

**University of California
Lawrence Livermore National
Laboratory**

**Business Process Internal Control
Assessment**

June 4, 2003

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Ms. Anne C. Broome
Vice President-Financial Management
University of California
1111 Franklin Street
Oakland, California 94607-5200

Subject: Report on Business Process Internal Control Assessments for Lawrence Livermore
National Laboratory

Dear Ms. Broome:

Ernst & Young (E&Y) has completed analyses of the Lawrence Livermore National Laboratory (LLNL) processes and internal controls with respect to: (i) Procurement Business Process and Application Controls; (ii) Interfaces between Procurement and Property Management and between Procurement and Accounts Payable; (iii) Property Management and Property Accounting; (iv) Accounts Payable-Disbursements and Interfaces including Oracle settings; and (v) Cash Receipts Controls in connection with Work for Others.

Our Report is attached. The report is intended solely for the information and use of the University of California Management.

Implementation of the recommendations contained in the attached Report will provide for an enhanced control environment for the LLNL processes addressed. We recommend periodic follow-up to determine accomplishment of the actions LLNL plans to implement.

We appreciate the cooperation and assistance provided to us during the course of our work. If you have any questions, please contact Mr. J. Roger Holbrook at 949.437.0312.

Sincerely,



J. Roger Holbrook
West Region Director
Government Contract Services

**University of California
Lawrence Livermore National Laboratory
Business Process Internal Control Assessment**

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I. Introduction

The University of California, Vice President - Financial Management, retained Ernst & Young LLP (E&Y) to conduct independent analyses of certain Lawrence Livermore National Laboratory (LLNL) processes and internal controls as follows:

- Analyze Procurement Business Process and Application Controls.
- Analyze interfaces between Procurement and Property Management and between Procurement and Accounts Payable.
- Analyze Property Management and Property Accounting.
- Analyze Accounts Payable-Disbursements and Interfaces including Oracle settings.
- Analyze Cash Receipts Controls in connection with Work for Others (WFOs).

In accordance with E&Y's Engagement Letter dated February 14, 2003, E&Y is pleased to provide the results of E&Y's analyses performed. The E&Y report is comprised of four (4) parts. The four parts are: an introduction (Section I), overview (Section II), procedures performed (Section III), and the detailed observations and recommendations (Section IV).

The E&Y services were performed in accordance with the Statement on Standards for Consulting Services (CS100) of the American Institute of Certified Public Accountants (AICPA) as stated in the Engagement Letter. The Standards for Consulting Services (CS100) do not result in issuance of an opinion and do not constitute an audit or an examination made in accordance with generally accepted auditing or attestation standards, the objective of which is the expression of an opinion on the elements, accounts, or items of a financial statement. As a result, E&Y does not express an opinion on LLNL's processes and internal controls. The procedures performed by E&Y did not constitute an audit or an examination made in accordance with generally accepted auditing or attestation standards.

II. Overview

A. Observations and Recommendations

During our analyses, we identified LLNL processes, procedures, and key system controls. At LLNL these include: automated system prevent and detect controls, written policies and procedures, system reports used to identify needed actions, and audits and self-assessments used to detect and correct errors or failures to follow established procedures.

As a result of the analyses performed, we have prepared observations and recommendations for enhancements to LLNL processes and internal controls. In many cases the LLNL processes require manual actions by knowledgeable employees for system operation. However, in some instances formal written policies and procedures are not in place. We observed opportunities to enhance controls through increased use of automated system features and new or revised procedures.

Section IV provides detailed observations and recommendations in the areas of (a) acquisition, (b) receipt of property, (c) use of purchase cards, (d) property management, (e) tracking and control of WIP inventory, (f) property accounting, (g) accounts payable-disbursements, (h) cash receipts in connection with WFOs, and (i) information technologies general controls. Information technology observations that relate to particular functions or interfaces are included in the observations for that area (e.g., Accounts Payable-Disbursements). Observations and recommendations concerning information technologies general controls are provided separately. We believe that implementation of the recommendations will provide for enhanced controls for the LLNL processes addressed.

B. Background

LLNL is organized in Directorates that are distinctive in their disciplines, lines of research, experiments, and expertise. By definition, the property items required for each Directorate could be very different. The specialized nature of each Directorate, makes specific knowledge of its mission(s), requirements, projects, funding, etc., key to executing day-to-day business tasks and decisions. Each Directorate is effectively a self-contained unit with many of the Property and Finance functions (e.g., Technical Release Representatives [TRRs]) reporting to the Director through Associate Directors, (e.g., Associate Director Property Representative [ADPR], Associate Director Resource Analysts [ADRA]). The Directorates operate within a framework of policies, procedures, training programs, and business system applications that are maintained and disseminated by central organizations (e.g., Finance) and are generally applied uniformly across LLNL.

1. Acquisition of Property at LLNL

LLNL has a property acquisition process defined in the Procurement and Materiel (P&M) Procedures and other media maintained by LLNL. It is supported by two major systems with a number of interfaces. The two systems are TOPS (Total On-Line Purchasing System), which includes: (1) the OLR (On-Line Requisition) subsystem, and (2) PARIS (Purchasing and Receiving Information System). TOPS is the vehicle used for generating and tracking the various types of requisitions/requests/releases/orders that either feed PARIS or form the basis for a purchasing card transaction. PARIS is the vehicle used for generating and tracking subcontracts, purchase orders, and releases against

blanket orders. PARIS is also the vehicle used for recording the receipts of property, with the exception of UniCard purchases.

Fiscal Year (FY) 2002 Purchasing awards were summarized for Internal Audit No. 03-10 as follows:

FY 2002 Purchasing		
Transaction Type	Number of Transactions	Amount (Millions)
Purchase Orders	4,900	\$341.0
Blanket Order Release	5,400	110.0
Procurement Card	97,900	75.0
Electronic Ordering System	1,500	9.0
Material Requests	15,200	4.0
Total	124,900	\$539.0

The determination of how to acquire property at LLNL can generally be regarded as a four-step assessment process to select the ordering method. In order of precedence:

- If the item is available from the LLNL Stores, purchase from the on-line LLNL Catalogue. (This method is not authorized for the purchase of attractive or controlled property)
- If the item is authorized for a UniCard purchase – make the purchase from an Electronic Data Interchange (EDI) Vendor or with UniCard direct to a supplier. (This method is not authorized for the purchase of attractive or controlled property)
- If the item is on an authorized release, make the purchase against a blanket order through an on-line requisition.
- If the item is authorized on a requisition, the buyer makes the purchase by purchase order or subcontract.

The LLNL UniCard program was instituted in 1995 after the completion of a cost-benefit analysis that focused on a possible reduction in the cost to process low-value acquisitions and did not involve “attractive” or “controlled” items. LLNL Procurement management advised us that the analysis showed significant

savings could occur through the use of credit cards by a limited number of authorized employees.

Achievement of the savings inherently involves some level of additional risk using a streamlined process and control structure for the lower value purchases that are made using UniCards. LLNL believed the potential cost savings warranted the implementation of the process, providing that it included substantive planned audits and ongoing oversight and reconciliation(s) aimed at preventing and/or identifying any inappropriate use of the credit cards.

The LLNL UniCard process has been audited a number of times; most recently by the LLNL Internal Audit and Oversight (A&O) Directorate. While some opportunities for improvement were identified, the audits have generally found that the controls in place provided a reasonable balance between controls and risks.

Prior to the new FY, the Deputy for Subcontracts submits the FY Procurement System Evaluation Plan to the Contracting Officer, National Nuclear Security Administration (NNSA), Oakland Site Office. A critical element of this plan is the self-assessment plan and criteria for the coming year. A dedicated review group and other personnel perform self-assessments throughout the year. They address the various types of purchase order/subcontract transactions performed by Procurement & Materiel's Procurement personnel. The assessments also include weekly, quarterly and special reviews of UniCard/UniCheck and release transactions performed by the LLNL TRR reviewers under P&M's cognizance.

