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BY THE U.S. GENERAL ACCOUNTING OFFICE

Report To The Secretary Of State

Department Of State's Progress In Implementing The Federal Managers' Financial Integrity Act

GAO reviewed 23 federal agencies' continuing efforts to implement the Federal Managers' Financial Integrity Act of 1982. The act was intended to help reduce fraud, waste, and abuse in the federal government through annual agency assessments of internal controls and accounting systems and correction of systems' weaknesses.

This report focuses on State's progress and efforts to correct identified weaknesses in its internal controls and accounting systems and efforts to improve its assessment program.

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GAO/NSIAD-85-135
SEPTEMBER 25, 1985

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

NATIONAL SECURITY AND
INTERNATIONAL AFFAIRS DIVISION

B-216946

The Honorable George P. Shultz
The Secretary of State

Dear Mr. Secretary:

This report presents the results of our review of the Department of State's continuing efforts to comply with the Federal Managers' Financial Integrity Act (FIA) of 1982 [31 U.S.C. 3512(b) and (c)]. The act is aimed at strengthening internal control and accounting systems in federal agencies to help detect and reduce fraud, waste, and abuse, and thereby improve management of government operations.

This review was part of a governmentwide review to assess the progress and problems during the second year of implementing the act. Emphasis was placed on (1) determining whether actions taken as a result of the act are improving internal control and accounting systems, (2) evaluating State's progress in implementing its program for evaluating systems of internal control and accounting, and (3) assessing the reasonableness of State's December 28, 1984, FIA reports. Details on the objectives, scope, and methodology of our review are contained in appendix I. Some terms associated with implementation of the act and used throughout the report are defined in appendix V.

BACKGROUND

The FIA requires agency heads to report annually on the adequacy of internal controls and accounting systems. The internal controls report must state whether the agency's controls fully comply with the act's requirements, which are to establish controls in accordance with standards prescribed by the Comptroller General and which provide reasonable assurance that (1) obligations and costs comply with law; (2) assets are safeguarded against waste, loss, unauthorized use, or misappropriation; and (3) revenues and expenditures are properly recorded and accounted for. Any material control weaknesses, along with plans and schedules for their correction, must also be reported if agency controls do not fully comply with the act's requirements.

The accounting report must state whether the agency's accounting systems conform to the Comptroller General's principles, standards, and related requirements, hereafter referred to as the Comptroller General's requirements.

STATE'S 1984 FIA REPORTS

State's 1984 report on internal controls stated that with the exception of property management; accounting systems, procedures and certain related activities; physical security for U.S. embassies and personnel; automated data processing (ADP) operations; and cashiering; its internal control systems, taken as a whole, provide reasonable assurance that, within recognized limits, the act's requirements were met. State excepted property management and the other listed activities from its statement on meeting the act's requirements because material control weaknesses were found in each activity. Additionally, State's report included plans for correcting weaknesses reported in both 1984 and 1983. The "except for" reporting format used by State followed an approach similar to that discussed in the House of Representatives, Committee on Government Operation's August 1984 report on first-year implementation of the FIA.

We believe it is important to point out that the areas excepted from State's statement are of major importance to its operations. State reported that its central ADP operations are vulnerable to disruption of activities that are necessary to carry out its mission. The central complex supports such functions as payroll, personnel management and checking names against a central name file to determine eligibility for approximately 4 million U.S. passport and 7 million U.S. visa applicants annually. State also reported that there are numerous control deficiencies at its three overseas ADP centers. One of these centers, located in Paris, has an automated system that is used to manage purchasing of $2.5 billion in foreign currencies each year. State also reported its accounting systems do not provide adequate control over billions invested in property, and that annual inventories and reconciliations are seldom accomplished for about $250 million of personal property.

We also believe it is important to point out that State's FIA implementation program has not yet resulted in detailed evaluations and tests of all its systems of internal control. Some vulnerability assessments were not completed during 1984 and the assessments that were completed had not been fully analyzed by the end of the year. Also, State has performed only three detailed internal control reviews and recognizes that more need to be performed. In asserting reasonable assurance for areas not excepted in the internal control report, however, State relied on other factors in addition to what it had learned while conducting its FIA evaluations. Among these factors were the judgment of officials, in charge of its bureaus and offices, that their systems of internal control comply with the acts requirements and their consideration of whether recent reports issued by us and State's Inspector General (IG) had noted the existence of material control weaknesses. We believe these

other factors merit consideration by State in judging whether a statement of reasonable assurance should be made. However, we believe that State will have a stronger analytical basis to support its future reasonable assurance statements if it completes detailed reviews of all its major systems of internal control.

State's 1984 report on accounting systems stated that its accounting systems are not in conformance with the Comptroller General's requirements. The report also discussed plans for corrective action. We believe the report adequately reflects the status of State's accounting systems.

PROGRESS AND PROBLEMS IN IMPROVING INTERNAL CONTROL AND ACCOUNTING SYSTEMS

State has made progress toward correcting most of the internal control weaknesses and accounting system conformance problems which we reviewed from among those reported in its 1983 FIA reports or surfaced by its FIA process during 1983. Also, it has developed, or is in the process of developing, plans to correct weaknesses and problems reported in 1984. Effective action has not been taken or planned, however, to correct the accounting and internal control weaknesses in personal property management which were reported in State's 1983 FIA reports.

Internal control weaknesses and accounting systems conformance problems reported in 1984

State's 1984 FIA report on internal control included two areas with material internal control weaknesses which were not included among the nine areas reported in 1983. It also listed separately and expanded on a material weakness which had been reported as part of a group of weaknesses in 1983. The weakness areas were not discovered by vulnerability assessments and internal control reviews performed during FIA implementation; but rather, came from other sources such as IG audits, and State's Information Systems Security Office's ADP reviews. The weakness expanded on involved controls over overseas cashiering. The newly reported weakness areas involved controls over physical security for U.S. embassies and personnel abroad, and ADP operations.

The overseas cashiering function was reported as being vulnerable to theft and embezzlement because unannounced cash verifications are not conducted in a timely manner at many posts. U.S. embassies and personnel abroad were reported vulnerable to terrorist threats because U.S. embassies operate in an open environment which is highly accessible to the public. State classifies about one quarter of its foreign posts as critically or highly vulnerable to terrorist threats. State was reported

vulnerable to disruption of activities necessary to carry out its mission because there is no back-up site for its central ADP complex. Moreover, its three major overseas ADP centers have antiquated software and lack technically competent, American supervisors to assure good control over password management, software changes, computer storage media, remote dial-in-access, and contingency planning.

State's 1984 FIA report on accounting systems conformance included deficiencies at the International Boundary and Water Commission which were not reported in 1983. The specific problems, which were discovered by performing accounting conformance evaluations in 1984 as part of State's FIA implementation effort, were not listed in the FIA report; however, the report made reference to the problems and characterized them as minor accounting deficiencies and ADP control weaknesses.

A more detailed description of the material internal control weaknesses and accounting deficiencies reported in 1984 and plans for correcting them, as well as for those reported in 1983, are included in the appendices to this report. (See app. II for the internal control weaknesses and app. III for the accounting systems conformance problems.)

Corrective actions taken and planned on internal control weaknesses and accounting systems deficiencies reported in 1983

State's 1983 FIA reports included nine material internal control weaknesses and several conformance problems in its four major accounting systems. The internal control weaknesses were identified by analyzing our recent reports and recent IG reports and drawing on the knowledge of some experienced State officials, while the accounting deficiencies were identified by analyzing our reports and IG reports and systems evaluations State conducted before passage of the FIA.

Accounting systems deficiencies

The accounting problems that State reported in 1983 involved deviations from the Comptroller General's requirements, such as inadequate accounting control over billions of dollars in real and personal property; not using full accrual accounting; and not maintaining a system of general ledger and subsidiary accounts to control and account for an amount estimated at $3.5 billion for fiscal year 1985.

State initiated efforts in 1979 to replace or enhance its major accounting systems, and its 1983 FIA report stated that the systems under development will correct the accounting systems' problems.

