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REVIEW OF PREMATURE PAYMENTS  
AND CASH DISCOUNT ACTIVITY  
IN AID/WASHINGTON OFFICES

AUDIT REPORT NO. 84-27

May 7, 1984

AID/Washington is paying some vendors too early, thus incurring excess interest costs; paying some vendors too late, thus losing cash discounts; and not taking all cash discounts earned. These conditions will continue unless (1) actions are taken that ensure compliance with prescribed procedures, and (2) new procedures are established and implemented that more effectively direct cash payment efforts.

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## EXECUTIVE SUMMARY

U. S. Government laws and directives require the effective management of the Government's cash transactions. Accordingly, AID established and implemented policies and procedures to insure that its bills were paid on time and to maximize the earning of economical cash discounts.

We made this review in order to evaluate AID's controls over the timing of payments and taking of cash discounts. This review essentially covered payments made by the Washington headquarters offices of AID during Fiscal Year 1983. We also tested Fiscal Year 1984 transactions because of indicated weaknesses in controls over scheduling invoices for payment. The offices examined are under the Office of Financial Management headed by the Controller. The review did not include the activities of AID overseas missions.

Most headquarters payments were concentrated in two offices--the Support Services Division and the Program Accounting Division. Precise figures on payments made by these divisions were not available. We estimated that the Fiscal Year 1983 disbursements in these divisions subject to the 30 day prompt payment requirement were about \$150 million. Disbursements subject to cash discount provisions were about \$5 million.

Our limited review in one paying division showed that excess interest costs of about \$320,000 on an annualized basis could be incurred because invoices were being scheduled for payment prematurely. At our request, the Controller agreed to review the situation in all headquarters paying offices with a view toward identifying and correcting any erroneous practices.

With respect to cash discounts, appropriate policies and procedures had been established but were not being satisfactorily implemented. As a result, paying offices did not take an estimated \$32,000 or 26 per cent of the available cash discounts of \$120,000 in Fiscal Year 1983. Of the \$32,000, invoices with cash discounts of about \$16,000 were paid within the discount period but the discounts were not taken. Compliance with established procedures needs to be improved, otherwise, these losses will continue. Increased management awareness to the problem also would reduce the amount of cash discounts being lost.

### Premature Payments Were Made

In the Program Accounting Division, most invoices included in our limited test were paid between 14-23 days after receipt of the invoice. This practice appeared to result in payments being made an average of thirteen days earlier than necessary because most invoices should not be paid until 30 days after receipt. These early payments increase the Government's cost of borrowing funds. The Controller agreed to undertake a study of the situation; consequently, we did no further work in this area. (see pp. 3-4)

### Cash Discounts Were Lost

In Fiscal Year 1983, we estimated discounts totaling about \$32,000 were lost because voucher examiners did not appropriately identify available discounts, or because the required supporting documentation for payments was not received on time. Prescribed procedures need to be effectively implemented to preclude missing out on available discounts. In the Support Services Division, the system for tracking receiving reports and administrative approvals needs to be implemented so that vouchers can be prepared for payment within the discount period. (see pp. 4)

### Discounts Were Earned But Not Taken

During Fiscal Year 1983, AID paid vendors' invoices with available cash discounts of about \$16,000, but did not take the discounts. This happened because voucher examiners apparently overlooked the terms noted on the invoices. Recoupment of these earned discounts needs to be pursued. (see pp. 5)

### Administrative Procedures Needed to be Improved

AID's guidelines provide the direction necessary for an effective cash discount program. Nevertheless, prescribed procedures were not being followed. Determinations were not made concerning the economic feasibility of taking discounts. When discounts were mistakenly taken after the discount period expired, penalties should have been paid to vendors for the differences between the due dates and the dates paid. There was no system in place, however, for determining such late payments. Vouchers were not annotated with the reasons why cash discounts were missed. Finally, reports were not made to the Central Accounting Division on cash discount activity which would have alerted management to such problems. (see pp. 7)

### Conclusions and Recommendations

Management attention needs to be focused on the cash payments area because current practices do not ensure that AID's operations are carried out efficiently or economically. Regarding financial impacts, the main problem appears to be the practice of paying invoices too early. Of lesser financial consequence, but important nevertheless, is the problem of lost discounts. Although adequate guidance exists on most matters, prescribed procedures are not always followed. In other cases, such as the failure to correlate receiving reports and administrative approvals with discount periods, there is a need for new procedures.

