# Office of Inspector General

## FY 2010 Financial Statements Management Letter

A11-02A

February 2011

# FEDERAL MARITIME COMMISSION

**FEDERAL MARITIME COMMISSION**
800 North Capitol Street, N.W.
Washington, DC 20573

January 31, 2011

***Office of Inspector General***

TO: Chairman Richard A. Lidinsky Jr.
Commissioner Joseph Brennan
Commissioner Rebecca Dye
Commissioner Michael Khouri

FROM: /Adam R. Trzeciak/
Inspector General

SUBJECT: Transmittal of the FY 2010 Management Letter

When performing an audit of an agency's major financial systems and accounting processes, auditors often detect deficiencies in internal controls that do not rise to a level of seriousness to be reported in the auditor's opinion. These findings are communicated to the auditee in a management letter. Attached is a copy of the FY 2010 Financial Statement Management Letter that reports on such findings.

During the annual review, findings within the same general area as earlier findings are likely to occur. Consequently, the Management Letter begins with reporting on the status of prior year findings. This is not necessarily an indication that management is not addressing these issues. Rather, it reflects that certain areas are vulnerable to accounting errors or system breakdowns and need constant oversight.

This year's management letter contains the status of five prior-year findings and four current-year findings.

The OIG will continue to review areas vulnerable to accounting error and report any findings in next year's management letter.

I am available to discuss the letter at your convenience.

Attachment

Dembo, Jones, Healy, Pennington & Marshall, P.C.

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January 31, 2011

**Federal Maritime Commission**
Washington, D.C.

In planning and performing our audit of the financial statements of the **Federal Maritime Commission (FMC)** as of **September 30, 2010**, in accordance with auditing standards generally accepted in the United States of America and Government Auditing Standards, issued by the Comptroller General of the United States, we considered the FMC's internal control over financial reporting as a basis for designing our auditing procedures for the purposes of expressing our opinion on the financial statements, and not for the purpose of expressing an opinion on the effectiveness of the agency's internal control. However, based on our audit, we are providing the following findings and recommendations.

**Prior Year Findings - Updated**

**Finding 1. Accounts Payable is understated**

Accounts payable (or payables) represent amounts owed for purchases of goods or services. During the year, payables are recorded when an invoice, packing slip or receiving report is received by the agency. The Office of Management Services (OMS) reviews all obligations at year-end and establishes an accrual for all services and goods received by year-end (e.g., to recognize that money is owed in the period that the goods were received). For example, an invoice for computer monitors that were delivered on September 15th (FY 2009) may not be sent by the manufacturer until October 10th (FY 2010). The expense should be recorded on the FY 2009 books because the monitors were received in FY 2009.

We reviewed accounts payable at year-end to ensure that all expenses for goods and services were properly recorded in the appropriate period. During our review, we identified approximately $94,000 in additional FY 2009 payables that were not recorded by the agency. Without making the necessary adjustments, the payables were erroneously recorded as FY 2010 expenses, even though the goods or services were received in FY 2009. This understated the FMC's liabilities on its financial statements.

> Identifying expenses when they occur near the end of the fiscal year is a two-step process requiring agency staff (generally finance or procurement staff) (i) to identify large contract and purchase items and to follow-up with the Contracting Officer's Technical Representatives (COTR) or other contact points to inquire whether the goods were received, and (ii) to estimate the dollar amount of services or goods that were received since the prior invoice up through the end of the fiscal year (September 30). The amounts are then accrued as payables.



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Under this standard operating procedure, OMS identifies all procurements over $10,000 at year end then contacts the COTR to determine any amounts that should be accrued. The audit team noted that OMS staff sent a letter to all COTRs requesting this accrual information but only half responded. The remaining COTRs either did not respond or did not provide the needed information.

The audit team also noted that when COTR responses indicated that accruals were required, the accruals were not always made. According to OMS staff, she informed the Bureau of Public Debt (BPD) finance staff but did not follow up to verify the amounts were recorded. Generally, agency finance staff is responsible for all accounting functions; however, the FMC's Office of Budget and Finance (OBF) is not involved in the year end accrual process.

