Memorandum

Date JUL 31 1992

From Richard P. Kusserow
Inspector General For Bryan Mitchell

Subject Financial Audit of the National Institutes of Health's Management and Service and Supply Funds (A-15-91-00044)

To James O. Mason, M.D., Dr. P.H.
Assistant Secretary for Health

The attached final report was prepared by Clifton, Gunderson and Company (CGC), Certified Public Accountants, under contract with the Office of Inspector General. They present the results of their audit of the National Institutes of Health's (NIH) Management and Service and Supply Funds (Funds) financial statements for the fiscal year (FY) ended September 30, 1991. We believe based on our review of their work and report, that their audit provides a reasonable basis for the conclusions reached and recommendations contained in the audit report.

The Chief Financial Officers Act requires that the audit report be prepared in accordance with Government Auditing Standards and the Office of Management and Budget's (OMB) Bulletin 91-14, Audit Requirements for Federal Financial Statements and be issued by June 30, 1992. However, due to significant form and content omissions in the Funds' financial statements submitted to OMB on March 31, 1992, the Department of Health and Human Services (Department) notified OMB that issuance of the final audit report would be delayed until July 31 in order to allow time for revision of the statements and completion of the audit.

The CGC did not express an opinion on the financial statements because of concerns about amounts shown for (1) inventory, (2) property, plant and equipment and related accumulated depreciation, (3) accounts payable, and (4) accrued expenses. They found significant internal control weaknesses, and noncompliance with Title 2--the General Accounting Office's Policy and Procedures Manual for Guidance to Federal Agencies (which is incorporated in the Department's accounting guidance) in the following three areas:

- Inventory Management. The perpetual inventory records did not accurately reflect the value of inventories on hand and these records were not reconciled regularly with the general ledger. Test counts of NIH's Clinical Center noncontrolled drugs disclosed differences in 27 percent of the items tested--shortages in 2 units and overages in 7 units, as well as differences of up to 62 percent of the items tested for other categories of inventory.

the items tested for other categories of inventory. Physical security of hospital supplies is inadequate to preclude unauthorized use including the potential for theft.

- o Accounts Payable. There was an absence of a proper procedure for accrual of accounts payable on a timely basis, periodic review and aging of accounts payable.

  -- The auditors identified 26 transactions totaling in excess of $7 million which were not recorded as accounts payable at September 30, 1991.

  -- Over half of the Funds' $30 million in "Accounts Payable - Non-Federal" were over a year old. This happened because NIH had not implemented procedures to periodically review the status of accounts payable. Moreover, rather than matching invoices with already recorded obligations when recording payables, it sometimes simultaneously recorded a payable, an accrued expenditure and an obligation. This process would result in duplicate recording of obligations. Having invalid obligations on the books hinders use of funds that could have been used for other activities.

- o Electronic Data Processing Security Controls. The administrative data base and the utility system of the computer system operated by the Funds' Division of Computer Research and Technology are susceptible to unauthorized access. This is because access controls were not properly implemented and passwords were not adequately protected. Also, there is no uninterrupted power source to preclude loss of data processing services during a power outage, backup data tapes are not stored in an off-site location and there is no policy specifying retention periods for tapes and source documents. These problems result in noncompliance with OMB's Circular A-130, Management of Federal Information Resources.

A slippage in the estimated completion date for resolution of a significant material weakness in property management that affects the Funds' and NIH's other personal property was also noted. This weakness involves the loss of control over personal computers, centrifuges and other items valued at about $63 million due to a lack of periodic physical inventories (none had been conducted since 1972), reconciliation of inventory results with accountable records, and weaknesses in the control and disposition of property. By June 1992, NIH reported that the amount of unaccounted for items had been reduced to $53.6 million. The amount of unaccounted for property belonging to the Funds could not be

readily determined. However, almost a year has elapsed since NIH engaged a contractor to conduct a physical inventory. The estimated date for correcting this material weakness was changed from FY 1992 to FY 1993, and the Public Health Service recently established a Board of Survey to investigate discrepancies.

We believe that weaknesses identified by CGC auditors in the areas of inventory management, accounts payable, and electronic data processing security meet OMB criteria for three material internal control weaknesses that should be reported to the President and Congress under the requirements of the Federal Managers' Financial Integrity Act. These weaknesses, together with the slow progress in correcting the material weakness in the area of property management and two other declared material weaknesses affecting the Funds in FY 1991--(1) operating controls in the Delegated Procurement System and NIH's centralized station support and (2) acquisition of excess computer capacity--indicate that NIH's financial management system needs improvement.

This report contains recommendations to you for improving the Funds' internal controls and compliance with laws and regulations. The NIH officials generally agreed with our recommendations for corrective action but raised concerns about whether the discrepancies noted in the report should be disclosed as material weaknesses. Their comments have been incorporated throughout the final report.

If you wish to discuss this report, please call me or have your staff contact Daniel W. Blades, Assistant Inspector General for Public Health Service Audits, at (301)443-3583. We would appreciate receiving written comments as soon as possible on the recommendations and a status report by August 15, 1992, on the progress being made in implementing our recommendations. A copy of this report is being sent to other interested departmental officials.

We would like to express our appreciation for efforts by NIH officials in producing the Funds' first financial reports. These efforts represent a substantial commitment to improving the Funds' financial management.

Attachment

cc:
Arnold Tompkins, Chief Financial Officer
Department of Health and Human Services

Anthony L. Itteilag, Chief Financial Officer
Public Health Service

John D. Mahoney, Chief Financial Officer
National Institutes of Health

Department of Health and Human Services

OFFICE OF INSPECTOR GENERAL

FINANCIAL AUDIT OF THE NATIONAL INSTITUTES OF HEALTH'S MANAGEMENT AND SERVICE AND SUPPLY FUNDS

Richard P. Kusserow
INSPECTOR GENERAL

A-15-91-00044

NATIONAL INSTITUTES OF HEALTH
SERVICE AND SUPPLY FUND
AND
MANAGEMENT FUND

FINANCIAL STATEMENTS

September 30, 1991

Clifton,
Gunderson & Co.
Certified Public Accountants & Consultants

To the Inspector General and the Assistant Secretary for Health
Department of Health and Human Services
Washington, D.C.

INDEPENDENT AUDITOR'S REPORT

We were engaged to audit the financial statements of the Management Fund of the National Institutes of Health as of and for the year ended September 30, 1991. These financial statements are the responsibility of the Agency's management.

This was the first year that the Management Fund was required to be audited in accordance with the Chief Financial Officers Act of 1990. We were not engaged to audit the financial statements until after September 30, 1991.

As more fully described in Note 6 to the financial statements, no depreciation has been recorded on property, plant and equipment. In our opinion, depreciation should be recorded on all property, plant and equipment over their estimated lives to conform to Title 2 of GAO Policy and Procedures Manual for Guidance of Federal Agencies, which is incorporated by reference in departmental accounting guidance. The effects on the financial statements of not recording depreciation are not reasonably determinable.

There were no counts of physical inventory made at September 30, 1991 or 1990, stated in the accompanying financial statements at $3,562,000 and $3,598,000, respectively, and we were unable to satisfy ourselves concerning inventory quantities on hand at those dates by other auditing procedures. Furthermore, there is no process for reconciling detailed property records to the general ledger and certain prior year records and supporting data were not available for our audit. Therefore, we were also not able to satisfy ourselves about the amount of property, plant and equipment, stated in the accompanying financial statements at $57,969,000. In addition, accounts payable and accrued expenses records contain approximately $10,000,000 in amounts over one year old. The records are not accurately stated or appropriately reconciled. These records do not permit the application of sufficient auditing procedures to accounts payable and accrued expenses, recorded in the accompanying statement of financial position at a total of $43,612,000 at September 30, 1991.

Because of the significance of the matters discussed in the preceding paragraphs, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the financial statements referred to in the first paragraph.

We were engaged for the purpose of forming an opinion on the financial statements described above. We have reviewed the financial information presented in management's overview of the National Institutes of Health Management Fund. The information presented in the overview section is presented for the purpose of additional analysis. Such information has not been audited by us and, accordingly, we do not express an opinion on this information. This information is addressed, however, in our auditor's report on compliance in accordance with Section 6.a.(3), (4) and (5) of OMB Bulletin No. 91-14.

Clifton, Gunderson & Co.

Baltimore, Maryland
July 2, 1992

Clifton,
Gunderson & Co.
Certified Public Accountants & Consultants

To the Inspector General and the Assistant Secretary for Health
Department of Health and Human Services
Washington, D.C.

INDEPENDENT AUDITOR'S REPORT

We were engaged to audit the financial statements of the Service and Supply Fund of the National Institutes of Health as of and for the year ended September 30, 1991. These financial statements are the responsibility of the Agency's management.

This was the first year that the Service and Supply Fund was required to be audited in accordance with the Chief Financial Officers Act of 1990. We were not engaged to audit the financial statements until after September 30, 1991.

Included in the activities of the Service and Supply Fund is a lease agreement for computer equipment. The initial period of the lease agreement was for the period October 1, 1988 through September 30, 1989. The lease also contains nine one-year renewal options. Options for the years ended September 30, 1990 and September 30, 1991 were exercised. The lease states that it is the intent of the National Institutes of Health to renew the lease. The lease contract for the year ended September 30, 1991 obligated total funds in excess of $39,000,000.

The accompanying financial statements treat this lease agreement as an operating lease. Further, there are no disclosures in the notes to the financial statements regarding this lease. In our opinion, this lease should be recorded as capital lease to conform to Title 2 of GAO Policy and Procedures Manual for Guidance of Federal Agencies, which is incorporated by reference in departmental accounting guidance. The effects on the financial statements of not recording this lease as a capital lease are not reasonably determinable.

There were no counts of physical inventory made at September 30, 1991 or 1990, stated in the accompanying financial statements at $8,078,000 and $7,377,000, respectively, and we were unable to satisfy ourselves concerning inventory quantities on hand at these dates by other auditing procedures. Furthermore, detailed property records have not been reconciled to the general ledger and certain prior-year records and supporting data were not available for our audit. Therefore, we were not able to satisfy ourselves about the amounts at which property, plant and equipment, and related accumulated depreciation are recorded in the accompanying statement of financial position at September 30, 1991 (stated at $13,798,000, net), and the amount of depreciation expense for the year then ended (stated at $1,664,000). In addition, accounts payable and accrued expenses records contain approximately $9,000,000 in amounts over one year old. The records are not accurately stated or appropriately reconciled. These records do not permit the application of sufficient auditing procedures to accounts payable and

accrued expenses, recorded in the accompanying statement of financial position at a total of $30,188,000 at September 30, 1991.

Because of the significance of the matters discussed in the preceding paragraphs, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the financial statements referred to in the first paragraph.

We were engaged for the purpose of forming an opinion on the financial statements described above. We have reviewed the financial information presented in management's overview of the National Institutes of Health Service and Supply Fund. The information presented in the overview section is presented for the purpose of additional analysis. Such information has not been audited by us and, accordingly, we do not express an opinion on this information. This information is addressed, however, in our auditor's report on compliance in accordance with Section 6.a.(3), (4) and (5) of OMB Bulletin No. 91-14.

Clifton, Gunderson & Co.

Baltimore, Maryland
July 2, 1992

Clifton, Gunderson & Co.
Certified Public Accountants & Consultants

To the Inspector General and the Assistant Secretary for Health
Department of Health and Human Services
Washington, D.C.

INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE

We were engaged to audit the financial statements of the Service and Supply Fund and the Management Fund of the National Institutes of Health (NIH) as of and for the year ended September 30, 1991, and have issued our reports thereon dated July 2, 1992. Our reports indicated that the scope of our work was not sufficient to enable us to express, and we did not express, an opinion on the financial statements referred to above.

Compliance with laws and regulations applicable to the Service and Supply Fund and the Management Fund is the responsibility of NIH's management. As part of our engagement, we tested compliance with certain provisions of the following laws and regulations that may directly affect the financial statements:

- The Chief Financial Officers Act of 1990
- Budget and Accounting Procedures Act of 1950
- The Federal Managers' Financial Integrity Act of 1982
- The Prompt Payment Act
- The Debt Collection Act of 1982
- Public Law 100-166, Limitation of Administrative Expenses
- Program Fraud Civil Remedies Act
- GAO Policy and Procedures Manual for Guidance of Federal Agencies, Title 2
- OMB Circular A-25, User Charges
- OMB Circular A-123, Internal Control Systems
- OMB Circular A-127, Financial Management Systems
- OMB Circular A-130, Management of Federal Information Resources
- OMB Bulletin No. 91-15, Guidance on Form and Content of Financial Statements on FY 1991 Financial Activity

As part of our engagement, we reviewed management's process for evaluating and reporting on internal control and accounting systems as required by the Federal Managers' Financial Integrity Act (FMFIA) and compared the agency's most recent FMFIA reports with the evaluation we conducted of the entity's internal control system. We also reviewed and tested the entity's policies, procedures, and systems for documenting and supporting financial, statistical and other information presented in the Overview of the Reporting Entity and Supplemental Financial and

Management Information. However, our objective was not to provide an opinion on overall compliance with such provisions.

Material instances of noncompliance are failures to follow requirements, or violations of prohibitions, contained in law or regulations that cause us to conclude that the aggregation of the misstatements resulting from those failures or violations is material to the financial statements or the sensitivity of the matter would cause it to be perceived as significant by others. The results of our tests of compliance disclosed the following instances of noncompliance with certain provisions of the FMFIA and OMB Circulars A-123, A-127, and A-130 which require agencies to (i) establish a cost-effective system of internal controls to provide reasonable assurance that Government resources are protected against fraud, waste, and mismanagement; (ii) develop systems that feature reasonable controls to ensure systems integrity; (iii) protect sensitive data from loss, disclosure, alteration, or destruction; and (iv) establish a process for performing annual evaluations of the adequacy of their internal control systems. The weaknesses in controls over property, inventories, accounts payable and EDP security are discussed in greater detail in our report on internal controls. In addition, we noted that NIH did not fully comply with certain provisions of the Chief Financial Officers Act. We have included oral responses to our recommendations as we did not receive written responses from the Public Health Service in sufficient time to include them in our report.

FEDERAL MANAGERS' FINANCIAL INTEGRITY ACT. OMB Circular A-123 defines a material weakness as one which would significantly impair the fulfillment of an agency component's mission; deprive the public of needed services; violate statutory or regulatory requirements; significantly weaken safeguards against waste, loss, unauthorized use or misappropriation of funds, property, or other assets; or result in a conflict of interest. OMB also has set forth additional criteria which provides that a material weakness should:

- merit the attention of the agency head/senior management, the Executive Office of the President, or the relevant Congressional oversight committee;
- exist in a majority of agency components or in a major program or activity;
- risk or result in the actual loss of either $10 million or 5% of the resources of a budget line item; or
- reflect adversely on the credibility of the agency report when subsequently made public.

In its departmental 1990 FMFIA report, HHS reported four material weaknesses that were applicable to the Service and Supply Fund and the Management Fund. A corrective action plan was completed for one of the material weaknesses, and corrective actions are in process for the remaining three material weaknesses. In addition, two new material weaknesses were reported in 1991. The material weaknesses that had not been corrected as of the end of FY 1991 were as follows:

- Lack of accountability over personal property.
- Operating controls in the Delegated Procurement System (DELPRO) and NIH's centralized station support did not assure that small purchases were obtained at the best possible prices.
- Lack of adequate quality of care and environmental conditions for some research animals.
- Inadequate internal controls led to the acquisition of excess computer capacity.
- Weaknesses in controls over time and attendance reporting.

With respect to the lack of accountability over personal property, we noted slower than expected resolution of the material weaknesses. Title 2 requires that agency property records must control physical quantities of government-owned property and its location; enable periodic independent verification of the accuracy of the accounting records through periodic physical counts; and provide a basis for determining asset values and disclosing in the financial statement additions to and retirements of property, plant and equipment each fiscal year. The lack of periodic physical inventories coupled with weaknesses in the control and disposition of property resulted in the loss of control over a significant portion of NIH's personal property. Preliminary results of a recent physical inventory, the first since 1972, indicated that accountability could not be established for about $63 million or almost 16 percent of the book value of personal property. Further research reportedly has reduced the amount of property that has not been accounted for to about $53 million. The portion of the unaccounted for property that belongs to the Funds cannot be readily identified. HHS has reported this condition as a material weakness in its FMFIA report and indicated that the target date for completion of actions to correct the material weakness was changed to FY 1993 rather than 1992.

In addition to the material weaknesses that HHS reported in the 1991 FMFIA report, we identified three significant control weaknesses that we believe meet the OMB criteria for material weaknesses and should be reported as material weaknesses under the FMFIA. These reportable conditions are briefly described below:

Inventory Management. Title 2 provides that the cost of assets acquired is to be recorded net of purchase discounts taken; and property records must control physical quantities and locations of property, and be integrated with or reconciled with the accounting systems. As discussed in detail in our report on internal controls, the perpetual inventory records did not accurately reflect the value of inventories on hand in the Service and Supply Fund and the Management Fund. For both Funds, the perpetual inventory records were significantly inaccurate, inventory values did not reflect actual prices paid, locator records were inaccurate, and perpetual inventory records were not reconciled monthly with the general ledger. In addition, quantities issued from stock in the Service and Supply Fund reflected quantities requisitioned which may not always agree with actual quantities issued to customers. We also noted that physical security of Management Fund's hospital supplies is not adequate to preclude loss. We concluded that these inventory management weaknesses have a material effect on the financial statements, present inadequate safeguards against losses of property, and constitute a material weakness reportable under the FMFIA.