The LLNL acquisition process has been designed around a decentralized procurement strategy that includes the functions and responsibilities of the TRR assigned to each Directorate. The approximately 280 TRRs are responsible for initiating and tracking all requisitions. With the exception of UniCard purchases and material requests and releases within a TRR's authorized purchase threshold, the TRR relies on Buyers to place orders, and Central Receiving to receive items. The TRR remains responsible for overseeing the process for the items ordered. In the case of UniCard transactions, the TRR purchases the item(s) and can receive the purchased item(s).

LLNL has found that the distribution of acquisition authority and responsibility to the TRR function has a number of advantages. However, LLNL recognizes that it also involves some level of risk and requires ongoing oversight. TRRs are generally experienced employees who have served in other capacities at LLNL. Additionally, an ongoing training program supports the TRR function, including 40 hours of initial training and annual recertification training.

Upon receipt, purchased items are processed as required (i.e., counted, inspected), dispositioned for resolution if not complete or acceptable, and accepted if appropriate. Property that is to be controlled by reason of its:

- (a) planned service life and/or its acquisition cost, or
- (b) “attractive” nature, i.e., has alternative personal use and can be easily concealed for removal

is uniquely tagged, assigned a property number, and is entered into the Property Management system. Items of lesser value, but whose nature and value would not warrant tracking, are “blue tagged” but are not given a property number and are not recorded in the Property Management system.

The table below summarizes certain key performance measures, as defined by Procurement and Materiel for the University of California in accordance with Contract W-7405-ENG-48, Appendix F – Objective Standards of Performance, for the 2002 FY:

**Reported LLNL Procurement & Materiel Key Performance Measures
For the FY Ended 30 September 2002**

Financial	
P&M Costs to Spending Ratio	1.3%
Internal Business Processes	
Subcontract Administrator/Buyer File Quality	93.4%
TRR File Quality	97.1%
Purchase Placement Average Cycle Time	12.6 days
Transactions by Rapid/Alternative Techniques	96.7%

2. Property Management

Property items include controlled and attractive/sensitive items. They are tracked and controlled at LLNL through Property Centers. Each Property Center has a Property Representative. The Property Centers are unique to each Directorate. Property Centers are the overall responsibility of each ADPR. The Property Representatives are responsible to the ADPR. Within each Property Center, individual property items are assigned a custodian, who is responsible for the location and care of the item.

The Property Center is an organizational entity established to administer a Directorate's stewardship functions for property belonging to that organization. The Property Center Representative is responsible for stewardship functions such as assigning custodians, tracking custodial changes, approving requests to remove property from the site, etc. The Property Center Representative maintains records in Sunflower Assets. There are a total of 106 Property Centers, containing approximately \$1,078,400,000 in controlled and attractive property items.

The core system supporting the Property Management function is Sunflower Assets. Within Sunflower there is an Inventory module that contains all of the active and controlled property items that have been assigned a property number. These records are the baseline used for the measurement of inventory accuracy. Each item record contains property center, custodian, and location, as well as data about the item and how it was acquired. There is also a Financial module that supports capitalized items. (This is further addressed in the next section.)

Work-in-process (WIP) items are processed using both Sunflower and PARIS. Property items that would otherwise be defined as controlled or capital items, purchased in support of a Fabrication or Construction project, may or may not be identified as property items in Sunflower prior to the completion of the project. The basis for including Fabrication/Construction property in Sunflower is typically the "property flag" setting in PARIS. WIP items are usually flagged as "N" (i.e., not requiring a property tag) and are not tagged. In only one program, NIF, are WIP items tracked and controlled (not tagged) in an inventory control system (GLOVIA), from the time they are received to their eventual consumption as a part of a Fabrication/Construction end item.

Items purchased by purchase or blanket orders enter Sunflower by a data feed from PARIS. When the data is transferred to Sunflower, the data is initially held in a suspended state until such time as a Property Control Administrator can review the data for completeness and accuracy. To support this effort, all of the PARIS purchase orders for items anticipated to be "tagged" are printed and reviewed, line-item by line-item, for each property item that is loaded into Sunflower. The objective is a 100 percent data confirmation against the purchase order for every item in Sunflower. As necessary, the Property Control Administrator is able to revise the suspended Sunflower record to match the purchase order or otherwise correct what is determined to be an incorrect record.

Prior to 1996, the accuracy of the Property records was evaluated by annual cycle counts. In 1996, Department of Energy (DOE) approved the use of stratified statistical sampling for each of two fiscal years (1996 to 1997), followed by a wall-to-wall inventory in 1998 to confirm the results of the

sampling methodology. In 1999, based upon the positive outcome of the three-year statistical sampling pilot, DOE approved a 5-year pilot. A statistical sampling methodology was used for 1999 through 2002 with a wall-to-wall inventory employed for FY 2003. At the time of our review, the wall-to-wall inventory was in process. The FY 2002 sample consisted of 3,349 controlled items with an accuracy measurement of 99.92 percent, and 1,668 attractive items with an accuracy measurement of 100 percent. The measurements are binary, i.e., the item is either found or not found during the period of the inventory.

Property data from the FY 2003 wall-to-wall inventory was summarized for Internal Audit No. 03-10 as follows:

Attractive and Controlled Property FY 2003 Wall-to-Wall Inventory Results		
Property Category	Items	Dollar Value (Millions)
Attractive	36,786	\$ 107.9
Controlled	21,601	970.5
Total	58,387	\$ 1,078.4

As items reach the end of their useful lives, or are damaged beyond repair, become contaminated, obsolete, and excess, etc., they are dispositioned and transferred to Donation Utilization and Sales (DUS). They are first offered to other potential users within LLNL, then DOE and the Federal Government, and if not claimed, are sold. Such items are retired from the active Sunflower records but are not purged from the Sunflower system; there is a record of retired (inactive) property.

The table below summarizes certain key performance measures, as defined by Property Management, for the University of California in accordance with Contract W-7405-ENG-48, Appendix F – Objective Standards of Performance, for the 2002 FY:

**Reported LLNL Property Management Key Performance Measures
For the FY Ended 30 September 2002**

Measures	
Percent of Sensitive Item Inventory Accounted for by Value	100 %
Percent of Equipment Inventory Accounted for by Value	99.9%
Percent of Property Items Recorded via Electronic Purchasing/Receiving	94.2%
Percent of Property Tagged When Received	98.5%

3. Property Accounting

Property items can be identified to one of four types of cost: 1) Operating Funded cost, 2) Capital Equipment Purchase, 3) Fabrication, or 4) Construction. The selection is made within the Directorates and the Resource Analysts (RA) open the project account. The Resource Analysts will typically determine which account should be charged when an acquisition is initiated.

Property items are either expensed as part of the project cost, or are capitalized. Capitalized items are defined as those with an acquisition cost greater than \$25,000 and a service life greater than two years. Items that are expensed are charged at the purchase order unit price. Capital equipment items that are capitalized include the associated costs of acquisition (e.g., freight-in), as defined by LLNL's CAS Disclosure Statement, as well as the acquisition cost (i.e., purchase order unit price). Depreciation is based on a straight-line algorithm used to assign depreciation cost over the defined service life of the asset.

Property items over \$25,000 purchased to support Fabrication or Construction projects may or may not be capitalized prior to the completed project being placed in service. The current practice has been to capitalize large dollar items while they are considered WIP, and to incorporate the remaining depreciation for such items into the depreciation for the entire Fabrication/Construction end-item when it is placed in service. Current policies require that betterments be capitalized.

Property Accounting is provided numerous reports and on-line screens to monitor accounting for the costs of property, including the types of cost (e.g., Fabrication), accounts used, whether an item should be capitalized, etc. These manual efforts are necessary to maintain adequate discipline in the recorded costs.

4. Accounts Payable - Disbursements

In fulfilling LLNL's financial management responsibility, LLNL employs a Financial Policies and Procedures Manual. The policies and procedures reference requirements of the DOE Accounting Handbook and Contract W-7405-ENG-48, and include certain LLNL requirements for Accounts Payable and Disbursements. The DOE Accounting Handbook presents DOE's standards, procedures, and operational requirements in support of accounting policies, principles, and other requirements for DOE operations. LLNL also employs certain working level procedures such as the Accounts Payable Procedures for Oracle Applications.