Our review of State's efforts to correct problems in its accounting systems showed that with the exception of the personal property portions of the systems, which are discussed below, development and implementation of the new systems should improve accounting and financial management. However, the decision on whether the systems will be in conformance with the Comptroller General's requirements can only be made after the systems are implemented and properly tested in operation. (See app. V for a discussion of techniques to be used for properly testing systems in operation.) State planned to begin reviewing the new systems in 1985.

Thus far, State has made progress in developing and implementing most parts of the new accounting systems and plans to continue these efforts. A new financial management system which includes accounting, budget execution, and disbursing modules has been implemented in Bonn, West Germany and is scheduled for implementation at other locations during 1985 and 1986. Also, a disbursing module has been implemented at five posts and others are scheduled; and a cost module has been implemented at the Foreign Service Institute. Some system implementation dates have slipped, however. For example, the new payroll systems for American and Foreign Service National employees have slipped about 6 months and 1 year, respectively. State needs to avoid further slippages since it does not plan to take interim actions to correct conformance problems in the current systems.

Internal control weaknesses

The internal control weaknesses State reported in 1983 involved (1) visa issuance, (2) passport issuance, (3) accountability for Security Enhancement Program equipment, (4) overseas currency operations, (5) personal property management, (6) billing for administrative support to other agencies overseas, (7) a need to update financial management manuals, (8) the competency of certain personnel, and (9) the design and operation of a major accounting system. During our review, we selected six of these weaknesses and evaluated State's progress in correcting them. The six selected were visa issuance, passport issuance, accountability for Security Enhancement Program equipment, overseas currency operations, personal property management, and the need to update financial management manuals. The reported actions, taken or planned, to correct the weaknesses are shown in appendix II. These actions should improve control in all of the areas except personal property management. A brief discussion of the progress and problems in personal property management is provided below.

For at least 16 years, we,[1] and more recently the State IG, have reported serious deficiencies in State's management and control of domestic and overseas personal property. The problems stem mainly from the lack of a departmentwide system for managing, and accounting for an estimated $250 million of personal property, and the continued failure to perform physical inventories at all locations and reconcile the inventories to financial records. The result is that State's property records are incomplete and unreliable, excess property is not identified, and effective procurement planning, and financial accounting are hampered.

Two December 1984 State IG reports[2] provided some good examples of the problems. The IG found that only 4 of 15 overseas locations, and 8 of 14 domestic locations visited had performed inventories in 1983. Additionally, none of these locations had performed reconciliations between inventory records and financial records. Also, at two locations alone, as much as $3 million in personal property was not accounted for in financial records and reports. Further, one analysis performed at seven locations disclosed that 1,469 out of 4,305 household appliances, or 34 percent, valued at nearly $600,000, were in excess of existing needs. Another analysis performed at three locations revealed that 734 typewriters were onhand, although there were only 590 total personnel.

State recognized deficiencies in its control over personal property in its 1983 and 1984 FIA reports, and has initiated plans for correcting some of the reported weaknesses. The 1984 FIA report stated that (1) a nonexpendable personal property system, which will provide inventory and other management data, is in the advanced stages of development; (2) a study will be conducted to identify problems and corrective actions needed to effectively manage and account for personal property; and (3) contingent on additional resources, a central personal property office will be established to provide policies, procedures, and training. Moreover, State has told its IG that it will emphasize to all property managers the need for performing inventories and reconciliations. Given the fact that State has not corrected personal property management problems reported in the past, however, and the inadequacies in its current plans, which are discussed below, we do not believe State's plans will

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[1] Improvements Made or To Be Made In the Acquisition and Management of Nonexpendable Personal Property Overseas (B-165867, Mar. 12, 1969), and Acquiring and Managing Non expendable Personal Property Overseas: A Followup Review (ID-75-66, Jun. 9, 1975).

[2] Personal Property Management, Overseas Operations, A-849, Dec. 1984. Personal Property Management, Domestic Operations, A-848, Dec. 1984.

ensure that inventories and reconciliations will be performed at all locations and that personal property at all locations will be adequately controlled and accounted for in accordance with the Comptroller General's requirements.

We evaluated the nonexpendable personal property system and found that it applies only to overseas posts, and that only those overseas posts which have a specific computer can use the system. Of the 40 overseas posts which had the necessary computer as of January 1985, only 17 posts had implemented the system, and there were no plans or schedules for implementation at the other 23. As of January 1985, approximately 206 overseas posts did not have the computer capability needed to use the system, and no system is presently being developed to account for personal property at these locations. State is currently exploring ways to adapt the system to run on other computers, but the ad hoc committee created to do this has no established date for making recommendations.

In addition to the limited application of the system, we found that there is a need to ensure that the system is in conformance with the Comptroller General's requirements. For example, the system currently does not include the requirement to record the acquisition cost of personal property. This requirement is essential for providing proper accountability and control over the government's investment in the property for which the agency has management responsibility. Accumulation of the acquisition cost is also necessary to provide the basis for reconciling financial records with the results of physical inventories.

In commenting on a draft of this report, State agreed that controls over personal property management are not adequate. State believes, however, that the problems stem from a lack of compliance with published departmental regulations and procedures, rather than from the lack of a system and stated that actions are being planned and taken to increase compliance. We agree with State's comments on the lack of compliance with regulations and procedures. However, we do not consider these regulations and procedures to constitute a departmentwide personal property accounting system that conforms to the Comptroller General's requirements.

Corrective actions taken and planned on other weaknesses surfaced during FIA implementation

As indicated earlier, almost all of the internal control weaknesses and accounting conformance problems reported in State's yearend FIA reports came from our reports, IG and other reports, and the knowledge of State's officials rather than from

performing FIA process evaluations, such as vulnerability assessments and internal control reviews. State's FIA vulnerability assessments and other implementation efforts, however, surfaced many internal control weaknesses which were not considered material, and thus did not have to be reported in the yearend FIA report. We believe that surfacing and correcting such weaknesses is one of the benefits being derived from FIA implementation. We evaluated State's progress in correcting these weaknesses.

We examined 42 completed and planned actions which were designed to correct 24 of the 131 weaknesses recorded in State's tracking and follow-up system at the time of our review. At that time, only weaknesses surfaced during State's 1983 implementation had been entered in the system. We found that State is making good progress. Twenty-five of the 42 corrective actions have been completed and the other 17 are proceeding on schedule. Examples of the actions are (1) the establishment of automated systems to replace manual reporting systems, (2) installation of a cypher lock on a door to prevent unauthorized telephone use, and (3) issuance of instructions on authorized use of telephones. Although testing will be required to ensure that corrective actions are effective, the 42 completed and planned actions generally appeared reasonable to address the identified weaknesses.

STATE'S IMPLEMENTATION PROGRAM FOR FIA

Our report on State's 1983 FIA implementation[3] noted that the first-year effort was impressive, considering the scope and complexity of State's operations and the intent of the FIA. The report also noted, however, that the first-year effort was weak in some areas.

State's 1984 internal controls evaluation program did not proceed as fast as it initially estimated. For example, State initially planned to distribute vulnerability assessment guidelines in early June and to have the assessments completed and analyzed by the end of September 1984. Many overseas posts did not complete and return the assessments on time, however, and assessment guidelines for the domestic bureaus and offices were not completed and distributed until October 1984. As a result, State's vulnerability assessments were not all completed and analyzed by year's end. Thus, the scheduling of internal control reviews and other actions based on vulnerability assessment results had to be postponed until 1985. During 1984, however, State took or began to take a number of actions that should

[3] Department of State's First-Year Implementation of the Federal Managers' Financial Integrity Act, (GAO/NSIAD-84-91, May 1, 1984).

improve its implementation program. We believe these actions will help overcome some of the problems experienced in 1983. Some of State's first-year problems and actions taken or underway to overcome them are shown below.