Accounts Payable. NIH was not in compliance with Title 2 with respect to establishing procedures for ensuring proper internal controls over accounts payable; nor with Title 2 provisions that require complete and accurate recording of accounts payable and monthly reconciliation of the general ledger with subsidiary records. The accounts payable balances reported in the financial statements for both the Service and Supply Fund and the Management Fund do not accurately reflect amounts owed for goods and services received. NIH accounting procedures did not provide for accrual of accounts payable on a timely basis, reconciliation of the general ledger with subsidiary records, nor the systematic review and aging of accounts payable. Accounts payable representing goods or services received during FY 1991 were not entered into accounts payable until FY 1992. In addition, accounts payable totaling about $19 million remained on the records of both the Service and Supply Fund ($9 million) and Management Fund ($10 million) for up to several years. Many of these recorded liabilities obviously were invalid. These long outstanding liabilities should be researched and written off, and funds obligated for these liabilities should be deobligated. Since these questionable liabilities represent over half of total "Accounts Payable - Non-Federal" for the two Funds, we believe they have a material effect on the financial statements and represent a material weakness reportable under the FMFIA.

EDP Security. The Division of Computer Research and Technology (DCRT), which provides computer support to NIH activities as well as other Federal agencies, was not fully in compliance with provisions of OMB Circular A-130 regarding security of automated information systems. We noted significant weaknesses in security controls that can be attributed to the lack of clearly defined responsibilities and comprehensive operating policies and procedures. These weaknesses included incomplete implementation of the Resource Access Control Facility security

control plan, ineffective control of passwords, the lack of an alternative off-site data processing facility to be used in emergencies, and lack of an uninterrupted power source to preclude loss of EDP services during a power outage. Because of the potential effect of these security control weaknesses on sensitive data in automated systems such as the accounting and procurement systems, we consider this to be a material weakness reportable under the FMFIA.

This condition is similar to a PHS-wide material weakness in automated information systems security which was disclosed in the Department's annual FMFIA reports from 1988 until 1991, when the Department noted that the material weakness had been corrected. We believe that, to a large extent, this weakness continues to exist at NIH.

Recommendation. We recommend that PHS:

1. Reevaluate its process for assuring that all the Funds' activities are effectively evaluated as required by the FMFIA, and that these activities are in compliance with the requirements of Title 2 and OMB Circular A-130.

   NIH Comment

   The NIH officials concurred and stated that they will take steps to improve the management control program.

THE CHIEF FINANCIAL OFFICERS ACT. We found that NIH's overview of the Reporting Entity could be improved and that NIH's system for accumulating the costs of preparing financial statements was not formalized. NIH's Overview of the Reporting Entity did not clearly: identify the mission, goals and objectives of the Funds; discuss the efficiency of the Funds operations; nor provide performance indicators and measures which could be related to the mission and objectives of the Funds. In addition, NIH does not have a formal system in place for tracking and recording the costs of preparing annual financial statements and identifying the benefits derived from them as required by Section VII of the OMB Bulletin.

Recommendations. We recommend that PHS ensure that:

2. The Overview of the Reporting Entity section of the financial statements clearly: identify the mission, goals and objectives of the Funds; discuss the efficiency of the Funds' operations; and provide performance measures that can be related to the mission and objectives of the Funds.

   NIH Comment

   The NIH officials believe they did an adequate job for an initial effort. They stated that they would attempt to improve the Overview next year.

3. A formal system is established to accumulate the costs of preparing financial statements and a methodology for identifying benefits derived.

NIH Comment

The NIH officials concurred and are developing a methodology to accumulate costs. However, they believe it will take a number of years to determine if it is feasible or cost effective to develop a formal plan for identifying benefits derived.

* * * * *

We considered the material instances of noncompliance with the FMFIA in determining, in our reports dated July 2, 1992 on the financial statements, that the scope of our work was not sufficient to express an opinion on the financial statements.

The results of our tests of compliance, as described above, indicate that, with respect to items tested, the Service and Supply Fund and the Management Fund, did not comply, in all material respects, with the provisions referred to in the second paragraph of this report. The extent of noncompliance noted in our testing indicates that, with respect to items not tested, there is more than a relatively low risk that the Service and Supply Fund and the Management Fund, had not complied with the provisions referred to in the second paragraph of this report.

Clifton, Gunderson & Co.

Baltimore, Maryland
July 28, 1992

Clifton, Gunderson & Co.
Certified Public Accountants & Consultants

To the Inspector General and the Assistant Secretary for Health
Department of Health and Human Services
Washington, D.C.

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROLS

We were engaged to audit the financial statements of the Service and Supply Fund and the Management Fund of the National Institutes of Health (NIH) for the year ended September 30, 1991 and have issued our report thereon dated July 2, 1992. Our reports indicated that the scope of our work was not sufficient to enable us to express, and we did not express, an opinion on the financial statements referred to above.

In planning and performing our engagement to audit the financial statements of the NIH's Service Supply Fund and the Management Fund for the year ended September 30, 1991, we considered the Funds' internal control structures. The purposes of this consideration were to determine: (i) our auditing procedures for the purpose of expressing our opinion on the financial statements; and (ii) whether the internal control structure meets the objectives identified in Government Auditing Standards and OMB Bulletin 91-14. This included obtaining an understanding of the internal control policies and procedures and assessing the level of control risk relevant to all significant cycles, classes of transactions, or account balances; and for those significant control policies and procedures that have been properly designed and placed in operation, performing sufficient tests to provide reasonable assurance that the controls are effective and working as designed.

Management officials of the Service and Supply Fund and the Management Fund are responsible for establishing and maintaining an internal control structure for their respective funds. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable but not absolute assurance that:

- obligations and costs are in compliance with applicable laws;
- funds, property and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation; and
- revenues and expenditures applicable to agency operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports to maintain accountability over assets.

For the purpose of this report, we have classified the significant internal control structure policies and procedures in the following categories:

- Financial reporting
- Budget
- Cash/Treasury
- Revenue and accounts receivable
- Expenses and accounts payable
- Payroll and related liabilities
- Fixed assets and inventories
- Data processing
- Administrative controls over compliance with laws and regulations

Our consideration of the internal control structure for the two Funds included all of the categories listed above. For each of the categories, we obtained an understanding of the design of the relevant policies and procedures and whether they have been placed in operation, and assessed control risk. Our tests of control procedures were not sufficient to express, and we do not express, an opinion on the system of internal controls taken as a whole.

We noted certain matters involving the internal control structures of the Funds that we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants and OMB Bulletin 91-14. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure that, in our judgment, could adversely affect the organization's ability to ensure that obligations and costs are in compliance with applicable law; funds, property and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation; and revenues and expenditures applicable to agency operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports in accordance with applicable accounting standards and to maintain accountability over the assets. Reportable conditions may be classified as a material weakness when the design or operation of one or more of the internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. OMB Circular A-123 defines a material weakness as one which would significantly impair the fulfillment of an agency component's mission; deprive the public of needed services; violate statutory or regulatory requirements; significantly weaken safeguards against waste, loss, unauthorized use or misappropriation of funds, property, or other assets; or result in a conflict of interest. OMB also has set forth additional criteria which provides that a material weakness should:

- merit the attention of the agency head/senior management, the Executive Office of the President, or the relevant Congressional oversight committee;

- exist in a majority of agency components or in a major program or activity;
- risk or result in the actual loss of either $10 million or 5% of the resources of a budget line item; or
- reflect adversely on the credibility of the agency report when subsequently made public.

We believe that the weaknesses in internal controls over inventory, accounts payable, and EDP security that we noted meet the criteria specified by OMB Circular A-123 for material weaknesses under the Federal Managers' Financial Integrity Act (FMFIA). Because of these material weaknesses, we do not believe that the internal control structure provided adequate assurance that the Funds' internal control objectives were being met. These conditions are discussed in the following paragraphs. We have included oral responses to our recommendations as we did not receive written responses from the Public Health Service in sufficient time to include them in our report.

PROPERTY MANAGEMENT SYSTEM. NIH has identified and reported under the FMFIA significant material weaknesses in its property management practices which affect all NIH personal property including that of the Service and Supply Fund and the Management Fund. Title 2 of GAO's Policy and Procedures Manual provides that agency property records must control physical quantities of government-owned property and its location; enable periodic independent verification of the accuracy of the accounting records through periodic physical counts; and provide a basis for determining asset values and disclosing in the financial statements additions to and retirements of property, plant and equipment each fiscal year. The lack of periodic physical inventories and reconciliation of inventory results with accountable records combined with weaknesses in the control and disposition of property resulted in the loss of control over a significant portion of NIH's personal property. As part of its corrective action plan, NIH in 1991 engaged a contractor to perform a physical inventory of all personal property, the first physical inventory performed since 1972. Although reconciliation of the inventory results with the accounting records has not been completed, preliminary results indicate that about $63 million or almost 16 percent of the $403 million book value of personal property has not been accounted for. Unreconciled items included about 1,300 personal computers valued at $4.5 million and about 1,600 centrifuges valued at more than $5 million. In June 1992, NIH reported that a concerted effort had reduced the unaccounted for items to $53.6 million. The amount of unaccounted for property belonging to the Funds could not be readily determined. Because of these significant weaknesses, the NIH Intramural Property Management System is not reliable.

We noted other instances where the lack of internal control procedures and system weaknesses have resulted in incorrect data in the financial accounting records:

- The general ledger was not reconciled with subsidiary records monthly.

- A large number of assets valued at less than the $5,000 threshold prescribed in Title 2 were capitalized. We noted numerous recorded transactions for equipment valued at less than $1,000.

- Service contracts were incorrectly capitalized and recorded in the property account. For example, an expenditure for $173,632 for food service operations was charged to the property account.

- Acquisition costs did not always include transportation, installation and related costs of obtaining the assets and, in some instances, reflected the mean cost of like items rather than actual costs. For example, a tunnel washer costing $90,237 was recorded in the property records as costing $52,991 which was the mean cost of like items purchased previously.

- Assets acquired as the result of a trade-in of other property were recorded at the net cash paid amount without regard to the net book value of the traded-in property. As an example, four Kodak duplicating machines were purchased at a total net cost of $205,300 and recorded in the general ledger in that amount. Although four Canon copiers were traded in as part of this purchase, no adjustment was made for the net book value of the Canon copiers.

In many of these instances, implementation of a series of computer edit checks would have precluded the improper entries, particularly those concerning capitalization criteria.

In view of the large discrepancies between the physical inventory results and the property records and the difficulties in reconciling the differences, the NIH established a Board of Survey to review its property shortages, determine responsibility and establish the extent of liability of employees for the missing responsibilities for property management. Almost one year has elapsed since the NIH engaged a contractor to conduct the physical inventory. With the passage of time, it becomes more difficult to reconcile differences and pinpoint accountability. We believe NIH should accelerate its efforts to complete the reconciliation and determine liability, particularly since the property involved is susceptible to theft.

As discussed earlier in this report, NIH has reported its Intramural Property Management System as a material weakness. Our review of the Funds' property management practices confirmed that the weaknesses in internal controls constitute a material weakness as defined in OMB Circular A-123 which provides that a material weakness significantly weakens safeguards against waste, loss, unauthorized use or misappropriation of funds, property, or other assets.

Recommendations. In view of the actions in process as part of NIH's corrective action plan, we are making no recommendations regarding the weaknesses in internal controls over personal property that are already a matter of record. In its December 1991 FMFIA report, the Department of Health & Human Services indicated that the target date for completion of actions to correct the material weakness was changed to FY 1993 rather than 1992. The target date was revised because the scope of the reconciliation is more extensive than originally anticipated, and the Board of Survey will need additional time to investigate discrepancies.

With respect to the internal control weaknesses identified during our review, we recommend that PHS implement procedures to ensure that:

1. Appropriate edit checks are incorporated into the data processing system to reject fixed asset transactions for items valued at less than $5,000 and contracts for services. Such transactions should be recorded on an exception listing for further review and reclassification.

   NIH Comment

   The NIH officials concurred that better controls are needed. They will explore a number of options to ensure appropriate assignment of object classification codes, as well as the feasibility of using the Property Management Information System (PMIS) database as the basis for capitalization accounts in the general ledger.

2. The general ledger is reconciled monthly with subsidiary records, the acquisition cost of assets include all costs of acquiring and installing assets, and recorded value of assets reflects the value of traded-in property.

   NIH Comment

   The NIH officials concurred and have developed detailed actions to implement the recommendation. The NIH officials indicated that implementation is expected to take one year.

INVENTORY MANAGEMENT. The perpetual inventory records did not accurately reflect the value of inventories on hand in the Service and Supply Fund and the Management Fund. Annual physical inventory are taken, however, they are not taken at the fiscal year end. Moreover, the general ledger and perpetual inventory records were not in agreement at any point in time during the year except when adjustments were made prior to preparation of the FY 1991 financial statements to reduce the general ledger balance of the Service and Supply Fund by $1.5 million to bring it into balance with the perpetual inventory. The general ledger balance of the Management Fund was increased by $2.3 million to account for hospital supplies that previously had not been recorded in the general ledger. The inaccurate balances were the result of misclassification of non-inventory transactions as inventory, inadequate inventory reconciliation procedures, inaccurate unit prices, inaccurate stock locator records and poor physical security.

Service and Supply Fund. The September 30, 1991 financial statements for the Service and Supply Fund showed that the Fund had approximately $8.1 million of inventories held for sale to its customers. The Supply Branch inventory accounts for 66 percent of the total inventory, the Materials and Supply Branch accounts for 27 percent, and two other branches account for the remaining seven percent. The perpetual inventory records were not reconciled monthly with the general ledger. The inventory balance in the general ledger was reduced by $1.5 million to bring the general ledger into balance with the perpetual inventory records before the September 30, 1991 financial statements were prepared. The reasons for the large adjustment were not adequately explained.

We believe that one of the principal factors contributing to the imbalance between the general ledger and perpetual inventory records is the misclassification of certain non-inventory transactions. Some NIH organizational elements, including the Office of the Director, requisitioned supplies for their consumption and erroneously coded the transactions as Object Classification Code 269Z, "All Other - Inventory" and other inventory codes. Our limited review identified about $200,000 of such transactions in FY 1991. Transactions such as these cause increases in the general ledger inventory account, but will not be recorded in the perpetual inventory records. The use of "inventory" object classification codes should be restricted to Service and Supply Fund offices responsible for purchasing supplies and materials for inventory. A computer edit could be implemented to prevent all other NIH offices from using these object classification codes.

We assessed the reliability of the perpetual inventory records by making test counts of 127 judgementally selected items in the Supply Branch and the Materials and Supply Branch inventories prior to the start of business on June 1, 1992, using the prior workday's perpetual inventory balances as the basis for the verification. Our tests revealed that quantities on hand differed significantly from the perpetual inventory records for over 62 percent of the items tested. The quantity differences ranged from a shortage of 427 units of 9,018 to an overage of 79 units where no units were recorded. Inventory locator records were not always accurate. We noted a few locations that were incorrect. Several other locations were vague, such as "BW" for back wall. There were also a number of items that had multiple locations. The inventory records identify the primary location only. In addition to these stock control problems, we noted problems with inventory pricing procedures. Inventory was priced on the basis of purchase order prices which may not be the same as actual prices, inventory value was not adjusted to reflect actual prices less discounts paid for the items. The magnitude or financial impact of these differences could not be determined due to lack of readily available records.

Management Fund. The Management Fund's financial statements for FY 1991 reported inventories valued at $3.6 million which consisted of $1.3 million of drugs located in the Clinical Center pharmacy and approximately $2.3 million of hospital supplies. Although perpetual inventory records were maintained for the hospital supplies, they were not recorded in the general ledger. A journal voucher adjustment was made to increase the inventory account by $2.3 million in preparing the FY 1991 financial statements.

Clinical Center drug inventory contains pharmaceutical and controlled substances. Our test counts of 30 line items judgementally selected from the Clinical Center inventory of non-controlled substances showed that quantities on hand differed from perpetual inventory balances for 8 items, or 27 percent of the items tested. The differences ranged from a shortage of two units to an overage of seven units. A similar test of the accuracy of the perpetual inventory records for the Material Management Section's supplies disclosed that quantities on hand differed from recorded inventory balances for 33 items, or 66 percent, of the 50 items tested. The differences ranged from a shortage of 106 units to an overage of 7,980 units.

The problems regarding the pricing of inventory that affected the accuracy of the Service and Supply Fund's financial records is a system-wide problem that equally affects the Management Fund's inventories. In addition, some of the discrepancies in inventory value also can be attributed to differences in units of issue, e.g., "each" according to inventory records versus "box" used in requisitions. For example, the unit of issue for an integrated shunt system is "each" according to the inventory report. In our test count, we counted 8 cases of 10 boxes each containing 100 units for a total of 8,000. The NIH records showed a quantity of 20; we believe they were counting boxes. We also noted that the warehouse for the Material Management Section's supplies is not adequately secured (it is used as a thoroughfare for unauthorized employees from surrounding offices); the warehouse was disorganized; and the locator system was unreliable.

