of miscellaneous obligations in VA accounting.

Unfortunately, for the reasons stated below, that level of detail would be extraordinarily difficult to produce with any accuracy. As noted, VA is improving its accounting systems in numerous ways, including tracking this category of obligations.

A computer application called Integrated Funds Distribution, Control Point Activity, Accounting and Procurement (IFCAP) is used by over 150 VA facilities to obligate funds. There is a separate IFCAP installation (including a separate database holding source transactions) at each of these sites.

There are two main types of documents created in IFCAP: VA Form 1358 (Estimated Miscellaneous Obligation or Change in Obligation) and VA Form 2237 (Request, Turn-In and Receipt of Property or Services).

Each locally based IFCAP system transmits obligation data through an interface to VA's core accounting system, the Financial Management System (FMS), on a daily basis. The obligations are then processed and recorded in FMS.

Due to current system design limitations in FMS, the obligation data sent from IFCAP to FMS does not include enough information to distinguish between the two document types (1358 or 2237). Once the data is in FMS, it is impossible to tell the difference between data applicable to a 1358 and data applicable to a 2237. Therefore, it is currently not possible to use FMS to derive the total dollar figure for Miscellaneous Obligation (1358) documents only.

Getting this information directly from the IFCAP system would involve a massive effort. Data in each of the 150 separate systems would need to be extracted and compiled in a meaningful manner. Even more problematic is the fact that much of the data going back over 20 years has already been archived. This would require that VA reload many years worth of data at each of the 150 sites to even begin an attempt to develop the requested numbers. This would be a very labor-intensive effort, and present various other technical and logistical issues. It is not feasible to compile this data from IFCAP without tremendous effort, and any resulting information would be of questionable accuracy.

Going forward, we acknowledge that the affected systems need to be changed so that 1358 data can be easily isolated from the other obligation data. We have plans to implement a system change which will provide this capability in the future. IFCAP will add a notation to 1358 documents that are sent through the interface to FMS. This data will then be recorded in FMS for each 1358, and reports can then be created on 1358 activity only. This change is scheduled for implementation in August 2009.

The future financial accounting system, FLITE, has also addressed these issues during requirements development. Not only will the ability to report on detailed miscellaneous obligations be available in FLITE, but the system will further restrict miscellaneous obligations and increase internal control mechanisms surrounding them.

Prepared by: Department of Veterans Affairs
Office of Finance, Office of Financial Business Operations
POC: Jonathan W. Lambert, (202) 461–6173
January 14, 2009, 12 p.m.

Mr. SPACE. Mr. Murray, what is your official title?

Mr. MURRAY. Deputy Assistant Secretary for Finance and Deputy CFO.

Mr. SPACE. And how would you define in no more than two or three sentences your job description?

Mr. MURRAY. Review the accounts and financials, be the financial steward for VA, review financial processes, prepare the financial statements.

Mr. SPACE. Prior to the GAO audit and prior to the hearings that this Subcommittee held, had it ever crossed your mind that there may be a problem with spending upwards of $6 billion a year in miscellaneous expenditures that lacked basic and fundamental accounting principles?

Mr. MURRAY. To the extent that the separations of duties are adhered to, to the extent that contracts are reviewed, and obligations were appropriate for those procurement items, and there is a contract or other vehicle to support those procurement items. It is a service order. On the face of it, what it becomes in the official accounting system is a service order.

So if the separation of duties are in place, the formal contract or procedures were appropriate, it would be okay to spend billions of dollars if all those things were being done.

Mr. SPACE. They were not, though, were they?

Mr. MURRAY. Well, as we discovered through Grant Thornton's review under A–123 and through the GAO report recently drafted for review, we are finding that there are serious deficiencies in our control structure.

Mr. SPACE. For how long have you been working in your current capacity?

Mr. MURRAY. About 6 years.

Mr. SPACE. All right. So in the first 4 years, you had no indication that these basic and fundamental guidelines were not being adhered to?

Mr. MURRAY. We are working a number of various issues and there are a number of control issues throughout the VA that are being tackled. So this has come more to the forefront in the last few years.

Mr. SPACE. And, Mr. Murray, I am not doing this to point fingers. I mean, I am not interested in that. I am not trying to intentionally embarrass anybody. But if we have a systemic problem that allows something so blatant and so obvious to go ignored for so many years with such huge potential for waste and fraud, then I think we have an obligation to address it.

And I am trying to figure out what is wrong with our system where someone in your position who is knowledgeable, intelligent, works hard, it would not occur to you that there is a significant problem here.

Now, you heard Ms. Daly's testimony. You have read the report. And I know my time is growing short. You understand that the GAO thinks you need to do much more in terms of segregation and oversight than what you have done in terms of your interim findings or action.

Are you committed to doing those additional, taking those additional steps that the report cites?

Mr. MURRAY. Absolutely.

Mr. SPACE. Thank you.

Mr. MITCHELL. Thank you.

Mr. Rodriguez.

Mr. RODRIGUEZ. Thank you, Mr. Chairman.

Mr. Murray, I know I asked GAO what they could do to help us out in the process. I am going to ask you the same question.

You are in a situation where you have this occurring. What can we do to help out or how can the GAO help you make that happen, you know, in a quick way to expedite because I know that you—let me ask you first of all, are you a political appointee or——

Mr. MURRAY. I am a career employee, sir.

Mr. RODRIGUEZ [continuing]. Career. Okay. So you are a—I do not mean this in a negative—you are a bureaucrat, so you are going to be there no matter what.

What do we need to do to help you make it happen or what do you need the GAO to do to make it happen because I know you have got a bureaucracy there that is hard to deal with also? How can you go into all those systems and make something happen as quickly as possible?

Mr. MURRAY. Continued emphasis, oversight, assistance from GAO, from our Inspector General, from our auditors, both Grant Thornton and Deloitte and Touche, as well as the Office of Business Oversight, keeping our gaze on resolution of this problem is in my experience when the VA has gotten things done.

So I would encourage GAO's assistance, meeting with them periodically, discussing progress, as well as with our Inspector General. I continue to do so with Grant Thornton and our Office of Business Oversight.

I think what gets measured gets done. So that sort of emphasis, I think, will get this done.

Mr. RODRIGUEZ. Do you feel you might need, in addition to the GAO, any other external group coming in? I know you have the auditors, I guess, coming in. They can also be extremely helpful in making some additional recommendations.

Now, what kind of time table do you think is appropriate in moving forward in trying to make things happen?

Mr. MURRAY. I would like to see within a year, next year, when the Office of Business Oversight does their reviews starting in 2009, at 70 to 80 site visits, vast improvement first in the separation of duties and the appropriate use of miscellaneous obligations as well as I would like to see those contracting reviews, where applicable, being done.

So I would like to see those GAO statistics and I would use them as a baseline for those three sites to ensure they have changed dramatically by the end of fiscal year 2009. In the fourth quarter, I would like to see that be a small number, maybe one, maybe two.

Mr. RODRIGUEZ. And I would gather that a lot of the institutions out there might be operating—I know the Chairman mentioned—I will mention a school district with all the local campus that they might be stand-alone situations that are very difficult to change.

Do you have any suggestions as to how to deal with that?

Mr. MURRAY. Well, institutionalizing good behavior is a challenge. We recently implemented an end-to-end web-based system that enforces very strong controls and approvals through work flow. We used to have four travel systems with pretty weak controls in the VA.

You know, that is ultimately where I would like to see us go across the board. It takes time though. But, what I would really

like to work with is the Logistics Service, with the VA CFO Office applying all resources, both the Departmental resources as well as the VHA resources, to institutionalize change.

Mr. RODRIGUEZ. Do you have the power to be able to go into those other institutions and tell them what they need to do?

Mr. MURRAY. I believe I do. And I want to be up front here. I have never had the VHA CFO or Mr. Downs, Chief Logistics Officer, tell me or the Inspector General not to offer every assistance. We can get on board and work collaboratively with Mr. Feeley, Under Secretary for Health Operations, to get this done.

Mr. RODRIGUEZ. Okay. Let me ask you, who keeps the liabilities? For example, the—I am not an attorney—but the lawsuits, when people have felt that they have been done wrong in contracting, who keeps a record of that?

Mr. MURRAY. We are not talking about the medical liabilities and torts.

Mr. RODRIGUEZ. More contracts and those kind of things.

Mr. MURRAY. The judgment fund. We work with Treasury to reimburse the judgment fund for those claims.

Mr. RODRIGUEZ. Okay. How many lawsuits have we had or who keeps records of that?

Mr. MURRAY. Go ahead, Phillipa, General Counsel.

Ms. ANDERSON. We would have to get back to you on the judgment fund issue.

Mr. RODRIGUEZ. Okay. Because I would like to know the liability of all this in terms of—because if there has been problems or, abuse and if some people have been going to certain contractors, then the only other one that would be complaining are the ones who did not get the contract. And you might have a lot of lawsuits out there that has created a liability for the institution.

So I would ask that you get that to the Committee here, the number of lawsuits, the number of, complaints, and those kind of things and any kind of whistle blowing that you have had, I would appreciate it, and any other items that you think might be helpful. And that would also be helpful for you to also ID some areas that are more problematic than others that you need to zero in on as quickly as possible.

Thank you very much.

[The following information was subsequently received from the VA:]

> Congressman Space asked about records regarding liabilities arising from contract claims against VA.
>
> The following is the response to the Congressman's request for data showing the number of challenges to VA's decisions to sole-source.
>
> Research by our Office of General Counsel showed four cases in which VA sole-source contracting was an element of the contract award challenge. In one of the 4 GAO found the VA failed to demonstrate a reasonable basis for the sole-source award. In that matter GAO did not disturb the acquisition since the order had been placed, but GAO ordered the VA to pay the protester its costs of prosecuting the protest including reasonable attorney's fees. Matter of Bausch & Lomb, Inc, 2006 CPD ¶ 135.
>
> As a point of clarification on VA's testimony, the Department of the Treasury Judgment Fund is not a source of funding for GAO-ordered costs. The source of funding is the VA account from which the requirement is to be funded.

Mr. MITCHELL. Thank you.

Mr. Walz.

Mr. WALZ. Thank you, Mr. Chairman.

And thank you, Mr. Murray and the rest of you, for being here today. I would echo a little bit of what my friend from Texas said.

First of all, I do want to thank you for serving this country and serving our veterans. I think it was a very important question that he asked you about being career in this. You are working in the largest healthcare system in the world and we are cognizant of that.

Our job is to be here to help provide whatever we can to make your job as successful as possible because that translates into care of our veterans. That protecting of the public trust in the VA system is one of the highest priorities I see in my job of sitting here.

And so maybe it is like the Chairman. I am also a high schoolteacher. We can always find the silver lining anywhere. I can tell you that. To survive, you must. And there is a lot of good.

And so I think that there are some things happened here that I think should give us reason to be optimistic, but I think each of my colleagues brought up very legitimate concerns, which you have acknowledged, and the GAO has done a fine job of doing what they are supposed to do.

My first positive, I guess, is the IG process seemed to have worked back in 2007 in Boston and identified what was going on. I have been, as this Committee, I think, has been, a strong proponent of making sure the IG is there as a partner, make sure they are well funded, make sure they have the ability to do what they are supposed to do.

And I would applaud the Chairman and Ranking Member Brown-Waite for also bringing this up.

I guess my concern is, and maybe it is a little esoteric and it went to where Mr. Rodriguez was speaking about, one of the areas I have spent a lot of time on in my doctoral work was in organizational design. And so I appreciate the challenges you have, but I also know there are things that we can do to make this work.

I am trying to get at that Boston report came out in June of 2007 and here we sit on July 31st of 2008 talking about what we are going to do. My concern has always been with the VA, that we provide you not only the necessary oversight but we provide you the necessary flexibility and tools to be able to do your job with several basic, I guess, mission statements for you. The highest quality of care for this Nation's veterans that we can provide in the most fiscally responsible manner that we can do that.

So my question, I guess, and this is maybe where we can let Mr. Downs—I kind of wanted to hear a little bit from that—we are seeing this is there. I wish the sense of urgency were higher. It does appear like the GAO offered nothing more than basic best practices. You have agreed to that. And I think, as you said, let us hope that it did not get into waste, fraud, and abuse.

What are we going to do, though? What is specifically going to be done? And I guess the question was maybe answered already, how quickly you think this will take over. I understand cultural change inside an organization is much longer than structural or, you know, these directives.