*FY 2009 Recommendation:* Consistent with best practices at other federal agencies, the audit team recommends that OBF assume responsibility for contacting COTRs to ensure that all accruals are identified and recorded on agency books and records. OBF should also establish procedures to follow-up with COTRs to ensure that all COTRs respond to the request letter and that the appropriate accruals are made.

**FY 2010 Follow-up:** During the Office of Inspector General (OIG) testing all accounts payable tested were properly recorded based on the estimates provided by the COTRs. This comment is considered closed.

**Finding 2. Close out procedures on contracts need improvement**

Obligations represent the amount of orders placed, contracts awarded, services received, and similar transactions during a given period that will require payment during the same or future periods. Undelivered orders are obligations that are awaiting the receipt of the goods or services ordered before funds are paid. During the normal course of business, officials may cancel an obligation (i.e. undelivered order) that is no longer needed. An example of a service that is frequently canceled after an obligation has been established is travel. Once canceled, the funds may be used for other purposes, subject to appropriation limitations.

Periodically, and at the end of each fiscal year, federal agencies are required to reconcile their obligation controlling accounts to the total amount posted to supporting records. In addition, program and support offices are to review obligations to determine whether the amount obligated on the books is a valid commitment of funds. In the absence of adequate system controls to perform deobligation of invalid or unneeded orders, obligations will both accumulate and remain open until they expire (i.e. 5 years). In certain situations these funds, if deobligated timely, may be used for other contracts.

The OIG reviewed 10 undelivered orders to ensure payables were properly recorded. During this review, we identified one FY 2008 undelivered order for $155,850 where services were completed and the amount remained in undelivered orders at September 30, 2009. The amount was deobligated in FY 2010 and returned to Treasury after identification by the OIG. While it did not appear that these funds could have been used for other unmet agency needs because the order was issued in FY 2008 and services were provided in FY 2009, the discipline to deobligate funds timely, i.e., within the fiscal year the funds are obligated, will provide the agency the flexibility to use funds where they are needed.

*FY 2009 Recommendation:* The OIG recommends that the Office of the Managing Director establish contract closing procedures where COTRs notify OMS and OBF staff when contracts are completed so deobligation can be made timely and funds used to meet other agency needs when appropriate. The OIG also recommends that OMS provide training for COTRs on this procedure.

**FY 2010 Follow-up*:*** The OIG noticed improvements in the close out procedures during the year, however, the OIG identified two information technology contracts for a total of $21,000 that were completed that needed to be closed out and deobligated.

***FY 2010 Recommendation 1:*** The OMS work with the Office of Information Technology (OIT) to improve close out procedures in that department.

**Finding 3. Formal procedures needed to account for internal use software**

The mission of the Federal Accounting Standards Advisory Board (FASAB) is to promulgate federal accounting standards after considering the financial and budgetary information needs of citizens, congressional oversight groups, executive agencies, and the need of other users of federal financial information. In June 1998 FASAB issued standard number 10, "*Accounting for Internal Use Software.*" This standard identifies when to capitalize costs of software developed or obtained for internal use. This includes the software used to operate an entity's programs (e.g., financial and administrative software, including that used for program management). In this standard there are three phases (i.e. preliminary design phase, software development phase, and Post-Implementation/Operational phase) of development of software. These phases establish the standards of when and how software should be capitalized.

During the financial statement audit the OIG identified that the agency will begin developing in FY 2010, two new software programs, including a new optical electronic method for filing Form FMC-18, "*Application for a License as an Ocean Transportation Intermediary*" and teleconferencing software. Although the agency plans to develop these software programs there is not a formal procedure on how the agency will capture costs associated with these programs.

*FY 2009 Recommendation:* OBF, in consultation with OMS, should establish procedures on how costs will be accumulated for these programs and work with the COTRs in accumulating the costs. The costs then should be capitalized or expensed and reported on the agency's financial statements as appropriate.

**FY 2010 Follow-up*:*** The OIG identified several software projects that needed to be capitalized by the agency. The OIG worked with OBF to ensure that approximately $298,000 of improvements to the phone and teleconferencing system were capitalized and $180,000 of software in development was capitalized during fiscal year 2010.