We believe that the inventory management weaknesses described above have a material effect on the financial statements, significantly weaken safeguards against waste, loss, unauthorized use or misappropriation of property, and constitute a material weakness reportable under the FMFIA. The current management control plan shows the NIH inventory area as low risk, and indicates than an alternative internal control review performed in FY 1991 classified the inventory area as a non-material weakness. Because the report could not be located, we were unable to review the finding and planned corrective actions.

Recommendations. We recommend that PHS ensure that:

3. Physical inventories are taken annually at September 30.

NIH Comment

The NIH officials concurred with the recommendation to take annual physical inventories. They will explore the feasibility of conducting the inventories as close to fiscal year end as possible.

4. The results of periodic physical inventories are reconciled with the perpetual inventory records and general ledger accounts. Also, reconcile perpetual inventory records with the general ledger monthly. Discrepancies are thoroughly researched before the general ledger or inventory records are adjusted.

NIH Comment

The NIH officials stated that adjustments to increase or decrease inventory records are normally processed within a month after a physical inventory has been completed. They stated that they are developing a process to reconcile the perpetual inventory with the general ledger on a monthly basis. They will stress the importance of the research function to the appropriate inventory managers.

5. The use of "inventory" object classification codes are restricted to only those offices responsible for purchasing inventory.

NIH Comment

The NIH officials concurred. They stated that a process has been initiated to restrict the use of inventory sub-object classification codes, which should be working by the end of calendar year 1992.

6. Locator records are tested periodically to assure that they are accurate and current.

NIH Comment

The NIH officials believe this is being done, however it is not occurring on a routine basis. Accordingly, they stated that they will take action to develop policies that will require all warehouse and store operations to conduct periodic location testing.

7. Physical security of the Material Management Section's warehouse is strengthened and access to the warehouse is limited to authorized personnel.

NIH Comment

The NIH officials concurred. However, while they believe an increased level of security is desirable, they stated that operational requirements preclude restricting access through the storeroom. They are pursuing other approaches that will restrict non-essential traffic through the storeroom area. They stated that the Clinical Center will ask the NIH Division of Security to do an audit of the area to see how physical security can be improved.

8. Unit prices used to value inventory reflect actual prices paid rather than purchase order prices which may not represent actual costs; and correct units of issue are used.

NIH Comment

The NIH officials concurred that inventory values should reflect actual prices paid. With respect to correct units of issue, NIH officials stated that this is being addressed through increased use of standard packaging specifications.

9. Weaknesses in control over inventories are reported as a material weakness in FMFIA reports.

NIH Comment

The NIH officials stated that they believe designation of inventory management as a material weakness is premature. Accordingly, NIH officials believe this area should be designated a potential material weakness. NIH officials stated that they plan to conduct a comprehensive study of this area in all warehousing operations by September 30. If the study reveals the existence of significant problems in this area, NIH officials stated that they will designate inventory management a material weakness by September 30.

ACCOUNTS PAYABLE. The NIH accounting system has significant internal control weaknesses in the accounts payable area that preclude the preparation of accurate financial statements for both the Service and Supply Fund and the Management Fund. The weaknesses include the absence of a proper procedure for accrual of accounts payable on a timely basis; and the lack of procedures for the periodic review and aging of accounts payable.

NIH does not have sufficient year end cut-off procedures for recording accounts payable. Goods and services received during FY 1991 were not entered into accounts payable until FY 1992. As a result, liabilities and expenses are understated in the financial statements. We reviewed subsequent disbursements in excess of $75,000 on the Service and Supply Fund, and $100,000 on the Management Fund. This review identified 26 transactions totalling in excess of $7 million which were not recorded as accounts payable at September 30, 1991.

NIH had not implemented procedures to periodically review the status of long outstanding accounts payable. Accounts payable remained on the records of both the Service and Supply Fund and Management Fund for several years. Of the Service and Supply Fund's approximate $13 million of "Accounts Payable - Non-Federal," about $9 million was over 1 year old. In the Management Fund, about $10 million of the $17 million of "Accounts Payable - Non-Federal" was over 1 year old. We believe the practice of simultaneously recording an obligation, accrued expenditure, and payable when an invoice is received that cannot be readily matched with a

previous recorded obligation contributed to the large number of old accounts payable, many of which are invalid. While such a procedure may be necessary to ensure that vendors are paid on time, such transactions should be thoroughly researched to preclude duplicate obligations. Also, procedures should be established to periodically age and review accounts payable to ensure that invalid accounts payable are canceled and funds are deobligated.

We believe that the weaknesses in controls over accounts payable have a material effect on the financial statements, have hindered the timely and effective use of a significant amount of funds, merit the attention of the agency head, and should be reported as a material weakness.

Recommendations. We recommend that PHS ensure that:

11. The year-end cut-off date be extended to ensure that all accounts payable are properly recorded and that sufficient procedures are established to review documents for goods and services received.

    NIH Comment

    The NIH officials concurred. They stated that the cut-off date will be extended until the preparation of the year-end financial reports.

12. Invoices that cannot be readily matched to obligations are thoroughly researched before obligations are recorded to avoid duplicate obligations.

    NIH Comment

    The NIH officials concurred. They stated that procedures are being developed and implemented to eliminate duplicate obligations that occur when invoices cannot be readily matched to obligations.

13. Procedures are implemented to periodically age and review accounts payable to identify and cancel invalid payables and deobligate funds.

    NIH Comment

    The NIH officials concurred. They stated that procedures are being developed that will establish schedules for review of accounts payable balances during the fiscal year. In addition, training will be provided to accounts payable personnel.

14. Weaknesses in controls over accounts payable are reported as a material weakness in FMFIA reports.

NIH Comment

The NIH officials did not concur that this was a material weakness. They stated that they are developing further information which will enable the accounts payable staff to understand and use the automated system more effectively. They stated that with the development and implementation of procedures that describe the process of reviewing and correcting of accounts payable balances on a routine basis during the fiscal year, the controls will be improved.

EDP SECURITY CONTROLS. The Division of Computer Research and Technology (DCRT), which provides computer support to NIH activities as well as other Federal agencies, had not implemented adequate EDP security measures to preclude unauthorized access to sensitive accounting and procurement information which could adversely affect the conduct of the Service and Supply and Management Funds. Access controls were not properly implemented, passwords were not adequately protected, and contingency plans did not provide viable alternatives. As a result, the administrative data base (ADB) and utility (WYLBUR) systems are susceptible to unauthorized access. Also, NIH does not have adequate assurance that EDP operations will continue uninterrupted if a catastrophic event were to occur.

The Resource Access Control Facility (RACF) security control plan, if properly implemented, provides an effective means of monitoring and controlling access to computer systems operations and resources. DCRT, however, has not implemented RACF system-wide. Instead, users were given the option of implementing RACF for certain computer applications. Because invoking RACF requires additional processing steps most users, including those with sensitive applications such as accounting and procurement, often choose not to invoke RACF and instead rely on other secondary security measures such as user identification and passwords to protect their data. RACF should be centrally administered to achieve maximum security benefits rather than provided for use on an optional basis.

The security of sensitive data was further jeopardized by ineffective control and usage of passwords. Passwords were not changed on a periodic basis; about 1,100 of the 3,600 passwords for the ADB system had not been changed since before January 1991 and some had not been changed for several years. Information was not available to determine when passwords were changed for the WYLBUR system. The longer a password is in use, the higher the risk of undetected compromise of the password. Federal Information Processing Standards Publication (FIPS PUB) Number 112 states that passwords should be changed periodically (it recommends passwords be changed at least every 6 months for medium protection requirements) and the password system should have automated features to enforce such changes. In addition, passwords were shared by more than one individual resulting in diminished accountability and audit trails, and possible unauthorized access. We also noted that passwords had a fixed length

of three characters. Short, fixed-length passwords make it easier for an intruder to try various combinations to penetrate the system. FIPS PUB 112 calls for the use of variable-length passwords with a range of four to eight characters for medium protection requirements and six to eight characters for high protection requirements.

Procedures also were needed to modify or delete access authority of individuals when they change positions or leave NIH. During our review, we noted one instance where someone using a former employee's password attempted to access the ADB system. We also identified three individuals who left NIH in January and February of 1991 who were still on the authorized access list for WYLBUR. Further inquiry disclosed that there were no formal procedures to modify or cancel access authority. At a minimum, biweekly personnel activity reports should be reviewed to identify personnel terminations and position changes. We also noted that users may make an unlimited number of attempts to log on to the ADB system without being locked out. On the other hand, the WYLBUR system locks out users after three attempts to log on to the system. This is consistent with FIPS PUB 112 which considers that three attempts is adequate for most uses.

While NIH has done an excellent job of identifying the criticality of applications, and has completed risk assessments of several applications, compliance with OMB Circular A-130 is not complete. The contingency plans are inadequate in that they rely on the use of manual procedures in the event of a catastrophic loss of data processing capability. In addition, there is no uninterrupted power source to preclude interruption of service during a power outage, backup tapes are not stored in an off-site location and there is no policy specifying retention periods for tapes and source documents. The use of manual procedures are an impractical alternative for the on-line interactive systems in use at NIH except as a short-term, interim measure. Arrangements should be made to enable NIH to continue data processing operations at an alternative facility in the event of a catastrophe.

In view of the sensitivity of certain accounting, procurement and personnel data, we believe the weaknesses in security controls significantly weaken safeguards against loss, unauthorized use or misappropriation of funds, or other assets and constitutes a material weakness.

This condition is similar to a PHS-wide material weakness in automated information systems security which was disclosed in the Department's annual FMFIA reports from 1988 until 1991, when the Department noted that the material weakness had been corrected. We believe that, to a large extent, this weakness continues to exist at NIH.

Recommendations. We recommend that PHS:

15. Require sensitive accounting and procurement data by RACF protected.

NIH Comment

The NIH officials concurred. They stated that they will develop and issue a policy in fiscal year 1993 that directs systems managers of high-critical/high-sensitive systems to use RACF and possibly other available means of protecting data.

16. Strengthen the effectiveness of passwords for both the ADB and WYLBUR systems by:

a. Implementing and automated feature which forces the changing of passwords on a periodic basis, at least semiannually.

NIH Comment

The NIH officials stated that they will implement this immediately.

b. Using variable-length passwords and increasing the number of characters commensurate with the protection requirements.

NIH Comment

The NIH officials stated that they will institute use of six character variable ADB passwords in conjunction with an NIH-wide security awareness program being planned by the newly established NIH Office of Information Resources Management. They also stated that WYLBUR passwords will be expanded to six characters, if feasible.

c. Ensuring that passwords are issued only to individuals rather than to groups.

NIH Comment

The NIH officials stated that this could be corrected easily.

d. Establishing procedures to modify or cancel passwords when personnel change positions or leave NIH. This can be accomplished by reviewing the biweekly personnel activity report to identify personnel losses or transfers or by establishing formal clearance procedures when personnel transfer within NIH or leave NIH. During our audit, we were advised that NIH has initiated steps to develop such a procedure.

NIH Comment

The NIH officials stated that the Office of Information Resources Management will assure that all NIH components are aware of their responsibility to modify or cancel passwords or terminate accounts affected by personnel actions within their areas.

17. Adopt similar log-on restrictions for ADB as are currently in use for WYLBUR to lock out users after three unsuccessful attempts to access the system.

NIH Comment

The NIH officials stated that they will institute automatic log-off after three unsuccessful attempts to access the ADB.

18. Revise contingency plans to include provisions for an alternative off-site processing facility in case of an emergency.

NIH Comment

The NIH officials concurred. They stated that they are currently developing plans for an alternative off-site processing facility. They also stated that a consultant will assist in the development of a business recovery plan that will take effect in the event of a disaster.

19. Make provisions to acquire an uninterrupted power source and off-site storage of backup tapes, and establish a retention policy for tapes and source documents.

NIH Comment

The NIH officials concurred. They stated that they have requested the approval of the Office of the Secretary to utilize an existing Department of the Air Force contract mechanism to acquire an uninterruptable power supply. They also stated that they are awaiting assignment of an off-site storage area for the ADB at Executive Plaza.

20. Reinstate the weaknesses in EDP security controls as a material weakness in the FMFIA reports.

NIH Comment

The NIH officials did not concur. They stated that they have made great strides in the development of a contingency and disaster recovery plan. They stated that a Contingency Planning Module has been added to the NIH Standard Risk Protocol and that PHS confirmed that NIH was proceeding in the right direction with contingency planning.

The NIH officials further stated that they are currently conducting, under contract, a study that will lead to total Contingency and Disaster Recovery Plan. The ADB manual procedural plan was developed as an interim measure.

* * * * *

A material weakness is a reportable condition in which the design or operation of the specific internal control structure elements do not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the Statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be reportable conditions, and accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses as defined above. We believe the conditions reported in the previous paragraphs regarding weaknesses in internal controls over personal property, inventories, accounts payable and EDP security are material weaknesses as defined in the immediately previous paragraphs.

We also noted other matters involving the internal control structure and its operation that we have reported to the management of the Service and Supply Fund and the Management Fund of the NIH in a separate letter dated July 2, 1992.

Clifton, Gunderson & Co.

Baltimore, Maryland
July 28, 1992

NATIONAL INSTITUTES OF HEALTH

NARRATIVE

SERVICE AND SUPPLY FUND
AND
MANAGEMENT FUND

FISCAL YEAR 1991

TABLE OF ABBREVIATIONS

AAALAC	American Association for Accredition of Laboratory Animal Care
Admin.	Administrative
AM	Acquisitions Management
Anes.	Anesthesiology
BEIP	Biomedical Engineering and Instrumentation Program
CAP	Corrective Action Plan
CFO	Chief Financial Officers
CC	Clinical Center
DCRT	Division of Computer Research and Technology
DPM	Division of Personnel Management
DRG	Division of Research Grants
FMFIA	Federal Managers' Financial Integrity Act
FMS	Financial Management Services
FTS	Federal Telecommunications System
GE	General Expense
IMU	Inventory Management Unit
LAN	Local Area Network
MAPB	Medical Arts and Photography Branch
MASB	Materials Acquisition and Supply Branch
Med.	Medical
MF	Management Fund
MIS	Medical Information System
NCI	National Cancer Institute
NCRR	National Center for Research Resources
NEI	National Eye Institute
NHLBI	National Heart, Lung, and Blood Institute
NIA	National Institute on Aging
NIAAA	National Institute on Alcohol Abuse and Alcoholism
NIAID	National Institute of Allergy and Infectious Diseases
NIAMS	National Institute of Arthritis and Musculoskeletal and Skin Diseases
NICHD	National Institute of Child Health and Human Development
NIDCD	National Institute on Deafness and Other Communication Disorders
NIDDK	National Institute of Diabetes and Digestive and Kidney Diseases
NIDR	National Institute of Dental Research
NIH	National Institutes of Health
NIMH	National Institute of Mental Health
NINDS	National Institute of Neurological Disorders and Stroke
ORS	Office of Research Services
OTT	Office of Technology Transfer
PMIS	Property Management Information System
PPB	Personal Property Branch
Rad.	Radiology
SB	Supply Branch
SERP	Scientific Equipment Resources Program
SSF	Service and Supply Fund
TCB	Telecommunications Branch
VRP	Veterinary Resources Program

OVERVIEW OF NATIONAL INSTITUTES OF HEALTH

Introduction

The National Institutes of Health (NIH) began as a one-room Laboratory of Hygiene in 1887, and today is one of the world's foremost biomedical research centers. An agency of the Department of Health and Human Services, the NIH is the Federal focal point for health research.

Its mission is to uncover new knowledge that will lead to better health for everyone. The NIH conducts research in its own laboratories; supports the research of non-Federal scientists in universities, medical schools, hospitals, and research institutions throughout this country and abroad; helps in the training of research investigators; and fosters and supports biomedical communication.

The NIH is located in Bethesda, Md., a suburb of the District of Columbia. On its campus-like grounds, the NIH maintains hundreds of laboratories containing complex and highly sophisticated research equipment. It also contains a 540-bed research hospital known as the Warren Grant Magnuson Clinical Center, and the National Library of Medicine, the world's largest repository of medical literature and a national center for biomedical communication.

The NIH's FY 1991 obligations totalled $8.2 billion, which represents an increase from FY 1990 of 8%.

The Chief Financial Officers (CFO) Act of 1990 requires executive agencies to prepare financial statements for all accounts that involve substantial commercial activity. The NIH Service and Supply Fund and the Management Fund will be subject to an audit in FY 1992. These two accounts represent 8% of the total NIH budget. Some programs are funded by both accounts. All direct appropriations, gift funds, and royalty accounts are excluded from the audit. These are outside the requirements of the CFO Act for FY 1991.

NIH SERVICE AND SUPPLY FUND
and
MANAGEMENT FUND
Executive Summary

Service and Supply Fund

Three significant events occurred in FY 1991. First, beginning in April 1991, the Telecommunications Branch (TCB) revised the billing program for a significant amount of the telecommunication charges. All C&P, FTS, and smaller vendor bills were charged directly to the Institutes instead of to the TCB funds. This successfully resulted in an approximate reduction of $13 million in spending authority to the SSF in FY 1991.