But, Mr. Downs, if you could tell us for just a minute or so just some basics of what is going to change.

Mr. DOWNS. Sir, we have a short-term goal and, of course, a long-term goal. Short-term is working with our antiquated data systems to work-arounds and such to start to pull the reports out so electronically we can begin to review what is going on across the field.

In fact, the issue of 1358s was discovered by my office when we first became an office and began looking at data. Well, we needed to find out what are we buying, where are we buying it from, what does it cost, et cetera, et cetera.

That is when we went into the IFCAP system, found out we had basically, I think, seven different stovepipe data systems within each one of the 154 Medical Centers and none of them were—we could not pull data up at a national level very well. So we have had a lot of data people in my office working on that. Now they are pulling reports up.

And when we discovered the 1358, we brought it to the attention of appropriate folks and then, of course, things rolled downhill from there because we want to find out what the problems are and then we need to solve it.

And going back to Mr. Murray a while ago when he was being questioned, you know, part of the fact is that we are a team. And in VHA, there was not a Logistics Office for 25 years and so this office was formed. And then we have to work with them.

So I found this information or my staff found out. We immediately went to the CFO, Paul Kearns here, and Mr. Murray and said here is our problem, Mr. Frye. We shared that information because we have to work as a team to solve it.

So we are dealing with legacy systems. We are developing work-arounds so we can do these reports. We are as intense about this as you all are, in fact more so because we have an obligation to make this thing work.

And it is appalling when we come in and we are not able to provide you the answers you want nor are we able to properly conduct our oversight and monitoring if we do not have the tools in front of us to do it. And manual reports just do not cut it. You have to have the ability to electronically pull data in so that you can then do the reviews.

So what we are doing here with our first data runs as we did the method of processing report, which brought up the 1358 issue, now we are looking at the on-off contract report. In other words, we are looking at obligations. Do they have a contract or do they not have a contract. We are looking at the miscellaneous obligation open and closed.

So one thing that we can do with that is are they leaving these 1358s open or are they closing them like they should be. What is going on there. And we are looking at the budget object codes to see what is going on with that. The expendable inventory reports, our GIP, how does that tie in.

The FPDS matching report is something new that we have just been able to put together, which would show the contracts that we have and are they being reported properly into FPDS.

See, all of these things are integrated. They cannot be just taken one at a time. And we have a number of other issues that we are

going through, looking at our item file and our vendor file. They are all confused. And so trying to pull that together.

And to also help put it in perspective is that when core FLS came into being many years ago, it was supposed to solve many of these problems because we knew some of these things existed or our predecessors did. But, of course, that all fell apart.

In the interim, though, we have come new on the scene and we see the problems. And now we are trying to do these work-arounds to get them going again. And so we now as of today, as a matter of fact, there is a Request For Proposal on the street for the integration of the strategic asset management system, which we hope to begin a pilot in January.

And to answer the questions that have been asked about time, this particular part of flight, if the pilot will take place, we hope starting in January, it will take place about a year and then we will do about ten more stations and the next year roll that out and then the third year begin rolling out nationwide.

So in the long term, we are looking at a 3-year project if all goes well. In the short term, we are going to continue working with these issues as we develop work-arounds with the data systems that we have. And we are looking at that information.

And then, more importantly, we are sharing it back with the field because the field has been doing this for years. No one has given them feedback, so I think in many cases, they did not even know they were doing it wrong. They just sort of drifted into it as personnel changed and such.

Mr. WALZ. My time is up, Mr. Downs. This information technology (IT) issue, and I asked the Chairman and the Ranking Member, how many hearings have we had that we come back around to the IT issue, whether it is the electronic medical record and now we are hearing it here?

This is an issue that the Members who have been on this Committee for 10, 15 years and they keep coming around to the IT issue. And my belief is if that is where this is all stemming from, boy, we have to figure that out.

I am a big fan of Mr. Henke who I think brought a new vision to this on the IT side of things, but I still keep hearing and it is still frustrating.

So I thank you for what you have done on that and, of course, Mr. Downs, I thank you any time you are wearing a Combat Infantry Badge. We welcome you at this Committee.

Mr. DOWNS. Thank you.

Mr. MITCHELL. Thank you. Thank you very much.

You know, one thing that has kind of been hinted at from everybody up here, and I appreciate what you are doing—this is the second largest department in the Federal Government, which is obviously huge. And as you mentioned, it is pretty hard to institutionalize good behavior and change. And I appreciate all your efforts in doing that.

What I want to ask you very quickly is, what do you need from Congress? Do you need resources? Do you need legal authority? Do you need anything from us to help fix the problems that have come up?

Mr. DOWNS. A magic wand would help. But, anyway, it is a difficult question to answer. But this continued oversight is, I think, one of the keys because it keeps the attention level up and keeps the focus up.

Each individual who is back there in headquarters, whether it's the CIO or the VHA or the Veterans Benefits Administration, we are all trying to struggle to solve these problems and it is just a humongous organization and it takes time to sort through it.

And the focus by the Committee is helpful to us when a request goes up for resources or support among ourselves. We all know the attention is there. So I think the best thing is the continued oversight and our ability to come back and report to you our progress.

Mr. MITCHELL. Mr. Murray, did you——

Mr. MURRAY. I would like to add that from my vantage point, support of FLITE, our modernization of our core accounting system which would replace IFCAP, is just paramount. I do not have the tools that industry has because I am running kind of a band-aid set of applications that are very, very old. And it is hard to do the work without some of the tools that many others enjoy. I would appreciate your support of our tool building initiative. It is named FLITE.

Thank you.

Mr. MITCHELL. Well, I can assure you, Mr. Downs, there will be continued oversight. But also I think everybody on this Subcommittee and the larger Committee wants to provide the resources and whatever you need to serve our veterans. So if it is money or any other type of resources, we need to know that.

Mr. DOWNS. We need IT attention on our clinical issues that we have been working on in VHA. We need IT attention on our organizational administrative issues, which is what we are here about.

For years, we have achieved success and honor with a high quality of healthcare. Now we need to maintain that with the infrastructure that takes it to support it. And that is where our needs for this IT, as you can tell from these presentations, is so great.

Mr. MITCHELL. Thank you.

Mr. Bilbray.

Mr. BILBRAY. Mr. Chairman, I want to clarify that we are not talking about behavior here. We do not know about the behavior. We have not done enough of the research. We have not done a deep enough dive here to find out about behavior. We are talking process, procedure.

Mr. Murray, is there any reason at all why, from your lofty position in the Department, that you cannot immediately send out a directive that you will not have any miscellaneous expenditures unless we get three signatures on a document that justifies it? And from this point, to this point, to this point, it does not take computers to do that.

Mr. MURRAY. You are absolutely correct, sir. In fact, we have such a document in review and concurrence right now.

Mr. BILBRAY. Okay. Review and concurrence on it, because let me tell you guys I have sat in front of Department heads and staffers since I was 25 years old. What I hear you say about this oversight process is, Congressman, keep having meetings, keep talking, you know, we can do this back and forth, back and forth.

My problem is, you know, this is a great game of intellectual tennis that we are playing here, but does it get the job done? And by 1940 to here shows you that oversight and talking about it does not get it done. There need to be some thresholds. There should be some minimum standards. In the private sector, you set a minimum standard. If someone does not fix it, Mr. Downs, you know exactly what happens.

The fact is here, Mr. Murray, this really sits on you because you are the guy at the top of this financial review process. There should be some minimum standards saying, I do not care if you cannot do it on a computer. Take a piece of paper and write it down, but I want to see those three signatures. I want to have three people that are willing to put their head and their reputation on the line. When miscellaneous is on that, that should be a big red flag that somebody has an extraordinary reason not to play by the rules, which I understand. We do not want to have, you know, road blocks, but we certainly want to have some accountability.

And I still do not see, Mr. Murray, why we cannot put a time certain that any miscellaneous in the 2009 budget has to have three signatures and here are the ones I am requiring and I do not want to hear excuses about it.

Is there any reason why you cannot do that in 2009?

Mr. MURRAY. Our policy, separation of duties, strong controls, whether it is a miscellaneous document or a 2237 purchase order document, any kind of financial obligation needs strong controls. It is kind of Accounting 101.

However, we intend to mandate those separation of duties in our policy.

Mr. BILBRAY. Well, let me tell you something, Mr. Chairman. We have upped the budget appropriately of the VA. But I will tell you something. Rather than talking about your IT system, I think the shot across the bow could be the fact that we are going to up the audits. We are going to start doing a deep dive.

We are not going to mess with 42. We are going to be talking about, you know, 42,000 audits. And if that is where we have to go because the system has such a potential for abuse to scare the hell out of people to understand that, do not be tempted because the Oversight Committee is already looking at this.

I serve as Ranking Member on Procurement for Government Oversight. This is right up my alley and I am sure the Subcommittee Chairman will love to look at this because we should be making sure that this situation does not happen anywhere in the Federal system.

So I am saying this very firmly because I do not want to hear about anything coming out of there like Boston anymore. I think we need to send a signal to the entire process that even if you have been doing this in the past, you better keep your nose clean because we are doing the deep dive and are going to come looking for you.

Thank you very much. I appreciate it.

Mr. Murray, any comment you want to make on that, you are obviously——

Mr. MURRAY. We are going to begin doing the deep dive on our own, the three of us. You have the folks here at the table. We are

going to begin using our audit resources to do that deep dive internally and we hope to be able to say that we made great improvement in the future.

Mr. MITCHELL. Again, I would like to thank all of you for the work that you are doing. And as I said, you can expect a followup on this.

And I appreciate the tools that you need and the financial system, we have been told over and over. Hopefully that is coming to an end, that you will get the IT systems that you need so that you can do the job that is expected of you, which, as we have said before, is expected in the private sector. They would do it immediately and they have those resources.

We hope that you get those resources and I hope anything, that we can do to help expedite that, but let us know. I will give you a little warning ahead of time. We want to revisit this early in the next Congress with another accountability because I think not only you but also Ms. Daly said that probably the best role that we can play is oversight and just to make sure that people are doing what they should.

And, again, I want to thank you for being here and thank you for what you are doing and working in the largest or second largest government agency that we have and sometimes not getting the tools that you need to be up to date. And I appreciate that.

So thank you very much. And with that, that ends this hearing.

[Whereupon, at 11:30 a.m., the Subcommittee was adjourned.]

APPENDIX

Prepared Statement of Hon. Harry E. Mitchell, Chairman, Subcommittee on Oversight and Investigations

We are here today to examine an issue of great importance. The Department of Veterans Affairs is the second largest in the Federal Government. It is authorized to spend billions of dollars of the taxpayers' money every year to care for those who bravely stepped forward to defend our Nation.

We have an obligation to ensure that the VA uses these funds appropriately and they are not lost through waste, fraud, or abuse. We must also be sure that they use adequate internal financial controls and management.

Unfortunately, the VA does not have adequate internal controls. Worse, is that this problem is not new—VA's auditors yearly have found material weaknesses in VA's financial management system functionality and in financial management oversight.

We will hear from the Government Accountability Office that the VA procured billions of dollars in goods and services by way of "Miscellaneous Obligations" that should not have been procured this way. Improper use of Miscellaneous Obligations obscures how taxpayer money is being spent. In addition, goods and services that should have been procured competitively can be subverted using this process.

Even when Miscellaneous Obligations are properly used, GAO's review disclosed significant defects in VA's internal financial controls and reporting. For example, VA employees often failed to describe the purpose of a Miscellaneous Obligation or used uncertain descriptions like "3rd quarter invoice," which would not adequately describe its purpose to an unbiased audit.

GAO's review also disclosed serious failures in a bedrock principle of financial management—the segregation of duties.

It is elementary that the person authorized to sign the checks cannot be the same person that approves the expense. In 30 out of 42 transactions that GAO looked at, VA failed to ensure the proper segregation of duties.

Just a few years ago, VA spent 350 million dollars on a failed attempt to create a modern electronic financial system. VA has embarked on redoing that project, but even if successful it is many years away from completion. We cannot wait. Even with the imperfect financial and procurement systems it has, VA must ensure compliance with basic principles of financial control. We look forward to hearing today from VA about how it is going to do this.

Prepared Statement of Hon. Brian P. Bilbray

Mr. Chairman,

Thank you for calling this hearing. Our fiduciary oversight responsibility over the VA is important, particularly when we view the budget each year and see billions of dollars spent by the VA categorized as "miscellaneous obligations." When questioned about this line item in the budget, VA does not appear to have any clear knowledge of exactly how this money is being spent. This is something that gravely concerns me, as well as several of my colleagues on both sides of the aisle, and I believe it is important to get to the root of this problem.