PROBLEMS IN FIRST-YEAR EFFORT	ACTIONS TAKEN OR UNDERWAY TO OVERCOME PROBLEMS
Too few central level staff assigned to guide and monitor program.	Additional staff assigned at central level.
State did not expect internal control responsibilities to be included in all managers' work requirements statements during the first year of FIA.	Efforts underway to include internal control responsibilities and many statements now have it.
Many domestic offices and almost all foreign posts not covered by State's 285 assessable units.	Over 3,400 assessable units developed to provide broader coverage of all domestic and foreign offices.
It was hard to rate the degree of vulnerability among assessable units because of inconsistent evaluation methodology.	Developed vulnerability assessment questionnaires which will be centrally scored to assure consistency.
Training not given all managers assessing vulnerability.	Developed questionnaires designed to be answerable without classroom training.
Only three detailed internal control reviews begun--visa issuance, passport issuance and overseas citizens' federal benefits--and none completed.	Three internal control reviews completed and efforts to correct weaknesses found begun. More reviews to be done in 1985.
No tracking and follow-up system to monitor actions to correct control weaknesses.	Tracking and follow-up system implemented.

In addition to the actions shown above, during 1984, State issued a more comprehensive internal control directive to guide implementation of its internal controls evaluation program. For example, the new directive contains more specific requirements for documenting the evaluation efforts. State also required domestic assessable units to begin documenting internal control techniques as part of the vulnerability assessment process.

Nonetheless, State should continue to improve its implementation program. We found that: (1) State is not certain if internal control responsibilities are included in all appropriate managers' work requirements statements; (2) some vulnerability assessments were incomplete, indicating a need for more training; (3) internal control reviewers did not fully understand the review methodology, nor did they adequately assess ADP general controls; (4) FIA process inputs were not thoroughly reviewed by organizational component's internal control managers before submission to State's Comptroller's Office; (5) some control weaknesses and corrective actions were not entered in the tracking and follow-up system, and no formal requirements existed to review the reasonableness of proposed corrective actions or to test and evaluate their effectiveness after implementation; and (6) an accounting system conformance evaluation methodology had not been issued for ensuring consistency in performing future evaluations. These matters are discussed in more detail in appendix IV.

CONCLUSIONS

The State Department is making progress toward correcting reported internal control weaknesses and accounting systems conformance problems. Also, the implementation of FIA has surfaced numerous internal control weaknesses not significant enough to report, but which State is taking actions to correct. Adequate progress has not been made, however, nor have adequate plans been developed, to correct long known internal control weaknesses and accounting deficiencies related to personal property management.

During 1984, State's internal controls evaluation program did not proceed as fast as it had initially estimated; therefore actions, such as internal control reviews, based on vulnerability assessment results, could not be scheduled by the end of the year. State did, however, begin taking actions in 1984 to improve its FIA implementation program and it planned more improvements during 1985. The result is an improved implementation program in terms of coverage, and potentially, in terms of quality. Nevertheless, we believe some additional efforts are needed to

--assure that internal control responsibilities are included in appropriate managers' work requirements statements and considered in preparing performance appraisals and making promotion decisions;

--provide internal controls training to appropriate managers throughout the Department;

--revise training and guidelines to provide internal control reviewers a thorough understanding of the review methodology, including how to assess ADP general and application controls;

--require that FIA process inputs are thoroughly reviewed by internal control managers before submission to the Comptroller's Office;

--assure that identified weaknesses are entered in the tracking and follow-up system, that the reasonableness of proposed corrective actions is assessed, and that the effectiveness of implemented actions is tested and evaluated; and

--assure consistency in the methodology used for performing accounting conformance evaluations as portions of the Department's new accounting systems are implemented.

RECOMMENDATIONS TO THE SECRETARY OF STATE

During the course of our review, State officials in the Office of the Comptroller and the Bureau of Personnel have agreed to take actions needed to improve the FIA program in all but one of the areas mentioned above and have developed milestone dates for completing most improvement actions. We plan to monitor the proposed actions. The one exception is with respect to accounting deficiencies and internal control weaknesses in personal property management. While some actions are underway to improve accounting and control over personal property, the planned actions, partially because of resource constraints, are not totally adequate. To correct accounting conformance problems and improve internal control in this area, we recommend that you direct the Under Secretary for Management and the Assistant Secretary for Administration and Security to:

--Design and implement at all domestic and foreign locations, a personal property accounting system that will conform to the Comptroller General's requirements.

--Develop and implement procedures to assure that inventories are taken and reconciled annually at all locations as required by State regulations, including conducting periodic supervisory visits. Moreover, Assistant Secretaries and office heads should be required to certify annually that inventories of personal property have been taken and reconciled at all headquarters, other domestic and foreign locations under their purview, or to explain why these inventories and reconciliations were not performed.

AGENCY COMMENTS

State generally agreed with the report's contents, and stated that it will work during 1985 to implement the suggestions and recommendations made. (See app. VI.)

State outlined actions it is currently taking or planning to improve control and accounting for personal property. These plans modify and improve on the actions planned at the time of our review and reported in State's 1984 FIA report, and include: (1) establishing a central property office, (2) establishing a reporting mechanism to provide better control over performing physical inventories and reconciliations, (3) developing computer software to allow posts with personal computers to use the new nonexpendable personal property system, and (4) making property acquisition cost a mandatory system data entry item. Further, plans for the personal property study, which were included in State's 1984 FIA report, were dropped because the 1984 IG reports have already identified system weaknesses to State's satisfaction.

Regarding our recommendation that inventories be taken and reconciled annually, State commented that it is developing a mechanism to provide better control over performing physical inventories and reconciliations. This mechanism provides for geographic bureaus, rather than Chiefs of Mission, as our draft had recommended, to certify that inventories and reconciliations have been performed at each foreign post. We believe that certification by the Assistant Secretaries of Geographic Bureaus would provide the same type of control we had intended and, therefore, have modified our recommendation to reflect this.

We believe State's modified plans are responsive to our recommendations and have the potential to improve control and accounting for personal property.

. . . . .

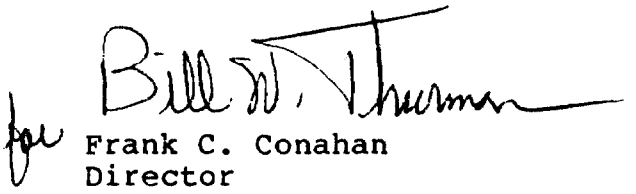
As you know, 31 U.S.C. §720 requires the head of a federal agency to submit a written statement on actions taken on our recommendations to the Senate Committee on Governmental Affairs and the House Committee on Government Operations not later than 60 days after the date of the report and to the House and Senate Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of the report.

We are sending copies of this report to the Chairmen of the above Committees. Copies are also being sent to the Chairmen,

House and Senate Committees on the Budget, Senate Committee on Foreign Relations, and House Committee on Foreign Affairs; and to the Director, OMB.

We appreciate the courtesy and cooperation extended to us during our review.

Sincerely yours,



for Frank C. Conahan
Director

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ABBREVIATIONS

ADP	Automated Data Processing
FIA	Federal Managers' Financial Integrity Act
FMS	Financial Management System
GAO	General Accounting Office
IG	Inspector General
OMB	Office of Management and Budget

OBJECTIVES, SCOPE, AND METHODOLOGY

The major objectives of our review were to

--determine whether actions taken as a result of the act are improving State's internal controls and accounting systems,

--update and evaluate progress made by State in implementing its program for evaluating systems of internal control and accounting, and

--assess the reasonableness of State's second annual FIA reports.

We conducted our review at the Department of State Headquarters in Washington, D.C.; at nine overseas posts in Europe and Southeast Asia; at passport offices in New York, Philadelphia, and Washington, D.C.; and at the U.S. section of the International Boundary and Water Commission in El Paso, Texas. Our review was conducted from May 1984 through April 1985.

We analyzed the three internal control reviews started by State in 1983 and completed in 1984, and interviewed eight of the ten persons who conducted the reviews. We examined the adequacy of State's documentation of review activities; evaluated some of the written procedures; and observed the operations of two of the three reviewed functions at four overseas posts and three domestic passport agencies; and discussed the results of the reviews with the key administrative officials of the three functions. Our purpose was to determine (1) whether the reviews were conducted according to State and the Office of Management and Budget (OMB) guidelines, (2) the extent to which ADP internal controls were considered, and (3) whether the results of the reviews were reasonable and supported by available evidence.