LLNL's obligations for purchased materials, subcontracts, and services procured under Contract W-7405-ENG-48 are established and accounted for using the Oracle Accounts Payable (AP) System and General Ledger. Purchase order and receiving information is received into Oracle AP from the PARIS and other feeder systems.

The Accounts Payable Group processes invoices received. They are input into Oracle AP by an Accounts Payable expediter and are to be paid based on purchase order terms. For material receipts, the expediter has the system match the invoice to purchasing and receiving information in PARIS before the invoice is processed for payment. This is referred to as a three-way-match. Where a purchase order for services requires certification, Oracle AP holds the invoice until receipt of certification from the user is entered into the system.

The interface between PARIS and Oracle AP requires manual actions by Accounts Payable as part of the ongoing work process. The Accounts Payable practices include use of invoice aging reports, PARIS Interface Reject and Warnings reports, and the accounts payable trial balance to identify items for review and any further processing actions required.

Payments for Accounts Payable are made by check, wire transfer, or electronic funds transfer (EFT). The Disbursement Operations Group processes the daily AP check register prepared by Accounts Payable. Bottomline Technology software is used to print the daily check run. The checks are maintained in a locked cabinet until distributed. A Positive Pay routine between LLNL and the Bank of America is employed by LLNL to guard against erroneous or fraudulent checks.

The Financial Operations Group processes wire transfers. Through Oracle AP, the Production Control Group initiates and encrypts the electronic transfer of funds to the appropriate bank.

The table below summarizes certain key performance measures, as defined by the Accounts Payable department, for the University of California in accordance with Contract W-7405-ENG-48, Appendix F – Objective Standards of Performance, for the 2002 FY:

**Reported LLNL Accounts Payable Key Performance Measures -
For the FY Ended 30 September 2002**

Invoice Processing	
Total Processing Costs	\$1,116,790
Cost per Transaction	\$5.55
On-time Payment Performance - PO Related Invoices	
Total PO Related Invoices	81,328
Percent Paid On-time	97.1%
Electronic Funds Transfer Payments	
Total Payments	\$883,156,846
Percent EFT Payments	83.9%
Discounts Taken	
Discounts Available	\$106,797
Percent of Discounts Taken	84.8%

5. Cash Receipts in Connection With WFOs

WFO projects are performed on a reimbursable basis for three types of customers. For FY 2002, the total WFO billings amounted to approximately \$276.3 million. The three types of customers, and their respective billing amounts, were: Other Federal Agencies (\$119.2 million), Non-Federal Agencies (\$38.2 million), and Integrated Contractors (\$118.9 million).

Three general types of transactions flow through the WFO process: (1) Cash advances for LLNL work to be performed for Non-Federal Agencies, and in some instances Federal Agencies, (2) direct billings to all three types of customers, and (3) transfers for other Federal Agencies through the Intergovernmental Payment and Collection system or transfers for Integrated Contractors through non-cash transfer vouchers. The billing amounts follow:

WFOs
FY 2002 Billings (Millions)

	Total Billings	Other Federal Agencies	Non Federal Agencies	Integrated Contractors
Transfers	\$200.0	\$84.6		\$115.4
Cash Advances	38.5	2.4	\$36.1	0.0
Direct Billings	37.8	32.1	2.1	3.5
Total	\$276.3	\$119.1	\$38.2	\$118.9

The WFO Support Group, within the Sponsor Funding and Directorate Support Division, exercises responsibilities in a number of WFO areas including: proposals, proposal reviews, funds processing, contractual terms and conditions, cost monitoring against funding limits, project closeout and billings for WFO cash advances. The Revenue Management and Business Analysis Group of the Financial Management Support Division prepares WFO billings other than for cash advances. WFO projects are generally billed monthly. The Reimbursable Work System (RWS) module of Revenue Management System and Oracle Accounts Receivable (AR) are used in WFO billing/invoicing. The WFO Support Group and others also use the RWS system for such information as WFO cost and funding status.

For direct or advance WFO billings, the invoice specifies check remittance to a LLNL Post Office Box. For those receipts, a Designated Administrator in Finance endorses the checks, prepares the cash receipts log, and stores the receipts in a safe. Each day the Cash Administrator, in the separate Revenue Management and Business Analysis Group, applies the cash receipts in Oracle AR and prepares the daily bank deposit. The practice of the Cash Administrator is to confirm that the cash log totals agree with the cash applied in Oracle AR. Cash receipts that cannot be readily matched to an invoice or other accounts receivable activity are deposited into the Bank of America and recorded in a suspense account until resolved.

LLNL maintains sub-cashiering stations for cash received by Programs (e.g., miscellaneous receipts) or other payments received. Procedures to be followed by sub-cashiering stations are contained in the LLNL Financial Policies and Procedures Manual. Receipts from sub-cashiering stations are sent to the Designated Administrator for processing in the same fashion as other cash receipts.

The Financial Operations Group performs monthly bank reconciliation(s) using deposit remittances and other financial information related to the Vendor and Payroll bank accounts.

The table below summarizes certain key performance measures, as defined by the Accounts Payable department, for the University of California in accordance with Contract W-7405-ENG-48, Appendix F – Objective Standards of Performance, for the 2002 FY:

**Key Performance Measures - AR
For the FY Ended 30 September 2002**

Performance Measures	
Number of Days to Reconcile Vendor Bank Account	2.2 days
Controllable Reconciling Items Over 60 Days Old	2.5%
Effective Debt Collection -- Collection Within 30 Days	91%
Cost Per AR	\$78.4

III. Procedures Performed

A. Objectives of Analyses

The objectives of the business process and internal control analyses were to:

- Identify LLNL’s key internal controls, including LLNL’s stated policies, procedures, and systems. Assess written policies, procedures, and internal controls related to the selected business processes for compliance with DOE and contract requirements.
- Analyze the application and adequacy of LLNL’s policies, procedures, and systems to assess compliance with applicable contractual provisions.
- Assess operation of policies, procedures, and controls by a system walk-through and review of sample transactions.

B. Scope of Analysis

The scope of compliance and internal control work for Procurement, Property Management and Accounting, Accounts Payable and Cash Receipts in connection with WFOs (the Functions) included the following:

- Understand the processes employed for the functions' activities.
- Perform interviews of key personnel.
- Review written policies, procedures, and internal controls related to functions for compliance with DOE and contract requirements.
- Analyze the adequacy of the Procurement general and application controls.
- Analyze Accounts Payable-Disbursements Oracle settings.
- Analyze interfaces between Procurement (PARIS System) and Property Management (Sunflower System).
- Review the results of internal audit and self-assessment reviews, including the A&O Department Internal Audit on Property and Selected Purchasing Controls.
- Review selected sample transactions as part of system walk-through and selected transactions included in LLNL self-assessments and internal audits.

C. A&O Review of Property and Selected Purchasing Controls

LLNL A&O performed a review of Property and Selected Purchasing Controls, Internal Audit Report No. 03-10, during the time of our analyses. We were provided testing and other information from the A&O work that we considered as part of our analyses. A&O concluded, based on its work, that the LLNL Property Management (PM) system was generally adequate to provide effective stewardship over accountable (attractive/controlled) and administratively controlled property and made several recommendations to strengthen the Purchasing and Materiel system and selected procurement activities.

IV. Observations And Recommendations

A. Acquisition

1. Purchase Requisition Approvals

a. Observation

Current policies and procedures require that all purchase order and blanket order requisitions are to be approved in accordance with the delegation of authority established in the Account Management System (AMS) Signature Responsibility module, before they are available to the Buyers or Subcontract Administrators for action in PARIS. In addition, specific unique approvals or reviews are required for certain purchases. These unique approvals and reviews are defined in the Controlled Items/Services List published and maintained by the Procurement & Materiel Operational Directorate.