On October 5, 2007, following a staff briefing by the Veterans Health Administration, you and Ranking Member Brown-Waite sent a letter over to the Government Accountability Office requesting an audit of VHA procurement spending under miscellaneous obligations to determine whether (1) procurement obligations and disbursements were properly reported, (2) adequate budgetary and procurement controls are in place for the underlying transactions, and (3) there are indications of fraud or abuse in the underlying transactions. During the staff briefing, it was noted by VHA officials that $4.8 billion (over 55 percent) of the reported $8.6 billion in procurements through the third quarter of fiscal year 2007 were based on miscellaneous obligating documents. I appreciate both of your leadership on this issue.

Mr. Chairman, miscellaneous obligations represents an enormous percentage of VHA procurements. I am concerned that VHA may not know the full scope of what this money is purchasing. I question how VA can plan the coming FY 2009 budget, not knowing where the needs are, and how to best meet these needs if so much funding is being placed under miscellaneous obligations. I understand that GAO has issued their report based on our request this week, and I look forward to hearing about their review and the results of the audit. I also would like to hear from VA about what type of controls are currently in place, whether VA believes these controls are working, what are they doing to tighten the use of the miscellaneous obligations documents for purchasing at VHA.

This is not the first time our Subcommittee has reviewed VHA procurement issues. During the 108th Congress, we held a series of three hearings both at the Subcommittee and the full Committee on eliminating waste, fraud, and abuse and mismanagement in veterans' programs at VA. Included in these hearings were discussions on VA's purchase cards, as well as third party billing. I believe it is our job, as the oversight Committee to help VA in getting a handle on this issue, and finding solutions to the problems that exist.

While I do not want to say procurement at the Department of Veterans Affairs is broken, it appears seriously dysfunctional and decentralized to such a point that appropriate procurement oversight does not adequately exist throughout the procurement chain. When you don't know where the money is spent, how do you know where your greatest needs arise?

Thank you again, Mr. Chairman and I yield back my time.

Prepared Statement of Kay L. Daly Acting Director, Financial Management and Assurance, U.S. Government Accountability Office

GAO Highlights

Why GAO Did This Study

The Veterans Health Administration (VHA) has been using miscellaneous obligations for over 60 years to record estimates of obligations to be incurred at a later time. The large percentage of procurements recorded as miscellaneous obligations in fiscal year 2007 raised questions about whether proper controls were in place over the authorization and use of billions of dollars.

GAO's testimony provides preliminary findings related to (1) how VHA used miscellaneous obligations during fiscal year 2007, and (2) whether the Department of Veterans Affairs (VA) policies and procedures were designed to provide adequate controls over their authorization and use. GAO recently provided its related draft report to the Secretary of Veterans Affairs for review and comment and plans to issue its final report as a followup to this testimony. GAO obtained and analyzed available VHA data on miscellaneous obligations, reviewed VA policies and procedures, and reviewed a nongeneralizable sample of 42 miscellaneous obligations at three case study locations.

GAO's related draft report includes four recommendations to strengthen internal controls governing the authorization and use of miscellaneous obligations, in compliance with applicable Federal appropriations law and internal control standards.

What GAO Found

VHA recorded over $6.9 billion of miscellaneous obligations for the procurement of mission-related goods and services in fiscal year 2007. According to VHA officials, miscellaneous obligations were used to facilitate the payment for goods and services when the quantities and delivery dates are not known. According to VHA data, almost $3.8 billion (55.1 percent) of VHA's miscellaneous obligations was for fee-based medical services for veterans and another $1.4 billion (20.4 percent) was for drugs and medicines. The remainder funded, among other things, state homes for the care of disabled veterans, transportation of veterans to and from medical centers for treatment, and logistical support and facility maintenance for VHA medical centers nationwide.

GAO's *Standards for Internal Control in the Federal Government* states that agency management is responsible for developing detailed policies and procedures for internal control suitable for their agency's operations. However, based on GAO's preliminary results, VA policies and procedures were not designed to provide adequate controls over the authorization and use of miscellaneous obligations with respect to oversight by contracting officials, segregation of duties, and supporting documentation for the obligation of funds. Collectively, these control design flaws increase the risk of fraud, waste, and abuse (including employees converting government assets

to their own use without detection). These control design flaws were confirmed in the case studies at Pittsburgh, Cheyenne, and Kansas City.

Summary of Control Design Deficiencies at Three Case Study Locations

Station	Number of obligations reviewed	No documented approval by contracting official	Inadequate segregation of duties [a]	Inadequate supporting documentation		
				Incomplete purpose description [b]	Blank vendor field	Blank contract field [c]
Pittsburgh	14	14	9	3	6	3
Cheyenne	11	11	11	1	6	4
Kansas City [d]	17	17	10	4	8	9
Totals	42	42	30	8	20	16

Source: GAO analysis of VHA data.

In May 2008, VA issued revised guidance concerning required procedures for authorizing and using miscellaneous obligations. GAO reviewed the revised guidance and found that while it offered some improvement, it did not fully address the specific control design flaws GAO identified. Furthermore, according to VA officials, VA's policies governing miscellaneous obligations have not been subject to legal review by VA's Office of General Counsel. Such a review is essential in ensuring that the policies and procedures comply with applicable Federal appropriations law and internal control standards.

Mr. Chairman and Members of the Subcommittee:

Thank you for the opportunity to discuss the Veterans Health Administration's (VHA) use of miscellaneous obligations. VHA officials said that they have been using miscellaneous obligations for over 60 years to record estimates of obligations [1] to be incurred at a later time.[2] According to the Department of Veterans Affairs (VA) policy,[3] miscellaneous obligations can be used to record estimated obligations to facilitate the procurement of a variety of goods and services, including fee-based medical and nursing services; beneficiary travel; and for other purposes.

VHA officials briefed your Subcommittee staff in September 2007 about various financial reporting weaknesses in the agency and initiatives under way to address them. In the briefing, VHA officials disclosed that $4.8 billion (56 percent) of the reported $8.6 billion in procurements through the third quarter of fiscal year 2007 had been done using funds categorized as miscellaneous obligations. In addition, VA's Office of Inspector General (OIG) issued a report in May 2007 on the alleged mismanagement of funds at the VA Boston Healthcare System. According to OIG officials, they obtained documents showing that a miscellaneous obligation for $200,000 was requested, approved, and obligated by the same fiscal official, calling into question the adequacy of the segregation of duty controls over miscellaneous

[1] An obligation is a definite commitment that creates a legal liability of the government for the payment of goods and services ordered or received, or a legal duty on the part of the United States that could mature into a legal liability by virtue of actions on the part of the other party beyond the control of the United States. Payment may be made immediately or in the future.

[2] A miscellaneous obligation can be used as a funds control document to commit (reserve) funds that will be obligated under a contract or other legal obligation at a later date. VA Office of Finance Director, VA Controller Policy MP–4, Part V, Chapter 3, section 3 A.01 states in pertinent part that "it will be noted that in many instances an estimated miscellaneous obligation (VA Form 4–1358) is authorized for use to record estimated monthly obligations to be incurred for activities which are to be specifically authorized during the month by the issuance of individual orders, authorization requests, etc. These documents will be identified by the issuing officer with the pertinent estimated obligation and will be posted by the accounting section to such estimated obligation."

[3] VA Office of Finance Directives, VA Controller Policy, MP–4, Part V, Chapter 3, section A, Paragraph 3A.02—Estimated Miscellaneous Obligation or Change in Obligation (VA Form 4–1358).

obligations.[4] In light of these concerns, you requested that we review whether the design of VHA's internal controls over the use of miscellaneous obligations was adequate for fiscal year 2007.

Today, my testimony will focus on our preliminary observations related to (1) how VHA used miscellaneous obligations during fiscal year 2007, and (2) whether VA's policies and procedures are designed to provide adequate controls over the authorization and use of miscellaneous obligations. We recently provided our draft report, including recommendations, on the results of our audit to the Secretary of Veterans Affairs for review and comment. We plan to incorporate VA's comments as appropriate and issue our final report as a followup to this testimony. We conducted this audit from November 2007 through July 2008 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. Details on our scope and methodology are included in appendix I. Further background information on VHA's operations is included in appendix II.

Summary

According to our preliminary analysis, in fiscal year 2007, available information from the Integrated Funds Distribution, Control Point Activity, Accounting and Procurement (IFCAP) database show that VHA used miscellaneous obligations to record over $6.9 billion against its appropriations for the procurement of mission-related goods and services. According to the IFCAP data, almost $3.8 billion of this total (55.1 percent) was for fee-based medical and dental services for veterans and another $1.4 billion (20.4 percent) for drugs, medicines, and hospital supplies. The remainder covered, among other things, state homes for the care of disabled veterans, transportation of veterans to and from medical centers for treatment, and logistical support and facility maintenance for VHA medical centers nationwide. VHA officials said they used miscellaneous obligations to administratively reserve estimated funds required to facilitate the payments for goods and services for which specific quantities and timeframes were uncertain. Another cited benefit was that miscellaneous obligations simplify the procurement process when no underlying contract or purchase order exists. For example, VHA centers used miscellaneous obligations to record estimated obligations for an umbrella agreement for fee-based medical services that can then be used to fund the work performed by a number of different physicians. Nonetheless, without effectively designed mitigating controls, using miscellaneous obligations may also expose VHA to increased risk of fraud, waste, and abuse.

Our preliminary findings indicate that VA policies and procedures were not designed to provide adequate controls over the use of miscellaneous obligations with respect to oversight by contracting officials, segregation of duties, and supporting documentation for recording the obligation of funds. Specifically, although VA's September 29, 2006, policy required contracting officials to review miscellaneous obligations to help ensure their proper use, the supporting procedures did not describe how such reviews should be carried out. Further, the design of the current control process did not include detailed procedures for conducting either an automated or manual review of miscellaneous obligations by contracting officials. With regard to segregation of duties, the miscellaneous obligation automated system and associated policies and procedures were not designed to prevent one person from performing multiple roles in the process of authorizing and executing miscellaneous obligations. Finally, with regard to documentation, we found that current guidance did not include detailed procedures on what was to be included in the purpose field of the miscellaneous obligation authorization document and did not require that the vendor name and contract number be included. These control design flaws were confirmed in our case studies at Pittsburgh, Cheyenne, and Kansas City. Such VHA-wide policy and procedure design flaws increase the risk of fraud, waste, and abuse at the 129 VHA stations using miscellaneous obligations in fiscal year 2007. New guidance for the use of miscellaneous obligations was issued in May 2008. This guidance, while it offered some improvement, did not fully address the three problem areas. Also, we understand that VA attorneys have not reviewed these policies to help ensure compliance with applicable appropriations law and other requirements.

[4] Department of Veterans Affairs, Office of Inspector General, Audit of Alleged Mismanagement of Government Funds at the VA Boston Healthcare System, Report No. 06–00931–139 (Washington, D.C.: May 31, 2007).

Our draft report, recently provided to the Secretary for review and comment, included four recommendations for actions that, if effectively implemented, should reduce the risks associated with using miscellaneous obligations.

Miscellaneous Obligations Used Extensively for Mission-Related Activities in Fiscal Year 2007

According to the IFCAP database, in fiscal year 2007 nearly 132,000 miscellaneous obligations, with a total value of nearly $9.8 billion, were created (see table 1). While VA's Central Office had $2.9 billion in miscellaneous obligations during fiscal year 2007, our review focused on the $6.9 billion in miscellaneous obligations used by VHA's 129 stations,[5] located in every Veterans Integrated Services Network (VISN) throughout the country, for a variety of mission-related activities. (See app. III for a listing of the use of miscellaneous obligations by VISN, and app. IV for a listing of the use of miscellaneous obligations by station.)

Table 1: Miscellaneous Obligations at VHA and VA for Fiscal Year 2007
(Dollars in billions)

VISN name	Number of miscellaneous obligations	Dollar amount of miscellaneous obligations	Percentage of total dollar value
VHA[a]	127,070	$6.9	70%
VA's Central Office[b]	4,839	$2.9	30%
Total	131,909	$9.8	100%

Source: GAO analysis of IFCAP data.
[a] Includes miscellaneous obligations for VISNs 1–12 and 15–23 (VISNs 13 and 14 were consolidated and designated VISN 23).
[b] VA's Central Office (VISN 0) is responsible for the administration of the Consolidated Mail Outpatient Pharmacy (CMOP) initiative that provides mail order prescriptions to veterans using automated distribution centers located throughout the country. In fiscal year 2007, VISN 0 obligated about $2.08 billion in miscellaneous obligations for drugs, medicines, and other supplies, and almost $800 million for various fee-based medical, dental, and other services.