We examined the questionnaires designed by State to assess vulnerabilities during 1984 in its domestic and overseas units. We reviewed most of the completed questionnaires from 15 domestic offices and 9 overseas posts and discussed the contents with the overseas respondents. We discussed the administration of the vulnerability assessment process with State's FIA central staff and coordinating officials at 9 overseas posts and 14 domestic offices. Our purpose was to (1) evaluate State's methodology for compliance with OMB guidelines, (2) assess the quality of guidance provided by State to its organizational units, (3) determine the accuracy of questionnaire information provided by these units, and (4) determine the usefulness of State's assessment methodology to the units.

We obtained and reviewed corrective action plans for internal control and accounting weaknesses identified in State's 1983 FIA reports, its three internal control reviews, and 29 of the 285 vulnerability assessments it conducted in 1983. We discussed these plans with the State officials responsible for implementing the actions, and State's IG. Our purpose was to assess the reasonableness of the corrective action plans.

We queried officials in State's Comptroller Office who were responsible for coordinating FIA activities on their procedures for identifying material weaknesses for inclusion in State's 1984 internal controls report. We reviewed memoranda on identifying and reporting material weaknesses disseminated to the bureaus by the Comptroller's Office. We reviewed the 1984 internal controls report and the individual assurance letters from the bureaus, and discussed the reported weaknesses with our cognizant personnel. Our purpose was to determine whether all reportable weaknesses were included in the report. Other review steps included

--reviewing State's internal control and draft accounting conformance directives and organization to implement the FIA;

--reviewing State's segmentation of departmental activities into assessable units;

--reviewing State's FIA guidelines and questionnaires covering ADP general and application controls;

--observing and assessing State's accounting systems conformance evaluation efforts;

--reviewing State's 1984 FIA report on accounting systems;

--reviewing 640 work requirements statements of State managers to verify inclusion of internal control responsibilities; and

--reviewing and testing State's system of tracking corrective actions for weaknesses identified in 1983.

We limited our review to evaluating State's FIA implementation and reporting process. We did not attempt to independently determine the extent to which all of State's systems of internal control comply with the Comptroller General's internal control standards, or the extent to which its accounting systems conform with the Comptroller General's requirements. Instead, we relied to a large extent on our prior reports and IG reports which had noted internal control weaknesses and accounting systems compliance problems. We evaluated the reasonableness of some

corrective actions State has taken or planned to improve its reported control weaknesses and conformance problems but did not fully assess and test their adequacy.

During the course of our review, we kept agency officials informed of the status of our work and, in February 1985, we briefed them on the positions we would take in our draft report so they could consider our views in planning their 1985 FIA implementation effort. Our review was performed in accordance with generally accepted government auditing standards.

INTERNAL CONTROL WEAKNESSES AND CORRECTIVE ACTIONS REPORTED TO THE PRESIDENT AND THE CONGRESS IN THE DEPARTMENT OF STATE'S DECEMBER 1984 FIA STATEMENT

The Department of State's December 1984 FIA statement on internal controls reported three new areas which contain material internal control weaknesses. In addition, the statement listed the actions taken, actions underway, and actions planned to correct these weaknesses and the nine weaknesses reported in 1983. A synopsis of those weaknesses and corrective actions follows:

1984 Internal Control Weaknesses

Reported weaknesses	Reported corrections	Corrections planned or underway
Overseas cashiering function is vulnerable to theft and embezzlement because unannounced cashier verifications are not being conducted in a timely manner.	None.	Evaluating options to reduce weakness. Formulate plan to correct problem, March 1985.
U.S. facilities and personnel abroad physically vulnerable to terrorist threats.	Organizational and procedural changes made to strengthen management controls in the area. Increased emphasis made by the Secretary on managers' responsibility for physical and personal security. Also, Secretary and other senior officials briefed daily on security concerns.	Evaluation of function and resource requirements to continue.
	Comprehensive plan developed to make use of recently appropriated funds. Progress against the plan being reported monthly to the Congress.	Comprehensive plan to include: --constructing perimeter barriers at existing facilities, --constructing better protected missions,

Reported weaknesses	Reported corrections	Corrections planned or underway
		--expediting the implementation of security enhancement measures, --increasing the number of armored vehicles, and --increasing the number of security officers.
ADP operations are highly vulnerable because --the central ADP complex lacks back-up site to support its daily activity in the event of a prolonged outage.	Studies conducted to identify milestones and develop cost estimates for inclusion in a construction plan for a back-up site.	Adding model features to existing processor to ensure operation in case of malfunction in one processing unit. Also, an internal control or a comprehensive resource review to be made in 1985.
--the Regional Administrative Management Centers lack qualified American supervisors for their operations, causing deficiencies in physical, procedural, environmental and system security. The centers also have antiquated financial systems software.	Comprehensive surveys completed at two Regional Administrative Management Centers. Also, full contingency plans developed, hardware systems upgraded, and emphasis on security increased at all centers.	Regional Administrative Management Centers standardizing to a single operating system by summer 1985. The obsolete software will be replaced with the implementation of the Consolidated American Payroll Processing System and FMS.

1983 Internal Control Weaknesses

Reported weaknesses	Reported corrections	Corrections planned or underway
Inadequate training is resulting in certain administrative and program management staff lacking sufficient competency and	One hundred non-officer positions categorized into language-preferred support positions. Also, comprehensive plan developed and needed resources	Plan to send all appropriate personnel to a basic language proficiency training course.

Reported weaknesses	Reported corrections	Corrections planned or underway
foreign language proficiency.	requested to provide enhanced training in Russian and other East European languages.	
	Awarded contracts to upgrade administrative training for both American and Foreign Service National personnel.	Continuing to upgrade administrative training for both American and Foreign Service National personnel.
The Foreign Affairs Manual portions on "Financial Management" require major updating.	Chapter 000, Organization, Policy and Principles and Standards, published in May 1984. Various sections of chapters 300 (cash accounting), 400 (vouchers and claims), and 500 and claims), and 500 (payroll accounting) revised, updated, and published.	Chapter 000 to be reviewed for compliance to new principles and standards of the Comptroller General. Chapter 300 to be completed and published during 1985. Remaining chapters to be revised and prepared for publication.
State lacks a coordinated property management program. Annual property inventories are seldom accomplished, hampering efforts to effectively plan procurement actions and identify excess properties.	Partially completed software for an automated nonexpendable property system.	Continuing to develop an automated nonexpendable property system to assist in the management of personal property both in the posts and in the Department. A property management study will be conducted in 1985.
The Foreign Affairs Administrative Support System, which calculates reimbursements for services to other agencies overseas, is inaccurate because its procedures are complex and labor intensive, and its cost system is based on prior year usage.	The reimbursement module of the new FMS developed to provide data on reimbursement from serviced agencies, implemented at 11 overseas sites and in 3 domestic offices.	Developing personal computer version of the reimbursement software. Personal computer and minicomputer versions to be implemented at 36 overseas posts in fiscal year 1985. Also, negotiating with other agencies a new system for costing services.

Reported weaknesses	Reported corrections	Corrections planned or underway
The visa issuance function is a target for fraud and abuse by individuals who seek to subvert the visa and legal entry process.	Full-scale internal control review of the visa issuance process completed. Some recommendations implemented.	Continuing to execute internal control review recommendations.
	The Automated Visa Lookout System enhanced. Obsolete teletype terminals replaced with modern computer terminals which require an authorized password to access the system.	Expand Automated Visa Lookout System to six additional posts during January 1985. Also, complete analyzing requirements by April 1985 to determine what should be developed to replace Automated Visa Lookout System.
	Less experienced officers assigned to single officer posts in high fraud areas are now required to first serve for six months in a larger linked facility for on-the-job training.	
	Regular meetings now held with Immigration and Naturalization Service to exchange anti-fraud information and policies. Consular officers routinely routed through appropriate Immigration and Naturalization Service port of entry for maximum coordination in specific cases and full sharing of fraud ring information.	
	The Immigrant Visa Application Control System expanded to three additional posts.	