Second, a project was implemented to improve the accountability of the NIH personal property in accordance with the Federal Managers' Financial Integrity Act (FMFIA) of 1982. Under the supervision of the Personal Property Branch (PPB), Division of Logistics, a comprehensive physical inventory of the NIH personal property was conducted. The cost of this project was $1.1 million and was funded by the PPB, through reimbursement from the Institutes.

The new Property Management Information System (PMIS), a module under the NIH Administrative Data Base, was developed in FY 1991 to account for personal property. The new system was developed to improve the timeliness and accuracy of the property records and to provide improved detailed support for the general ledger balances. The PMIS performs the property functions in a decentralized manner, but provides centralized review and control. A Board of Inquiry will be convened to authorize appropriate changes. These changes will be reported in FY 1992.

Third, a material weakness was declared under the FMFIA regarding the Division of Computer Research and Technology's (DCRT) computing capacity (See NIH-FMFIA-1). The NIH recognizes the need for improved capacity planning and management at the DCRT, and has developed a corrective action plan to address the material weakness identified by the General Accounting Office.

The NIH and the DCRT firmly support excellence and efficiency in both scientific and administrative computing. The NIH fully intends to use the GAO findings contructively with ongoing management initiatives to help chart strategic course adjustments in our business plan for providing biomedical computing and to improve our service and reduce costs.

Management Fund

There were two significant achievements in 1991. The first achievement was the accreditation of the Clinical Center (CC) by the Joint Commission on Accreditation of Health Care Organizations (JCAHO). In addition to being granted accreditation, the CC was also commended by the JCAHO for surpassing JCAHO standards. Among the actions taken by the CC in achieving accreditation were the implementation of a Quality Assurance System to ensure the development of the highest quality research initiatives, protocols, and enhancements made to the medical records systems.

The second achievement was the continued advancement of the ten-year master utility plan which includes the Infrastructure Modernization and Improvement Program (IMIP) and the Clinical Center Complex Infrastructure Modernization and Improvement Program (CCC-IMIP). Among the improvements realized in 1991 were: the installation of an emergency chill water line to the Clinical Center; significant progress in the construction of additional chillers to increase capacity; and completion of the design for the removal of PC contaminated transformers.

OVERVIEW OF NATIONAL INSTITUTES OF HEALTH

Management's Discussion & Analysis

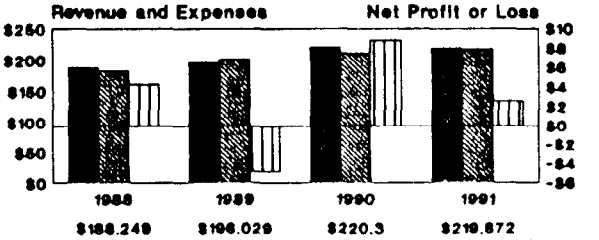
Service and Supply Fund

The NIH Service and Supply Fund (SSF) was established on July 3, 1945 under 42 U.S.C. 231. This fund finances a variety of centralized research support and administrative activities required for the efficient and effective operation of numerous NIH programs and facilities.

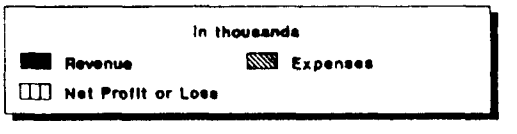
The SSF provides a mechanism for consolidating the financing and accounting of business-type operations involving the sales of services and commodities to customers. The majority of these services and commodities can be identified to specific customers; therefore, their costs are charged to the recipient appropriations on a fee-for-service basis. However, the General Expense costs are general in nature. The General Expense costs are assessed on a formula basis, which is a percentage of each institutes total appropriation, less the budgeted assessment for the Management Fund, to the total of all appropriations.

The services and commodities provided by the SSF activities include mainframe computing, engineering planning and design, printing, telecommunications, procurement, shipping and receiving, motor pool, research animals, fabrication and maintenance of scientific equipment, and other administrative support services.

SERVICE AND SUPPLY FUND
STATEMENT OF OPERATIONS

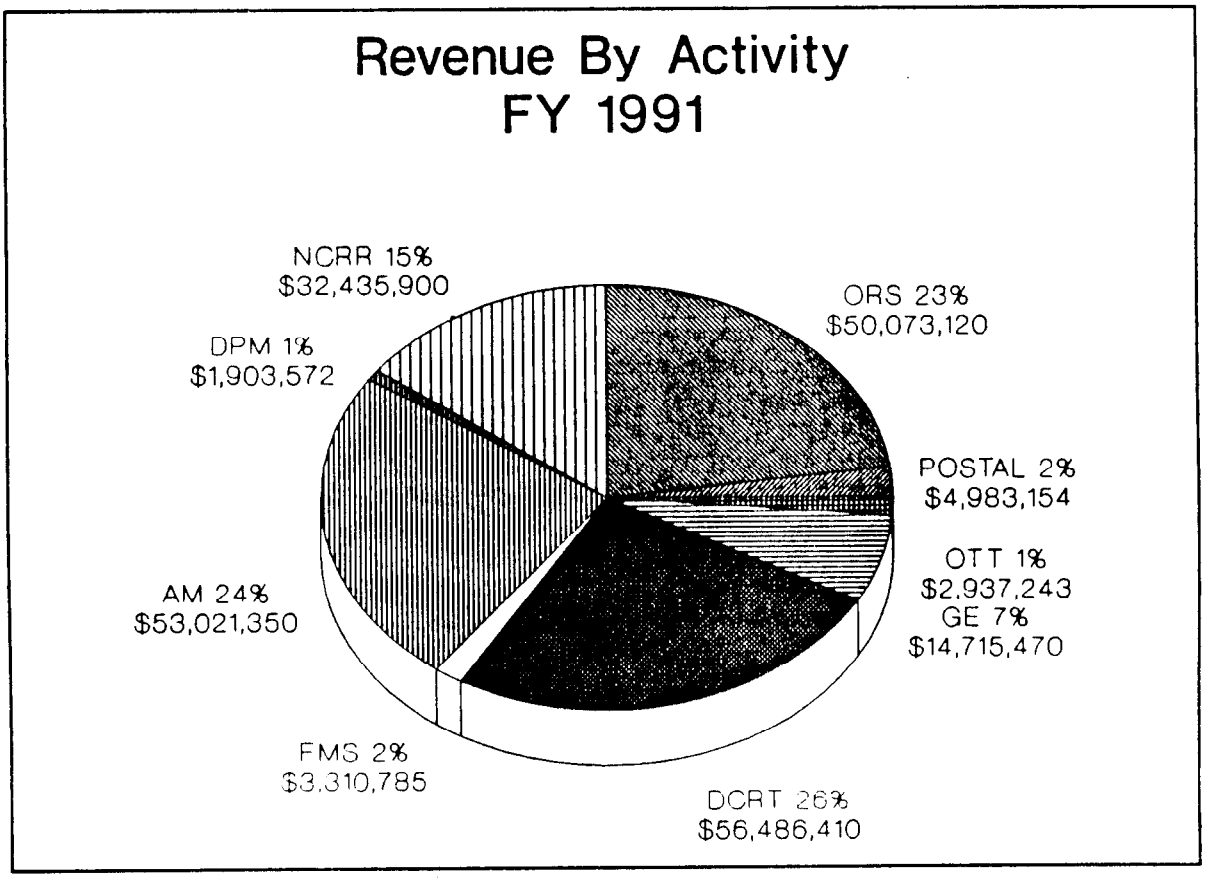


	1988	1989	1990	1991
Revenue	$188.249	$196.029	$220.3	$219.872
Expenses	$182.53	$200.835	$211.421	$217.257
Net Profit or Loss	$4.327	-$4.806	$8.879	$2.615

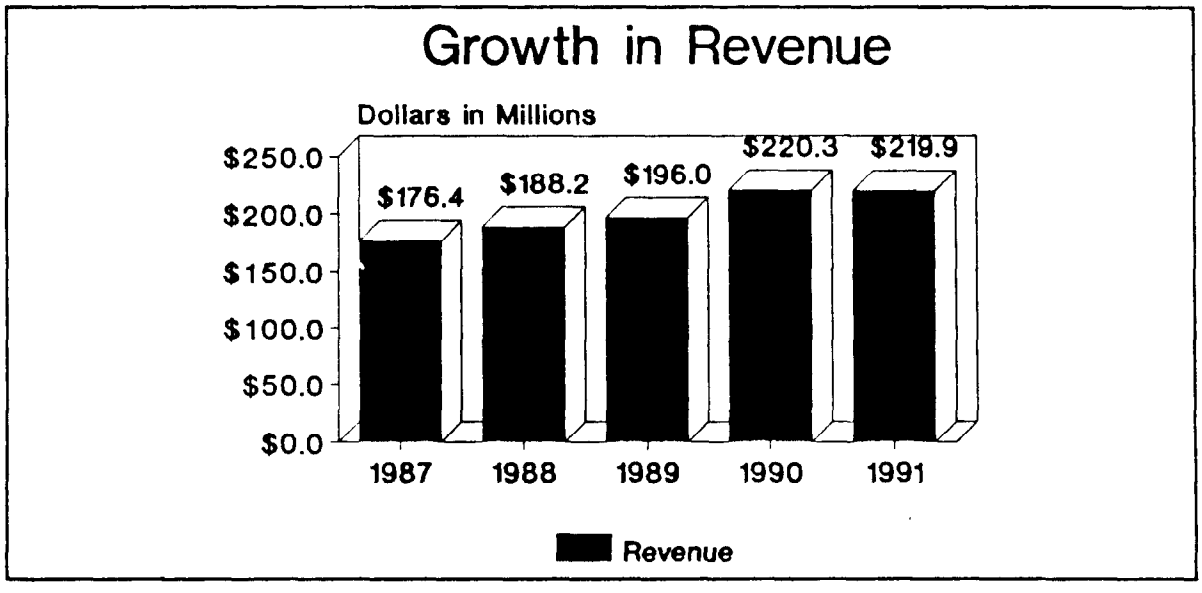


The available resources enabled the SSF operations to provide support services of the highest quality to the medical research programs of the Institutes. The following is a list of the SSF organizations and the revenue they generated in FY 1991.

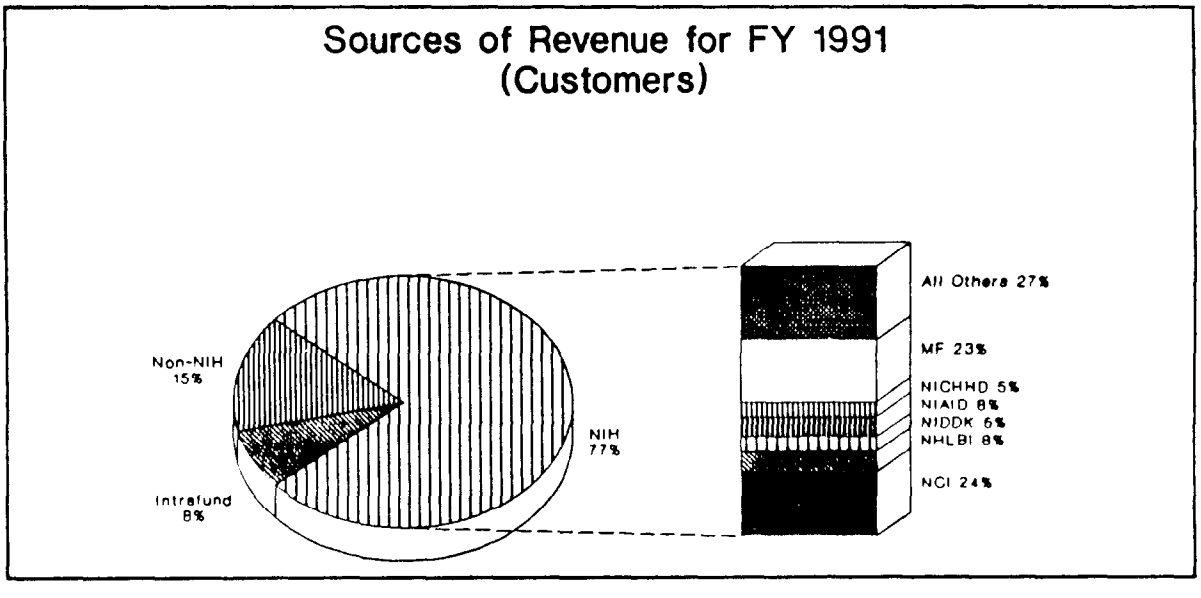
Organization	FY 1991 Revenue (in millions)
o Division of Computer Research and Technology	$56.5
o Office of Acquisitions Management:	
Division of Procurement	10.1
Division of Logistics	42.9
o Office of Research Services	
Division of Technical Services	34.9
Division of Engineering Services	17.9
Division of Safety	2.3
o National Center for Research Resources	32.5
o Office of the Director	
Division of Personnel Management	1.9
Division of Financial Management	3.3
Office of Technology Transfer	2.9
General Expense	14.7



The SSF generated revenue of $219.9 million in FY 1991. With the exception of FY 1991, the SSF's revenue has steadily increased. The TCB revised its billing program in FY 1991 which reduced its revenue by approximately $13 million.



The majority, 77%, of the FY 1991 services were provided to the Institutes. Sales to non-NIH customers totalled 15% of all SSF sales while intrafund sales represented 8%.



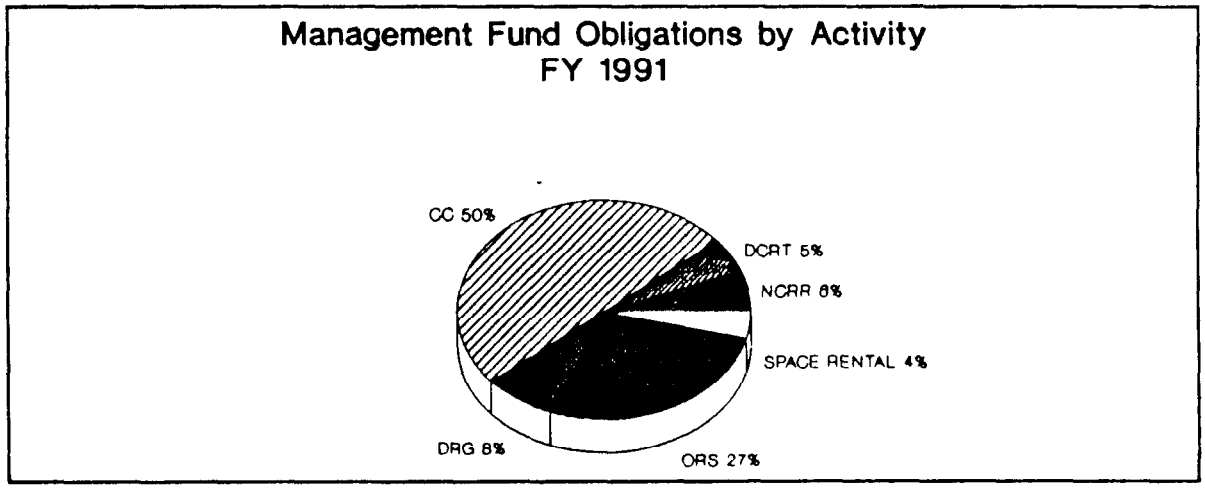
Management Fund

The Management Fund (MF) was established on June 29, 1957, by Public Law 85-67. The MF was created to finance a variety of centralized research support services and administrative activities which are required for the efficient and effective operation of all NIH programs and facilities. Because these services and activities do not readily lend themselves to a system of charging recipient appropriations on a fee-for-service basis, they are assessed to the individual appropriations on a formula basis. The MF organizations providing these services do not receive an appropriation from Congress. Their costs are incorporated into the various NIH appropriations during the formulation phase of the budget process.

The services provided by the MF include utilities and plant maintenance, a 540 bed hospital and outpatient clinic, receipt, review and referral of research and training grant applications, collaborative computer science research, biomedical engineering, and general administrative support services.

The following is a list of the MF organizations and the FY 1991 obligations:

Organization	Obligations (in millions)
o Clinical Center	$200.5
o Intramural Research Support Services (Includes Office of Acquisitions Mgmt. and Office of Research Services	110.0
o Division of Research Grants	34.3
o National Center for Research Resources	26.1
o Division of Computer Research and Technology	19.8
o Standard Level User Charges (Rents)	16.2



In 1991, MF obligations totalled $406,910,000. These obligations enabled the MF organizations to provide support services of the highest quality to the medical research programs of the Institutes. During 1991, these services included: completion of the NIH Backbone LAN (32 buildings connected); renovations and improvements to animal care facilities in accordance with the American Association for Accreditation of Laboratory Animal Care (AAALAC) standards; establishment of an in-house pediatric clinical care service; continued clinical support to the NIH AIDS research program; back-up support to the U.S. Navy for Operation Desert Storm; continued development of a modern database system to improve the current grant reporting systems; and continued development of the NIH Revitalization Program to effectively modernize the aging utilities and building infrastructure.