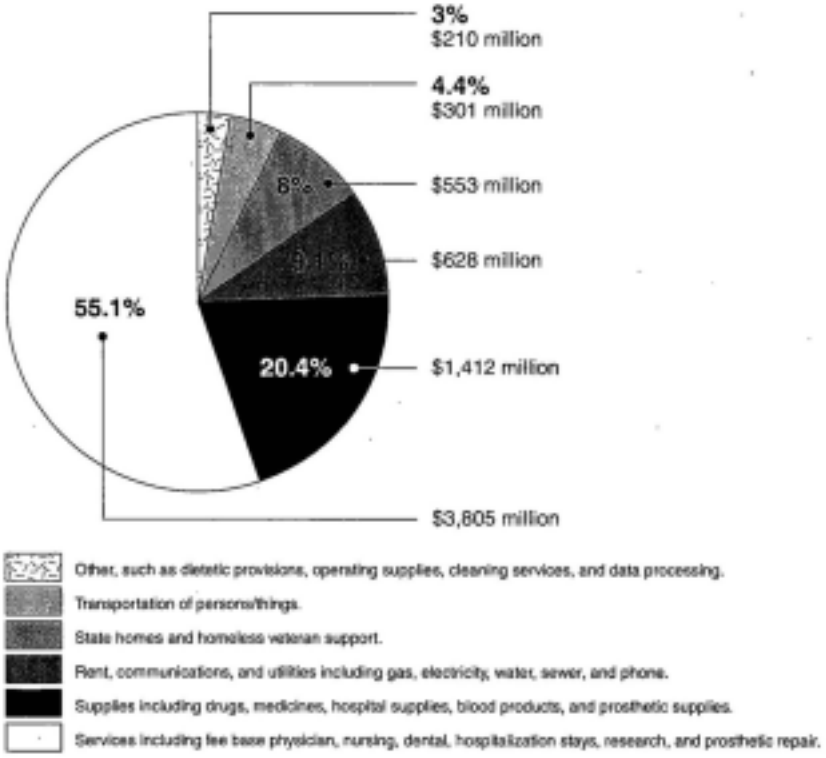
According to available VHA data, VHA used miscellaneous obligations to record estimated obligations of over $6.9 billion for mission-related goods and services. As shown in figure 1, about $3.8 billion (55.1 percent) was for fee-based medical and dental services for veterans, and another $1.4 billion (20.4 percent) was for drugs, medicines, and hospital supplies. The remainder was for, among other things, state veterans homes,[6] transportation of veterans to and from medical centers for treatment, and logistical support and facility maintenance for VHA medical centers nationwide.

According to VHA contracting and fiscal service officials, using miscellaneous obligations tends to reduce administrative workload and facilitates the payment for contracted goods and services, such as drugs, medicines, and transportation, and for goods and services for which no pre-existing contracts exist, such as fee-basis medical and dental services and utilities.

VHA officials stated that miscellaneous obligations facilitate the payment for contracted goods and services when the quantities and delivery dates are not known. A miscellaneous obligation can be created for an estimated amount and then modified as specific quantities are needed or specific delivery dates are set. When a purchase order is created, however, the obligated amount cannot be changed without a modification of the purchase order. According to VHA officials, the need to prepare numerous modifications to purchase orders could place an undue burden on the limited contracting personnel available at individual centers and could also require additional work on the part of fiscal services personnel.

[5] The IFCAP database included 129 VHA stations. A VHA station may include more than one medical center.
[6] State veterans homes are established by individual states and approved by VA for the care of disabled veterans. The homes include facilities for domiciliary nursing home care and adult day healthcare.

Figure 1: VHA Miscellaneous Obligations for Fiscal Year 2007



Source: GAO analysis.

VHA officials stated that the use of miscellaneous obligations can simplify the procurement process when no pre-existing contract or purchase order exists. For example, providing medical care on a fee-basis to veterans outside of VHA medical centers may involve the services of thousands of private physicians nationwide. Attempting to negotiate a separate agreement or contract with each of these individuals would be a difficult task for VHA's contracting staff. Under the policies and procedures in place during fiscal year 2007, VHA centers could use miscellaneous obligations as umbrella authorizations for fee-based medical services for work performed by a number of different physicians. In effect, in cases for which there is no pre-existing contract, the miscellaneous obligation form becomes the record of an obligation. However, use of miscellaneous obligations may also increase the risk of fraud, waste, and abuse. Consequently, mitigating controls must be designed to help compensate for the lack of a negotiated contract. Absent contractual terms, one risk area is the authorized fee schedule for the medical services being provided. In this case, Federal regulations call for payments to non-VA physician services associated with outpatient and inpatient care provided at non-VA facilities to be the lesser of the amount billed or the amount calculated using the formula developed by the Department of Health and Human Services under Medicare's participating physician fee schedule for the period in which the service is provided.[7] However, we did not verify that VHA officials were properly following the fee schedule.

Deficiencies in Design of Controls over Miscellaneous Obligations Increase the Risk of Fraud, Waste, and Abuse

Our preliminary observations on VA policies and procedures indicate they were not designed to provide adequate controls over the use of miscellaneous obligations. According to GAO's *Standards for Internal Control in the Federal Government*, agen-

[7] 38 CFR 17.56.

cy management is responsible for developing detailed policies and procedures for internal control suitable for their agency's operations and ensuring that they provide for adequate monitoring by management, segregation of duties, and supporting documentation for the need to acquire specific goods in the quantities purchased. We identified control design flaws in each of these oversight areas, and we confirmed that these weaknesses existed at the three locations where we conducted case studies. Collectively, these control design flaws increase the risk of fraud, waste, and abuse (including employees converting government assets to their own use without detection). New guidance for the use of miscellaneous obligations was released in January 2008 and finalized in May 2008. We reviewed the new guidance and found that while it offered some improvement, it did not fully address the specific control design flaws we identified. Furthermore, VA officials told us that this guidance was not subject to any legal review. Such an analysis is essential to help ensure that the design of policies and procedures comply with all applicable Federal appropriations law and internal control standards.

We reviewed 42 miscellaneous obligations at the three case study locations and developed illustrative, more detailed information on the extent and nature of these control design flaws. Table 2 summarizes the locations visited, the miscellaneous obligations reviewed at each location, and the extent and nature of control design deficiencies found.

Table 2: Summary of Case Study Results

Station	Number of obligations reviewed	Dollar value of obligations reviewed	No documented approval by contracting official	Inadequate segregation of duties [a]	Inadequate supporting documentation		
					Incomplete purpose description [b]	Blank vendor field	Blank contract field [c]
Pittsburgh	14	$ 6,694,853	14	9	3	6	3
Cheyenne	11	$ 2,076,648	11	11	1	6	4
Kansas City [d]	17	$27,274,395	17	10	4	8	9
Totals	42	$36,045,896	42	30	8	20	16

Source: GAO analysis of VHA data.

[a] In 30 of the 42 obligations we reviewed, one official performed two or more of the following functions: requesting, creating, approving or obligating funds for the original miscellaneous obligations, or certifying delivery of goods and services and approving payment.

[b] In 8 of 42 instances, we could not determine the nature, timing, or the extent of the goods and/or services being procured from the description in the purpose field without reference to supporting invoices.

[c] In these instances, we confirmed that contracts existed, but no contract number was listed on the miscellaneous obligation document.

[d] Includes facilities located in Kansas City, KS; Wichita, KS; Columbia, MO; and eastern Kansas.

Inadequate Contracting Oversight of Miscellaneous Obligations

To help minimize the use of miscellaneous obligations, VA policy stated that miscellaneous obligations would not be used as obligation control documents unless the contracting authority for a station had determined that purchase orders or contracts would not be required. Furthermore, VA policy required review of miscellaneous obligations by contracting officials to help ensure proper use in accordance with Federal acquisition regulations, but did not address the intended extent and nature of these reviews or how the reviews should be documented. Contracting officials were unable to electronically document their review of miscellaneous obligations and no manual documentation procedures had been developed. Our review of 42 miscellaneous obligations prepared at three VHA stations showed that contracting officers were at times familiar with specific miscellaneous obligations at their facilities, but that they had no documented approvals available for review. Furthermore, none of the three sites we visited had procedures in place to document review of the miscellaneous obligations by the appropriate contracting authorities.

Effective oversight and review by trained, qualified officials is a key factor in identifying a potential risk for fraud, waste, or abuse. Without control procedures to help ensure that contracting personnel review and approve miscellaneous obligations prior to their creation, VHA is at risk that procurements will not have safeguards established through a contract approach. For example, in our case study at the VA Pittsburgh Medical Center, we found 12 miscellaneous obligations, totaling about $673,000, used to pay for laboratory services provided by the University of

Pittsburgh Medical Center (UPMC). The Chief of Acquisition and Materiel Management for the VA Pittsburgh Medical Center stated that she was not aware of the UPMC's laboratory testing service procurements and would review these testing services to determine whether a contract should be established for these procurements. Subsequently, she stated that VISN 4, which includes the VA Pittsburgh Medical Center, was going to revise procedures to procure laboratory testing services through purchase orders backed by reviewed and competitively awarded contracts, instead of funding them through miscellaneous obligations.

Another Pittsburgh miscellaneous obligation for about $141,000 was used to fund the procurement of livers for transplant patients. Local officials said that there was a national contract for the services, and that livers were provided at a standardized price of $21,800. However, officials could not provide us with a copy of the contract, nor documentation of the standardized pricing schedule. Therefore, we could not confirm that VHA was properly billed for these services or that the procurement was properly authorized.

Furthermore, in the absence of review by contracting officials, controls were not designed to prevent miscellaneous obligations from being used for unauthorized purposes, or for assets that could be readily converted to personal use. Our analysis of the IFCAP database for fiscal year 2007 identified 145 miscellaneous obligations for over $30.2 million that appeared to be used in the procurement of such items as passenger vehicles; furniture and fixtures; office equipment; and medical, dental, and scientific equipment. Although the VA's miscellaneous obligation policy did not address this issue, VA officials stated that acquisition of such assets should be done by contracting officials and not through miscellaneous obligations. Without adequate controls to review and prevent miscellaneous obligations from being used for the acquisition of such assets, it is possible that the VHA may be exposing the agency to unnecessary risks by using miscellaneous obligations to fund the acquisitions of goods or services that should have been obtained under contract with conventional controls built in.

Inadequate Segregation of Duties

One tenet of an effectively designed control system is that key duties and responsibilities need to be divided or segregated among different people to reduce the risk of error or fraud.[8] These controls should include separating the responsibilities for authorizing transactions, processing and recording them, reviewing the transactions, and accepting any acquired assets. The basic principle is that no one individual should be permitted to control all key aspects of a transaction or event, such as acquiring a good or service.

However, IFCAP control design allows a single official to perform multiple key roles in the process of creating and executing miscellaneous obligations, and VA policies and procedures do not specifically prohibit this practice. Control point officials are authorized to create, edit, and approve requests for miscellaneous obligations. In addition, these same individuals can certify the delivery of goods and services and approve payment. Such weak control design could enable a VHA employee to convert VHA assets to his or her own use, without detection (such as the personal property acquired through the use of miscellaneous obligations described in the previous section).

Our review of the previously mentioned 42 miscellaneous obligations at three case study locations indicated that controls in place at these locations were not designed to ensure sufficient segregation of duties for procurements. Specifically, as noted in table 3, we found inadequate segregation of key duties in 30 of the 42 obligations we reviewed. In these instances, controls were not designed to prevent one official from performing two or more of the following key functions: (1) requesting the miscellaneous obligation, (2) approving the miscellaneous obligation, (3) recording the obligation of funds, or (4) certifying delivery of goods and services and approving payment.

As noted in table 3, in 13 of the 42 obligations we examined, the same official performed three of the four functions. In 11 of these cases, the same official requested and approved the miscellaneous obligations, and then certified receipt of goods and services. For example, in one case in Pittsburgh, one official requested and approved a miscellaneous obligation of over $140,000 for medical services and then certified receipt and approved payment for at least $43,000 of those services. In another case in Cheyenne, we found one miscellaneous obligation for utilities where one official requested, approved, and certified receipt and approved payment of over $103,000 in services.