We are making three recommendations to correct these problems. No formal recommendation is being made at this time about the early payment of invoices because the Controller agreed to study the situation and, if appropriate, make any necessary changes. Appendix 1 contains our recommendations.

### Management Comments

We provided a draft of this report to the Controller who generally agreed with the findings. He concurred with our findings on cash discounts, but did not believe our findings on premature payments were sufficiently documented to include in our audit report. We believe our tests adequately identified the issues, and due to their significance, the related observations merited inclusion in the report.

## BACKGROUND

U. S. Government operating standards and procedures for taking cash discounts are set forth in the Prompt Payment Act (Public Law 97-177), the Office of Management and Budget Circular No. A-125, and the Department of the Treasury Fiscal Requirements Manual. These directives are incorporated into AID Handbook 19, the Office of Financial Management Internal Procedures Manual and the Controller Guidebook. In accordance with the Prompt Payment Act, AID guidelines address, among other things, (a) the economic feasibility of taking cash discounts, (b) when to pay discounted invoices, (c) the computation of penalties when cash discounts are improperly taken, (d) documentation procedures for recording lost cash discounts, and (e) the reporting of lost cash discounts to AID and to Treasury.

Effective cash management requires that appropriate policies and procedures be established and implemented so as to ensure the timely payment of invoices and the maximum earning of economical cash discounts. AID payment systems require the incorporation of payment procedures which take advantage of cash discounts as a matter of routine and eliminate any need for special handling. According to the procedures, discounts will be taken only when the discount terms yield an effective annual interest rate equivalent to, or greater than the percentage rate based on the current value of funds to the Treasury. Consistent with this prudent use of Federal funds, all discounted payments will be scheduled for check issuance on the last day of the discount period. In the event a discount is taken after the discount period has expired, an interest penalty must be paid automatically, unless corrected within 15 days. With cash discounts lost, the reason for the loss must be noted on the voucher and, upon request, the lost discounts are to be summarized and reported to AID's Central Accounting Division and to Treasury.

Payments of vendors' invoices in AID/W are made by several offices in the Office of Financial Management. Two offices, the Support Services Division and the Program Accounting Division, comprise the bulk of payment activity involving cash discounts. Each of these offices uses voucher examiners who review the invoices and eventually schedule them for payment by Treasury. Logbooks are used to track the movement of vendors' invoices through the review and approval processes. The Support Services Division logbook does not maintain the necessary information concerning receiving reports and administrative approvals to support payment. Also, the Support Services and Program Accounting Divisions do not account for or report on cash discounts earned or lost.

In March 1983, we issued Audit Report No. O-000-83-44, Survey of AID's Excess Property Program. The report disclosed cash discounts were available under the terms of certain reconditioning contracts, but that AID's voucher examiners were unaware of the terms and had not taken advantage of the discounted payment terms. Our follow-up showed that the responsible examiners were checking payment terms to the contracts. Also, the Central Accounting Division has been preparing quarterly reports of cash discounts lost for the excess property transactions. The increased attention and awareness of the

condition resulted in a sharp decrease in the number and amount of cash discounts lost under reconditioning contracts.

### OBJECTIVES, SCOPE, AND METHODOLOGY

We reviewed the cash discount activity for Fiscal Year 1983 in the Support Services Division and the Program Accounting Division of the Office of Financial Management. Little or no activity was observed in other paying offices. The objective of this part of our review was to determine how well cash discounts were being controlled.

Our examination included tests and analyses of the disbursement records and discussions with cognizant personnel. Our basic approach was to scan the files for invoices that indicated discounts were available. We then checked the payment records to see if the discounts were taken. Division officials were asked to explain why discounts were not taken.

Due to apparent weaknesses in scheduling invoices for payment, we made a test of Fiscal Year 1984 transactions to see if invoices were being paid prematurely. This condition was called to the attention of the Controller who agreed to do a more complete study of our findings and report back to us on them.