THE WARREN GRANT MAGNUSON CLINICAL CENTER

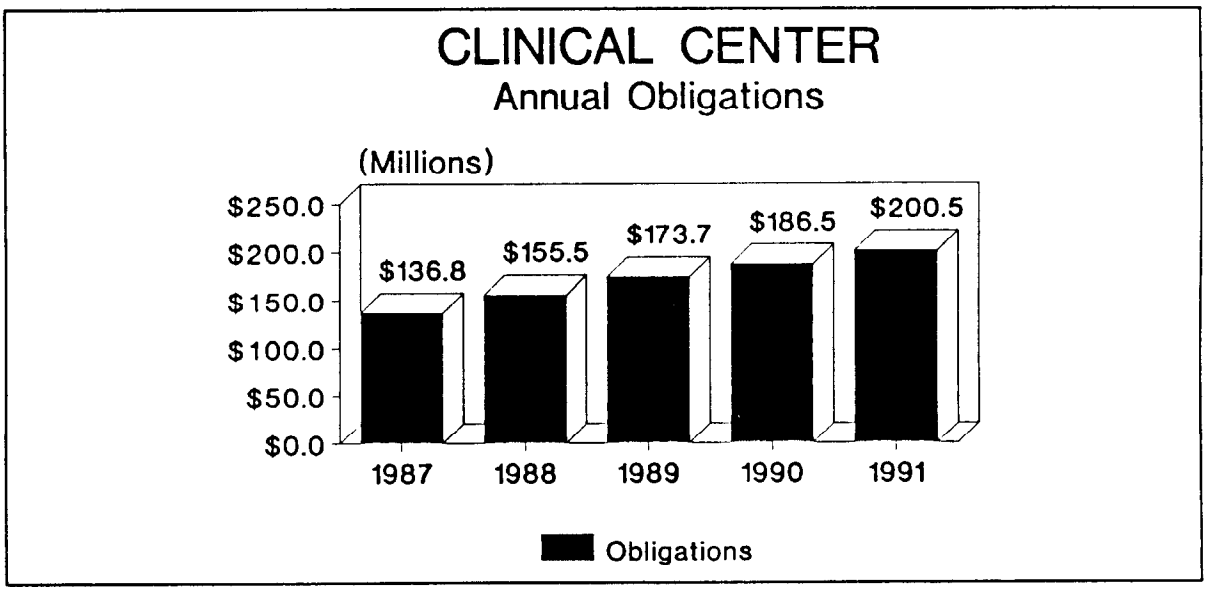
The Clinical Center (CC), built in 1953, is the world's largest hospital devoted exclusively to clinical investigation and other biomedical research. It was specially designed to foster the exchange of information between scientists and clinicians. In FY 1991, scientists in more than 1,200 NIH laboratories worked side by side with clinicians caring for patients and conducted more than 2,700 research projects, which made it one of the largest research sites in the world.

The Center housed 4,500 NIH employees consisting of CC and Institute employees and numerous guest scientists from around the world. The 13-story hospital admitted approximately 9,000 patients and 150,000 visits to the outpatient clinics in FY 1991. Five hundred healthy people are also admitted each year to serve as "normal volunteers." Almost 1,000 physicians and more than 800 registered nurses provide professional care to patients. The Clinical Center is funded by the MF. It is organized into medical and administrative departments that are specially equipped to serve the needs of the NIH Institute's intramural biomedical research programs.

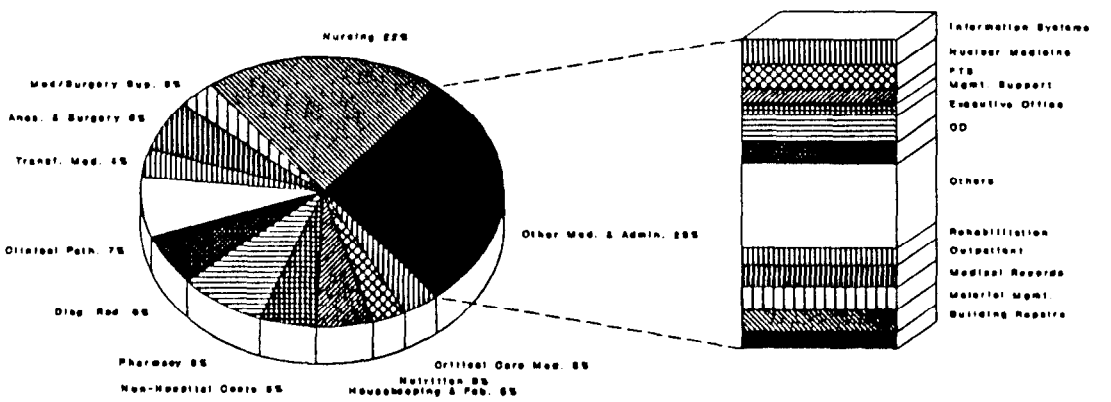
The departments include Diagnostic Radiology, Nuclear Medicine, Clinical Pathology, Transfusion Medicine, Rehabilitation Medicine, Nursing, Pharmacy, Outpatient and Critical Care Medicine. The CC has other departments designed to support the nutritional, social, physical, and spiritual needs of patients. Other units provide administrative support to research service departments.

In FY 1991, the CC accounted for 50 percent of the MF obligations. Over half of the CC services were provided to the National Cancer Institute and the National Heart, Lung and Blood Institute.

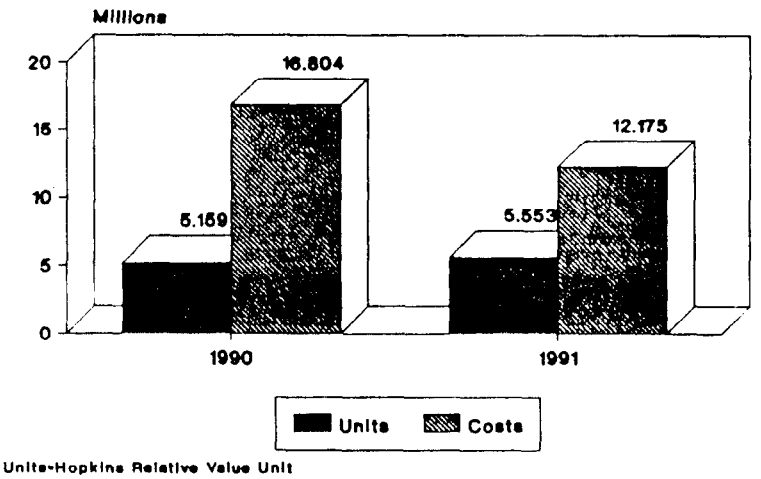
The CC has a computerized Medical Information System (MIS) for physicians and nursing personnel to record medical orders and patient information. This system collects workload units for various medical care and research services. Many of the workload units are based on industry standards, such as the Hopkins Relative Value Unit for Diagnostic Radiology.

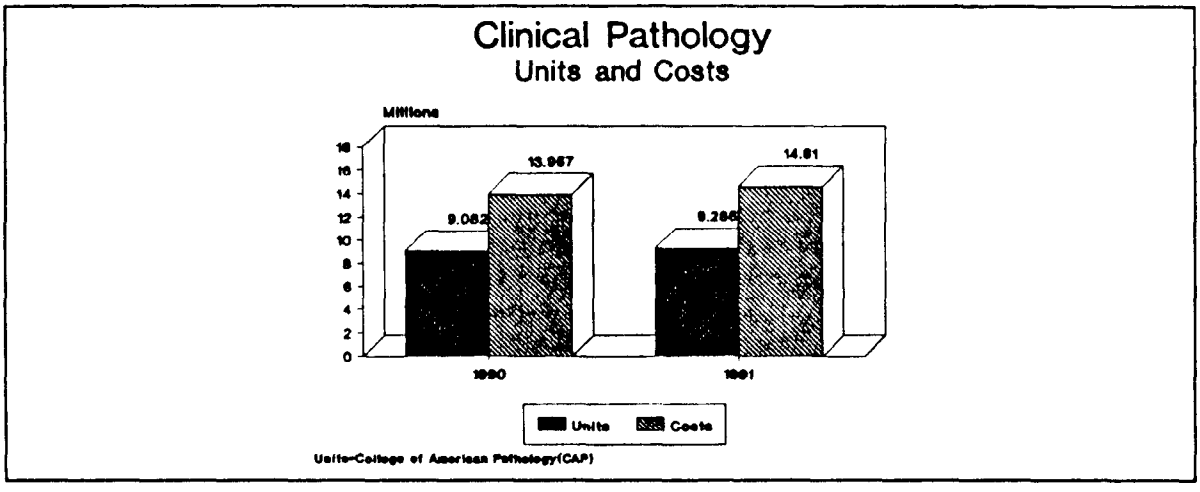


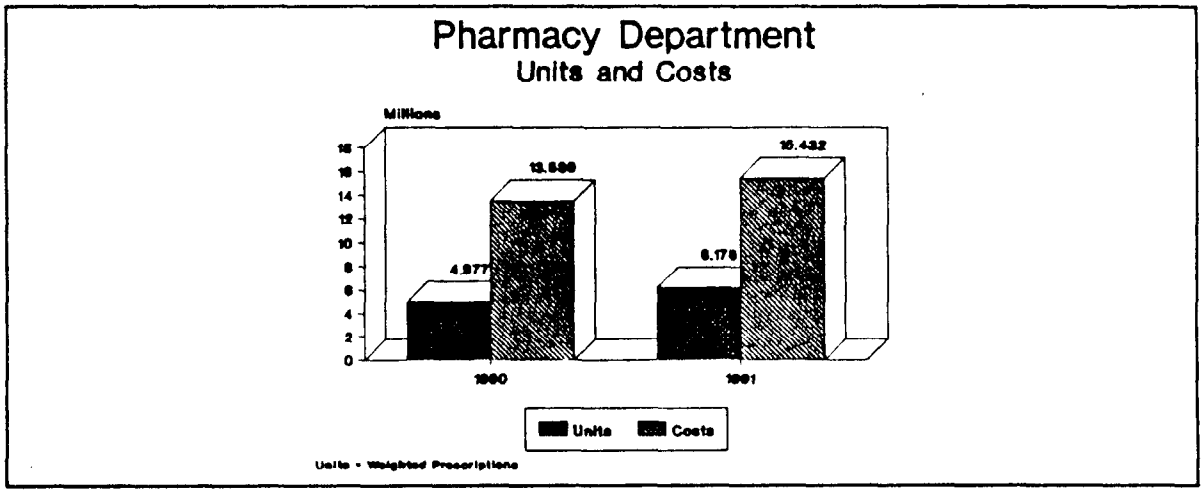
Allocation of Clinical Center Costs
Fiscal Year 1991



Diagnostic Radiology
Units and Costs







The Nursing Department recruited high quality staff in FY 1991. They hired 35% more nurses than in FY 1990. The passage of various public laws under Title 38 helped to resolve the serious nursing recruitment and retention problems. In FY 1991, the Nursing Department responded to Operation Desert Storm by developing a written understanding with the National Naval Medical Center to support their surgical training and patient care programs during the early stages of the war. Subsequently, four CC nurses were sent to Kuwait for six weeks in early April.

In FY 1991, the Pharmacy Department developed a number of pilot projects including an outpatient self-administered, computerized medication history system and a computerized therapeutic drug monitoring system. The Clinical Pathology Department performed fourteen additional commercial tests in-house with cost reductions and quality improvements. A Thrombosis Section was established in the Hematology Service. This Section collaborates with Institute investigators on ways to decrease thrombotic complications of invasive procedures and chemical and biologic therapies.

OFFICE OF RESEARCH SERVICES

The Office of Research Services (ORS) provides advisory services to the Director, NIH, and staff on the management and provision of technical and administrative services to all components of NIH in support of research. It plans and directs service programs for engineering services, safety, space management, and technical services. The ORS is composed of an Office of the Director and five divisions which include the Division of Space Management, Division of Technical Services, Division of Safety, Division of Security Operations, and the Division of Engineering Services. These divisions are funded by the NIH MF or dually funded with the NIH SSF.

The ORS utilized 27 percent of the total MF resources in FY 1991. In meeting the demands of the aging infrastructure, the ORS continued to provide exceptional quality utilities, plant maintenance, safety, and other support services to the NIH community.

Engineering Services

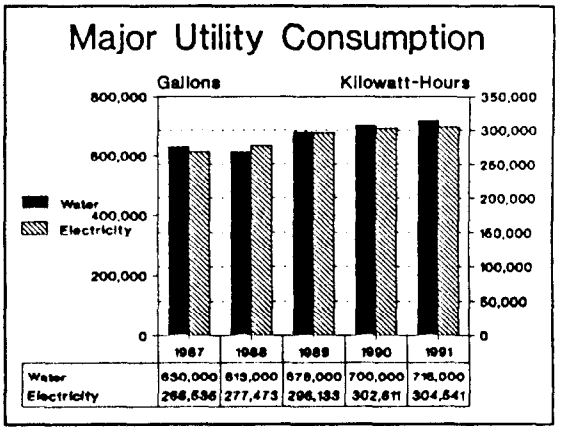
The Division of Engineering Services (DES) provides planning, design, construction, and maintenance and alteration services to the NIH facilities to meet the ever-changing needs of the research community. The division has a staff of over 500 employees which includes more than 80 engineers, architects, and engineering technicians. Engineering specialties include mechanical, electrical, and civil/structural.

In FY 1991, 77% of the DES funding came from the MF while 23% was from the SSF. The DES contributed 8% of the total SSF revenue in FY 1991. The DES provided services through work order requests submitted by the Institutes for alterations and by its own staff for maintenance and repair of the facilities. The average size of the individual work orders has increased in recent years due to extensive repairs caused by a deteriorating building infrastructure and the growth of more urgent and complex alterations to support laboratory research.

The DES initiated several programs in FY 1991 to improve customer satisfaction. At the Division level, they began developing a customer survey that would allow management to determine the level of customer satisfaction with respect to the products and services provided. The Shops Branch developed another mechanism for customer feedback. At the completion of each project, customers rate specific criteria on a numerical scale as well as make additional comments on the services provided.

Utilities and Maintenance

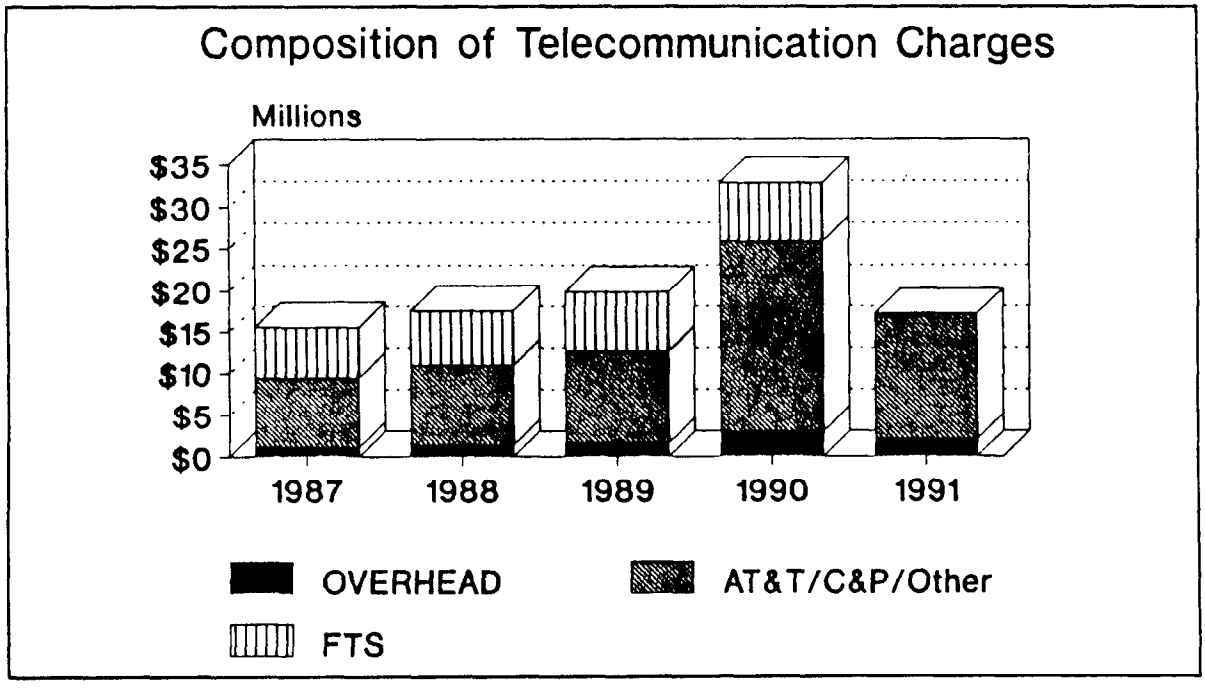
In FY 1991, the ORS obligated $33.7 million for plant maintenance and $26.2 million for utilities. The ORS were provided 304.5 million kilowatt hours of electricity and 716 million gallons of water, representing increases over 1987 of 13% and 14%, respectively. The utilities and maintenance services were funded by the MF. These services were provided in response to an increasingly complex demand from the NIH research programs which continually utilized state-of-the-art technology. These services supported the varied NIH campus facilities which included 7.3 million square feet in FY 1991. Since FY 1987, the ORS has provided utility services to four new buildings encompassing an additional 91.5 thousand square feet.