All requisitions are entered into the On-line Requisitions (OLR) subsystem in TOPS, and the signature authority is advised by e-mail that the requisition is in the queue to pass to PARIS. In addition, the CFO Budget Office is advised of planned purchases of \$50,000 or more, and the Small Business Office is advised of appropriate orders of \$25,000 or more. The system also provides automatic notification to the approvers and reviewers listed in the Controlled Items/Services List based on an OLR Approval table. The designated approvers have the option of placing the requisition on hold in OLR/TOPS, or canceling it.

Unless the requisition is placed on hold or rejected by signature authority, the Budget Office, the unique approver, or the TRR, it will pass through to PARIS after a 24-hour window. In other words, if the approvers do not take an action (as is the case when an approver may be absent), the OLR subsystem assumes the requisition is approved and passes it to PARIS. This is referred to as an “Implied Approval.”

b. Recommendation

Eliminate “implied approvals” and require positive approval confirmation before the requisitions are fed to PARIS for further processing. Develop and implement a procedure that addresses review and approval of changes to the OLR Approval table and validation of the table based upon the Controlled Items/Services List.

2. Account Signature Authority Notification

a. Observation

By default, TOPS sends a notification e-mail to the account signature authority (person who owns or is responsible for the account to be charged for the cost of the property) when requisitions are created. TRRs have the capability to “turn off” the e-mail notification before the approval request is routed. The account signature authority was created to approve/control spending on an account. If this notification can be turned off, the account expenditure approval control feature is effectively invalidated.

b. Recommendation

Remove the checkbox in TOPS that allows TOPS users to avoid notifying the account signature authority when creating requisitions.

3. LLNL Federal Supply Classification (FSC) Codes

a. Observation

LLNL utilizes FSC codes to categorize and identify property in a number of ways. FSC codes are used in the Controlled Items/Services List to group and identify items that require unique actions, such as reviews or approvals, before a purchase action is initiated. FSC codes are used to group like items for the assignment of requisitions to Buyers for purchase actions. FSC codes are also used in the determination as to whether property items are to be tagged and, if so, the type of tag. (i.e., the determination is made based on a combination of the FSC code and the unit price and the PARIS property tag flags are set by the system.)

The LLNL FSC codes are patterned after, but are not the same as, the FSC Groups and Classes. The FSC codes are designed to address the broad spectrum of LLNL needs. The LLNL FSC codes are carried in a table in PARIS that is used to validate the codes as requisitions are passed to PARIS, as well as to perform the functions noted above.

As currently structured, the LLNL FSC codes do not necessarily address the full range of attributes required to validate that property is properly tagged at the time of receipt. This may be due to limitations in the sub-class options for complex FSC codes (e.g., computer peripherals), or the planned use of items that otherwise would be tagged (e.g., betterments that should be capitalized, but are not charged to capitalized equipment).

Subcontract Administrators (SCAs) and Buyers can change the LLNL FSC code on purchase orders, in PARIS, without the knowledge or approval of the TRR, Property Management, or Property Accounting. Uncoordinated changes or errors in the FSC codes, regardless of how inadvertent, can create additional unnecessary work later in the process.

b. Recommendation

Designate one subject matter specialist (and alternate) as the authority for assigning and interpreting the applicability of the LLNL FSC codes. Develop and implement a procedure for the assignment and review of FSC codes. Provide specific guidance/direction for the coding of more complex transactions, such as “betterments,” and/or require the approval of Property Accounting before purchases can be made for “upgrades” or “improvements.” Require that SCAs and Buyers obtain the concurrence of the TRR, Property Management and Property Accounting, before changing FSC codes in PARIS. Where appropriate, expand or revise the LLNL FSC codes to improve the control and utility of the PARIS property flags.

4. Controlled Items List vs. Controlled Equipment

a. Observation

The TRR Policy Manual contains the following definitions:

- “Controlled Items/Services List: A list containing items on which acquisition restrictions have been placed and require notification and/or approval from a cognizant organization. The list also contains the authorized method of acquisition and level of notification or approval required.”
- “Controlled Equipment: Equipment with an acquisition or fabrication cost of \$5K or more that justifies maintaining continuous records. The purchase of controlled equipment using UniCard and UniCheck is prohibited.”

There are distinct differences between the two. However, we found that a number of LLNL employees use the terms almost interchangeably, apparently because of the use of the word “Controlled” and the fact that LLNL FSC codes relate to both.

The LLNL FSC codes are patterned after, but are not the same as, the FSC Groups and Classes, with exceptions, including services that are not

included in the Federal list. There is a common belief that the PARIS “controlled” and “attractive” property flags are based on the LLNL FSC codes, which is partly true. The flags are based on a PARIS FSC List table in PARIS (used to validate the FSC codes used on the requisitions) with designations for “controlled,” “attractive,” and “blue tag” that is maintained and updated by Procurement Customer Services and a PARIS algorithm that uses the item purchase cost in conjunction with the table designations to determine whether the flag should be set to Y (yes) or N (no).

The property flags are also partially shown on the “Req/Order Line” screen in OLR; partially because while there is a box for “Blue Tag” and “Attractive” there is only a “Capital” box for controlled items, both those in the \$5,000 to \$25,000 range (non-capitalized) and those to be capitalized (over \$25,000). There isn’t a box titled “Controlled.”

It was noted that there have been instances where FSC codes were not correctly assigned by RAs/TRRs/Buyers. Buyers/TRRs cannot revise the property flags in PARIS, but they can revise/correct the FSC codes. Property Control can revise/correct the property flags in the Sunflower system as a part of the data entry function to Sunflower such that the property flag in the Sunflower system will not match the property flag in PARIS.

b. Recommendation

Consider renaming either the Controlled Items/Services List or Controlled Equipment in order to use the word “controlled” for one or the other. Add a box to the “Req/Order Line” screen for the non-capitalized items in the \$5,000 to \$25,000 range (using whichever name is determined to be appropriate). Formally publish the PARIS FSC List table, with the property tag designators that have been assigned, and distribute it to Property Management, Property Accounting, RAs, TRRs and Buyers. Prepare a procedure that addresses review and approval of changes to the table. (See also Observation and Recommendation A.3.a. and b., LLNL FSC Codes.)

5. On-Line Catalogue Updates

a. Observation

Currently, 16 users have the capability to update the on-line catalog (updates to items and/or item prices). Based on our interviews, it is our understanding that only one of these users usually performs this function and requires this level of access. Additionally, no approval requirement could be identified for adding new items to the on-line catalog.

b. Recommendation

Review the list of current users with the capability to update the on-line catalog and remove those users without a current business need. Establish approval requirements for adding new items or revising the prices in the on-line catalogs. We understand that with the implementation of the Electronic Ordering System (EOS), scheduled to commence pilot operation with five or six suppliers on June 25, 2003, catalogue management will be consolidated into a single individual (with backup).

6. Tracking Missing or Over-Due Receipts

a. Observation

It is the responsibility of the Buyer and/or TRR to track goods ordered but not received. PARIS has a feature to support this task. PARIS has a field at the “head level” of the order, which can be used to track receipts against the due date (use of this field is optional). The field is the “*expedite date.*” Basically that is the date when the buyer anticipates or requires delivery of the purchase order item(s). If the Buyer fills in an expedite date, a report can be run on request to review those orders which are past due or are approaching the due date. We were advised that the use of this field and the corresponding reports has been discontinued.

b. Recommendation

Develop a meaningful definition of “critical items” (e.g., direct critical path impact) and limit use of the field and the related reporting to those items that are deemed to be “critical,” then reinstate the practice.

7. Purchase Order Approvals

a. Observation

PARIS contains user Profiles that were designed to provide a basis for validating purchase order (PO) transaction dollar limits, ensuring that SCAs or Buyers could not issue a PO that exceeded their individual dollar authority. The current system (i.e., manual and automated components) is not dependent on PARIS user profiles and it is not clear what value is obtained from maintenance of the profiles.