Related internal control systems covering guidance, procedures, and performance were reviewed and evaluated. The resulting economy and efficiency review was conducted in accordance with the Comptroller General's Standards for Audit of Governmental Organizations, Programs, Activities, and Functions. Our work was done during February and March 1984.

## AUDIT FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

We found that the Program Accounting Division established target dates for paying vendors' invoices and reimbursements to grantees that were earlier than necessary. This practice increased the cost of borrowing U.S. funds. We also found that AID/W had established operating procedures for cash discounts, but some procedures were only partially implemented, however, and others not at all. In addition, further procedures needed to be developed and implemented. As a result, available discounts were not taken in all cases.

### PREMATURE PAYMENTS WERE MADE

Our tests of Fiscal Year 1984 activity indicated that the Program Accounting Division was paying vendors and reimbursing grantees earlier than prescribed by the Prompt Payment Act and AID cash management policies. A minor change in vouchering procedures in this division could save the U. S. Government over \$300,000 per year in unnecessary interest costs. We did not analyze scheduling practices in other AID/W paying divisions nor in overseas paying offices.

The limited testing of payments in the Program Accounting Division indicated that the average invoice was paid in 17 days, or 13 days earlier than most prescribed due dates. Our test of early payments covered one week in each month for the period November 1983 through February 1984. We ascertained the receiving date, due date, and payment date for each of the vouchers included in the payment schedules that were prepared during the test period. The test showed that Program Accounting officials assigned due dates for payment 23 to 26 days after receipt of the invoices for 122 of 213 vouchers. However, since Treasury disregards due date instructions, most of the payments (134 of 213) were made 14 to 23 days after receipt of the invoice.

We estimated these early payments could cost Treasury about \$320,000 in additional interest costs during Fiscal Year 1984. This estimate is based on Program Accounting Division disbursements, excluding payments for advances, payments to other U.S. Government entities, and no-pay expenditures, for the four month period ending in February 1984. We estimated there would be about \$100 million of disbursements during Fiscal Year 1984 for which payments should be made within 30 days. The excess interest costs were computed by applying the average early payment period of 13 days at the current Treasury borrowing rate of 9 per cent per year ( $9\% \times \$100 \text{ million} \times 13/365 \text{ days}$ ).

The early payments result from Division officials applying two incorrect premises. The first premise assumes that payees should receive checks by the due date. The second premise assumes that Treasury complies with the due dates when it prepares and mails checks. With respect to these matters

- AID's cash management guidelines require that payments be made for receipt by the payee as close as possible to the due date where due dates are specified in the invoice, contract, or other agreement. When no due date is specified, the guidelines impose a 30 day due

date to be scheduled for the check to be mailed on that date. According to Office of Contract Management officials, most contracts and grants do not specify due dates. As a result, the payment target date for most vouchers is earlier than necessary.

- Under current vouchering instructions, voucher examiners are required to note each voucher's due date on the payment schedule. This assumes that Treasury will issue the related check on the noted due date. Treasury personnel told us that they do not take due dates into account when issuing checks. Instead, they prepare and mail checks as soon as possible after receiving payment schedules. As a result, vouchers are often paid in advance of the due date established by AID.

As a result of our findings, the Program Accounting Division initiated an expanded study of the premature payments problem and offered to report their results to us. Consequently, we did no further work in this area. Their most recent advice to us noted that the Division's target dates for payment have been advanced and they are continuing to evaluate the premature payment activity.

#### CASH DISCOUNTS WERE LOST

Our tests of AID/W disbursements disclosed cash discounts were available under contracts for excess property repairs, storage charges, disaster relief supplies, security equipment, and miscellaneous support commodities and services. We estimated that in Fiscal Year 1983 there were 456 invoices which offered cash discounts of \$120,000. We found that cash discounts of about \$32,000 or about 26 per cent of the \$120,000 available, were lost because voucher examiners did not identify available discounts. Some of these discounts were lost because receiving reports or administrative approvals were not received in time for the invoices to be paid.

The following analysis shows the estimated activity by division.