Telecommunications Services

The Telecommunications Branch (TCB) was funded by the SSF and contributed 8% to the total FY 1991 revenue. The TCB converted the 800 telephone numbers and data communications service to the Federal Telecommunications System (FTS) 2000 in FY 1991. In addition, they moved some of the telecommunication services of the National Institute of Allergy and Infectious Diseases to the Solar Building using new DS-3 technology. This technology uses high speed fiber optic data channels and has provided significant savings to the NIH on a monthly basis. Also, using new technology, the TCB upgraded the cabling and wiring of the Gateway Building so that voice and data operations can be provided more efficiently and expeditiously.

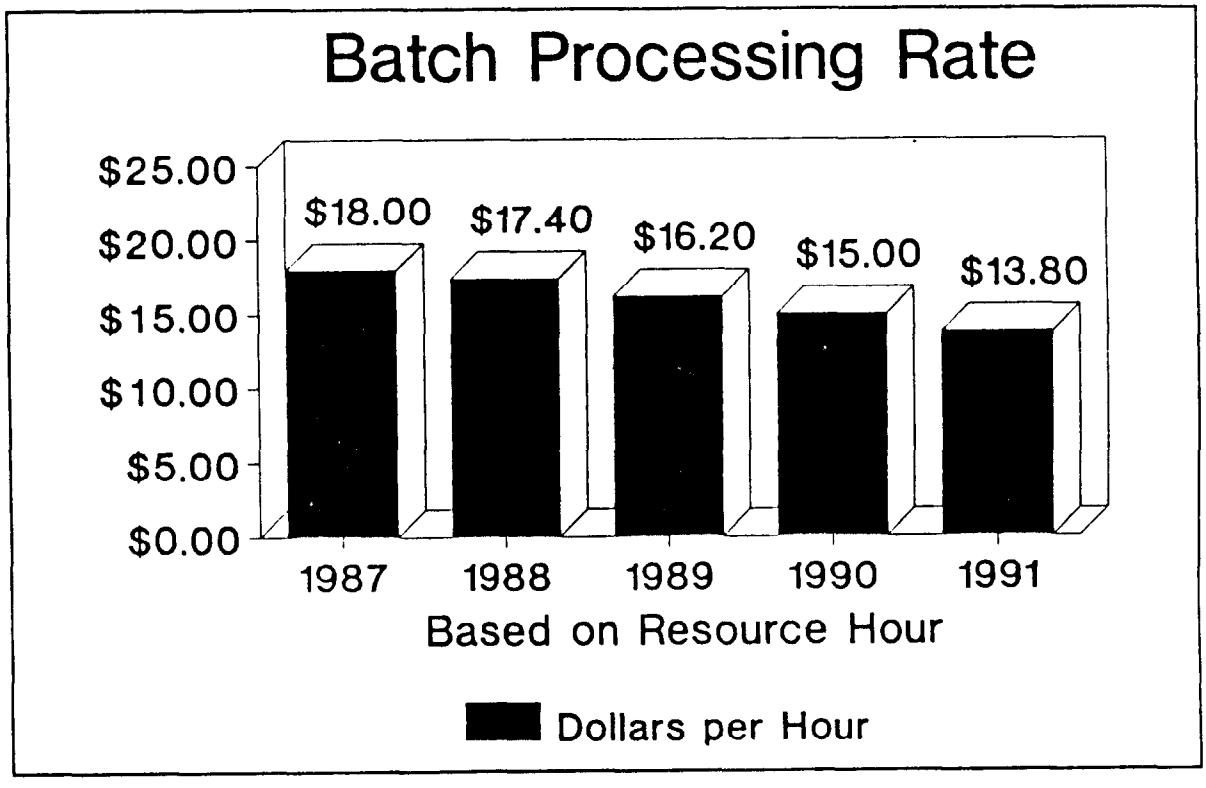
In FY 1991, the TCB revised its billing program to charge the Institutes directly for all C&P, FTS, and smaller vendor bills. This reduced their annual spending authority by $13 million in FY 1991.

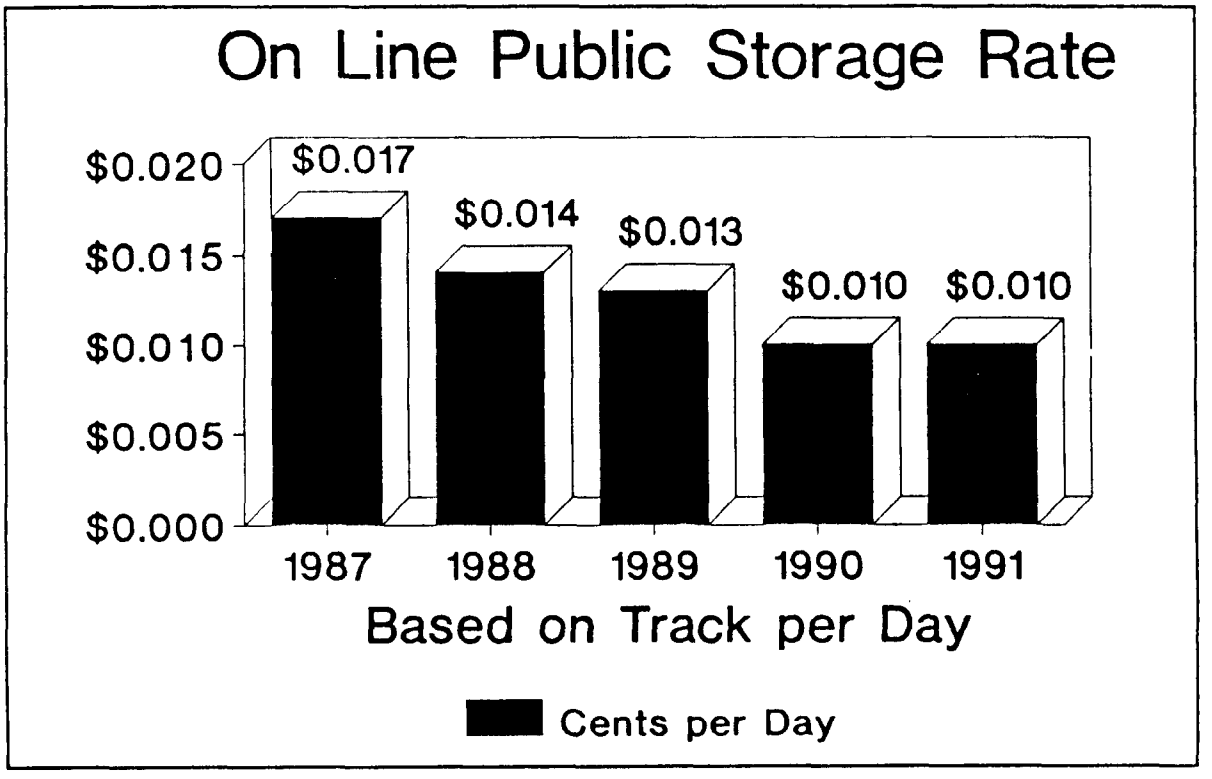


DIVISION OF COMPUTER RESEARCH AND TECHNOLOGY

The Division of Computer Research and Technology (DCRT) was established in 1964 to help incorporate the power of modern computers into the biomedical programs and administrative procedures of the NIH. The DCRT programs focus on three primary activities: conducting research, developing computer systems, and providing computer facilities. This division serves as a scientific and technological resource for other parts of the PHS, and for other Federal components with biomedical and statistical computing needs. DCRT is dually funded by the NIH SSF and the NIH MF.

In FY 1991, 29% of the DCRT funding came from the MF while 71% was from the SSF. The DCRT generated 26% the total FY 1991 SSF revenue and provided the NIH with an outstanding data processing facility. The NIH Computer Utility operated 24 hours a day, 7 days a week. It processed an average of 11,438 interactive sessions, 87,421 database transactions, and 18,000 batch jobs daily. Over 90% of all interactive commands were executed with subsecond response time, and six service classes for batch jobs provided turnaround times of from less than 30 minutes to overnight processing (at a discount).





Performance upgrades to equipment during the recent past, which resulted in DCRT's ability to relocate one of its mainframe machines, allowed the DCRT to provide improved service while reducing costs and rates. Rates for service continued to fall for the 23rd year with a reduction of 8% in the batch processing rate in 1991. The data storage rate was likewise reduced by 23% in 1991.

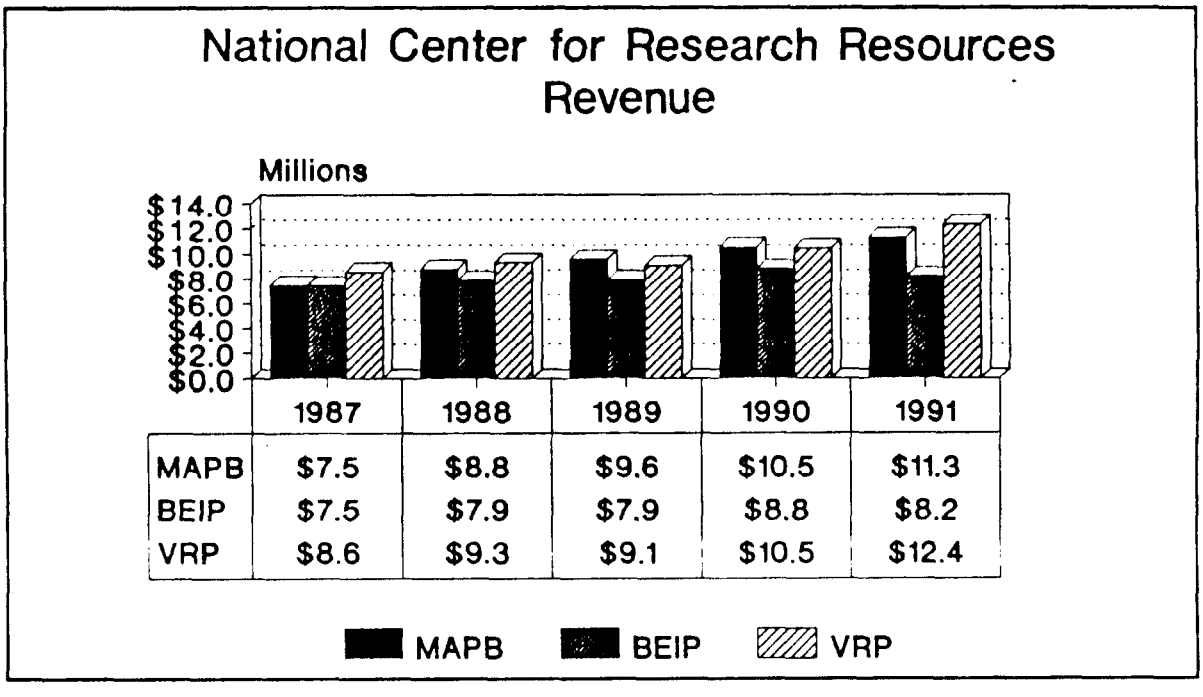
A major focus for the DCRT during the past several years has been the development and implementation of a NIH-wide backbone local area network, called NUnet. In 1990 and 1991, this network was expanded to provide interconnectivity among local area networks in all NIH buildings, both on and off campus, the Computer Center, and international data networks such as Internet and BITNET. Using the mainframe computers as a large 'server,' the DCRT staff developed a mail gateway which allows differing electronic mail systems to communicate with each other. The mail gateway now processes more than 9,000 messages a day. The DCRT staff is continuing to maintain and expand this major innovation in communications at the NIH.

NATIONAL CENTER FOR RESEARCH RESOURCES

The National Center for Research Resources (NCRR) was established on February 15, 1990. The NCRR was a merger of the Division of Research Resources (DRR), which provided extramural research resource to NIH-supported institutions, and the Division of Research Services (DRS), which provided resources to the intramural research programs of NIH. Research resources provided to the NIH intramural research programs include: biomedical engineering and instrumentation collaboration and services, professional and technical support services related to the care and use of laboratory animals, scientific library and translation services, and medical arts and photography.

The extramural portion of the NCRR is funded by direct appropriation. The intramural portion of the NCRR is funded by both the SSF and the MF. In FY 1991, the NCRR received 56% of their intramural funding from the SSF and 44% from the MF. The NCRR generated approximately 15% of the total SSF revenue in FY 1991. The NCRR consists of three areas under the SSF: Veterinary Resources Program (VRP); Biomedical Engineering and Instrumentation Program (BEIP); and the Medical Arts and Photography Branch (MAPB).

In FY 1991, the VRP developed plans to provide centralized rodent quarantine and isolation services and a NIH-wide animal health surveillance and diagnostic program. In addition, the BEIP increased the usage of fixed-fee, full service equipment maintenance contracts at rates lower than commercial sources. Also, the MAPB developed public information materials on issues such as women's health research, AIDs research and prevention, mammography screening, better eating habits, as well as a continued campaign against teenage smoking.

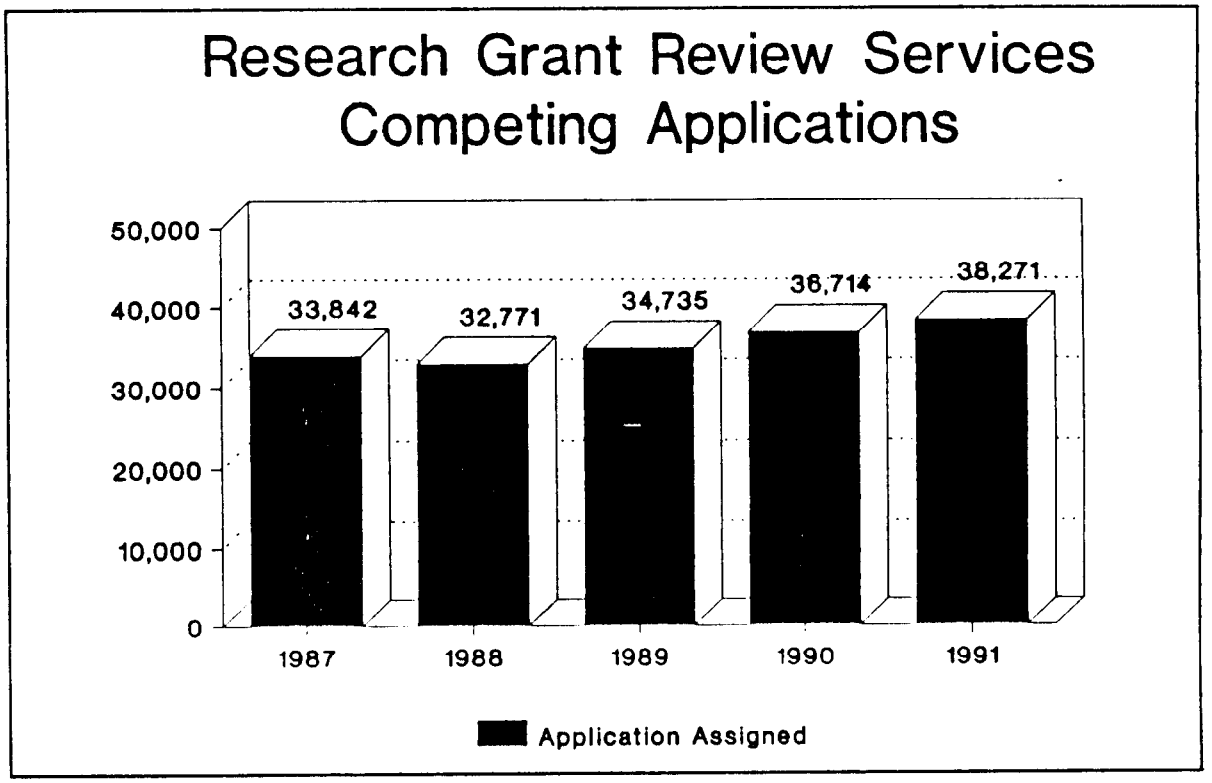


	1987	1988	1989	1990	1991
MAPB	$7.5	$8.8	$9.6	$10.5	$11.3
BEIP	$7.5	$7.9	$7.9	$8.8	$8.2
VRP	$8.6	$9.3	$9.1	$10.5	$12.4

DIVISION OF RESEARCH GRANTS

The Division of Research Grants (DRG) is funded by the MF. In FY 1991, the DRG accounted for 8% of the total MF resources. The DRG continues to provide superior quality grant review and referral services to the NIH research grant programs as well as to the research grant programs of other agencies within the Public Health Service (PHS). For FY 1991, the DRG obligated $34.4 million and utilized 447 FTEs, representing increases over 1987 of 52% and 14%, respectively. The total number of PHS competing research grant applications assigned by the DRG increased to 38,271 in FY 1991, a 4% increase over FY 1990.

The DRG continued to develop and implement several initiatives designed to enhance the services it provides to the NIH and PHS communities. The expedited review of AIDS research grant and fellowship applications has been advanced by the recruitment of specialized staff. Additional study sections have been established, either by splitting existing study sections or by creating new ones. The DRG has also undertaken an extensive restructuring of its automated systems, including the design of the new grant tracking and reporting system, the upgrading of computer equipment for the study sections, and the continued development and evaluation of the computer system for the electronic submission and receipt of grant applications.