***FY 2010 Recommendation 2:*** The OIG continues to recommend that OBF establish procedures during the year to identify the development of large software projects by the agency and to ensure that they are capitalized accordingly.

**Finding 4. Improvements needed in quality assurance review of Management's Discussion and Analysis**

The agency prepares and submits its Performance and Accountability Report (PAR) on an annual basis to the Office of Management and Budget. In this report the agency must complete a Management Discussion and Analysis (MD&A). This section includes items such as the President's Management Agenda, Financial Performance overview, and Financial Highlights. The Financial Highlights section includes a review of the agency's financial statements and explanations of changes occurring to the financial statements.

OBF and its staff members are integrally involved in the preparation of the PAR. The short time frame for compilation of the PAR limits the availability for the quality assurance (QA) review process. Further, the "over familiarity" with the details by staff compiling the PAR can be counterproductive when the QA review process commences.

During our financial statement audit the OIG noted that QA procedures were not adequate to ensure that errors would be discovered in the MD&A before issuance of the PAR. When the OIG reviewed a draft of the MD&A several errors were discovered that included formatting errors, addition errors and financial information that was inconsistent with the agency's financial statements.

*FY 2009 Recommendation:* The OIG recommends that the Office of the Managing Director establish a quality control review of the MD&A that reviews for mathematical errors, formatting and consistency with the financial statements and footnotes.

**FY 2010 Follow-up:** The OIG's review of the MD&A did not identify any error in reconciling the data to the agency's financial statements. The OIG considers this comment closed.

**Finding 5. Agency program officials risk unauthorized commitments and anti-deficiency violations when purchase orders are signed after services begin**

Federal Acquisition Regulation (FAR) 1.602-3, defines an unauthorized commitment as an agreement that is not binding - solely because the government representative who made it lacked the authority to enter into that agreement on behalf of the government.

Section 13(g) of Commission Order 112, *Procurement*, states that no employee shall enter into a formal or informal agreement to acquire services unless that employee has been delegated specific written authority to do so. The requesting office must not direct a contractor to perform services prior to being notified that a requisition has been approved.

The Anti-Deficiency Act prohibits federal agencies from obligating or expending federal funds in advance or in excess of an appropriation or apportionment. An Anti-Deficiency Act violation occurs when government officials make payments or commit the United States to make payments at some future time for goods or services when there are insufficient funds in the appropriation to cover the cost in full.

During our fieldwork, the OIG identified a number of unauthorized commitments by FMC managers and staff involving transactions processed in house and by the agency's procurement service provider, the Bureau of Public Debt. These transactions involved purchase orders for services that were "signed off" by the contracting officer (CO) after the period of service had already begun.[1] For example,

- The agency entered into a contract with a vendor to provide court reporting and transcription for Commission meetings. The order was signed by the contracting officer on November 7, 2009. Before funds were obligated, the vendor provided services for two Commission hearings on October 15th and 29th, 2009.
- The agency signed a contract (order) for cell phone services on December 3, 2008, for services received in October 2008 and November 2008.
- An order for document scanning services was signed by the contracting officer on June 13, 2009. However, the vendor provided daily services to the Commission in March 2009 through June 2009.
- A vendor provided keycard monitoring and maintenance services to the agency beginning on October 1, 2008. The contracting officer signed the order for these services on November 18, 2008.

In all of the above unauthorized commitments, the agency received services without a valid obligating document in place. This puts the vendor, the COTR and the agency at risk. The vendor is at risk of not being paid for services provided; the COTR is at risk of being personally liable for payment of these services and for an Anti-Deficiency Act violation if funds are not provided by Congress to fund the activity; and the agency at risk of a costly lawsuit if the vendor was told to provide the service by agency personnel.

One cause for late authorization of purchase orders is the timing of the procurement request (PR) by program staff. Section 8(a) of Commission Order 112, *Procurement*, requires staff to prepare a PR form to initiate the acquisition of a product or service and to route it through the FMC's automated procurement and contracting system for concurrence/approval at the required FMC management levels prior to being submitted to the CO for any appropriate action. Further, all PRs shall include sufficient information and lead time to allow for preparation of the procurement material (e.g., purchase order) in compliance with FAR time and content requirements.