Reported weaknesses	Reported corrections	Corrections planned or underway
	Guidance on fraud investigation, and anti-fraud training provided by Immigration and Naturalization Service.	
	Anti-fraud activities elevated to the Senior Deputy Assistant Secretary.	
Limitations in the process of checking criteria for passport denial result in the potential issuance of passports to some individuals who should have been denied.	Full-scale internal control review completed. Some recommendations implemented.	Continuing to execute internal control review recommendations.
	Management reviews of the insular passport operations at Guam, Puerto Rico, and the Virgin Islands, completed in February 1984 and recommendations therefrom sent to the Islands' Governors. Also, insular passport conference held, September 1984.	Follow-up action on recommendations to be made during fiscal year 1985.
	Acceptance agent coordinators established at field agencies.	Complete revision of new passport agent manual, January 1985. Developing plans to provide technical training in the adequacy of documentation and identity proofs to all passport application agencies.
	Anti-fraud efforts enhanced: —held conference in October 1984 for	Complete evaluating U.S. Custom Service Treasury Enforcement Computerized System to

Reported weaknesses	Reported corrections	Corrections planned or underway
	regional fraud coordinators. --scheduled training for agents of all passport acceptance agencies. --meetings with various investigative agencies held to obtain agreements on limits and authorities for conducting passport fraud investigations. --anti-fraud organization established within the Passport Services Directorate in March 1984, to oversee posts anti-fraud efforts.	supplement Automated Visa Lookout System, January 1985.
There is inadequate accountability over the purchasing, inventorying, and shipment of equipment for State's Security Enhancement Program.	Project management enhanced: --additional personnel dedicated to the program. --security construction completed on 22 projects. --average time to complete projects reduced. --reviewed all projects. --simplified projects. --budget projections reviewed and tightened. --shipments of security enhancement material now announced in advance to posts and receipts required from all posts upon delivery of material. --program responsibilities for the Security Enhancement Program directed to be transferred to the established offices normally responsible for implementing security measures at overseas posts.	Project management to continue through fiscal year 1987.

Reported weaknesses	Reported corrections	Corrections planned or underway
Control of funds overseas in disbursing, currency purchasing and cashiering needs closer monitoring and management supervision.	The overseas disbursing module, which includes stringent automated disbursing and fund accountability controls, operational at three financial management centers.	Additional financial management centers equipped with this module to be established; 5 in fiscal year 1985 and 12 in fiscal year 1986. The three Regional Administrative Management Centers to be operational under FMS, starting with Mexico in fiscal year 1986. The Foreign Service Institute upgrading the budget and management course and designing a cashiering course for Foreign Service National employees. Internal control responsibilities are being incorporated into the performance agreements of disbursing officers.
The Departmental Accounting System does not meet the principles, standards, and related requirements of the Comptroller General (also reported as an accounting conformance problem).	See app. III's section on 1983 Accounting Conformance Problems, p. 12.	See app. III's section on 1983 Accounting Conformance Problems, p. 12.

ACCOUNTING CONFORMANCE PROBLEMS AND CORRECTIVE ACTIONS REPORTED TO THE PRESIDENT AND THE CONGRESS IN THE DEPARTMENT OF STATE'S DECEMBER 1984 FIA STATEMENT

The Department of State's December 1984 FIA statement on accounting systems conformance reported problems in its smaller accounting systems at the International Boundary and Water Commission, U.S. Section. The statement also described, as still applicable, the problems reported in 1983 in its four major accounting systems. In addition, the statement listed the actions taken, actions underway, and actions planned to correct problems reported in 1984 and 1983. A synopsis of those problems and corrective actions follows:

1984 Accounting Conformance Problems

Reported problems	Reported corrections	Corrections planned or underway
Because of weaknesses in ADP, similar to those listed in app. II, ADP section, the accounting and payroll systems in operation at the International Boundary and Water Commission, U.S. Section, do not meet requirements prescribed by the Comptroller General.	Weaknesses analyzed.	Plans will be formulated by July 31, 1985, to correct the identified weaknesses.
As reported in 1983 (see below), the Departmental Accounting System still does not meet the principles, standards, and related requirements of the Comptroller General. (Also reported as an internal control weakness in 1983, see app. II p. 10.)	See below.	See below.

1983 Accounting Conformance Problems

Reported problems	Reported corrections	Corrections planned or underway
Departmental Accounting System		
The Departmental accounting system does not meet the principles, standards, and related requirements of the Comptroller General. See below.	Partially developed new FMS composed of modules for overseas and domestic locations. See below.	Complete development of new FMS, end of calendar year 1986. See below.
--The system does not provide readily or automatically for the preparation of all needed financial reports. Also, the full accrual basis of accounting is not used.	--See section on the control of funds overseas under 1983 Internal Control Weaknesses, app. II p. 10. --Overseas accounting module implemented in Bonn.	--See section on the control of funds overseas under 1983 Internal Control Weaknesses, app. II p. 10. --Accounting module to be installed at additional financial management centers in fiscal year 1985. A converted version of this module to be operated at the Regional Administrative Management Centers, with implementation work starting in fiscal year 1986. --Complete designing and developing domestic accounting and consolidated FMS, end of fiscal year 1986.
--Many policies and procedures for carrying out financial operations do	--See section on Revisions of the Foreign Affairs Manual portions on "Financial	--See section on Revisions of the Foreign Affairs Manual portions on "Financial

Reported problems	Reported corrections	Corrections planned or underway
not conform to applicable laws, external regulations or current management policies.	Management" under 1983 Internal Control Weaknesses, app. II p. 6.	Management" under 1983 Internal Control Weaknesses, app. II p. 6.
--State is not able to maintain a system of general ledger and subsidiary accounts.	--General ledger system modeled on a Wang microcomputer.	--Modeling concepts to be used in the functional requirements for the FMS departmentwide general ledger system, February 1985.
--Significant elements of costs incurred are not systematically measured, assembled, or reported.	--Cost accounting segment for the Foreign Service Institute implemented, September 1984.	--Refining interface of the Foreign Service Institute cost system with State's accounting system.
--There is no adequate system of records and related procedures to provide a proper accounting over billions of dollars invested in property.	--Washington-based inventory module installed.	--Data is being purified to provide an accurate list of real property by December 1984.
	--Post building inventory and work order system modules installed at the American Embassy in Paris.	--Installation is ongoing; up to about 50 posts will have the systems by fiscal year 1989.
		--Automate interface of real estate management system with FMS during fiscal year 1986.
		--Implementing a system to account for nonexpendable property at overseas posts, end of fiscal year 1986.

Reported problems	Reported corrections	Corrections planned or underway
--The system does not provide reliable financial data needed in determining and supporting hundreds of millions of dollars to be reimbursed from other government agencies.	--See section on the Foreign Affairs Administrative Support System under 1983 Internal Control Weaknesses, app. II p. 6.	--See section on the Foreign Affairs Administrative Support System under 1983 Internal Control Weaknesses, app. II p. 6.
Payroll System		
The payroll system for American employees are not integrated which sometimes results in incorrect pay and other problems when employees transfer. Also, the Washington based system does not have adequate controls to assure accurate payroll processing.	None.	The current method of payrolling Americans will be replaced with the Consolidated American Payroll Process System, June 1985.
The three payroll systems for Foreign Service National Employees are old, different in design, difficult to maintain, and do not adequately support the unique compensation schemes around the world.	Letter contract signed for the design, development, and installation of a new worldwide Foreign Service National Payroll System, August 1984.	Full implementation of system scheduled for September 1988.
Working Capital Fund System		
The working capital fund system is labor intensive and does not produce prompt financial reports, adequately account for certain costs, nor have an adequate system of records and	None.	Contractor automating those operations which are particularly labor intensive. Installation of available software packages to be completed in March 1985.