SCA and Buyers are asked to draft contracts/POs that are consistent with their knowledge, experience, expertise, and availability. The draft document may be for a purchase far in excess of their defined approval authority. Once drafted, the document will be circulated for approval in accordance

with Procurement Standard Practice (SP) 1.2., Delegation of Procurement Authority. After obtaining the necessary approvals, the SCA or Buyer will complete and place the purchase orders. PARIS is designed to validate a subcontract/buyer identification number against the user profile, which is not the appropriate validation step (i.e., the buyer drafted the document; he or she did not approve it). In order to execute a meaningful validation, the subcontract/PO amount would have to be matched to the type of layered approval responsibility as used in the AMS Signature Responsibility module.

b. Recommendation

LLNL currently operates with a manual subcontract approval methodology, as defined by SP 1.2. It may not be economically reasonable to replace or revise the functionality of PARIS user profiles to effectively validate approvals. LLNL should consider including the requirement for electronic approval authority in any future PARIS replacement or integrate it with the AMS Signature Responsibility module.

B. Receipt of Property

1. Release of Distressed Items

a. Observation

Distressed items (e.g., damaged items, over shipments) are held in Receiving pending resolution. The responsible Buyer or TRR is contacted and advised that they have 15 days to determine the action that should be taken to clear the “hold.” If at the end of the 15 day period there has been no response, a Notification is sent advising the Buyer/TRR that resolution must occur within an additional 15 days. If at the end of the second 15-day period (total now 30 days from receipt) there is no response, the Buyer/TRR is advised that the item is being delivered, and it is delivered.

b. Recommendation

Establish a period for resolution that is acceptable to all parties (e.g., 15 days, 20 days). If at the end of that period there has been no response from the Buyer or the TRR, a Notification should be sent to the TRR’s supervisor as well as the TRR Reviewers self assessment organization. Should a pattern of Notifications be identified, the Procurement and Material Manager should be advised of the need for additional action in order to achieve the agreed-to objective.

2. Dock-to-Custodian Delivery Physical Control

a. Observation

Once property items have been accepted in Receiving, they are delivered to the location of the custodian. This process includes the custodian, or a designee, signing for the items to confirm delivery. In some cases, such as delivery to a restricted area, the custodian or a designee is not readily available and MDD personnel scan the property to the location to document that the delivery has been made. The property is left at the gate/fence creating the risk of unplanned movement of the property within LLNL.

In its recent Internal Audit Report No. 03-10, Property and Selected Purchasing Controls, A&O noted an opportunity to improve control over property distributed at two delivery areas and recommended the use of secure inventory cages for those areas.

b. Recommendation

LLNL should refine, as necessary, the current routing of deliveries to the users. Define and publish all designated drop-off locations and consider physically marking those locations. Publish a route schedule for each designated drop-off location. Establish a LLNL-wide policy that all items delivered are to be removed by the users within three hours of the drop-off. Perform periodic assessments/audits to confirm adherence to the policy is occurring.

3. Property Tag Work-Around(s)

a. Observation

At present, it is not practical for Receiving personnel to rely exclusively on the property tag indicators in PARIS to determine whether an item should be tagged. In some cases, the item is not reasonably configured to receive a tag, although the LLNL FSC code triggered a “yes” indicator (e.g., printer cartridges). PARIS was designed to require the entry of a property number on a pop-up screen when a property tag is required for the processing sequences for the item to be completed.

In other cases, there have been items that had been previously received (e.g. three months ago), or could be recognized by Receiving personnel as being of relatively high value, but were not currently required to be tagged based on the PARIS property flag (N). Receiving personnel recognized that this was likely an oversight or error and their research proved this to be the case. Although the system does not automatically provide a screen to record a

property number, it is possible to access the appropriate screen in this circumstance.

Receiving has developed work-around(s) for both conditions (i.e., not tagging an item when the PARIS property flag is set to “yes,” and tagging an item when the PARIS property flag is set to “no”). In those cases where an item is not tagged, comments are added to the PARIS receipt screen for transmittal to Sunflower. In those cases where an item has a PARIS “N” tag indication but is tagged, an exception report is generated.

b. Recommendation

Until such time as there is an improved ability to set the flags with greater precision, it does not appear practical to eliminate the work around(s). Further, because of the nature of LLNL’s work, it may never be practical to expect that the PARIS property flags can be reliably set in 100 percent of the cases based on tables and algorithms.

Develop and implement procedures that specify the conditions under which Receiving personnel will not strictly adhere to the PARIS property flags, the acceptable work-around practices, and the instances where approvals are required prior to the use of a work around. Develop and implement reports that identify the frequency of work-arounds and the causes so that improvements in LLNL FSC code delineation and training may be considered.

C. Use of Purchase Cards

1. Resolution of Unmatched UniCard Transactions

a. Observation

UniCard transactions charged to the credit card do not always match the UniCard orders. UniCard users are expected to review and resolve these unmatched transactions. A working-level procedure on reconciliation notes that where orders are not matched, the TOPS Comments field is used to explain discrepancies.

We observed that evidence of review and resolution of unmatched transactions could not be located in some cases, indicating the procedures to ensure all unmatched transactions are reviewed and resolved are not always followed. LLNL had also noted matching discrepancies and notified TRRs to resolve them.

The P&M self-assessment for October through December 2003 included a sample of 171 UniCard orders. The assessment, which considered whether the order was properly matched and reconciled, identified one matching and reconciliation exception from the 171 orders reviewed.

LLNL A&O observed the opportunity to improve control in this area and recommended that procedures require TRRs to check the reviewed box in TOPS when they have reconciled order detail to bank charges, in its recent Internal Audit Report No. 03-10, Property and Selected Purchasing Controls.

b. Recommendation

LLNL should revise its TRR Policy Manual to further define the reconciliation process and steps performed to reconcile; require TRRs to check the “reviewed box” in the TOPS screen when the reconciliation has been completed and document the resolution of matching discrepancies and in the screen TOPS provides or the TRR’s file.

2. 425 Card Reconciliation(s)

a. Observation

Material Request orders received through EDI are charged on the Institutional Credit Card Number 425 (UniCard). This card follows the matching process of other UniCard orders to correlate the billing items with the orders (and associated responsible TRR). Any additional unmatched items are manually reconciled. Individual ownership of the 425 card has not been identified (e.g., for resolving unreconciled bills, etc). LLNL is deploying an Electronic Ordering System (EOS) that will incorporate all the existing material request suppliers and ordering processes, effectively eliminating the need for an Institutional Credit Card. All orders placed through the EOS will be charged to a TRR’s credit card, and that TRR will be responsible for reconciling the orders.

b. Recommendation

Develop formal reconciliation procedures for orders charged to the Institutional Card 425 and define the responsibility for reconciling the card, including resolution of unreconciled items. LLNL should consider eliminating the use of a single Institutional Credit Card for these types of orders in favor of an approach that provides individual responsibility for the orders. We understand that LLNL will be eliminating the Industrial Credit Card as they move the Material Requests to EOS.

3. Edits Allowed to Posted UniCard Orders

a. Observation

Once UniCard orders are reconciled to bank charges, the bank transactions are sent to the General Ledger for posting on the following Friday. Once the transactions are posted, the status of the original UniCard orders will be updated to “Posted.” The following fields can be changed for UniCard orders with “Posted” status:

- Unit price can be changed even when the order is in “Posted” status, i.e., the bank charge has been posted to the General Ledger for internal allocation.
- Estimated order dollar amount, (derived from unit price times quantity ordered), can be changed.

Having the ability to revise the order data, particularly after the item has been approved, received, and posted weakens data integrity and obscures the system audit trail.

b. Recommendation

Develop and implement a monthly change history report that identifies all UniCard transactions that were revised subsequent to the order being posted. Implement audit procedures to confirm that the TRRs have entered appropriate comments in TOPS. LLNL is modifying its procedures to require TRRs to annotate in the TOPS UniCard Comments Field any changes to a credit card order after it has been posted. This will support the history of Unicard order edits/changes.