For the four orders identified above, the OIG noted that PRs for three of the four orders were dated after the beginning of the performance period. The remaining PR was submitted one day before the performance period, as the following table illustrates:

| SERVICE | PROCUREMENT REQUEST | PURCHASE ORDER | PERFORMANCE PERIOD |
|---|---|---|---|
| Court Reporting | 09/30/08 | 11/07/08 | 10/01/08 |
| Cell Phone | 10/15/08 | 12/03/08 | 10/01/08 |
| Document Scanning | 06/04/08 | 06/13/08 | 03/06/08 |
| Keycard Monitoring | 11/12/08 | 11/18/08 | 10/01/08 |

[1] According to FAR 2.101, a purchase order is an offer by the Government to buy supplies or services upon specified terms and conditions, using simplified acquisition procedures.

It is unclear why managers are submitting purchase requisitions after the performance period has already begun. Based on discussions with staff, it appears that, in some of the cases, the timing of vendor invoices may contribute to some of the delay. Agency managers often know in advance when the agency will be billed for a service. For services that bill at the end of each quarter, we were told that that PRs and orders are often prepared just prior to invoicing. However, waiting to obligate funds means that services are being provided to the agency without funding authority, which creates risks to the vendor and the agency, as discussed above.

We also noted that, in all cases, the agency was operating under a continuing resolution (CR) at prior year funding levels. During these periods, it cannot obligate funds for a full year to a vendor due to funding uncertainty. Rather, the agency will "incrementally" fund an activity for some period of time not exceeding the CR. When interim funding runs out, or when a new CR or appropriation bill is enacted, program staff must revise the order for services to, again, obligate funds. Unless COTRs actively monitor the funding timeframes in the purchase order, they are unlikely to prepare PRs (and by extension, purchase orders) timely.

Regardless of managers' intent to spend funds cautiously during CR funding, it is important to have purchase orders in place at the beginning of the period of performance because the purchase order obligates funds for the activity. This ensures that funds will be available to pay for services received, regardless of when the agency is billed.

The OIG commends management for recognizing the seriousness of this issue. On February 4, 2010, the FMC's Managing Director spoke to FMC participants at the annual COTR refresher training about the need to monitor funding to avoid unauthorized commitments.

*FY 2009 Recommendation:* The OIG recommends that the Managing Director establish a procedure to notify COTRs when funding on purchase orders are about to expire to assist them to submit timely purchase requests to continue funding.

**FY 2010 Follow-up*:*** The Office of the Managing Director anticipates having these procedures written and completed by January 31, 2011. The OIG will follow-up on this finding during next year's audit.

## Current Year Comments

### Findings 6. Formal Procedures Needed to Track Civil Penalties

The Bureau of Enforcement is the prosecutorial arm of the Commission. Under the direction and management of the Bureau Director, Bureau attorneys participate as trial counsel in formal Commission proceedings, and work closely with the Commission's Area Representatives on investigations of potential violations of the Shipping Act and Commission regulations.

The Bureau prepares and serves notices of violations of the relevant shipping statutes and Commission regulations, and often enters into negotiations to compromise (i.e., settle) civil penalty demands arising out of those violations. If settlement is not reached, Bureau attorneys may recommend commencement of a formal Commission proceeding seeking the assessment of civil penalties or other relief for conduct or practices violating the shipping statutes. Bureau attorneys are designated to serve as the prosecuting attorneys on behalf of the Commission in such formal proceedings before the agency's Administrative Law Judge. After the penalty is assessed, the Office of Budget and Finance (OBF) records collections against the assessment.

The Office of General Counsel (OGC) assigns penalty cases to staff attorneys in the office to monitor progress and outcomes. However, information on civil penalty judgments is not centrally maintained in OGC; i.e., there is no centralized tracking system that would enable it to easily identify all outstanding penalty judgments, i.e., amounts assessed, amounts collected, balance due and due dates. Further, OBF does not know what judgment collections to expect and whether amounts received represent full or partial payments unless indicated by the defendant.