Reported problems	Reported corrections	Corrections planned or underway
related procedures for accounting for investment in property.		Contract to be awarded to review and adjust procedures and documentation and to complete automation of working capital fund operations. Contract completion slated for September 1985.
Foreign Service Retirement and Disability Fund System		
The Foreign Service Retirement and Disability Fund System has not met the reporting deadline established by law, is improperly documented, and has inadequate accounting procedures, segregation of functions and audit coverage.	Contract to fully automate system awarded, August 1984.	Implementation of a fully automated system scheduled for August 1985.

OBSERVATIONS ON THE DEPARTMENT OF STATE'S FIA IMPLEMENTATION PROGRAM

The State Department took numerous actions to improve its FIA implementation effort during 1984. However, it needs to continue improvement of its implementation program, particularly in the areas discussed below.

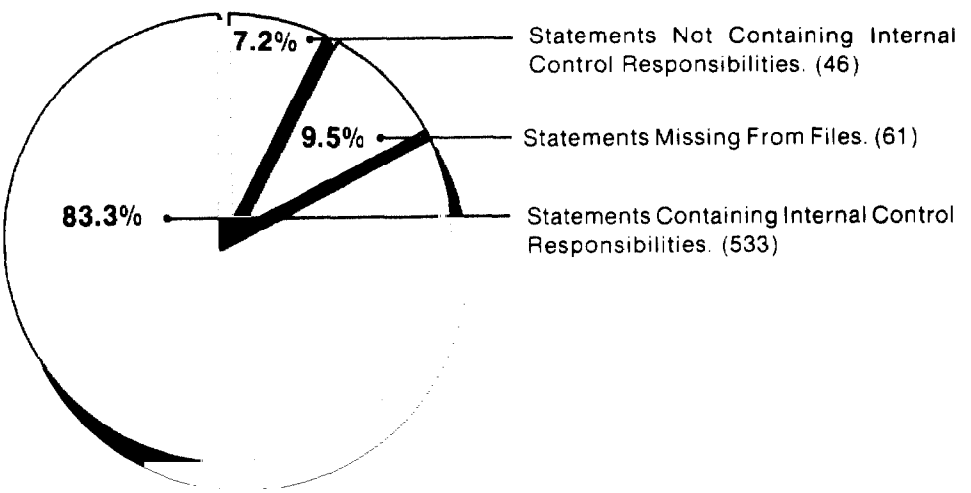
INCLUDING INTERNAL CONTROL RESPONSIBILITIES IN WORK REQUIREMENTS STATEMENTS

State's Bureau of Personnel issued a directive in February 1984, requiring all bureaus to determine the number of bureau managers having internal control responsibilities and to include these responsibilities in the managers' work requirements statements. The directive also requested that each bureau Executive Director review the requirements statements to assure that they were amended. It initially required the bureaus to report back to personnel on compliance by June 15, 1984, but the date was later extended to September 25, 1984.

By the end of January 1985, 21 bureaus had reported to the Bureau of Personnel that they had complied with the directive. They had identified 2,606 managers with internal control responsibilities. However, during November and December 1984, when we were reviewing inclusion of the responsibilities in the statements, only 17 bureaus, which were responsible for 1,353 managers having internal control responsibilities, had reported compliance. We asked to review 1,290 of these 1,353 managers' work requirements statements; however, we were able to review only 640 statements because some statements from overseas locations were either unavailable or arrived too late. Two bureaus, bureaus, the Bureau of African Affairs and the Bureau of East Asian and Pacific Affairs, respectively, reported 90 and 215 overseas personnel with internal control responsibilities, but declined to ask their overseas posts to send copies of the statements for our review. They stated that cables had been sent advising their overseas posts of the directives requirement and felt that this was sufficient to report compliance. Therefore, the two bureaus, assuming action had been taken, reported that they were in compliance, even though the requirements statements have not been reviewed. Further, two other bureaus, the Bureau of Near Eastern and South Asian Affairs and the Bureau of International Narcotics Matters, requested that the statements be sent in for our review, but most did not arrive in time for us to examine them. The Bureau of Near Eastern and South Asian Affairs was able to provide only 52 of 390 work requirements statements, and the Bureau of International Narcotics Matters was able to provide 8 of 15.

The chart below illustrates the number of work requirements statements we reviewed and details the numbers which (1) contained internal control statements, (2) did not contain internal control statements, and (3) were missing from bureau files.

Status of Work Requirements Statements GAO Reviewed



Total: 640 (100%)

As already indicated, we found that some bureaus have little knowledge that the directive has been complied with, even though they reported compliance. Moreover, we found that the bureaus have no follow-up plans to assure inclusion of internal control responsibilities in the managers' statements in future years. Therefore, we believe that the Bureau of Personnel should monitor and check compliance to assure that the managers' internal control responsibilities are included in the statements. Further, performance of these responsibilities should be considered when performance appraisals are prepared and promotion decisions are made.

PERFORMING VULNERABILITY ASSESSMENTS

During 1984, State developed four sets of vulnerability assessment questionnaires. Different sets were to be answered by foreign posts, domestic assessable units, the major domestic and three major foreign ADP centers, and ADP assessable units in domestic bureaus and offices. These questionnaires were designed to be answerable without classroom training, and to allow State to score them centrally to assure more consistency

in determining the level of assessable units' vulnerability to fraud, waste, and abuse. However, by the end of 1984, the process of scoring the questionnaires and determining levels of vulnerability for each assessable unit was not completed because many questionnaires were not turned in on time and the evaluation methodology had not been completed.

We reviewed the assessment questionnaires and found that those related to assessing non-ADP activities covered most factors required by OMB guidelines. We also found that the questionnaires for domestic assessable units went beyond OMB requirements, in that managers were required to list the control techniques they used. State added this requirement to begin documenting control techniques, as required by the Comptroller General's standards for internal control. Further, we found that some assessment questionnaires, particularly those developed for foreign posts, provided managers an opportunity to test for compliance with some important controls prescribed by State because some questions asked specifically when or how often an important control was exercised. (The ADP questionnaires are discussed later in this appendix.)

We also examined some completed questionnaires and interviewed some managers who were involved in the process. Most of the managers thought the questionnaires were easy to answer. However, we noticed that the listings of control techniques on domestic assessment questionnaires varied widely among offices with similar procedures, and some questionnaires were not completely answered. As a result, we believe State still needs to provide managers, who have internal control responsibilities, with training on internal controls. We also believe that the internal control manager in each office should be specifically designated to review FIA process inputs before they are submitted to the Comptroller's Office, to assure their completeness and accuracy.

PERFORMING INTERNAL CONTROL REVIEWS

In June 1984, State reported the results of the three internal control reviews it had started in November 1983. Our evaluation of these reviews showed that they resulted in sound recommendations to improve controls over visa and passport issuance and services provided to Americans who receive federal benefits, but who are out of the country. We also found that the control techniques analyzed during the reviews were tested for effectiveness. We found, however, that the reviewers experienced some difficulty in identifying event cycles, risks, control objectives, and control techniques for the functions reviewed, and that some control techniques, such as spot-checking approved visas, and unannounced audits of the collection of passport fees were not analyzed and tested for

effectiveness. Further, the reviews were not documented as thoroughly as is called for in State's guidelines. We found that the reviewers had received training before performing the internal control reviews and most thought the training was adequate. Several suggested, however, that it would be helpful if case studies of State Department operations were used in the training and review guidelines instead of less directly related material. We believe that State should implement this suggestion to increase future reviewers' understanding of the review methodology, and to assure continuing performance of quality internal control reviews.

TRACKING AND FOLLOW-UP SYSTEM

During 1984, State implemented a manual system to track and follow up on actions needed to correct identified internal control weaknesses. State plans to automate the system during 1985. At the time of our review, weaknesses discovered, and corrective actions developed during the three internal control reviews performed by State had not been entered into the system; however, weaknesses and corrective actions resulting from 1983 vulnerability assessments had been entered.