4. Segregation of Duties for UniCard Orders

a. Observation

As a part of the UniCard implementation, a number of duties that otherwise would be segregated for the processing of purchase orders, have not been segregated for UniCard purchase. The duties include: (i) identifying the requirement, (ii) choosing the supplier, (iii) purchasing the material, (iv) assigning the shipment/delivery location, (v) receiving (or picking up) the item(s), and (vi) reconciling the charge for payment.

Individuals in a Directorate (an individual other than the TRR) initiate most requirements; but there are occasions where the TRR is the initiator of the requirement. There is no segregation of duties that would serve to prevent a

TRR from receiving items at home, or picking up items for personal use, although there is policy against it. However, TRR Policies and Procedures do require the TRR to generate the Transaction Summary Report (TSR) monthly from TOPS and obtain a signature from the TRR's immediate supervisor or resource manager. Signatures on the TSR attest that the Unicard and Unicheck orders were for official LLNL business.

b. Recommendation

To enhance the segregation of duties and mitigate segregation of duties risk LLNL should:

- (1) Require that a Supervisory or Managerial approval be obtained in those cases where a TRR is initiating a requirement for an item that will be purchased via UniCard by that same TRR.
- (2) Require that the individual picking up or receiving the item(s) and noting the receipt in TOPS is someone other than the TRR responsible for the other duties noted, in the cases where the requirement was initiated by the same TRR.

5. Delegated Dollar Limit Controls

a. Observation

TOPS application controls do not exist to prevent UniCard cardholders from exceeding their delegated purchase dollar limits. We noted that there are controls outside of the TOPS application which include:

- The Bank will stop transactions that exceed the monthly UniCard limit.
- TRRs are required to obtain approvals for their transactions based on the TRR policies.
- A weekly report is generated and reviewed which identifies the instances where the delegated dollar limits were exceeded.

b. Recommendation

Investigate the possibility of the Bank creating a validation check against the UniCard cardholders' delegation dollar limit during the Bank's approval check (that currently validates the UniCard limit).

D. Property Management

1. Accepting Property into Sunflower

a. Observation

Property items are entered into Sunflower based on data from PARIS. The Property Control Group validates the data in a Sunflower suspense “file” using “Edit” and “Maintenance” screens. Corrections and revisions are made, as necessary, before the data are released to the Sunflower Inventory module. The Sunflower data quality function performed by Property Control is largely based on the knowledge and experience of the Property Control Administrators and is currently not addressed in procedures or desk instructions. System data validations are documented, but the rationale and required steps, including approvals, for other data changes are not. While an audit trail of changes is maintained in Sunflower, the data is currently not used for problem or trend analysis.

b. Recommendation

Develop procedures or desk instructions for the PARIS to Sunflower data quality tasks performed by the Property Control Group Administrators, including steps to be performed, screening rationale, change approvals, and retention of records. Establish change “categories,” (i.e., types or reasons for changes) and periodic reports depicting the volume and nature of the changes. Consider using the change data provided for analysis of causes (e.g., incomplete training, out-of-date procedures).

2. Analysis of Purchase Orders

a. Observation

In an effort to capture all of the property that should be included in the Sunflower records, Property Control obtains a tabulation of all purchase orders, by line item, placed each day, including revisions. This voluminous document is manually reviewed to identify items that would need to be tagged so that Property Control can anticipate their arrival.

The performance of the screening is worthwhile, but its magnitude makes it a good candidate for a download of the file, and an automated process to match the characteristics of items to be tagged and to identify those items requiring attention.

b. Recommendation

Develop and implement an automated process for the established screening process, documented procedures, and a user-training module. Consider the needs of Property Accounting for screening potential capital items that may not have the correct project account number or tagging requirements (see item F.1.b.).

The PM Group Leader has recognized the advantage of an automated screening process and initiated action to develop it during the course of our review. This item is in process.

3. Retirements at Acquisition Cost

a. Observation

Property that is “written-off”, for whatever reason, is described at LLNL as being “retired.” Non-capitalized, controlled, and attractive retired property is shown at its original acquisition value. Retired capitalized items are shown at the acquisition or fabrication cost, as appropriate, and depreciated based on their service life. At any point in time, the cost yet to be depreciated for these items provides an indication of value which is reported as their net book value. However, when reported to DOE as having been retired, they are reported at their original acquisition cost, regardless of their age, net book value, or remaining service life.

b. Recommendation

Reporting retired, capitalized items at their acquisition cost, instead of their net book value, is not as representative or indicative of the remaining cost/value of the items as the net book value amount. As presently reported, the cost for items lost or retired appears to be substantially more than the remaining value, and can be misleading to those not sufficiently familiar with the accounting practice. LLNL should move forward with DOE to pursue a revised reporting basis that better reflects the value of retired property. We understand that discussions with DOE regarding the possibility of a revised reporting basis are underway.

E. Tracking and Control of WIP Inventory

1. WIP Inventory

a. Observation

The Sunflower property system identifies location of property by custodian and physical location, whether on-site or held-by-others. WIP inventory (i.e., project/program, Fabrication and Construction material) is not tagged and recorded in Sunflower. In the case of NIF, the inventory is appropriately tracked and controlled in the GLOVIA inventory control system.

Unlike property, there is not a need to tag WIP inventory, but there is a need to track and control it and measure the accuracy of the inventory records, even if the program/project is not as large as NIF.

b. Recommendation

Define and implement a single WIP inventory control methodology. The defined methodology should be based on a LLNL-wide standard that addresses:

- Necessary data content (e.g., part number, nomenclature, quantity)
- Updating and maintaining the data
- Count cycles and accuracy measurements
- Action taken for gains and losses
- Segregation of duties
- Standard Reports
- Applicability (i.e., use may not be required for programs with small amounts of inventory)

Each Directorate should be permitted to expand the data content, reports, etc., beyond the defined LLNL standard to satisfy its needs. Responsibility for the individual program inventories would be as delegated by the Director. Responsibility for the LLNL-wide standards, including accuracy measurement procedures should be assigned to Property Management.

2. NIF Inventory Procedures

a. Observation

Procedures do not currently exist for counting and measuring the NIF inventory accuracy. Desktop procedures do not currently exist for how to adjust GLOVIA records based upon physical count. The person performing the physical count is the same person making the inventory adjustments in GLOVIA.

b. Recommendation

Develop and implement procedures for determining inventory accuracy. The procedures should address the process for counting, measuring, and adjusting the inventory records. In addition, the individual(s) performing the inventory count should be separate from the individual(s) making the inventory adjustment(s) to enhance the internal control environment.

3. Disbursement of NIF Inventory

a. Observation

NIF program personnel are occasionally used as expeditors. Although the number of individuals typically used to expedite parts does not appear to be large, it was noted that the NIF inventory personnel indicated that they would release the part as long as the individual had a LLNL badge, a valid part number, and a note or memo requesting the part. There was no approved list of authorized expeditors or similar control feature.

b. Recommendation

Establish an approved list of authorized expeditors. Post the list in the NIF Warehouse and train the employees to validate the name/badge of the expeditor against the posted, approved list prior to disbursing inventory items.

F. Property Accounting

1. Assignment of Project Accounts to Purchases

a. Observation

Project accounts are opened by Directorate RAs using pre-assigned blocks of numbers within the General Ledger numbering scheme. As requirements

for purchasing action are identified the RAs forward these requirements to the Directorate TRRs, identifying the account(s) to be used to charge the costs. We noted that property items did not appear to be always charged to the correct cost type (i.e., Operating, Fabrication, or Construction). It appears that this is most often a result of the determination made by the RA. Property Accounting identified the assignment of an Operating Fund account to items that should be capitalized as a continuing concern and one of the processes that does not appear to be adequately understood. As a result, Property Accounting has to perform on-going queries, including of the Sunflower system, to identify tagged items over \$25,000 charged to open accounts for possible incorrect charges and make a transfer/correction as necessary.

b. Recommendation

Develop and implement additional reports and controls that can be used by Property Accounting to monitor and identify property items early in the acquisition process that may not be assigned to the correct project account. As an example, TOPS contains a “capital” field in a screen, which has a drop down window for selecting one of the valid reasons for not capitalizing a property item whose cost is greater than \$25,000 (e.g. service life of < 2 years, experimental). This field is not linked to PARIS, but if made mandatory for purchases in excess of \$25,000, it could be used to flag planned purchases to Property Accounting for review before the purchase order was placed.