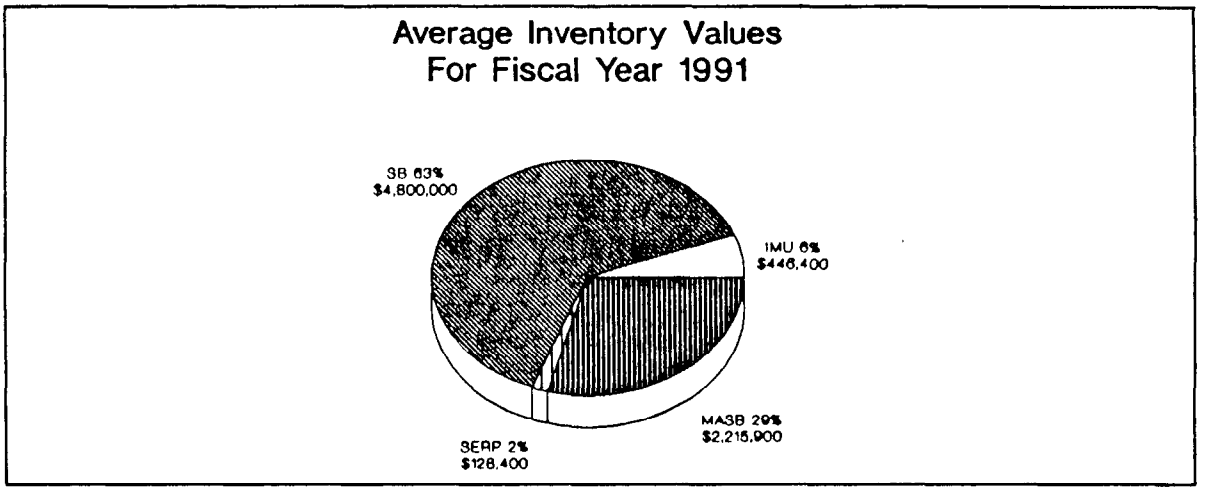


SSF INVENTORIES

In FY 1991, the SSF included four inventories. Sales of inventory stock accounted for 18% of the total SSF sales in FY 1991. The total value of the inventory purchased and issued in FY 1991 was $30.2 and $30.4 million, respectively. The Supply Branch availability rate for FY 1990/FY 1991 was 97%.

The inventories are composed primarily of:

1) administrative, laboratory, and office supplies;
2) construction material;
3) fabrication material; and
4) scientific equipment.



The Supply Branch (SB) and the Materials Acquisition/Supply Branch (MASB) are the largest inventory areas accounting for 95% of the total inventory sales. The other two areas are the Inventory Management Unit (IMU) and the Scientific Equipment Resources Program (SERP). The FY 1991 inventory turnover ratios are as follows:

Inventory Turnover

Inventory Area	Turnover Ratio
Supply Branch	3.8
Materials Acquisition/ Supply Branch	1.4
Inventory Management Unit	1.6
Scientific Equipment Resources Program	2.9

FEDERAL MANAGERS' FINANCIAL INTEGRITY ACT

The Federal Managers' Financial Integrity Act (FMFIA) of 1982 requires all federal agencies to have financial and other systems to ensure that the internal control objectives of the Act are met.

A limited FMFIA (Section 4) review of the NIH Central Accounting System was conducted in FY 1991. No material weaknesses, material nonconformances, or corrective actions were identified.

During FY 1991, the NIH staff worked within written corrective action plans (CAP) to correct 7 FMFIA (Section 2) material weaknesses, completing 2. Those weaknesses involved Animal Care, Small Purchases, Foundations, (Nonexpendable) Property, Computer Capacity Planning and Management, Program Income, and ADP Security.

The NIH Animal Care and Use Program was declared a material weakness in 1986 because it failed to achieve full accreditation by the American Association for Accreditation of Laboratory Animal Care (AAALAC). To achieve accreditation a series of facility construction projects were undertaken. Application for accreditation was made to the AAALAC on December 31, 1990, but a site visit was not made until late 1991. Provisional AAALAC accreditation up to 24 months duration is anticipated.

The NIH supports its intramural research programs and related activities through a three-pronged small purchasing system that includes the DELPRO (short for delegated procurement) purchasing system, the central Division of Procurement, and various "decentralized" purchasing offices. Deficiencies in the NIH DELPRO small purchases procurement system were identified in a 1988 Office of Inspector General report. The numerous action items in this CAP have either been completed, are in the process of completion, or have become new, ongoing processes.

A material weakness was declared in FY 1990 because the NIH lacked a policy regarding its employees' relationship with foundations. Progress to correct this weakness is continuing.

The NIH's property management system was identified as a material weakness in FY 1990. The CAP for this weakness included the development of a new automated Property Management Information System; increased management awareness of personal property management objectives; strengthened personal property policies and procedures; and a complete wall-to-wall physical inventory of accountable personal property. Completion of the CAP is anticipated in FY 1993.

A material weakness in capacity planning, management and oversight of the central computing facilities in the Division of Computer Research and Technology (DCRT) was declared. The primary result of the weakness was that mainframe capacity planning permitted an overcapacity of computing equipment to be acquired during the 1988-1990 period. Progress is being made to correct this weakness.

Two CAPs for material weaknesses were completed during FY 1991. The material weaknesses concerned the identification and disposition of program income from grant recipients and the other concerned security and contingency planning for applications computer programs.

NATIONAL INSTITUTES OF HEALTH

FINANCIAL STATEMENTS

SERVICE AND SUPPLY FUND
AND
MANAGEMENT FUND

FISCAL YEAR 1991

6/23/92

NATIONAL INSTITUTES OF HEALTH
SERVICE AND SUPPLY FUND

FINANCIAL STATEMENTS
September 30, 1991 and 1990

INDEX TO FINANCIAL STATEMENTS
NIH SERVICE AND SUPPLY FUND

National Institutes of Health
Service and Supply Fund
STATEMENT OF FINANCIAL POSITION
As of September 30, 1991 and 1990

(Dollars in Thousands)

	1991	1990
ASSETS		
Cash and Other Financial Resources		
Fund Balances with Treasury (Note 2)	$17,677	$20,515
Accounts Receivable - Non-Federal (Note 3)	120	95
Inventories Held for Sale (Note 4)	8,078	7,377
Advances and Prepayments - Non-Federal	33	15
Intragovernmental Items:		
Accounts Receivable - Federal	12,278	13,086
Other - Federal (Note 5)	2,261	1,626
Total Cash and other Financial Resources	$40,447	$42,714
Non-Financial Resources		
Property, Plant and Equipment, Net (Note 6)	13,798	9,698
Total Non-Financial Resources	$13,798	$9,698
Total Assets	$54,245	$52,412
LIABILITIES		
Funded Liabilities		
Accounts Payable - Non-Federal	$13,298	$13,065
Accrued Payroll and Benefits	3,483	2,947
Advances and Unearned Revenue, Non-Fed.	25	32
Other Funded Liabilities, Non-Federal (Note 7)	7,593	10,318
Intragovernmental Liabilities:		
Payables -Federal	3,220	2,463
Other -Federal (Note 7)	2,569	1,464
Total Funded Liabilities	$30,188	$30,289
Unfunded Liabilities		
Accrued Unfunded Leave (Note 8)	$2,880	$2,750
Total Unfunded Liabilities	$2,880	$2,750
Total Liabilities	$33,068	$33,039
NET POSITION		
Fund Account Balances		
Appropriated Fund Balances (Note 9)	$269	$269
Revolving Fund Balances (Note 9)	20,908	19,104
Total Fund Account Balances	$21,177	$19,373
Total Net Position	$21,177	$19,373
Total Liabilities and Net Position	$54,245	$52,412

The accompanying notes are an integral part of these statements.

National Institutes of Health
Service and Supply Fund
STATEMENT OF OPERATIONS
For the Period Ended September 30, 1991 and 1990

	(Dollars in Thousands) 1991	1990
REVENUE AND FINANCING SOURCES		
Revenue from Sales of Goods and Services to the Public	$312	$305
Intragovernmental Revenue:		
Reimbursements	197,075	202,388
Other Revenue and Fin. Sources:		
Donated for Travel Expenses	4	8
Total Revenues and Financing Sources	$197,391	$202,701
EXPENSES		
Cost of Goods Sold	$33,864	$31,278
Program/Operating Expenses (Note 10)	159,834	164,939
Interest Penalty	2	2
Depreciation	1,664	1,671
Other Expenses:		
Amortization	70	100
Accrued Leave Earned	190	89
Total Expenses	$195,624	$198,079
EXCESS OF FINANCIAL SOURCES OVER EXPENSES	$1,767	$4,622
Add Net Position, Beginning Balance	19,373	10,749
Plus Transfers & Other Adjustments (Note 11)	37	4,002
Net Position, Ending Balance	$21,177	$19,373

Excludes intrafund sales and expenses.

The accompanying notes are an integral part of these statements.

National Institutes of Health
Service and Supply Fund
STATEMENT OF CASH FLOWS
For the Period Ended September 30, 1991 and 1990
(Dollars in Thousands)

	1991	1990
CASH PROVIDED (USED) BY OPERATING ACTIVITIES		
Cash Provided		
Services Provided	$218,849	$219,396
Other Operating Cash Provided:		
Indemnity Refund	0	1
Total Cash Provided	$218,849	$219,397
Cash Used		
Goods and Services	$33,830	$28,885
Personnel Services and Benefits	45,579	41,654
Travel and Transportation	1,158	(2)
Rent Communications and Utilities	58,554	60,923
Printing and Reproduction	2,020	1,780
Other Contractual Services	61,961	61,336
Supplies and Materials	8,355	7,487
Insurance Claims and Indemnities	2	2
Other Operating Cash Used:		
Non-capitalized equipment purchases	1,401	1,376
Interest penalty	2	0
Advances issued	1,381	891
Payment of prior period expense	1,219	7
Total Net Used	$215,462	$204,339
Net Cash Provided (Used) by Operating Activities	$3,387	$15,058
CASH PROVIDED (USED) BY INVESTING ACTIVITIES		
Purchase of Property, Plant and Equipment	($6,225)	($5,433)
Net Cash Provided (Used) by Investing Activities	($6,225)	($5,433)
Cash Balance, Beginning of Period	$20,515	$10,890
Net Change in Cash	(2,838)	9,625
Cash Balance, End of Period	$17,677	$20,515

The accompanying notes are an integral part of these statements

National Institutes of Health
Service and Supply Fund
STATEMENT OF RECONCILIATION TO BUDGET
For the Period Ended September 30, 1991 and 1990

(Dollars in Thousands)

	1991	1990
Total Expenses (Note 12)	$217,256	$211,254
Add Adjustments for:		
Purchases of Inventory	37,176	32,805
Purchases of Property, Plant and Equipment	6,116	5,766
Total Adjustments Added	$43,292	$38,571
Less Adjustments for:		
Cost of Goods Sold	$33,866	$31,280
Depreciation	1,664	1,671
Other Unfunded Expenses:		
Accrued Leave Earned	190	89
Total Adjustments Deducted	$35,720	$33,040
Expended Appropriations	$224,828	$216,785
Less Reimbursements and Other Income	219,867	222,668
Expended Appropriations, Direct	$4,961	($5,883)
Less Change in Accounts Payable, Net	2,124	3,743
Budgetary Outlays	$2,837	($9,626)
Obligations Incurred, Net	$0	$0
Less Change in Unpaid Obligations, Net	(2,837)	9,626
Budgetary Outlays	$2,837	($9,626)

The accompanying notes are an integral part of these statements.

NATIONAL INSTITUTES OF HEALTH
SERVICE AND SUPPLY FUND
NOTES TO FINANCIAL STATEMENTS
September 30, 1991 and 1990

Note 1. Significant Accounting Policies

Reporting Entity:

The National Institutes of Health (NIH) is an agency of the Department of Health and Human Services (DHHS), which is a Department of the United States Government. The NIH is the Federal focal point for health research.

The accompanying financial statements present the financial activity of the NIH's Service and Supply Fund (SSF). The NIH SSF financial statements are prepared in conformity with generally accepted accounting principles for Federal Agencies - Title 2 of the General Accounting Office's (GAO) Policy and Procedures Manual. The DHHS has adopted the GAO's Title 2 for its audited financial statements. The NIH SSF is an Internal Service Fund that was established on July 3, 1945 under 42 U.S.C. 231. This fund finances a variety of centralized research support and administrative activities required for the efficient and effective operation of numerous NIH programs and facilities.

The SSF provides a mechanism for consolidating the financing and accounting of business-type operations involving the sales of services and commodities to customers. The majority of these services can be identified to specific customers; therefore, their costs are charged to the recipient appropriations on a fee-for-service basis.

Fee-for-Service Basis:

The SSF provides a single means for consolidating the financing and accounting for business-type operations involving the sale of services and commodities to customers. The customers are directly charged for the services/goods provided at the established unit rate.

Note 1. Significant Accounting Policies (continued)

Cost Recovery Process:

Each fiscal year, the Central Services Activities' managers present budget requests to the Central Service Review Committee for approval. This Committee is chaired by the Associate Director for Administration. Members of the Committee include selected Institute officials representing the scientific and administrative communities. Based on the approved NIH SSF budget, annual cost based operating budgets are prepared for each SSF activity which include the work units to be produced by the activity for their customers. The budgets are submitted to the Division of Financial Management for review, cost analyses, unit rate development, and approval. The approved budgets become the basis for measuring performance throughout the FY. Unit rates are published annually and reviewed periodically throughout the FY. If an activity varies significantly from its proposed budget, rate adjustments and/or rebates may be necessary.

Recognition of Revenue and Expenses:

The SSF operates on the accrual basis of accounting which recognizes financial transactions, events, or allocations as they are incurred. Revenue is recognized when earned and expenses are recognized when incurred, without regard to time of cash receipt or payment.

Inventories:

Inventories are valued at the lower of cost or market. Cost is determined by using the weighted average method. There are four areas that maintain inventories: the Supply Branch; the Materials Acquisition and Supply Branch; the Inventory Management Unit; and the Scientific Equipment Resources Program.

Annual, Sick and Other Leave:

The Personnel and Pay Systems, Office of Human Resources Information and Management, DHHS provides the amount of leave accruals on the payroll tapes. Annual leave is accrued as earned and reduced as taken. Sick and other types of leave are expended as taken but not accrued when earned.

Note 1. Significant Accounting Policies (continued)

Retirement Benefits:

All permanent employees participate in the contributory Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS) which became effective January 1, 1987. Temporary employees and employees participating in FERS are covered under the Federal Insurance Contributions Act (FICA). The NIH makes matching contributions to the CSRS, FERS, and FICA and matches employee contributions to the savings components of FERS up to five percent of basic pay but has no liability for future payments to employees under these programs. The NIH's costs associated with its employee retirement programs during fiscal years 1991 and 1990 amounted to approximately $2,895,000 and $2,532,000, respectively.

Land, Buildings and Equipment:

The land and many of the NIH buildings were donated to the NIH. These fixed assets are accounted for in the NIH Buildings and Facilities appropriation. However, renovations to areas occupied by a SSF activity are accounted for in the SSF appropriation. Equipment is capitalized if the initial acquisition cost is five thousand dollars or more and its useful life exceeds one year. Depreciation is recorded using the straight-line method.

Note 2. Fund Balances with Treasury:

Treasury Account Symbols	(Dollars in Thousands) Fund Balances FY 1991	FY 1990
75 X 4554	$ 17,677	$ 20,515

The NIH does not maintain cash in commercial bank accounts. Rather, its receipts and disbursements are processed by the U.S. Treasury. The balance of funds with the U.S. Treasury represents funds that are available to pay current liabilities and finance authorized purchase commitments relative to goods or services which have not been received.

Note 3. Receivables:

	(Dollars in Thousands) 1991	1990
Accounts and interest receivable - public:		
Current	$ 90	$ 95
Non-Current	30	
	$ 120	$ 95
Accounts receivable - federal	12,278	13,086
Total accounts and interest receivable	$12,398	$13,181

The NIH SSF does not currently record an allowance for bad debts because the majority of the customers are federal agencies. In addition, based on prior years' history of write-offs, there is no need to record an allowance.

Note 4. Inventory

	(Dollars in Thousands) FY 1991			1990
	Inventory Amount	Allowance for Losses	Inventory Net	Inventory Net
Goods held for sale	$ 8,078	$ 0	$ 8,078	$7,377

The inventory balance was composed of:

	(Dollars in Thousands) 1991	1990
Supply Branch:		
Administrative, laboratory and office supplies	$ 5,332	$ 4,677
Materials Acquisition and Supply Branch:		
Construction material	2,165	2,267
Biomedical Engineering and Instrumentation Program:		
Fabrication material	460	433
Scientific Equipment Resources Program:		
Scientific equipment	121	0
Total	$ 8,078	$ 7,377

Note 4. Inventory (continued)

The weighted average costing method is used by all inventory sections. There were no restrictions on inventory use, sale or disposition.

The inventory accounts were adjusted downward by $1,501,000 and $1,120,000 in FY 1991 and 1990, respectively. These adjustments were necessary to adjust the General Ledger balances to the subsidiary ledgers. An allowance account is not currently used to estimate future losses. Inventory losses are minimal and are expended when incurred.

Note 5. Other Assets - Financial Resources

	(Dollars in Thousands			
	Federal	Non-Federal	Total 1991	Total 1990
Travel advances and emergency salary payments	$	$ 45	$ 45	$ 54
Advances to federal agencies	492		492	369
Deferred charges	1,724		1,724	1,203
Total other assets - financial resources	$2,216	$ 45	$2,261	$1,626

Note 5. Other Assets - Financial Resources (continued)

The deferred charges represent the charges accumulated for the development of the Service and Supply Fund Activity System (SSFAS) and the Travel Voucher System (TVS). The total costs associated with the SSFAS was $1,467,000 while the TVS accumulated costs were $257,000. An estimated completion date for these systems is not available at this time.