Of the 285 vulnerability assessments conducted by State in 1983, 122 assessable units were initially determined to be highly or moderately vulnerable to fraud, waste, and abuse. We looked at 29 of the 122 assessments to see if identified weaknesses and corrective actions had been entered in the system and were being followed up. Nine assessable units had been reclassified to lowly vulnerable by State and for this reason, not entered into the system. Of the remaining 20, weaknesses identified in 17 had been entered in the system, while weaknesses identified in the other three (15 percent of the 20 assessments) had not.

Additionally, the system does not contain provisions for verifying whether milestone dates are met for taking the corrective actions, for determining the reasonableness of proposed actions, or for testing and evaluating the effectiveness of corrective actions, once implemented. State officials say they are working, as time permits, to assure that all weaknesses and corrective actions are entered into the system, and to assess the reasonableness of the proposed actions. The officials further stated that they plan to randomly select some completed actions and evaluate their effectiveness. We believe State should develop formal procedures to assure these steps are taken.

EVALUATING CONTROLS OVER ADP OPERATIONS

Automated operations and applications play a critical role in supporting an agency's missions and administrative

functions. Dependency on automation, the computer and its subsequent output of information to support such functions as payroll, inventory control and personnel, can be found throughout the government. Additionally, the use of automation interacts with activities which cut across organizational lines.

Elements of risks are associated with the use of automation. Among these risks are: unauthorized entry into an ADP system to get or change information; failure of computers to operate, thus delaying the output of needed information; and entry of inaccurate data, causing wrong or misleading information to be produced. These risks can increase the chances for the occurrence of fraud, waste, and abuse; however, internal controls can be used to reduce them.

During 1984, State developed questionnaires to assess the vulnerability of ADP operations at its foreign posts, its large domestic center, and its three large foreign ADP centers, and at each of its domestic bureaus. State is not sure if these questionnaires, as distributed, will result in assessing vulnerability for all of its many minicomputer operations. Therefore, it plans to develop another questionnaire and assess the minicomputer operations in 1985.

The questionnaires distributed during 1984 were not all answered and scored to determine vulnerability of the assessable units by year's end; therefore, we could not determine if they covered all ADP operations. Our evaluation of the questionnaires, however, showed that those developed to assess general controls at ADP centers and application controls in the bureaus are adequate for their intended purposes. However, the questionnaire developed for assessing ADP at foreign posts needs to be enhanced to better cover important ADP general and application controls. For example, reference was not made as to whether system software changes are properly authorized, documented, and tested before being implemented. This is an important control, necessary to prevent fraudulent changes to the software systems which help manage the physical and financial resources of foreign posts.

State's internal control review guidelines were developed in 1983. They provide that ADP be considered in performing the reviews, but contain no specific guidance on how to evaluate ADP general and application controls. Our evaluation of the three internal control reviews performed by State showed that application controls were adequately considered, where appropriate, in the reviews but that general controls, such as physical access to computer operations, were not. We believe State should revise its internal control review guidelines to provide more specificity on how to evaluate ADP general and application controls.

PERFORMING ACCOUNTING
CONFORMANCE EVALUATIONS

During 1984, State developed a draft directive to assign responsibilities for evaluating accounting systems. It also revalidated its list of accounting systems. Since the Department's major accounting systems had already been found not to conform with the Comptroller General's requirements and new systems were being developed for conformance, the major systems were not evaluated in 1984. Rather, State continued work on developing and implementing redesigned and enhanced systems.

Beginning in 1985, State's plans to conduct interim evaluations on some portions of one of the new systems--the Financial Management System (FMS)--soon after the portions are placed in operation. The first interim evaluation is planned for June 1985 at Bonn, West Germany. State does not plan to conduct detailed conformance evaluations of the new systems until a complete system or system module has been in operation for about a year. The first detailed evaluations will be conducted during 1985 for the cost accounting module of the FMS for the Foreign Service Institute, as well as for a real estate management module of the FMS for the Department. As a long-range goal, State plans to conduct a detailed conformance evaluation for each system or system module every 4 years after the first evaluation, except when a major system or procedural change occurs, in which case an evaluation will be conducted soon thereafter.

State's two smaller accounting systems, which are located at the International Boundary and Water Commission and account for about $14 million, are not scheduled for replacement and were evaluated by State during 1984. A combination of methods for evaluating conformance with the Comptroller General's requirements were used to perform the evaluations. These included a modification of a checklist developed by the Department of the Treasury, excerpts from GAO's Control and Risk Evaluation Methodology, GAO's Standards for Internal Controls in the Federal Government, and elements from OMB's draft Guidelines for Evaluating, Improving, and Reporting upon Financial Management/Accounting Systems in the Federal Government. This combination of methodologies was adequate to evaluate conformance of the systems. We believe that because State will be performing many evaluations as portions of its new accounting systems are implemented, it should take steps to ensure that a consistent methodology, including adequate testing, will be used to evaluate them.

GLOSSARY

We developed the following definitions that apply to our review of the implementation of the Federal Managers' Financial Integrity Act.

Accounting System

The total structure of the methods and procedures used to record, classify, and report information on the financial position and operations of a government unit or any of its funds, balanced account groups, and organizational components. An accounting system should assist in the financial management functions of budget formulation and execution, proprietary accounting, and financial reporting.

ADP Application Controls

Controls that are unique to each software application system. Application controls are intended to ensure the quality of data origination, input, processing, and output.

ADP General Controls

Controls that apply to the overall management of the ADP function in an agency. General ADP controls have a direct effect on the quality of service rendered to ADP users and cover the processing of all ADP application systems. These controls affect most ADP hardware and application software systems, and include:

--organizational controls for the ADP unit;
--system design, development, and modification controls;
--data center management controls;
--data center security controls;
--system software controls; and
--hardware controls.

These controls should be evaluated by ADP managers as part of an analysis of the general control environment.

Comptroller General's Requirements

Our Policy and Procedures Manual for Guidance of Federal Agencies contains the principles, standards, and related requirements to be observed by federal agencies. Specifically, title 2 prescribes the overall accounting principles and standards, while titles 4, 5, 6, and 7 specify requirements governing claims; transportation; pay, leave and allowance; and fiscal procedures, respectively.

Also, agency accounting systems must include internal controls that comply with the Comptroller General's internal control standards and related requirements such as Treasury Fiscal Requirements Manual and OMB circulars.

Documentation

That information which would allow an independent reviewer to understand the rationale for conclusions the reviewer reached regarding an agency's internal controls, as well as the methods used, and personnel involved. This information should be current and be available for review. "Documentation" of internal controls is one of the Comptroller General's Standards for Internal Controls in the Federal Government.

Internal Controls

The plan of organization and all coordinate methods and measures adopted by an agency to provide reasonable assurance that the three objectives of the Federal Managers' Financial Integrity Act of 1982 are achieved. Internal controls should be established in accordance with the Comptroller General's Internal Control Standards. Typically, an internal control represents the combination of a control objective, along with a control technique (or set of techniques) that is being relied on to achieve that control objective.

Internal Control Review

A detailed examination of a system of internal control to determine whether adequate control measures exist and are implemented to prevent or detect the occurrence of potential risks in a cost-effective manner. OMB guidelines recommend six steps for an internal control review: (1) identification of the event cycle, (2) analysis of the general control environment, (3) documentation of the event cycle, (4) evaluation of internal controls within the cycle, (5) testing of the internal controls, and (6) reporting the results. Internal control reviews should normally be conducted for those areas rated as highly vulnerable in the vulnerability assessment process, where corrective action is not readily apparent. An agency should allocate resources for these detailed reviews of internal control based on vulnerability. Those most vulnerable should be reviewed first.

Internal Control Standards

The Federal Managers' Financial Integrity Act of 1982 requires each executive agency to establish internal accounting and administrative controls in accordance with,

among other things, standards issued by the Comptroller General. In 1983, the Comptroller General issued a set of 12 Standards for Internal Controls in the Federal Government. The standards include five general control standards, six specific standards, and an audit resolution standard. The five general standards are: (1) reasonable assurance, (2) supportive attitude, (3) competent personnel, (4) control objectives, and (5) control techniques. The six specific standards are: (1) documentation, (2) recording of transactions and events, (3) execution of transactions and events, (4) separation of duties, (5) supervision, and (6) access to and accountability for resources.