LLNL is initiating a process where by Property Accounting will be notified, via E-mail, of equipment purchases greater than \$25,000 charged to operating accounts. Working level procedures should be developed and implemented that specifically address the basis for the assignment of project accounts. The RA training should be expanded to focus more attention on the basis for assigning project accounts.

2. Cost Transfers

a. Observation

LLNL’s disclosed cost accounting practice is to credit jobs/contract for transfers of material costs based on the original charges. We noted that there are occasions where LLNL transfers materials and related costs between cost objectives. The current Cost Transfer Policy and Procedures do not adequately address those circumstances under which cost transfers may be necessary.

b. Recommendation

Identify and examine those instances where cost transfers have occurred in FY 2002/03, or should have occurred, if any. Develop and implement policies and procedures and revise training materials to: (i) delineate the circumstances where costs are to be transferred due to material transfers; (ii) assign the responsibility for identifying and communicating the need for a cost transfer; and (iii) provide for maintenance of an audit trail and adequate documentation for the transfer. We noted that a new Policy and Procedure and improved guidance and training are currently under development that will address cost transfer criteria (i.e., “when” and “why” cost transfers are required).

3. Early Capitalization of Items

a. Observation

Property items that are purchased in support of a Fabrication or Construction project and that will become a part of the planned “end-item,” (i.e., they will not provide “stand-alone” service to the users) are included in the capitalized cost of the completed Fabrication or Construction project. In some cases, these items are identified and capitalized during the course of the project rather than when the “end-item” actually goes into service. The result is inconsistent capitalization with some items being prematurely capitalized and depreciated. (It should be noted that when a prematurely capitalized item is included in the capitalized cost of the “end-item,” it is only the remaining cost to be depreciated that is included. There is no double counting of the cost that has been included in depreciation.)

b. Recommendation

LLNL should not capitalize and begin depreciating assets before their service life commences. Significant property items that are purchased to support a Fabrication or Construction project should be tracked and controlled (e.g., entered into an inventory control system for WIP items), rather than be tagged as property and capitalized before the actual start of their service lives. (See item E.1.b. re: WIP inventory control.) In the meantime, such items should be tagged but not capitalized.

Once the method for tracing and controlling the WIP items has been implemented, revise the procedures accordingly.

4. Capitalization of Betterments

a. Observation

We noted purchases for machinery, equipment and software (items other than real property) that appeared to be betterments, but had not been capitalized because of the way the item was originally entered into TOPS/PARIS. Currently, procedures that define how betterments are to be identified and treated do not provide sufficient detail. The RA training material briefly addresses betterments, but does not appear to provide adequate direction and guidance.

b. Recommendation

Develop and implement detailed procedures that address the identification, classification, and treatment of betterments. Revise the RA training materials accordingly. LLNL should review past years for items purchased that were identified as upgrades or with similar descriptions to evaluate whether more detailed studies to identify betterments are warranted. Include key words and other characteristics to identify betterments in the screening process described in paragraphs D.2.b. and F.1.b.

5. Timeliness of Capitalizing Fabrication Projects

a. Observation

Upon completion of a Fabrication project, the project account is closed and the costs are capitalized. The process is triggered by an e-mail to Property Accounting that the project is complete and the project account is being closed. The value used for the capitalization is based on the costs collected in the project account. Account closure is accomplished using the “Fab Closing Addendum” screen. AMS will look into the Sunflower records and identify the tagged items, if any, which need disposition.

One of the areas of concern identified by Property Accounting was the difficulty in obtaining data/information regarding Fabrication projects (i.e., status, estimated completion date, etc.) and the project closeouts. RAs and program personnel do not appear to have given this a reasonably high priority with the result that costs are not necessarily being capitalized in a timely manner.

In its recent Internal Audit Report No. 03-10, Property and Selected Purchasing Controls, LLNL A&O observed that completed fabrication accounts are not being promptly included in the Property Management

database. A&O recommended review of fabrication accounts and entry of completed equipment in the Property Management database and accounting records.

b. Recommendation

Develop and implement a detailed procedure that addresses the need and method(s) for the programs to provide project status and estimate to complete (ETC) data to Property Accounting, which includes such elements as:

1. At project initiation, use of a Fabrication Account addendum to identify the expected date of completion.
2. An AMS e-mail notification to RA/ADRA and ADPR that alerts them that the project should be completing. The Notice will ask that they notify Property Management and Accounting for tagging and capitalization within 1-2 weeks (otherwise Accounting is to call on them) or change the completion date.
3. Follow-up by Accounting within a 2-week period.
4. Where Property Accounting is unable to obtain all the needed data, the Accounting Division Manager will send a memorandum to the ADRA/ADPR establishing a completion date for capitalization.

G. Accounts Payable-Disbursement

1. IRS 1099 Forms

a. Observation

For calendar year 2002, three of more than six hundred Contractors who should have received an Internal Revenue Service (IRS) 1099 Form notified Payroll and Tax Services Group that they had not. The contractor classification in Oracle, as either a Corporation or Sole Proprietorship is based on the data fed to AP from PARIS. The Disbursement Services Division is responsible for confirming that the classification is correct. Incorrect classification may result in failure to issue IRS 1099 Forms to some non-corporation service contractors. When a contractor is set up in Oracle through the Procurement Department, the contractor should be marked as a corporation or sole proprietorship based on the W-9 Tax Information Form. If sole proprietorship is not marked, the vendor will not be sent a Form 1099. Even if infrequent, failure to properly issue IRS 1099 Forms to all non-corporation service contractors may result in IRS fines and

penalties. We are informed that there are edit checks that may serve to detect an unmarked sole proprietorship in some circumstances (e.g., comparison of PO and Oracle vendor codes); however, under certain circumstances the failure to correctly set up a sole proprietor will not be detected by a system edit.

b. Recommendation

LLNL should establish additional controls for the proper classification of vendors in the Oracle system. If new system-edit checks are not feasible to detect the needed vendor classification, finance procedures should be developed that require periodic reviews to confirm the correct classification of vendors added during the year.

2. Accounts Payable-Disbursements Segregation of Duties

a. Observation

Oracle is not set up to maintain system segregation of duties for transactions that are incompatible in terms of segregation of duties in the AP process. The responsibilities of “A/P Manager,” “A/P Invoice/Payment Entry,” and “A/P Vendor EFT” have access that allow users to (i) create/modify vendors, (ii) create/modify invoices, and (iii) create/modify payments. During interviews, we were informed that AP employs procedures aimed at mitigating segregation of duties risk. They include the use of edit reports that delineate system activity, such as changes to vendor information by users other than the Vendor Code Desk personnel and individuals that have entered invoices in the system. AP personnel and the AP Group Leader review the reports for appropriate system access and entries made.

The Financial Policies and Procedures do not address the Accounts Payable-Disbursement practices aimed at addressing segregation of duty risks through review of edit and access reports.

b. Recommendation

LLNL should review AP system access needs for the “A/P Invoice/Payment Entry” and “A/P Vendor EFT” Oracle responsibilities. We recommend that system access be limited to eliminate current system access to incompatible functions. Where system access is necessary, procedures should be used to grant temporary access to incompatible transactions, and such system access should be logged and reviewed.

LLNL should prepare written procedures addressing Accounts Payable – Disbursements segregation of duties and the required use and review of system edit/access reports. The procedures should, in part, establish:

- Responsibility for reviewing system reports and segregation of duties risks.
- Frequency of report generation and reviews.
- Identification of segregation of duties risks (i.e., incompatible functions).
- Steps required to confirm appropriate system access and entries, and
- Documentation of the review performed and any required approvals.