As a hedge against staff losing track of individual penalties assigned to it to monitor (due to reassignments, departures or the press of daily business), and to enhance controls over civil penalty receivables, OGC should centrally track all penalties assigned, noting the attorney assigned, the judgment amount, amounts paid, balance owed, and due date. The due date is important to ensure that the agency complies with the requirements of Debt Collection Improvement Act of 1996.[2]

***<u>FY 2010 Recommendation 3</u>*****:** The Office of the General Counsel should maintain a database of all civil monetary penalties assessed by the agency. This database should identify the date of the penalty, the defendant's name, the monetary penalty amount, payment amount and payment date(s). The spreadsheet should be provided to the Office of Budget and Finance with each modification to enable it to record collections against the judgment and timely refer past due amounts to Treasury for collection in accordance with the Debt Collection Improvement Act. All payment activity should be noted on the spreadsheet and shared between OGC and OBF.

[2] The Debt Collection Improvement Act of 1996 centralizes the government collection of delinquent debt. Federal government agencies are required to refer delinquent debts of fines and penalties to Treasury that exceed 180 days. Treasury then acts as the collection agency for the federal government agency.

**Finding 7. Senior Executive Service Candidate Training Obligations and Bona Fide Needs**

Commission Order 119, *Senior Executive Service Candidate Development Program*, dated December 13, 2001, establishes the Senior Executive Service (SES) Candidate Development Program (CDP), whose objectives are to support succession planning, to provide participants with developmental assignments and formal training competencies, and to increase their awareness of public policy, programs and related issues. The candidate development program generally lasts for 18 months and includes participation in a current, formal, interagency executive level training experience of at least 80 hours. Training is to address the SES Executive Core Qualifications and promote competence and effectiveness by establishing a working knowledge of executive roles in government.

On September 27, 2010, the FMC Chairman announced the selection of four FMC employees into the SES/CDP. On September 30, 2010, the FMC contracting officer issued four purchase orders (FMC-FMC-00164 through FMC-FMC 00167) for senior executive service candidate training, each in the amount of $25,000. A training vendor was not specified on the order, rather *Citibank,* the agency's purchase card services provider, was identified as the vendor. No training locations or courses were identified for any of the candidates. Due to the timing of the order, all training would occur sometime in fiscal year 2011 or beyond.

The *Bona Fide Needs* rule is a fundamental principle of appropriations law. It states that a fiscal year appropriation may be obligated only to meet a legitimate or bona fide need arising in, or in some cases arising prior to but continuing to exist in, the fiscal year for which the appropriation was made. The guidance does not imply that an agency's obligation of an annual appropriation on or near the last day of the fiscal year can never constitute a bona fide need of that fiscal year. There are criteria used to determine whether funds obligated at the end of the fiscal year represent a bona fide need of that fiscal year.

The Government Accountability Office (GAO) has issued several opinions on various aspects of appropriations law, including guidance of bona fide needs. The audit team reviewed GAO decisions and sought specific guidance from GAO on whether the procurement action identified above represented a bona fide need in FY 2010.

According to GAO, bona fide needs questions frequently involve transactions that cover more than one fiscal year. In a typical situation, a contract (or purchase order) is made in one fiscal year with performance and payment to extend, at least in part, into the following fiscal year. In one decision,[3] GAO has opined that "*training that began on the first day of the fiscal year 1990 was held chargeable to 1989 appropriations where the training had been identified as a need for 1989,* ***scheduling was beyond the agency's control, and the time between procurement and performance was not excessive."*** (Emphasis added.)

Often, training requires pre-registration by attendees, often weeks in advance of the actual training dates. If the training is scheduled to occur at or near the start of the subsequent fiscal year, agencies can obligate funds while in the prior year to register participants. When required by the vendor to pre-register to guarantee a training slot, the scheduling is considered "beyond the control" of the participating agency. In the example cited above involving the four SES candidates, the agency did not preregister any of the four candidates in a training course or program in FY 2010.

3 See 70 Comp. Gen. 296 (1991)

In a November 18, 2010, conversation with GAO appropriations law legal staff regarding the SES training procurement identified above, the audit team was told that the lack of an identified vendor/coursework and the length of time that has already passed without efforts to secure training "*are indications that the bona fide needs rule requirements have not been met.*" GAO further advised "*(w)hen an agency does not identify any class, coursework, or program to send its employees, there isn't even an obligation to determine whether it meets the need of a particular fiscal year.*"

During the exit conference, staff in the managing director's office provided the OIG with correspondence that indicated that senior management "identified Harvard and OPM's Federal Executive Institute (FEI) as *potential* vendors…" for training (emphasis added). These schools were identified in discussions with staff earlier in the fiscal year and both were identified in a September 30, 2010 email from the managing director to the procurement office. Harvard was ultimately selected but not until after the close of the fiscal year.