[8] GAO, Standards for Internal Control in the Federal Government, GAO/AIMD–00–21.3.1 (Washington, D.C.: November 1999).

Table 3: Case Study Analysis of Segregation of Duties

Number of functions performed by agency officials [a]	Obligations
One official performed two out of the four functions	15
One official performed three out of the four functions	13
One official performed all four functions	2
Subtotal—Inadequate Segregation of Duties	30
Adequate segregation of duties—different officials performed each of the four functions	12
Total	42

Source: GAO analysis.
[a] Agency officials performed various combinations of the following four functions: (1) requesting the miscellaneous obligation, (2) approving the miscellaneous obligation, (3) obligating funds, and (4) certifying receipt of goods and services and approving payment.

In two instances in Cheyenne involving employee grievance settlements for about $22,000, one official performed all four functions. While our review found that these obligations were for legitimate purposes, the fact that one official was able to perform multiple functions is indicative of an inherent control system flaw. One individual, controlling all of the key stages of the transaction, leaves VHA vulnerable to potential fraud, waste, or abuse because of the opportunity for the creation of inappropriate, perhaps fraudulent, transactions.

The VA OIG noted a similar problem in its review of the alleged mismanagement of funds at the VA Boston Healthcare System.[9] According to OIG officials, they obtained documents showing that a miscellaneous obligation was used to obligate $200,000, and was requested, approved, and obligated by the same fiscal official. The OIG officials said that this transaction called into question the adequacy of segregation of duty controls over funds obligated through miscellaneous obligations.

Similarly, a July 2007 report by an independent public accountant (IPA) also found, among other things, the segregation of duties for VA's miscellaneous obligation process was inadequate.[10] The report noted that control point officials at a VISN, VA's Central Office, and two medical centers had the ability to act as the requester and approving official for the same transaction. This condition was observed at four of the six locations the IPA reviewed. The IPA recommended that the medical centers update their local policies to prevent control point officials from acting as a requester and approving official on the same transaction. Similarly, in 23 of the 42 miscellaneous obligations we reviewed in our case studies, the same individual served as the requester and approver for a miscellaneous obligation.[11]

Lack of Adequate Supporting Documentation

Another tenet of an effectively designed control system is that all transactions need to be clearly documented and all documentation and records should be properly managed and maintained.[12] Adequate documentation is essential to support an effective funds control system, is crucial in helping to ensure that a procurement represents a bona fide need, and reduces the risk of fraud, waste, and abuse. When a legal obligation is recorded, it must be supported by adequate documentary evidence of the liability.[13] An agency should use its best estimate to reserve an amount for future obligation when the amount of the government's final liability is undefined. Further, the basis for the estimate and the computation must be documented. Although VA's form entitled "Estimated Miscellaneous Obligation or Change in Obligation" (VA Form 4–1358) includes three key fields—the purpose, vendor, and contract number fields—that provide crucial supporting documentation for the obligation, VA policies and procedures were not sufficiently detailed to specifically require this type of information needed to adequately document miscellaneous obligations. During the period covered by our review, VA did not have specific guidance as to

[9] Department of Veterans Affairs, Office of Inspector General, *Audit of Alleged Mismanagement of Government Funds at the VA Boston Healthcare System*, Report No. 06–00931–139 (Washington, D.C.: May 31, 2007).
[10] Grant Thornton, *Department of Veterans Affairs, OMB Circular A–123, Appendix A—Findings and Recommendations Report (Procurement Management)*, (July 18, 2007).
[11] In 8 of the 23 cases, one official requested and approved a miscellaneous obligation. For the remaining 15 cases, one official performed those two tasks plus one or more other key tasks, such as recording the obligation of funds and certifying receipt of goods and services and approving payment.
[12] GAO, Standards for Internal Control in the Federal Government, GAO/AIMD–00–21.3.1 (Washington, D.C.: November 1999).
[13] 31 U.S.C. § 1501(a).

what information should be included in the purpose field, including such essential data as the nature and extent of the transaction. Further, during our case studies, we found many instances where these fields on the miscellaneous obligation form were left blank or did not provide adequate information as a result of this control design flaw.

Specifically, in our case studies, we found that these control design flaws resulted in the purpose field on 8 of the 42 miscellaneous obligations having insufficient data to determine whether the miscellaneous obligation represented a bona fide need. In many instances, while the stated purposes may have been adequate for the requesters and approving officials in the using services, this level of documentation was not sufficient for an independent reviewer to determine from the purpose field what items were procured and whether the appropriate budget object code was charged. As a result of these deficiencies in the design of controls, in several cases we had to rely on invoices to determine the probable purpose of the miscellaneous obligation and whether it represented a bona fide need. For example, in Kansas City, we found one miscellaneous obligation for over $1.3 million whose purpose was listed as "To obligate funds for the Oct 06 payment," while the associated invoices showed that the miscellaneous obligation was used to cover the services of medical resident staff. In another instance, we found a miscellaneous obligation for over $53,000 whose purpose was listed as "October billing," while the associated invoices showed that the miscellaneous obligation was used for the automated prescription services provided at the Kansas Soldiers Home in October 2007. In another case in Pittsburgh, we found a miscellaneous obligation for over $45,000 whose purpose was listed as "LABCORP 5/1–5/31/07," while the associated invoices showed that the obligation was for laboratory testing services. Without procedures calling for more definitive descriptions of the purpose, we could not confirm that these miscellaneous obligations were for bona fide needs or that the invoices reflected a legitimate use of Federal funds.

Although appropriation law provides that the basis for the amount obligated should be documented, we found deficient VA control design resulted in several miscellaneous obligations at one location with inadequate support for the recorded obligations.[14] For example, according to our analysis of the IFCAP database, 12 miscellaneous obligations, for a total of almost $1.3 million, were created using no-year funds[15] by the VA Pittsburgh Medical Center on September 28, 2007, to support the St. Clairsville community-based outpatient clinic. One miscellaneous obligation for $106,400 covered March 2008 services, and another miscellaneous obligation for $108,400 covered April 2008 services by the clinic. The purpose fields for the two miscellaneous obligations did not provide an explanation of how the estimates were calculated. When asked, medical center officials stated that the estimates were based on historical trends or calculations, but they did not provide any documentation to support the estimates. Furthermore, established control procedures did not require them to do so. In another instance, the VA Kansas City Medical Center obligated $200,000 for "patient care services at the Kirksville community-based outpatient clinic from 10/01/06 to 12/31/06." The purpose field did not provide an explanation of how the estimate was calculated.

Further, in the absence of explicit documentation requirements, data fields were left blank on a number of the miscellaneous obligations we examined. For example, the vendor field was left blank in 20 of the 42 miscellaneous obligations we reviewed. Current VA guidance states that the vendor field is to be left blank when multiple vendors exist since the IFCAP system allows only one vendor to be listed; however, we observed several cases where the field was left blank even when there was only one vendor. For example, in Kansas City we found obligations for electricity and natural gas where only one vendor historically had been used, but the vendor field was left blank. Similarly, in Kansas City another miscellaneous obligation was used in the procurement of $8.6 million in services at the Warrensburg Veteran's Home in Warrensburg, Missouri, but the vendor field was left blank. While payment was made to the vendor that invoiced VA in these instances, leaving the vendor field blank poses several problems for agency management, including establishing that the vendor is appropriate for the purpose of the miscellaneous obligation and verifying that the correct, authorized vendor is paid.

We also found the contract number field left blank in 16 of the 42 miscellaneous obligations reviewed, even though supporting contracts did exist for these miscella-

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[14] GAO, *Principles of Federal Appropriations Law: Third Edition, Volume II*, GAO–06–382SP (Washington, D.C.: Feb. 1, 2006).

[15] No-year funds are appropriations for which budget authority remains available for obligation for an indefinite period of time. A no-year appropriation is usually identified by language such as "to remain available until expended."

neous obligations. VA guidance did not require that the contract number be included in order to process the miscellaneous obligation. However, missing contract numbers make it difficult to determine whether VA is receiving the appropriate type and quantity of goods and services at the correct price.

Inadequate control requirements for supporting documentation and completing data fields concerning the purpose, vendor information, and contract numbers can hinder oversight by senior VA management officials. The Deputy Assistant Secretary for Logistics and Acquisition[16] said that he and other VHA officials use the IFCAP database to monitor the extent and nature of miscellaneous obligations nationwide, including analyzing the number and dollar amounts of miscellaneous obligations and identifying the types of goods and services procured using miscellaneous obligations. He told us that he was concerned with the extent and nature of the use of miscellaneous obligations at VA that he lacked adequate oversight or control over procurements made through miscellaneous obligations and that he often did not know what was being bought or who it was being bought from. Our analysis of the IFCAP database found that over 88,000 (69 percent) of 127,070 miscellaneous obligations did not include vendor information, accounting for over $5 billion of the $6.9 billion in recorded miscellaneous obligations in fiscal year 2007. Similarly, the IFCAP database did not have information on the quantities purchased or a description of what was purchased. As a result, important management information was not available to senior VA procurement officials.

New Guidance Does Not Address All Control Weaknesses

In January 2008, VA issued interim guidance effective for all miscellaneous obligations created after January 30, 2008, concerning required procedures for using miscellaneous obligations.[17] The guidance provides that prior to creating a miscellaneous obligation, fiscal service staff are required to check with the contracting activity to ensure that a valid contract is associated with the miscellaneous obligation, except in specific, itemized cases. Under this guidance, the using service is to have the contracting activity determine (1) if a valid procurement authority exists, (2) if a procurement needs to be initiated, and (3) the appropriate method of obligation. Also, this guidance requires that a copy of the head contracting official's approval be kept with a copy of the miscellaneous obligation for future audit purposes. In addition, the guidance provides that the fiscal service may not create a miscellaneous obligation without appropriate information recorded in the purpose, vendor, and contract number fields on the document. The guidance specifically cites a number of invalid uses for miscellaneous obligations, including contract ambulance, lab tests, blood products, and construction, but did not always specify a procurement process to be used for these items.

In May 2008, VHA management finalized the interim guidance.[18] This guidance represents a step in the right direction. It includes a manual process for documenting contracting approval of miscellaneous obligations and specifically states that a miscellaneous obligation cannot be created if the vendor, contract number, and purpose fields are incomplete. However, the new guidance does not address the segregation of duties issues we and others have identified and does not establish an oversight mechanism to ensure that control procedures outlined are properly implemented.

In our view, VHA has missed an opportunity to obtain an important legal perspective on this matter. According to VA officials, these policies have not been subject to any legal review. Such a review is essential in ensuring that the policies and procedures comply with Federal funds control laws and regulations and any other relevant VA policies or procedures dealing with budgetary or procurement matters. For example, such a review would help ensure that the guidance adequately addresses Federal Acquisition Regulations, requiring that no contract shall be entered into unless the contracting officer ensures that all requirements of law, executive orders, regulations, and all other applicable procedures, including clearances and approvals, have been met.[19] In addition, a review could help to ensure that this guidance (1) provides that all legal obligations of VA are supported by adequate documentation to meet the requirements of the recording statute 31 U.S.C. § 71501(a) and (2) prevents any individual from committing the government for purchases of supplies,

[16] This official acts as VA's Senior Procurement Executive and oversees the development and implementation of policies and procedures for departmentwide acquisition and logistics programs supporting all VA facilities.

[17] Department of Veterans Affairs Memorandum, *Interim Guidance on Miscellaneous Obligations, VA Form 4–1358*, dated January 30, 2008.

[18] Department of Veterans Affairs Memorandum, *Revised Guidance for Processing of Miscellaneous Obligations, VA Form 4–1358*, dated May 18, 2008.

[19] 48 C.F.R. 1.602–1 (b).

equipment, or services without being delegated contracting authority as a contracting officer, purchase card holder, or as a designated representative of a contracting officer.[20] The absence of a legal review to determine the propriety of VA's miscellaneous obligations policies and procedures places VA at risk of not complying with important laws and regulations.