The procedure may be incorporated in the Financial Policies and Procedures Manual or implemented as a lower level procedural document. In either case, it should be reviewed and approved within the CFO organization.

3. Check Generation Segregation of Duties

a. Observation

Accounts Payable provides a disbursement file to the Disbursements Operations Group. The Disbursements Operations Group is responsible for printing the paper checks using Bottomline Technology software. The process includes use of the signature generation disk that is secured in a locked area that is accessible to the Operations Group personnel when they print checks. There are three employees that have individual access to the Bottomline Check generation system. Current procedures do not require that more than a single individual be involved in the process.

b. Recommendation

LLNL should consider enhancing its control procedures so that the check generation process is performed under dual control (i.e., two individuals required in order to print signed checks -- one individual controlling the locked storage of the signature generation disk and another individual responsible for check printing).

4. Accounts Payable-Disbursements Working Level Procedures

a. Observation

Working level procedures that address Accounts Payable and Disbursement functions are an important part of the overall LLNL control environment. We noted that certain procedural documents used within Accounts Payable and Disbursements are not identified as LLNL procedures. Examples include documents describing practices to address segregation of duties risks and Oracle Applications procedures. The procedures: (i) are not maintained in a system for ready user access, and (ii) do not show effective/revision dates or cross-referencing to other LLNL procedures and DOE requirements. As a result, it is difficult to determine that they are current, appropriately coordinated and reviewed, and are communicated and accessible to users.

b. Recommendation

LLNL should identify working level procedures covering significant control and operating needs, such as segregation of duties and actions required for system suspense items and other control reports, and make them formal procedures of the CFO organization. The procedures should be approved, contain revision dates, and provide references to other LLNL procedures and DOE requirements, as appropriate. To provide ready access, we suggest that LLNL make the procedures accessible to employees on-line.

5. Oracle Holds

a. Observation

In Oracle AP a hold will prevent an accounts payable transaction from being posted to the general ledger. As part of our analysis of Oracle settings, we noted that certain Oracle holds are no longer needed. They include:

- Secondary Approval
- Funds Check
- Can't Try PO Close
- Final Matching
- No Rate
- Prepaid Amount

Although these holds are not in use, there is a risk that the settings in Oracle could be “turned on” and have adverse affects on system performance and/or data integrity.

b. Recommendation

LLNL should remove those Oracle holds from the system that serve no business use.

H. Cash Receipts In Connection With WFOs

1. Cash Receipts and WFOs - Working Level Procedures

a. Observation

Working level procedures that address cash receipts and WFO functions are an important part of the overall LLNL control environment. We noted that a procedure addressing the reconciliation for the activity in the suspense account unidentified/unapplied checks has been prepared in draft but has not been issued. Other procedural documents used within cash receipts and WFO are not identified as LLNL procedures. Examples include cash receipt deposit procedures and WFO billing process procedures. As a result it is difficult to determine that they are current, appropriately coordinated and reviewed, and are communicated and accessible to users.

b. Recommendation

We recommend that LLNL identify working level procedures that address significant control and operating needs, such as segregation of duties and actions required for system suspense items and other control reports, and make them formal procedures of the CFO organization. The procedures should be approved, contain revision dates, and provide references to other LLNL procedures and DOE requirements, as appropriate. To provide ready access, we suggest that LLNL make the procedures accessible to employees on-line.

2. Use of an Electronic Lockbox for Cash Receipts

a. Observation

Currently, invoices instruct recipients to send checks to a central LLNL Post Office. In some instances, programs receive checks and process them through sub-cashiering stations. The LLNL practice is to endorse checks immediately. However, where the correct endorsement is unclear, further processing is required to identify and make the correct endorsement. The

checks are maintained in a locked safe until they are deposited. Checks are deposited daily.

LLNL does not use an electronic lockbox for receipt of checks. An electronic lockbox could reduce check-handling risks, reduce the level of check processing activities, such as logging and endorsements, and support an efficient cash application process through daily electronic remittance statements provided by the bank.

b. Recommendation

To pursue best practices, LLNL should consider obtaining a lockbox account at a bank for receipt of checks to enhance control and gain efficiency.

I. Information Technologies General Controls

1. AMS User Administration Process

a. Observation

LLNL was not able to provide the original AMS user ID request forms for 3 of the 15 samples selected for AMS user access. Employee access for 1 of 15 sampled terminated employees was not removed from the AMS application in a timely manner. The employee was terminated in June 2002 and his AMS roles were still active at the time of our analysis in March 2003.

b. Recommendation

LLNL should review its AMS user access procedures and develop improvements for document retention and user access monitoring; including a formal process to review and manage access at key stages in the employee lifecycle.

The IDs of terminated employees should be removed or disabled timely.

2. Program Change Process

a. Observation

LLNL uses a change control process that includes service request tracking, notifications, and authorizations for the changes to be performed. The practices vary depending on the application – there is no standard process or system for managing and processing program change requests. We noted

procedures employed for program changes that are not formally documented.

During our analysis we noted that:

1. AMS program change and program change testing results and user approvals are not formally documented. As a result LLNL is not able to trace all AMS program changes to the original request and approvals.
2. Sunflower and Oracle Financials Program approvals for changes during the program change process that are obtained orally or through e-mail are not retained in the change history.
3. An audit trail within the PARIS and TOPS Program Change Process is not maintained to enable tracking of the changes from the initial request through the implementation of the developed code. Testing approvals of developed codes are not formally tracked and maintained.

b. Recommendation

To enhance control for the program change process, LLNL should develop written program change procedures and standards, and consider standardizing them across all applications. The procedures should provide for preparation of program change documentation and its retention to support the change process. LLNL should consider implementing the use of a program change form that would track a change and approvals through the entire program change process. The form should capture, in part:

- Vantive Ticket (Approved Request).
- Authorization by developer upon completion of development.
- Quality review approval.
- Authorization of implementer upon completion of implementation.
- Reference to a list of implemented/modified code that directly relates to the referenced “Vantive ticket.”

3. P-Accounts Passwords

a. Observation

P-accounts are used to access LLNL web-based applications such as Oracle Financials, Sunflower, and TOPS. The system does not currently enforce password changes at least every 180 days, the standard contained in the DOE Password Guide.

b. Recommendation

Password change procedures should be established that, at a minimum, meet the DOE Password Guide. We understand that LLNL is in the process of developing a new password verification program that will satisfy the DOE guide. In addition, LLNL should consider setting the password change procedures consistent with leading best practice guidelines such as, (1) maximum password age – 90 days and (2) minimum password age – 1 day.

4. AICSS Data Center Access

a. Observation

Approximately 321 individuals have access to the AICSS Data Center. Based on our discussion with Data Center management, periodic access reviews to validate continued employee access are not performed.

An AICSS Request Form is used in the process of authorizing access. ITS-SOP-200, Computer Center Access requires that the AICSS Request form be completed and approved for access to be granted. We noted instances where access had been authorized, but the AIC Computer Access Request Form had not been completed. At the time of our review data center management had initiated activities to review and validate access to the data center, including access forms and their retention.

b. Recommendation

LLNL should perform periodic reviews of the AICSS Data Center access list to identify data center use. Individuals who infrequently visit the Data Center can be removed from the access list and sign in using the visitor log when access is needed. The reviews should include steps to ensure that access forms have been completed and retained.

5. Developer System Access

a. Observation

Developers implement program changes and support other programming tasks for LLNL business applications. We noted that developers: (i) have access to the TOPS production environment and the TOPS database, and (ii) have access to the PARIS production environment and the ability to create PARIS users, and can edit FSC codes within PARIS. Developer access to apply changes is a segregation of duties risk when such users can both create changes and migrate those changes to the production environment. Developer access to the production data may increase the difficulty of detecting unauthorized access and subsequent loss or changes to the data or the availability of the production system.

b. Recommendation

LLNL should limit developer access to the TOPS and PARIS systems and monitor their access to these production systems where such access is necessary.