<u>Division and Source</u>	<u>Cash Discounts Available</u>		<u>Cash Discounts Lost</u>	
	<u>Number</u>	<u>Amount</u>	<u>Number</u>	<u>Amount</u>
<u>Support Services Division a/</u>				
Miscellaneous Support	77	\$ 11,968	53	\$10,431
Property Storage	80	25,450	-	-
	<u>157</u>	<u>\$ 37,418</u>	<u>53</u>	<u>\$10,431</u>
<u>Program Accounting Division</u>				
Excess Property	287	\$ 11,072	150	\$ 5,824
Disaster Relief	12	71,743	6	15,497
	<u>299</u>	<u>\$ 82,815</u>	<u>156</u>	<u>\$21,321</u>
	<u>456</u>	<u>\$120,233</u>	<u>209</u>	<u>\$31,752</u>

a/ Estimate based upon nine month analysis of Support Services Division transactions.

The two divisions used logbooks to record the movement of vendors' invoices through the review and approval processes. However, the Support Services Division did not use the prescribed AID logbook format to track the status of receiving reports and administrative approvals. Consequently, their follow-up on missing receiving reports and administrative approvals was often late and the related discounts were lost.

Recommendation No. 1

We recommend that the Office of Financial Management:

- a. establish in each AID/W paying office procedures for
  - (1) identifying invoices subject to cash discounts, and
  - (2) monitoring cash discount activity.
- b. implement in the Support Services Division the procedures prescribed for tracking the status of receiving reports and administrative approvals.

DISCOUNTS WERE EARNED BUT NOT TAKEN

Of the total discounts lost, \$957.41 in the Support Services Division and \$15,170.74 in the Program Accounting Division had not been taken, even though the invoices had been paid within the cash discount period.

<u>Vendors</u>	<u>Purchase Order, Contract, or Bureau Voucher Number</u>	<u>Discounts Lost</u>
<u>Support Services Division:</u>		
Mc-Graw Hill	843-0121	\$ 3.85
Mc-Graw Hill	843-1659	3.55
Stiffel Company	843-0352	30.45
Capital Radio	843-0364	4.54
Capital Radio	843-1705	3.48
R&R Lighting	843-0590	163.20
Eastman Kodak	843-1488	31.24
General Electric	843-1702	33.05
Visual Graphics	843-1784	11.69
Challenge Machinery	843-1871	78.20
Insulgard	OTR-000-C-00-2334-00	594.16
Subtotal		<u>\$ 957.41</u>
<u>Program Accounting Division:</u>		
Goodway Graphics	340-8934	\$ 59.50
Pfizer	440-2078	144.36
Outdoor Venture	340-7235	3,302.23
Outdoor Venture	340-7237	<u>11,664.65</u>
Subtotal		<u>\$15,170.74</u>
<u>Total</u>		<u>\$16,128.15</u>

We were told by Division officials that the reason for not taking the earned discounts was that the voucher examiners inadvertently overlooked the terms noted on the vendors' invoices. A representative of AID's General Counsel recommended that the vendors involved be contacted and reimbursement requested for the discounts not taken.

Recommendation No. 2

We recommend that the Office of Financial Management, where feasible, contact the vendors and request reimbursement for the cash discounts earned but not taken.

## ADMINISTRATIVE PROCEDURES NEEDED TO BE IMPROVED

AID Handbook 19, the Office of Financial Management Internal Procedures Manual, and the Controller Guidebook contain the direction necessary to direct an effective program for taking cash discounts. The guidance requires, among other things, that the economic feasibility of taking cash discounts be established, and that interest penalties be paid by AID when discounts are improperly taken. With respect to reporting, the guidance requires that lost discounts be reported upon the request of the Office of Financial Management or Treasury. Notwithstanding these requirements, the Support Services and Program Accounting Divisions were not following procedures necessary for effective control over cash discounts.

### Economic Feasibility of Taking Cash Discounts

Although required under AID instructions, voucher examiners were not determining the economic feasibility of taking cash discounts. The voucher examiners were either unaware of this requirement or had not been given implementing instructions. The computation involves making a comparison of the interest rates of return on the period of early payment and the cost to Treasury of borrowed funds.