Quality Assurance

The process(es) or system(s) of an agency which provide(s) reasonable assurance that the internal control evaluation, improvement, and reporting process established in accordance with the OMB guidelines is carried out in a consistent, accurate, and reliable manner. These processes or systems will form part of the basis for the annual assurance letters and statement to the President and the Congress. An agency's quality assurance has several essential elements, including appropriate documentation for the internal control evaluation process; appropriate Inspector General role in the process; adequacy of resources and overall organization of the process; appropriate training for managers with internal control responsibilities; and assuring that actions taken will correct weaknesses permitting fraud, waste, or mismanagement.

Reasonable Assurance

Internal controls systems should provide reasonable, but not absolute, assurance that the objectives of the system will be accomplished. This concept recognizes that the cost of internal control should not exceed the benefit expected to be derived therefrom, and that the benefits consist of reductions in the risks of failing to achieve stated objectives. Estimates and judgments are required to assess the expected benefits and related costs of internal controls. Errors or irregularities may occur and not be detected because of inherent limitations in any internal control, including those resulting from resource constraints, or congressional restrictions. "Reasonable Assurance" is one of the Comptroller General's Standards for Internal Controls in the Federal Government.

Segmentation

The process by which an agency identifies assessable units; that is, its programs and administrative functions. The inventory of assessable units developed as a result of this process must be appropriately detailed so as to provide a basis for the conduct of meaningful vulnerability assessments. OMB guidelines provide that all the agency activities, except those concerned with policymaking, should be included in the inventory. There is no single best method to segment an agency, particularly in light of variations in agency organization structure and responsibilities.

Testing Systems in Operation

Testing should be conducted on all critical system aspects and may include interviewing persons who operate the systems, observing operating procedures, examining system documentation, applying procedures on live transactions and comparing results, direct testing of computer-based systems by use of simulated transactions, and reviewing error reports and evaluating error follow-up procedures. Tests should be designed to disclose whether valid transactions are processed properly, and whether the system rejects invalid transactions. The tests should cover the entire transaction--from initial authorization through processing, posting to the accounts, and reporting. Accordingly, manual as well as automated operations should be included. In developing test plans, consideration should be given to the results of any prior system testing.

This testing criteria has been adopted by OMB and included in Appendix H of its publication, Guidelines for Evaluating Financial Management/Accounting Systems (May 20, 1985). In determining the tests that would be appropriate for any system, it is important to keep in mind that in most cases, using transaction testing as the key, more than one of the above techniques are needed to test all important aspects of an accounting system.

Vulnerability Assessment

A biennial review of the susceptibility of an assessable unit to the occurrence of waste, loss, unauthorized use, or misappropriation. OMB guidelines prescribe three basic steps for the conduct of vulnerability assessments: (1) analyze the general control environment, (2) analyze the inherent risk, and (3) perform a preliminary evaluation of existing safeguards. The primary purpose of vulnerability assessments is to determine if and in what sequence resources should be allocated for the performance of internal control reviews.

United States Department of State

Comptroller

Washington, D.C. 20520

August 12, 1985

Mr. Frank C. Conahan
Director
National Security and
International Affairs Division
U.S. General Accounting Office
Washington, D.C. 20548

Dear Frank:

I have reviewed GAO's draft report: "The Department of State's Implementation of the Federal Managers' Financial Integrity Act." I appreciate your acknowledgement of the Department's efforts to improve our internal controls and our accounting systems, as well as noting the improvements we made in implementing all aspects of the Federal Managers' Financial Integrity Act during 1984. We agree that further improvement is needed, and we intend in 1985 to work toward implementing the recommendation and the suggestions contained in your draft report.

In an informal meeting with Mr. Morrison, some editorial changes to the draft report were suggested by my staff. The enclosed memorandum contains the views of the Department, specifically the Bureau of Administration and Security, which has responsibility regarding the recommendation stated in the draft report.

I commend the work of Mr. Earl Morrison and his staff. Improvements made throughout the Department in implementing the Integrity Act are due in part to the responsiveness of your review team to questions asked by Departmental managers and to the positive nature with which the 1984 review was conducted.

I am determined and my staff stands ready to continue working toward improving our internal controls and our accounting systems in 1985 and beyond.

Sincerely,

Roger

Roger B. Feldman

Enclosure:
As stated.

GAO Note: Page number references have been revised to correspond to the page numbers in the final report.

APPENDIX VI

United States Department of State

Washington, D.C. 20520

August 12, 1985

MEMORANDUM

TO: M/COMP - Roger B. Feldman

FROM: A/OPR - Richard C. Faulk, Acting

SUBJECT: GAO DRAFT REPORT: The Department of State's Implementation of the Federal Manager's Financial Integrity Act

I have received S/IG comments and have revised our response to reflect their concern. We have reviewed the GAO draft report of the Department's implementation of the Federal Managers Integrity Act and, with exceptions noted, generally concur with property management deficiencies and weaknesses identified.

General Comments

1. A central property office is being established to establish policy, develop procedures, and provide training.

2. The statement (page 6) that the problems stem mainly from the lack of a Department-wide system is inaccurate. The Department does have a personal property system in place. Unfortunately, a great majority of the Bureaus and posts were not complying with published regulations and procedures and had not been performing the actions required by the system. S/IG has on numerous occasions commented in post audits that the system was adequate but that compliance was poor. This lack of compliance has been partially the result of a decentralized program and inadequate resources to centrally monitor compliance. The same paragraph also commented on the failure to perform and reconcile inventories. We are now in the process of establishing a reporting mechanism that should provide better control over physical inventory and reconciliation. For Foreign Service posts, the process requires that each geographic bureau provide us annually with a certification that all post inventories have been taken and reconciled or otherwise explain why a particular post has not performed these functions. The central property office will work directly with domestic offices to establish a similar compliance system.

3. Plans for the study commented on at the bottom of page 6 have been dropped. The S/IG audit identified weaknesses in both the domestic and Foreign Service property programs and recommended corrective action, making the proposed study unnecessary.

4. Page 7 states that no system is being developed to account for property at locations without VS capability. A program is currently being written that will give us a uniform system that can be used on both VS and PC machines. This will, of course expand computer capability to nearly all posts and allow those posts with PC machines to receive NEPA (comments p.7). In any event, the few remaining posts which will not have even a PC on site will have the manual system in place. There is nothing wrong with the manual system, if it is used properly.

5. NEPA software has been installed in 37 Foreign Service posts. At many posts, the system is either being used or is in various stages of data input. Those posts not using or inputting data are either awaiting training or being delayed because of other in-house problems.

6. The acquisition cost is being made a mandatory entry (comments p. 7).

Recommendations

-- Design and implement, at all domestic and foreign locations, a personal property accounting system that will conform to the Comptroller General' requirements.

Response: As indicated above, a program is being written for a uniform system. NEPA satisfies property management functions and M/COMP advises it does satisfy their needs for GAO requirements.

-- Develop and implement procedures to assure that inventories are taken and reconciled annually at all locations as required by Department regulations, including conducting periodic supervisory visits.

Response: See comments above regarding reporting procedure. With the exception of the reporting requirements, the central property office will have no supervisory control over the property management. However, the geographic bureaus will be encouraged to address the performance and reconciliation of physical inventories during their regular post management visits. Training and assistance visits are planned when the central property office is operational and after completion of a number of actions we consider prerequisite to such visits.

-- Assistant Secretaries and office heads and Chiefs of Mission should either be required to certify annually that inventories of personal property have been taken and reconciled or to transmit inventory and reconciliation to headquarters.

Response: The impending compliance requirement that the geographic bureaus submit an annual certification that inventories have been taken and reconciled, or furnish an explanation, should satisfy the reported 1983 Internal Control Weakness.

(390014)

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