Based on discussions with staff in other program areas, the OIG understands that management did plan to enroll staff in either FEI or Harvard. The OIG concurs that there was a bona fide need for training in fiscal year 2010. While management documented the need, it did not take the next step and prepare the required requisitions and purchase orders to implement that need. The purchase order completed on September 30 identifying "Citibank" should have instead identified an educational institution. Moving forward, better procurement planning needs to occur so the agency is not rushed in the waning days (or hours) to implement spending decisions.

***FY 2010 Recommendation 4*:** Establish controls over year end procurements to avoid last minute purchase decisions. All obligations made in the final week of the fiscal year, except routine year end subscription renewals, should document reasons for the delay and be approved by the managing director. These procurements will be reviewed by the OIG as part of the annual financial statement audit.

**Finding 8. Human Resources Contractor Evaluation did not Follow FAR Requirements**

In fiscal year 2010 the agency procured human resource services for approximately $20,000. The Director of Human Resources (HR) identified three vendors from the Federal Supply Schedule and evaluated each for its ability to meet FMC requirements. In addition, four government "cross-service" providers, offering some or all of the necessary HR disciplines, were considered in a prior evaluation. However, according to the HR Director, these providers did not fully meet the level of technical expertise necessary and/or per hour labor charges quoted for services they provide exceeded quotes obtained from General Services Administration (GSA) vendors. Consequently, they were not considered to be viable alternatives in this procurement action.

Each of the GSA vendors was evaluated based on the vendors' ability to meet three requirement factors: (i) cost/pricing, (ii) technical capabilities, and (iii) past performance. The evaluation was performed by the HR Director over the telephone. No vendor was provided a statement of work (SOW) and no written proposals were sought from the vendors.

We could not determine from our review of the file what specific services the agency sought to acquire. All firms provided various position classification, staffing and HR management support services. Without a specific need identified, we could not assess the adequacy of the evaluation of the vendors. The evaluation consisted of between two-three sentences for each vendor and did not provide specific examples to support a rating. For example, one firm's technical capabilities "ranged from fair to good," without describing why it was fair to good. We also noted a heavy reliance on price as a selection factor.[4] For the winning bidder, the evaluation noted that this firm offered a discounted price from its GSA schedule, which made it the least expensive firm.[5] However, it was not clear whether the evaluator asked the firm for a better price or the firm unilaterally lowered its price. More importantly, there was no indication that the competing firms were given an opportunity to lower their prices.

We also noted that there was no Federal Acquisition Regulation (FAR) required SOW prepared for this procurement. The SOW identifies the specific tasks to be accomplished, deliverables, timeframes and costs. The SOW and resulting bid and proposal are used to hold the vendor accountable should the performance on the task not meet the government's requirements. If this contract fails to meet expectations, the government would have little documentation to support its claims.

***<u>FY 2010 Recommendation 5</u>*****:** The Office of Management Services requires program offices to follow the FAR and prepare work statements, including deliverables and timeframes, for all service requirements, and that evaluations be performed by two or more employees based on the written responses of the vendors.

**Finding 9. Sole Source Contract Issued to Non-GSA Vendor Without Performing Market Research**

In October 2009, the FMC's Office of Management Services entered into a sole source contract with a vendor to provide HR-related advisory and assistance services. Total contract value was $55,000. The file contained a detailed statement of work, identifying work description and deliverables.

Federal Acquisition Regulation 6.3 provides guidance on the use of sole source contracts by Federal agencies. Each contract awarded without full and open competition must contain a reference to the specific authority under which it was so awarded (Sec. 6.301{b}). Further when not providing for full and open competition, the contracting officer shall still solicit offers from as many potential sources as is practical. (6.301{d}).