In conclusion, Mr. Chairman, without basic controls in place over billions of dollars in miscellaneous obligations, VA is at significant risk of fraud, waste, and abuse. Effectively designed internal controls serve as the first line of defense for preventing and detecting fraud, and they help ensure that an agency effectively and efficiently meets its missions, goals, and objectives; complies with laws and regulations; and is able to provide reliable financial and other information concerning its programs, operations, and activities. Although miscellaneous obligations can facilitate and streamline the procurement process, they require effectively designed mitigating controls to avoid impairing full accountability and transparency. In the absence of effectively designed key funds and acquisition controls, VA has limited assurance that its use of miscellaneous obligations is kept to a minimum, for bona fide needs, in the correct amount, and to the correct vendor. Improved controls in the form of detailed policies and procedures, along with a management oversight mechanism, will be critical to reducing the government's risks from VA's use of miscellaneous obligations.

To that end, our draft report includes specific recommendations, including a number of preventive actions that, if effectively implemented, should reduce the risks associated with the use of miscellaneous obligations. We are making recommendations to VA to modify its policies and procedures, in conjunction with VA's Office of General Counsel, to better ensure adequate oversight of miscellaneous obligations by contracting officials, segregation of duties throughout the process, and sufficient supporting documentation for miscellaneous obligations.

Mr. Chairman, this completes my prepared statement. I would be happy to respond to any questions you or other Members of the Subcommittee may have at this time.

GAO Contact

For more information regarding this testimony, please contact Kay Daly, Acting Director, Financial Management and Assurance, at (202) 512–9095 or dalykl@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this testimony.

Appendix I: Scope and Methodology

In order to determine how VHA used miscellaneous obligations during fiscal year 2007, we obtained and analyzed a copy of VHA's Integrated Funds Distribution, Control Point Activity, Accounting and Procurement (IFCAP) database of miscellaneous obligations for that year. IFCAP is used to create miscellaneous obligations (VA Form 4–1358) at VA, and serves as a feeder system for VA's Financial Management System (FMS)—the department's financial reporting system of record. According to VA officials, FMS cannot be used to identify the universe of miscellaneous obligations at VHA in fiscal year 2007 because FMS does not identify the procurement method used for transactions (i.e., miscellaneous obligations, purchase card, purchase order). Furthermore, FMS does not capture the contract number, requester, approving official, and obligating official for obligations. However, according to senior agency officials, the IFCAP database is the most complete record of miscellaneous obligations available at VHA and can be used to provide an assessment of how miscellaneous obligations were used during fiscal year 2007.

IFCAP's data included information on the appropriation codes, vendors, budget object codes (BOC), date and amount of obligations, obligation numbers, approving officials, and VISN and VHA station for VHA miscellaneous obligations. We converted the database to a spreadsheet format and sorted the data by VISN, station, and BOC to determine where and how miscellaneous obligations were used in fiscal year 2007 (see app. III and IV).

To determine whether VHA's polices and procedures are designed to provide adequate controls over the use of miscellaneous obligations, we first reviewed VHA's policies and procedures governing the use of miscellaneous obligations at VA. Specifically, we reviewed the *VA Controller Policy, MP–4, Part V, Chapter 3, Section A, Paragraph 3A.02—Estimated Miscellaneous Obligation or Change in Obligation (VA Form 4–1358)*; the VA Office of Finance Bulletin 06GA1.05, *Revision to MP–4, Part V, Chapter 3, Section A, Paragraph 3A.02—Estimated Miscellaneous Obligation or Change in Obligation (VA Form 4–1358)*, dated September 29, 2006; VA *Interim*

[20] 48 C.F.R. 801.601 (b).

Guidance on Miscellaneous Obligations, VA Form 1358, dated January 30, 2008; VHA *Revised Guidance for Processing of Miscellaneous Obligations, VA Form 1358*, dated May 18, 2008; and other VA and VHA directives, policies, and procedures. We also used relevant sections of the *Federal Acquisition Regulations* (FAR); VA's Acquisition Regulations; appropriation law; and GAO's *Standards for Internal Control in the Federal Government* in assessing the design of VA's policies and procedures, and we met with VA and VHA officials in Washington, D.C., and coordinated with VHA's Office of Inspector General staff to identify any previous audit findings relevant to our audit work. We also interviewed representatives of VA's independent public accounting firm and reviewed copies of their reports.

In order to better understand the extent and nature of VA policy and procedure design deficiencies related to miscellaneous obligations, we conducted case studies at three VHA stations in Cheyenne, Wyoming; Kansas City, Missouri; and Pittsburgh, Pennsylvania.[21] The stations in Kansas City and Pittsburgh were selected because they had a high volume of miscellaneous obligation activity, and they were located in different regions of the country. We conducted field work at the Cheyenne, Wyoming, station during the design phase of our review to better understand the extent and nature of miscellaneous obligation control design deficiencies at a small medical center. Inclusion of the Cheyenne facility in our review increased the geographic diversity of our analysis and allowed us to compare the extent and nature of miscellaneous obligation design deficiencies at medical centers in the eastern, midwestern, and western portions of the United States.

During the case studies, we met with senior medical center administrative, procurement, and financial management officials to discuss how VA policies and procedures were designed with regard to specific obligations, and assess the control environment design for using miscellaneous obligations at the local level. We discussed how miscellaneous obligations were used as part of the procurement process and the effect of new VHA guidance on medical center operations. We also reviewed the design of local policies and procedures for executing miscellaneous obligations and conducted walk-throughs of the processes.

To provide more detailed information on the extent and nature of the control design deficiencies we found at our case study locations, we identified a nongeneralizable sample of obligations for further review at each site. Through data mining techniques, we identified a total of 42 miscellaneous obligations for more detailed examination at our case studies: 11 from Cheyenne, 17 from Kansas City, and 14 from Pittsburgh. We based our selection on the nature, dollar amount, date, and other identifying characteristics of the obligations. For each miscellaneous obligation selected, we accumulated information on the extent and nature of control design weaknesses concerning miscellaneous obligations:

- review and documentation by contracting officials;
- segregation of duties during the procurement process; and
- the purpose, timing, and documentation for obligations.

Concerning the adequacy of control design with respect to contracting review, we reviewed miscellaneous obligations for evidence of review by contracting officials and, for selected miscellaneous obligations, followed up with contracting officials to discuss contracts in place for miscellaneous obligations, whether review by contracting officials was needed, and when and how this review could occur and be documented.

Concerning the control design deficiencies with respect to segregation of duties, we reviewed miscellaneous obligation documents to determine which officials requested, approved, and obligated funds for the original miscellaneous obligations and then which officials certified delivery of goods and services and approved payment. We noted those instances where control design deficiencies permitted one official to perform multiple functions.

With respect to control design deficiencies relating to the supporting documentation for the miscellaneous obligations, we reviewed the purpose, vendor, and contract number fields for each obligation. For the purpose field, we assessed whether the required description was adequate to determine the nature, timing, and extent of the goods and/or services being procured and whether controls provided for an adequate explanation for any estimated miscellaneous obligation amounts. For the vendor and contract number fields, we assessed whether controls were designed to ensure entered information was correct, and we identified those instances where control deficiencies permitted fields to be left blank.

[21] We visited the Cheyenne VA Medical Center in Cheyenne, Wyoming; the Kansas City VA Medical Center in Kansas City, Missouri; and the VA Pittsburgh Healthcare System, H. John Heinz III Progressive Care Center in Pittsburgh, Pennsylvania.

Because of time limitations, we did not review VHA's procurement or service authorization processes. In addition, in our case study approach, we were unable to analyze a sufficient number of obligations to allow us to generalize our conclusions to the sites visited, nor to the universe of VHA medical centers. The 42 obligations represented a total of approximately $36.0 million; however, the results cannot be projected to the overall population of miscellaneous obligations in fiscal year 2007. While we found no examples of fraudulent or otherwise improper purchases made by VHA, our work was not specifically designed to identify such cases or estimate its full extent.

Data Reliability Assessment

We assessed the reliability of the IFCAP data provided by (1) performing various testing of required data elements, (2) reviewing related policies and procedures, (3) performing walkthroughs of the system, (4) interviewing VA officials knowledgeable about the data, and (5) tracing selected transactions from source documents to the database. In addition, we verified that totals from the fiscal year 2007 IFCAP database agreed with a method of procurement compliance report provided to Subcommittee staff during a September 7, 2007 briefing. We did not reconcile the IFCAP miscellaneous obligations reported to us to FMS—the VA system of record—and published VA financial statements because FMS does not identify the procurement method used for transactions (i.e., miscellaneous obligations, purchase card, purchase order). We determined that the data were sufficiently reliable for the purposes of our report and that they can be used to provide an assessment of how miscellaneous obligations were used during fiscal year 2007.

We briefed VA and VHA headquarter officials, including the Deputy Assistant Secretary for Logistics and Acquisition, as well as VHA officials at the three case study locations, on the details of our audit, including our findings and their implications. During the briefings officials generally agreed with our findings and said that they provided useful insights into problems with the miscellaneous obligation process and corrective actions that could be taken to address them. We conducted this audit from November 2007 through July 2008 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. We recently provided our draft report to the Secretary of Veterans Affairs for review and comment. Following this testimony, we plan to issue a report, which will incorporate VA's comments as appropriate and include recommendations for improving internal controls over miscellaneous obligations.

Appendix II: Background

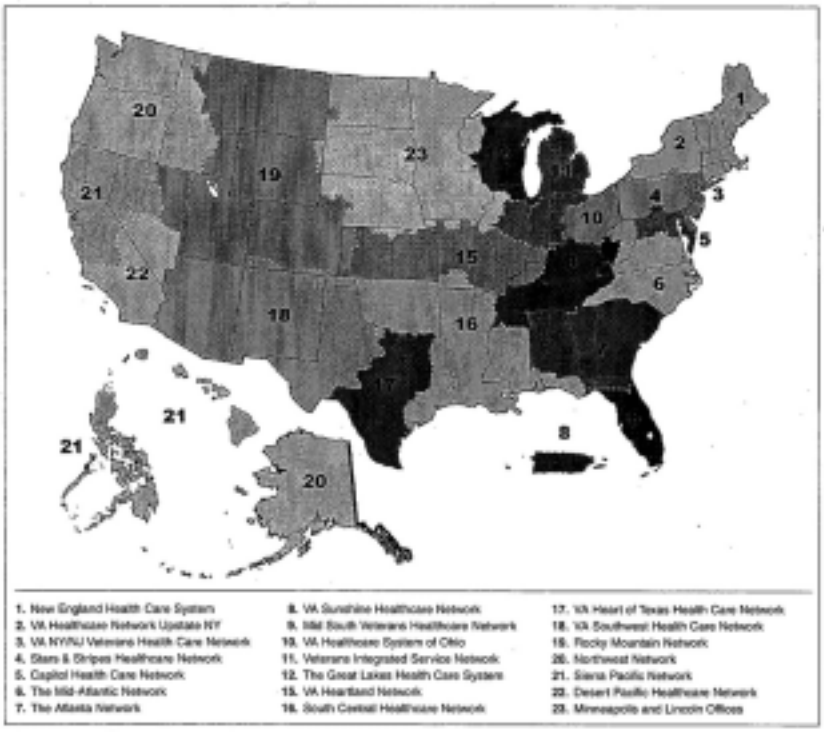
The Department of Veterans Affairs (VA) is responsible for providing Federal benefits to veterans. Headed by the Secretary of Veterans Affairs, VA operates nationwide programs for healthcare, financial assistance, and burial benefits. In fiscal year 2007, VA received appropriations of over $77 billion, including over $35 billion for healthcare and approximately $41.4 billion for other benefits. The Congress appropriated more than $87 billion for VA in fiscal year 2008.

The Veterans Health Administration (VHA) is responsible for implementing the VA medical assistance programs. In fiscal year 2007, VHA operated more than 1,200 sites of care, including 155 medical centers, 135 nursing homes, 717 ambulatory care and community-based outpatient clinics, and 209 Readjustment Counseling Centers. VHA healthcare centers provide a broad range of primary care, specialized care, and related medical and social support services. The number of patients treated increased by 47.4 percent from 3.8 million in 2000 to nearly 5.6 million in 2007 due to an increased number of veterans eligible to receive care.

As shown in figure 2, VHA has organized its healthcare centers under 21 Veterans Integrated Services Networks (VISN),[22] which oversee the operations of the various medical centers and treatment facilities within their assigned geographic areas. During fiscal year 2007, these networks provided more medical services to a greater number of veterans than at any time during VA's long history.

[22] VISNs 13 and 14 were consolidated and designated VISN 23.