Note 6. Property, Plant and Equipment

	(Dollars in Thousands)			
			Net Book Value	
	Depr. Method	Life	1991	1990
Equipment	Straight Line	1-10 years	$ 13,655	$ 9,485
Development Costs			143	213
Totals			$ 13,798	$ 9,698

The cost of equipment was $24,632,000 with accumulated depreciation of $10,977,000 as of September 30, 1991. A comprehensive physical inventory of the NIH personal property was conducted in FY 1991. The property account balance has not been adjusted to reflect the results of this inventory. A Board of Inquiry will be convened to authorize appropriate changes. These changes will be reported in FY 1992. The FY 1991 depreciation expense was $1,664,000. However, the majority of the depreciation expense for FY 1991 was estimated. March through September depreciation expense was based on February's actual. This was necessary due to the comprehensive physical inventory process and the transition to the new Property Management Information System.

The development costs represent the unamortized portion of the Travel Order System. This system was completed in FY 1990. The amortization expense in FY 1991 and FY 1990 was $70,000 and $100,000, respectively.

Note 7. Other Funded Liabilities

	(Dollars in Thousands)					
	1991			1990		
	Non-Federal	Federal	Total	Federal	Non-Federal	Total
Accrued liabilities	$2,569	$7,593	$10,162	$1,464	$10,318	$11,782

The accrued liabilities - non-federal agencies does not include accruals for payroll, benefits and benefit entitlements.

Note 8. Accrued Unfunded Leave Liability

The liability for accumulated annual leave and compensatory leave has been incurred and is payable to civilians and commissioned officers.

Note 9. Net Position

Net position consists of:

	(Dollars in Thousands) 1991	1990
Invested capital:		
Appropriated funds	$ 269	$ 269
Property transferred	5,412	5,398
Cumulative results of operations	15,496	13,706
Net position	$ 21,177	$ 19,373

The cumulative results of operations contains $16,415,000 of profits from the Division of Computer Research and Technology (DCRT) operations. The DCRT is on a multi-year breakeven budget cycle as opposed to a one-year cycle. This policy was adopted by the DCRT management due to a long-term total systems contract. The multi-year cycle was intended to prevent large rate variations to the DCRT customers. This retained amount was intended to offset future losses anticipated in the multi-year budget. This and other policies concerning this contract are currently under review.

Note 10. Program/Operating

	(Dollars in Thousands) 1991	1990
Operating Expenses by Object Classification:		
Personal services and benefits	$ 46,071	$ 41,935
Travel and transportation	1,498	841
Rental, communications and utilities	57,372	63,595
Printing and reproduction	2,969	2,663
Contractual services	41,003	50,555
Supplies, materials and low cost equipment	9,185	4,171
Other: non-capitalized equipment	1,736	1,179
Total expenses by object classification	$159,834	$164,939

Note 10. Program/Operating (continued)

	(Dollars in Thousands) 1991	1990
Operating Expenses by Program:		
Division of Computer Research and Technology	$ 48,045	$ 44,772
Division of Procurement	8,474	7,243
Division of Logistics	13,728	10,381
Division of Technical Services	26,205	42,208
Division of Engineering Services	12,450	12,199
Division of Safety	2,101	2,061
National Center for Research Resources	25,467	24,399
Division of Personnel Management	1,404	1,085
Division of Financial Management	3,316	2,426
Office of Technology Transfer	1,597	936
General Expense	12,679	13,098
Postal	4,368	4,131
Total expenses by program/ activity	$159,834	$164,939

Note 11. Adjustments to Net Position

	(Dollars in Thousands) (1991)	(1990)
Increases to net position	$ 37	$ 4,002

The increases to the net position are a result of transactions recorded during the year-end closing process. These transactions affected the retained earnings accounts, which we believe should not have occurred, and we are currently reviewing their appropriateness.

Note 12. Statement of Reconciliation to Budget

The total expenses on the Statement of Reconciliation to Budget does not agree with the expenses on the Statement of Operations. The difference is the result of intrafund transactions. An adjustment to this statement would not reflect a proper reconciliation to the Treasury Reports.

6/22/92

NATIONAL INSTITUTES OF HEALTH
MANAGEMENT FUND

FINANCIAL STATEMENTS
September 30, 1991 and 1990

INDEX TO FINANCIAL STATEMENTS
NIH MANAGEMENT FUND

National Institutes of Health
Management Fund
STATEMENT OF FINANCIAL POSITION
As of September 30, 1991 and 1990

	(Dollars in Thousands) 1991	1990
ASSETS		
Cash and Other Financial Resources		
Fund Balances with Treasury (Note 2)	$122,846	$111,415
Accounts and Interest Receivable, Net, Non-Federal (Note 3)	26	18
Advances and Prepayments - Non-Federal	848	198
Intragovernmental Items:		
Accounts Receivable - Federal	544	407
Advances to Federal Agencies (Note 5)	876	725
Total Cash and Other Financial Resources	$125,140	$112,763
Non-Financial Resources		
Inventories Not Held for Sale, Net (Note 4)	$3,562	$3,928
Property, Plant and Equipment (Note 6)	53,860	0
Fixed Assets	3,819	3,819
Total Non-Financial Resources	$61,241	$7,747
Total Assets	$186,381	$120,510
LIABILITIES		
Funded Liabilities		
Accounts Payable - Non-Federal	$17,179	$15,438
Accrued Payroll and Benefits	9,043	7,861
Accrued Benefit Entitlements	4,670	3,727
Other Funded Liabilities, Non-Federal (Note 7)	4,201	3,107
Intragovernmental Liabilities:		
Payables -Federal	2,964	3,943
Other -Federal (Note 7)	87,084	93,783
Total Funded Liabilities	$125,141	$127,859
Unfunded Liabilities		
Accrued Unfunded Leave (Note 6)	$8,194	$7,592
Total Unfunded Liabilities	$8,194	$7,592
Total Liabilities	$133,335	$135,451
NET POSITION		
Fund Account Balances		
Revolving Fund Balances	53,046	(14,941)
Total Fund Account Balances	$53,046	($14,941)
Net Position (Note 9)	$53,046	($14,941)
Total Liabilities and Net Position	$186,381	$120,510

The accompanying notes are an integral part of these statements.

National Institutes of Health
Management Fund
STATEMENT OF OPERATIONS
For the Period Ended September 30, 1991 and 1990

	(Dollars in Thousands) 1991	1990
REVENUE AND FINANCING SOURCES		
Intragovernmental Revenue:		
Reimbursements	$400,389	$360,507
Other Revenue and Financial Sources:		
Income Donated for Travel Expenses	71	88
Total Revenues and Financing Sources	$400,460	$360,595
EXPENSES		
Program/Operating Expenses (Note 10)	$383,383	$348,676
Interest Penalty	3	5
Other Expenses:		
Purchase of Capital Equipment	17,340	11,234
Unfunded Accrued Leave	217	142
Total Expenses	$400,943	$360,057
EXCESS OF FINANCING SOURCES OVER EXPENSES		
Before Prior Period Adjustments	($484)	$538
Prior Period Adjustments (Note 11)	308	92
Excess of Financing Sources Over Expenses	($176)	$630
Add Net Position, Beginning Balance	($14,941)	($17,133)
Plus (Minus) Transfers & Other Adjustments (Note 12)	68,163	1,562
Net Position, Ending Balance	$53,046	($14,941)

The accompanying notes are an integral part of these statements.

National Institutes of Health
Management Fund
STATEMENT OF CASH FLOWS
For the Period Ended September 30, 1991 and 1990

	(Dollars in Thousands) 1991	1990
CASH PROVIDED (USED) BY OPERATING ACTIVITIES		
Cash Provided		
Other Operating Cash Provided:		
Reimbursements	$408,492	$382,477
Total Cash Provided	$408,492	$382,477
Cash Used		
Personnel Services and Benefits	$166,974	$154,244
Travel and Transportation	1,916	1,863
Rent, Communications and Utilities	39,957	38,931
Printing and Reproduction	2,596	2,799
Other Contractual Services	115,762	103,165
Supplies and Materials	33,941	33,072
Insurance Claims and Indemnities	9	3
Other Operating Cash Used:		
Purchase of Non-Capitalized Assets	3,229	2,354
Land and Structures	120	5
Interest and Penalties	3	5
Advances including Travel Advances	12,517	8,937
Total Cash Used	$377,024	$345,378
Net Cash Provided (Used) by Operating Activities	$31,468	$37,099
CASH PROVIDED (USED) BY INVESTING ACTIVITIES		
Purchase of Property, Plant and Equipment	($18,384)	($10,951)
Net Cash Provided (Used) by Investing Activities	($18,384)	($10,951)
CASH PROVIDED (USED) BY FINANCING ACTIVITIES		
Funds Returned to Treasury	(1,654)	(3,498)
Net Cash Provided (Used) by Financing Activities	(1,654)	(3,498)
Cash Balance, Beginning of Period	$111,415	$88,766
Net Change in Cash	$11,431	$22,649
Cash Balance, End of Period	$122,846	$111,415

The accompanying notes are an integral part of these statements.

National Institutes of Health
Management Fund
STATEMENT OF RECONCILIATION TO BUDGET
For the Period Ended September 30, 1991 and 1990

(Dollars in Thousands)

	1991	1990
Total Expenses	$400,899	$360,057
Add Adjustments for:		
Purchases of Inventory	6,814	5,689
Total Adjustments Added	$6,814	$5,689
Less Adjustments for:		
Inventory Consumed	$9,699	$9,241
Accrued Annual Leave	217	142
Total Adjustments Deducted	$9,916	$9,383
Expended Appropriations	$397,797	$356,363
Less Reimbursements and Other Income	400,237	359,861
Expended Appropriations, Direct	($2,440)	($3,498)
Less Change in Accounts Payable, Net	10,645	22,649
Budgetary Outlays	($13,085)	($26,147)
Obligations Incurred, Net	($837)	($3,498)
Less Change in Unpaid Obligations, Net	12,248	22,649
Budgetary Outlays	($13,085)	($26,147)

The accompanying notes are an integral part of the statements.

NATIONAL INSTITUTES OF HEALTH
MANAGEMENT FUND
NOTES TO FINANCIAL STATEMENTS
September 30, 1991 and 1990

Note 1. Significant Accounting Policies

Reporting Entity:

The National Institutes of Health (NIH) is an agency of the Department of Health and Human Services (DHHS), which is a Department of the United States Government. The NIH is the Federal focal point for health research.

The accompanying financial statements present the financial activity of the NIH's Management Fund (MF). The NIH MF financial statements are prepared in conformity with generally accepted accounting principles for Federal Agencies - Title 2 of the General Accounting Office's (GAO) Policy and Procedures Manual. The DHHS has adopted GAO's Title 2 for its audited financial statements. The NIH MF was established on June 29, 1957 by Public Law 85-67 to facilitate the accounting and administration of funds spent on intra-governmental activities by two or more appropriations. These activities are required for the efficient and effective operations of all NIH programs and facilities. The MF organizations providing these services do not receive an appropriation from Congress. Their costs are incorporated into the various NIH appropriations during the formulation phase of the budget process.

Funding Process:

The funds needed for the MF activities are collected from other NIH appropriations and other federal agencies by a formula-based assessment based on estimated obligations. The objective of the formulas is to maintain a reasonably equitable system for charging the costs of the MF activities to the appropriations they support. The formulas applied include composite usage, the number of positions budgeted for full time employees, and the number of square feet.

Recognition of Revenue and Expenses:

The MF operates on the accrual basis of accounting which recognizes most financial transactions, events, or allocations as they are incurred. Funds are collected in advance and a liability is recorded. Revenues are realized and the liability is reduced when expenditures are incurred. Expenses are recognized when incurred.

Note 1. Significant Accounting Policies (Continued)

Inventories:

Inventories are valued at the lower of cost or market. Cost is determined by using the weighted average method.

Annual, Sick, and Other Leave:

The Personnel and Pay Systems, Office of Human Resources Information and Management, DHHS provides the amount of leave accruals on the payroll tapes. Annual leave is accrued as earned and reduced as taken. Sick and other types of leave are expended as taken but not accrued when earned.

Retirement Benefits:

All permanent employees participate in the contributory Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS) which became effective January 1, 1987. Temporary employees and employees participating in FERS are covered under the Federal Insurance Contributions Act (FICA). The NIH makes matching contributions to the CSRS, FERS, and FICA and matches employee contributions to the savings components of FERS up to five percent of basic pay but has no liability for future payments to employees under these programs. The NIH's costs associated with its employee retirement programs during fiscal years 1991 and 1990 amounted to approximately $11,036,000 and $9,724,000, respectively.

Property, Plant and Equipment:

The amount of capitalized acquisitions made by the NIH MF organizations is transferred to a consolidated NIH equipment account at year-end.

Note 2. Fund Balances with Treasury:

Treasury Account Symbols	(Dollars in Thousands) Fund Balances 1991	1990
75 3966	$122,846	$111,415

The NIH does not maintain cash in commercial bank accounts. Rather, its receipts and disbursements are processed by the U.S. Treasury. The balance of funds with the U.S. Treasury represents funds that are available to pay current liabilities and finance authorized purchase commitments relative to goods or services which have not been received.

Note 3. Receivables

	(Dollars in Thousands) 1991	1990
Accounts and Interest Receivable - Public		
Current	$ 26	$ 18
Accounts Receivable - Federal	544	407
Total Accounts and Interest Receivable	$ 570	$ 425

The NIH MF does not currently record an allowance for bad debts because the majority of the customers are federal agencies. In addition, based on prior years' history of write-offs, there is no need to record an allowance.

Note 4. Inventory

	(Dollars in Thousands) Inventory Amount	Allowance for Losses	Inventory, Net 1991	Inventory Net 1990
Method				
Not Held for Sale:				
Drugs	$ 1,287	$ 0	$ 1,287	$1,110
Medical Supplies	2,275	0	2,275	2,818
Total	$ 3,562	$ 0	$ 3,562	$3,928

Note 4. Inventory (continued)

There are no restrictions of inventory use, sale or disposition.

The inventory is valued at cost. Both inventories are located in the NIH Clinical Center (CC). One inventory represents the drugs held by the CC Pharmacy for patient and research use. Monthly, the inventory account is adjusted and an expense is recorded based on subsidiary inventory reports which reflect the amount of inventory consumed. An allowance account is not currently used to estimate future losses. Inventory losses are minimal and are expensed when incurred.

The Materials Management Department of the CC stocks hospital/medical supplies for use by the CC. The balances are based on a report issued by the Office of the Assistant Secretary for Health, Public Health Service, in February 1992. Currently, the stock is expensed as received. However, we are reviewing the appropriateness of this procedure.

Note 5. Other Assets - Financial Resources

	(Dollars in Thousands) 1991	1990
Advances to Federal Agencies:		
Letter of Credit	$ 299	$ 267
All Other	577	458
Total	$ 876	$ 725

Note 6. Property, Plant, and Equipment.

The NIH has treated the property in the MF as purchased from an annual appropriation. In such manner, the amount purchased each year has not been capitalized in the fund itself, but transferred to a control account with other NIH fixed assets. The assets in the control account are not depreciated.

The FY 1991 property balance is supported by accountable property subsidiary records with no depreciation recorded. Information relating to the FY 1990 property balance is not available.

Note 7. Other Funded Liabilities

	(Dollars in Thousands)			
	Federal	Non-Federal	Total 1991	Total 1990
Advances from Federal Agencies	$81,529	$ 0	$ 81,529	$ 90,022
Accrued Liabilities - Federal Agencies	5,555	0	5,555	3,761
Accrued Liabilities - Non-Federal Liabilities	0	4,201	4,201	3,107
Total	$87,084	$ 4,201	$91,285	$ 96,890

The Advances from Federal Agencies represent the net amount collected from the appropriations funding the MF that has not yet been expensed. However, these advances will be liquidated in subsequent fiscal years as expenses are incurred.

The Accrued Liabilities - Non-Federal Agencies amount does not include accruals for Payroll, Benefits and Benefit Entitlements.

Note 8. Accrued Unfunded Leave Liability

The liability for accumulated annual leave and compensatory leave has been earned and is payable to civilians and commissioned officers.

Note 9. Net Position

The net position consists primarily of the value of the MF property.

Note 10. Program/Operating Expenses

	(Dollars in Thousands) 1991	1990
Operating Expenses by Object Classification:		
Personal Services and Benefits	$169,071	$155,034
Travel and Transportation	2,198	2,209
Rental, Communications and Utilities	42,752	39,731
Printing and Reproduction	2,523	2,788
Contractual Services	126,283	111,616
Supplies, Materials and Low Cost Equipment	40,547	37,296
Insurance Claims and Indemnities	9	2
Total expenses by object classification	$383,383	$348,676

Note 11. Prior Period Adjustments

The adjustments reflect the changes in the unfunded leave for balances of annual leave previously earned but not used.

Note 12. Transfers and Other Adjustments to Net Position

The adjustments to net position include:

Restorations:	$15,085
Adjustments due to miscoding:	($116)
Property Transferred:	$53,860