Our review showed that terms of 1/4 per cent/20 days and 1/2 per cent/20 days were equivalent to 9 per cent and 18 per cent respectively. Treasury's borrowing rates in Fiscal Year 1983 ranged from 11 per cent to 13 per cent. Except for two excess property contractors, all terms offered to AID were 1/2 per cent/20 or greater and in Fiscal Year 1983 it was to AID's advantage to take the offered discount. Although AID experienced only a small loss when taking uneconomical discounts, the lost amount was a needless expense. In Fiscal Year 1984, Treasury interest rates could rise and the exercise of these controls may become more important.

### Interest Penalties for Late Cash Discounts

We found that 11 of the 18 cash discounts taken by the Support Services Division were on invoices that were not paid within the period allowed for discounts. Of these cash discount invoices, 5 were paid 1 to 5 days late and 6 were paid 8 to 31 days late. Five of the late payments were attributed to delayed schedule processing and late payment by Treasury, and one payment was due to the late receipt of a receiving report. Reasons why the other five were late were not determined.

When cash discounts are improperly taken, the paying office is required to pay the vendor an interest penalty based upon the difference in days between the due date and the date paid. Because the Support Services Division was unaware of the late payments, it did not address the issue and no interest penalties were paid. Computation of the penalties showed that none of the 11 cases exceeded \$1.00 in penalties. Related guidelines prescribe that interest penalties of less than \$1.00 need not be paid. Even so, the Support Services Division paid some vendors late, and our review showed there was no effective system to disclose late payments and the related need to make interest penalty payments.

## Reporting Cash Discounts

AID guidelines provide for reporting lost cash discounts at the request of the Central Accounting Division or Treasury. Other than for excess property disbursements, such reports have not been requested or prepared, primarily, because management was unaware of any problems in this area. At present, these reports would be difficult to prepare because the vouchering and accounting systems do not identify vouchers subject to cash discounts or lost cash discounts. Since the volume of discount transactions is not great, available and lost cash discounts could be noted in the voucher logbook where retrieval would be a simple matter. Periodic reports to the Central Accounting Division on cash discount activity would alert management to possible cash discount problems, and would appear to have special applicability at this time because of the provisions of the Prompt Payment Act.

Another procedure not being followed was the voucher examiner's notation on the invoice as to why the cash discount was lost. Reportedly, this was because management had not required compliance with this procedure. Noting the reasons for a lost discount on the invoice also would be a useful tool in alerting management to possible problems. First, it would make the certifying officer more aware of lost discounts. Secondly, it would provide management with important information concerning the cause and correction of the problems. As it is, certifying officers are generally unaware of the extent of lost cash discounts and have no information concerning the causes in specific cases.

### Recommendation No. 3

We recommend the Office of Financial Management implement in each AID/W paying office the established procedures for:

- a. determining the economic feasibility of taking cash discounts,
- b. determining late payments of vendors and related interest penalty payments,
- c. annotating vendors' invoices as to why discounts were lost,
- d. recording lost cash discounts, and
- e. reporting to the Central Accounting Division on lost cash discounts.

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LIST OF REPORT RECIPIENTS

Assistant to the Administrator for Management, AA/M	1
Controller, Office of Financial Management	2
Office of Financial Management, M/FM/ASD	1
Assistant to the Administrator, Bureau for External Affairs, AA/XA	1
Director, Office of Legislative Affairs, LEG	1
Office of Public Affairs, OPA	2
Office of General Counsel, GC	1
Bureau for Program and Policy Coordination, Office of Evaluation, PPC/E	1
Chief, Development Information Utilization Service, Bureau for Program and Policy Coordination	2
Director, Office of Management Operations, Directorate for Program and Management Services	1
Director, Executive and Overseas Management Service, Directorate for Program and Management Services	1
Inspector General, Office of the Inspector General	1
Assistant Inspector General for Audits, Office of the Inspector General	1
RIG/A/Dakar	1
RIG/A/Manila	1
RIG/A/Cairo	1
RIG/A/Karachi	1
RIG/A/Nairobi	1
AAP/New Delhi	1
RIG/A/LA/W	1
IG/II	1
IG/PPP	1
IG/EMS/C&R	16