Figure 2: Veterans Integrated Services Networks (VISN)



Source: U.S. Department of Veterans Affairs

VA Policies and Procedures Concerning the Use of Miscellaneous Obligations

VA has used "Estimated Miscellaneous Obligation or Change in Obligation" (VA Form 4–1358) to record estimated obligations for goods and services for over 60 years. According to VA policy,[23] miscellaneous obligations can be used to record obligations against appropriations for the procurement of a variety of goods and services, including fee-based medical, dental, and nursing services; non-VA hospitalization; nursing home care; beneficiary travel; rent; utilities; and other purposes. The policy states that miscellaneous obligations should be used as obligation control documents when a formal purchase order or authorization is not required, and when necessary to record estimated obligations to be incurred by the subsequent issue of purchase orders. The policy also states that the use of miscellaneous obligations should be kept to an absolute minimum, consistent with sound financial management policies regarding the control of funds, and should only be used in cases where there was a bona fide need for the goods and services being procured.

In September 2006, VA policy for miscellaneous obligations was revised in an attempt to minimize the use of miscellaneous obligations as an obligation control document.[24] The revision states that miscellaneous obligations should not be used as an obligation control document unless the head contracting official for the station

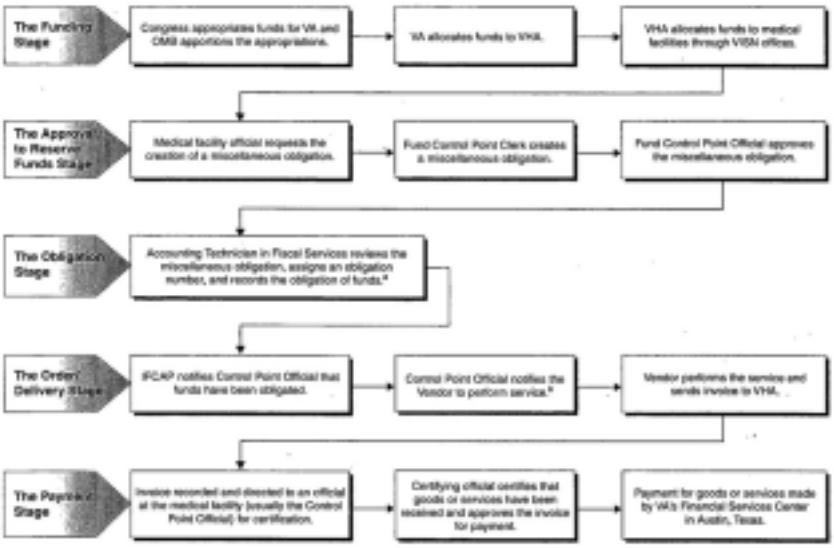
[23] VA Office of Finance Directives, *VA Controller Policy, MP–4, Part V, Chapter 3, section A, Paragraph 3A.02—Estimated Miscellaneous Obligation or Change in Obligation (VA Form 4–1358)*, accessed from www.va.gov on 12/12/2007.

[24] VA Office of Finance Bulletin 06GA1.05, *Revision to MP–4, Part V, Chapter 3, section A, Paragraph 3A.02—Estimated Miscellaneous Obligation or Change in Obligation (VA Form 4–1358)*, dated September 29, 2006.

has determined that a purchase order[25] or contract will not be required. However, the policy provides that fiscal staff can use miscellaneous obligations as a tracking mechanism for obligations of variable quantity contracts,[26] as well as for public utilities. In January 2008, VA issued interim guidance regarding the use of miscellaneous obligations;[27] however, the guidance did not apply to the fiscal year 2007 miscellaneous obligations we reviewed.

In recent years VHA has attempted to improve its oversight of miscellaneous obligations. For example, VHA's Clinical Logistics Group created the Integrated Funds Distribution, Control Point Activity, Accounting and Procurement (IFCAP) system database in April 2006 to analyze the use of miscellaneous obligations agencywide. The database is updated on a monthly basis and contains information on the miscellaneous obligations created monthly by the 21 VISN offices and their associated stations. VHA officials are using the IFCAP database to (1) analyze the number and dollar amounts of procurements being done using contracts and purchase cards, and recorded using miscellaneous obligations, and (2) identify the types of goods and services recorded as miscellaneous obligations. Prior to the creation of the IFCAP database, such information on the use of the miscellaneous obligations nationwide was not readily available to VHA upper level management.

Figure 3: VA's Miscellaneous Obligation Process



Source: GAO analysis of VA policy and procedures.

[a] In many transactions, the amount recorded reflects an administrative reservations of funds for which no obligations have yet been incurred.

[b] Our review did not include the processes VHA officials may use to incur legal obligations such as the issuance of purchase orders, delivery orders, or by other means.

VHA's Current Miscellaneous Obligation Process

The creation and processing of miscellaneous obligations (VA Form 4–1358) is documented in IFCAP—a component of VA's Veterans Health Information System and

[25] A purchase order is written authorization for a supplier to ship products to an agency at a specified price. Purchase orders may be supported by an underlying contract or function as the sole legally binding document.

[26] In variable quantity contracts, the quantity of goods to be furnished or services to be performed may vary. Variations may be at the option of VA or the contractor. Under variable quantity contracts, normally no amount is obligated at the time the contract is signed. The order, which comes after the contract, obligates VA for goods or services and the obligation must be recorded for the exact amount, or a reasonable estimate of the order.

[27] Department of Veterans Affairs Memorandum, *Interim Guidance on Miscellaneous Obligations, VA Form 1358*, dated January 30, 2008.

Technology Architecture (VISTA). The miscellaneous obligation request passes through several stages illustrated in figure 3.[28]

Appendix III: Miscellaneous Obligations by VISN in Fiscal Year 2007

VISN [a]	VISN Name	Number	Dollar Amount	Percent of Total
1	New England Healthcare System	6,638	$ 360,762,340	5.2%
2	VA Healthcare Network Upstate New York	2,910	$ 160,799,144	2.3%
3	VA New York/New Jersey Veterans Healthcare Network	7,248	$ 256,453,022	3.7%
4	Stars and Stripes Healthcare Network	12,321	$ 328,355,399	4.8%
5	Capitol Health Care Network	2,024	$ 185,679,821	2.7%
6	The Mid-Atlantic Network	2,808	$ 304,500,111	4.4%
7	The Atlanta Network	4,548	$ 440,137,101	6.4%
8	VA Sunshine Healthcare Network	9,985	$ 496,497,019	7.2%
9	Mid South Veterans Healthcare Network	4,461	$ 356,353,797	5.2%
10	VA Healthcare System of Ohio	5,093	$ 247,515,982	3.6%
11	Veterans Integrated Service Network	3,947	$ 261,290,926	3.8%
12	The Great Lakes Health Care System	4,284	$ 293,466,391	4.2%
15	VA Heartland Network	5,941	$ 300,314,177	4.3%
16	South Central Healthcare Network	9,859	$ 551,236,444	8.0%
17	VA Heart of Texas Health Care Network	2,388	$ 292,273,521	4.2%
18	VA Southwest Healthcare Network	6,308	$ 346,135,243	5.0%
19	Rocky Mountain Network	3,332	$ 220,514,581	3.2%
20	Northwest Network	9,370	$ 360,007,803	5.2%
21	Sierra Pacific Network	11,262	$ 403,378,623	5.8%
22	Desert Pacific Healthcare Network	1,906	$ 388,244,689	5.6%
23	Minneapolis & Lincoln Offices	10,437	$ 354,911,219	5.1%
	Total	**127,070**	**$6,908,827,084**	**100%**

Source: GAO analysis of IFCAP database.
[a] VISNs 13 and 14 were consolidated and designated as VISN 23.

Appendix IV: VHA Stations Ranked by Use of Miscellaneous Obligations

Rank	Station	Facility Number	VISN	Number	Amount
1	Omaha	636	23	6,832	$158,912,717
2	North Florida/South Georgia VHA	573	8	4,131	145,875,702
3	Kansas City	589	15	3,603	171,613,075
4	Pittsburgh HCS–University Drive	646	4	3,567	69,880,889
5	VA New York Harbor HCS–NY CA	630	3	3,280	85,275,329
6	San Francisco	662	21	3,200	89,361,982
7	N. California HCS–Martinez	612	21	3,166	88,567,989
8	Upstate New York HCS	528	2	2,910	160,779,144
9	Philadelphia	642	4	2,536	77,015,657
10	VA Boston HCS–Boston Div.	523	1	2,351	102,803,146
11	St. Louis–John Cochran	657	15	2,338	128,701,102

[28] Further details on processes in place are described in the *Integrated Funds Distribution Control Point Activity, Account and Procurement (IFCAP) PPM Accountable Officer User's Guide, Version 5.1*, Revised May 2007.

Appendix IV: VHA Stations Ranked by Use of Miscellaneous Obligations—Continued

Rank	Station	Facility Number	VISN	Number	Amount
12	Seattle	663	20	2,030	110,264,551
13	G.V. (Sonny) Montgomery VAMC	586	16	1,964	84,782,426
14	VAMC Bronx	526	3	1,743	37,336,434
15	Northern Arizona HCS	649	18	1,706	30,897,276
16	Miami	546	8	1,686	64,028,264
17	Middle Tennessee HCS	626	9	1,644	102,901,107
18	Cleveland–Wade Park	541	10	1,642	119,323,832
19	Portland	648	20	1,602	88,110,706
20	VA Palo Alto HCS–Palo Alto	640	21	1,498	100,993,614
21	Clarksburg	540	4	1,470	25,244,100
22	Amarillo HCS	504	18	1,453	32,694,257
23	Central California HCS (Fresno)	570	21	1,403	30,528,159
24	Fayetteville AR	564	16	1,386	42,468,351
25	Boise	531	20	1,385	35,371,800
26	New Orleans	629	16	1,369	57,125,143
27	VA New Jersey HCS	561	3	1,366	65,538,526
28	W Palm Beach	548	8	1,318	56,059,142
29	Dayton	552	10	1,306	43,574,791
30	Fort Meade	568	23	1,284	28,139,258
31	Bay Pines	516	8	1,128	76,081,613
32	Lebanon	595	4	1,105	29,330,151
33	Alaska HCS	463	20	1,090	55,377,371
34	Togus	402	1	1,085	52,777,782
35	Baltimore	512	5	1,060	92,856,732
36	Chillicothe	538	10	1,037	16,704,890
37	Oklahoma City	635	16	1,020	80,419,697
38	Roseburg HCS	653	20	996	21,172,773
39	Lexington–Leestown	596	9	987	48,090,092
40	Milwaukee WI	695	12	974	59,113,209
41	Walla Walla	687	20	964	13,199,190
42	Dallas VAMC	549	17	942	100,556,097
43	Fargo	437	23	937	26,988,919
44	Wilmington	460	4	923	24,534,375
45	Providence	650	1	900	31,961,444
46	Pacific Islands HCS (Honolulu)	459	21	894	57,759,481
47	Southern Oregon Rehabilitation	692	20	883	11,294,874
48	Phoenix	644	18	879	84,069,252
49	Columbia SC	544	7	870	70,594,890
50	Wilkes Barre	693	4	861	26,987,646
51	Houston	580	16	855	67,739,913
52	Augusta	509	7	846	53,390,674
53	Tampa	673	8	838	116,270,986

Appendix IV: VHA Stations Ranked by Use of Miscellaneous Obligations—Continued

Rank	Station	Facility Number	VISN	Number	Amount
54	Alexandria	502	16	830	25,417,175
55	Gulf Coast HCS	520	16	823	46,044,544
56	Hines	578	12	813	72,402,760
57	Eastern Colorado HCS	554	19	803	82,599,599
58	Salt Lake City HCS	660	19	803	68,390,644
59	San Antonio VAMC	671	17	801	113,175,496
60	Butler	529	4	792	15,272,087
61	West Haven	689	1	731	80,337,724
62	Ann Arbor HCS	506	11	715	50,017,830
63	N. Indiana HCS–Marion	610	11	706	33,501,439
64	Coatesville	542	4	702	17,933,344
65	Chicago HCS	537	12	700	53,085,848
66	El Paso HCS	756	18	699	24,242,716
67	Madison WI	607	12	696	46,845,867
68	VA Sierra Nevada HCS	654	21	691	31,948,186
69	Huntington	581	9	690	32,256,564
70	Greater Los Angeles HCS	691	22	670	113,284,821
71	Detroit (John D. Dingell)	553	11	667	41,810,942
72	New Mexico HCS	501	18	666	84,082,667
73	Tuscaloosa	679	7	650	20,128,372
74	Temple VAMC	674	17	645	78,541,658
75	Indianapolis	583	11	645	54,906,324
76	Muskogee	623	16	645	39,781,639
77	Montana HCS	436	19	645	32,278,047
78	Durham	558	6	639	61,960,744
79	Sheridan	666	19	629	12,501,607
80	Manchester	608	1	606	27,003,396
81	White River Jct	405	1	580	28,279,283
82	S. Arizona HCS	678	18	578	69,574,532
83	Columbus	757	10	570	25,461,020
84	Central AR. Veterans HCS LR	598	16	564	70,779,560
85	Washington	688	5	563	65,013,443
86	Illiana HCS (Danville)	550	11	543	19,659,628
87	Cincinnati	539	10	538	42,451,450
88	Minneapolis	618	23	534	93,816,762
89	Mountain Home	621	9	517	57,849,934
90	Orlando	675	8	505	9,342,539
91	San Diego HCS	664	22	503	76,890,097
92	Decatur	508	7	494	103,798,914
93	Richmond	652	6	490	50,242,036
94	Montgomery	619	7	488	33,582,736
95	Birmingham	521	7	481	75,609,201

Appendix IV: VHA Stations Ranked by Use of Miscellaneous Obligations—Continued

Rank	Station	Facility Number	VISN	Number	Amount
96	Iron Mountain MI	585	12	459	16,882,679
97	St. Cloud	656	23	456	17,539,831
98	Louisville	603	9	438	51,080,527
99	W.G. (Bill) Hefner Salisbury V	659	6	438	50,753,235
100	VAMC Nortport	632	3	433	45,155,858
101	VA Hudson Valley HCS–Montrose	620	3	426	23,146,875
102	Spokane	668	20	420	25,216,539
103	Manila	358	21	410	4,219,213
104	Charleston	534	7	407	44,239,266
105	Overton Brooks VAMC	667	16	403	36,677,997
106	Martinsburg	613	5	401	27,809,646
107	Sioux Falls	438	23	394	29,513,732
108	San Juan	672	8	379	28,838,772
109	North Chicago IL	556	12	353	31,553,133
110	Battle Creek	515	11	337	43,990,975
111	Saginaw	655	11	334	17,403,788
112	West Texas HCS	519	18	327	20,574,543
113	Salem	658	6	326	30,946,603
114	Dublin	557	7	312	38,793,048
115	Loma Linda VAMC	605	22	298	64,213,454
116	Tomah	676	12	289	13,582,895
117	Beckley	517	6	274	11,949,194
118	Cheyenne	442	19	250	13,484,935
119	Fayetteville NC	565	6	243	42,688,173
120	Southern Nevada HCS	593	22	236	95,628,301
121	Bedford	518	1	229	13,576,881
122	Asheville–Oteen	637	6	203	28,266,374
123	Grand Junction	575	19	202	11,259,749
124	Long Beach HCS	600	22	199	38,228,015
125	Hampton	590	6	195	27,693,752
126	Erie	562	4	191	15,333,253
127	Memphis	614	9	185	64,175,573
128	James E. Van Zandt VA (Altoona)	503	4	174	26,823,897
129	Northampton	631	1	156	24,022,684
	Total			127,070	$6,908,827,084

Source: GAO analysis of IFCAP database.

Prepared Statement of Hon. Robert J. Henke, Assistant Secretary for Management, U.S. Department of Veterans Affairs, as presented by Edward J. Murray, Deputy Assistant Secretary for Finance, Deputy Chief Financial Officer, Office of Management, U.S. Department of Veterans Affairs

Mr. Chairman and Members of the Subcommittee, I am pleased to have the opportunity to provide written testimony on the draft Government Accountability Of-

fice (GAO) report entitled "Veterans Health Administration: Improvements Needed in Design of Controls over Miscellaneous Obligations." Testifying on my behalf today and representing the Office of Management is Mr. Edward Murray, VA's Deputy Assistant Secretary for Finance. In 2007 the Department of Veterans Affairs (VA), Veterans Health Administration (VHA), used miscellaneous obligations to record over $6.9 billion against its appropriations that directly provide veteran care and support. Seventy-five percent of those obligations were related to providing medical and dental care, pharmaceuticals, and hospital supplies for veterans.

We agree with all four of GAO's recommendations and we are prepared to discuss the various initiatives planned or currently underway that support those recommendations to reduce the internal control risks associated with the use of miscellaneous obligations and to minimize their use. Our leadership is committed to clearly articulating the expectation that VA will work to improve the guidance, oversight, and business processes associated with the use of miscellaneous obligations in the delivery of services to our veterans.

We are issuing additional policy and guidance, which will result in improved accountability of the miscellaneous obligations process. We have reports that will enable us to track these improvements. Interim guidance was issued in January 2008 and was further refined in May 2008 by VHA since they are the predominant user of this method of financial obligation. The Office of General Counsel has reviewed the interim guidance and has determined that the new guidelines, coupled with existing VA accounting policy, meet legal recording requirements. A Department level policy will be issued in the near future.

I would like to begin by addressing VA's efforts to strengthen its policies and oversight related to the use of miscellaneous obligations while continuing to provide medical services and supplies for veterans. My Office of Finance has been collaborating with VHA to develop policies to achieve those recommendations. We will also coordinate with the Office of General Counsel. I would like to discuss the plan of action to address the four GAO recommendations:

GAO Recommendation 1. Establish a process for the review of miscellaneous obligations by contracting officials, including requiring appropriate documentation that the review has occurred.

The current process in the interim VHA guidance requires new requests for miscellaneous obligations be routed for review by the appropriate contracting official and documentation of this review be documented by e-mail and included in the record for the obligation. This interim process will be used until a system change can be made to accomplish this electronically in the Integrated Funds Distribution, Control Point Activity, Accounting and Procurement (IFCAP) system. The ability to create an electronic workflow, which allows the system to route documents through predefined reviews, is already a documented requirement for the Integrated Financial Accounting System (IFAS), the financial component of the Financial and Logistics Integrated Technology Enterprise (FLITE) Program.

GAO Recommendation 2. Segregate duties for (1) creating, approving, and recording miscellaneous obligations, (2) the certification and payment of invoices, and (3) the receipt of the resulting goods or services.

Miscellaneous obligation forms are used for both procurement and non-procurement expenditure obligations. If the miscellaneous obligation is for goods or services not required to follow formal procurement procedures (non-procurement items), such as fee basis medical or dental services, authorizations for individual patients are tracked in the Fee Basis software system, which includes the appropriate approval requirements by the Requesting Service Approving Official, and payment of invoices is approved by a Fiscal Office employee, which provides appropriate segregation of duties. Receipt for medical or dental services is documented by either an industry standard billing abstract document (UB04 or CMS 1500) or clinical information from the non-VA provider. Fee Basis obligations totaled approximately $3.8 billion in fiscal year (FY) 2007. Other non-procurement obligations, such as services from other Federal Government agencies, employee travel and tuition, residency agreements with affiliated universities, tort claims/settlements, and regulated utilities are all documented with backup source documents supporting the associated miscellaneous obligation document.

If the miscellaneous obligation is for one of the few procurement items approved to be documented by use of a miscellaneous obligation, such as nursing homes or home oxygen, separate software programs in the Veterans Health Information Systems Technology Architecture (VistA) are used to track all individual expenditures, which includes the appropriate approval by the Requesting Service Approving Official and the payment of invoices by Finance Service employees. Verification that

goods and services were received is made by the designated Contracting Officer Technical Representative (COTR) for the individual contracts. Contracting officers perform all procurement duties for awarding the Indefinite Delivery/Indefinite Quantity (IDIQ) contracts, and delegate authority to the COTR to place delivery or task orders against those established contracts and obligate the funds using a miscellaneous obligation method.

Future enhancements under IFAS include replacement of the de-centralized IFCAP system. The resulting centralized system will have one point for controlling user provisioning that precludes individual stations from granting users multiple accesses to various functions. This will improve and ensure segregation of actions.

One of the largest expenditures ($1.3 billion in FY 2007) obligated through miscellaneous obligation forms is for Pharmaceutical Prime Vendor drug purchases. These expenditures are made against an established Prime Vendor contract, which was competitively awarded by a contracting team. Between June 2 and July 2, 2008, ten web seminar training sessions were conducted for pharmacy and fiscal employees to establish a new mandatory process for documenting individual order information, using the electronic miscellaneous obligation form (VA Form 4–1358). This new process provides a check and balance between the ordering and payment processes. Receiving duties are performed by separate individuals.

GAO Recommendation 3. Document the purpose, vendor, and contract number for miscellaneous obligations.

The interim VHA guidance specifically requires that miscellaneous obligations not included on the exception list are documented with the purpose, vendor and contract number (if applicable). All exceptions for the use of miscellaneous obligations are stipulated in VHA "Revised Guidance on Miscellaneous Obligations, VA Form 4–1358" which specifies the authority to be provided when using that exception. These same requirements will be included in the official Departmental policy when it is issued. Under the IFAS system, these three fields will be required to be completed in order to process the miscellaneous obligation. Going forward the IFAS system which precludes processing of the miscellaneous obligation unless the 3 required fields are completed.

GAO Recommendation 4. Establish an oversight mechanism to ensure that these control policies and procedures are fully and effectively implemented.

VHA will now track and trend the number and dollar amount of funds obligated using miscellaneous obligations in VHA by Budget Object Code every month. This will enable VHA to determine whether our facilities are adhering to VA and VHA policy. At this time, VHA is pursuing a new IFCAP patch that will provide an automated method for verifying that the purpose, vendor and contract number fields have been recorded on the miscellaneous obligation. My Office of Business Oversight (OBO) will also review miscellaneous obligations during field reviews, with special emphasis on reviewing adherence to control policies and procedures in the use of miscellaneous obligations.

Summary

VA is taking meaningful steps to resolve the current challenges concerning the use of miscellaneous obligations. VA remains committed to improving its processes and we are confident that our challenges can be overcome for the benefit of both the veterans that we serve and the taxpayers. I assure you: VA understands our challenges and is dedicated to improvement.

This concludes my statement. The witnesses would be pleased to answer any questions the Subcommittee may have.

Statement of Hon. Cliff Stearns, a Representative in Congress from the State of Florida

Mr. Chairman,

I thank you for holding this hearing today to re-evaluate the quality of the system of controls in the VA's internal contracting process and its fervent use of Miscellaneous Obligations (MOs). The VA uses MOs to obligate funds when the amount to be spent on large expenditures—such as fee-basis care—is uncertain. The GAO has recently found that the VA procured billions through the use of MOs in FY2007. At a hearing last year, we also heard about cases of mismanagement of funds and circumventions of the control procedures in the contracting system. It's therefore no secret that the VA has a history of inadequate oversight of its procurement process, and it's important that we re-visit this issue today.

Last year, the Secretary of Veterans Affairs stressed, in a memorandum to key VA officials, the need for stronger internal controls. He said, "It is extremely important to me and to our constituents that we have effective internal controls in place to enhance the stewardship of taxpayers' assets and programs. It is imperative that we approach this responsibility as a Department wide initiative."

Significant time has passed since this memorandum was issued, and we are here today to determine if the VA has made adequate progress. In January 2008 the VA issued new guidance for the use of miscellaneous obligations; the VA subsequently finalized this new guidance in May. The GAO has reviewed this new guidance and has stated that "while it offered some improvement, it did not fully address the specific control design flaws" that GAO had previously identified and concluded that there were "serious deficiencies in internal financial control reporting."

The GAO has now made four rather basic recommendations for the VA to consider and hopefully implement, and I am encouraged to know that the VA agrees with all four of the recommendations. I personally believe that the VA shouldn't have any problem implementing such things, for example, as GAO Recommendation #3—"documenting the purpose, vendor, and contract number for miscellaneous obligations." I am astonished, as a former business owner, to know that the VA is not properly keeping track of such an important practice that utilizes taxpayers' dollars.

The bottom line, Mr. Chairman, is that the VA does not have adequate controls over its excessive use of miscellaneous obligations, and the VA has shown us that there are clearly risks associated with their excessive use of MOs.

I therefore look forward to hearing from our panel of witnesses, and I hope to see the VA fully implement all four of the GAO's recommendations, which will significantly reduce the internal risks associated with the use of miscellaneous obligations.

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