The contracting officer prepared a detailed "sole-source" memo, citing FAR 6.302-1, *"Only one responsible source and no other supplies or services will satisfy agency requirements"* as justification for the procurement method. However we found no evidence in the file to indicate that other sources were solicited or even considered.

[4] FMC's cross servicing procurement agent does not consider price in the evaluation. Rather, price is considered after the proposals are evaluated when identifying the best value for the government. The lowest price may not be the best value. This transaction was processed within the FMC's procurement office.

[5] We noted on the purchase order that the rate to be paid ($107/hr) to the vendor was the GSA schedule price. If a discount was offered, the agency did not take it.

FAR Part 10, *Market Research*, proscribes policies and procedures for conducting research to arrive at the most suitable approach to acquiring, distributing and supporting supplies and services. Agencies must conduct market research before soliciting offers for acquisitions. Agencies should use the results of market research to determine if sources capable of satisfying agency requirements exist. In other words, a determination that no other source exists has to be supported by efforts to find a vendor to meet the requirement.

FAR Part 8, *Required Sources of Supply*, requires agencies to satisfy their requirements for supplies or services from or through the sources listed in FAR 8.002, *Priorities for use of Government supply sources*. Agencies are required to use, for example, sources listed on GSA's Federal Supply Schedules before considering open market vendors.

Market research, when used in conjunction with FAR, Part 8, guarantees that agencies will be able to document their sole source decisions. For example, an agency could identify efforts made to use required sources and explain why these sources do not meet its need. The sole source justification would then be supported. We found no documentation if the file, including in the sole source justification memo, that indicated that the agency attempted to address its requirement by using other required sources first. The vendor selected is not on the GSA schedule and is considered to be an "open market" source by the FAR. Open market sources are to be the last option considered by federal agencies when selecting vendors.

The OIG raised similar concerns in a FY 2007 report on a contract for consulting services[6]; specifically that a sole source contract was improperly used to procure needed services.

***FY 2010 Recommendation 6*****:** Ensure that all future sole source actions are properly documented with market research results following FAR-required sources of services (FAR Parts 10 & 8, respectively).

We believe that the implementation of these recommendations will provide the **Federal Maritime Commission** with a stronger system of internal controls while also making its operations more efficient. We will be happy to discuss the details of these recommendations with you and assist in any way possible with their implementation.

Management comments to this letter are attached in their entirety.

While this report is intended solely for the information and use of the management of the **Federal Maritime Commission**, it is also a matter of public record, and its distribution is, therefore, not restricted.

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*Rockville, Maryland*

[6] See A07-02, *Audit of Contracts.*

UNITED STATES GOVERNMENT FEDERAL MARITIME COMMISSION

# Memorandum

**TO** : Inspector General **DATE:** January 31, 2011

**FROM** : Managing Director

**SUBJECT :** FY 2010 Financial Statement Management Letter

I have reviewed the recommendations contained in the instant Management Letter. Immediately below are responses to your recommendations.

**Management Letter Recommendation 1. (Finding 2)** The OIG recommends that OMS work with the OIT to improve closeout procedures in that department.

**OMD Response:** Management has taken several measures to enhance oversight and accountability within the OIT, including improvement in contract close out procedures. Most recently, in January 2011, the Chairman consolidated IT services into a single office, with the former Assistant Managing Director/Chief Information Officer being reassigned to serve as the Director of the OIT. The Director of OIT will be making changes in COTR assignments and, in fact, three employees are scheduled to receive 40 hours of COTR training beginning in February 2011.

In addition, OMS has undertaken measures to enhance and improve oversight of the agency's procurement process, and will continue to work with *all* COTRs to ensure that they adhere to the agency's contract close out procedures. As part of this effort, the OMS is in the process of revising the agency's procurement policy statement and its acquisitions procedural framework, i.e., Commission Order 112, *Procurement*. It is anticipated that this Commission Order will be revised by the end of September 2011 and be distributed to all agency management officials.

**Management Letter Recommendation 2. (Finding 3)** The OIG continues to recommend that OBF establish procedures during the year to identify the development of large software projects by the Agency and to ensure that they are capitalized accordingly.

**OMD Response:** OBF is currently in the process of revising its existing policy regarding capitalization of software projects with a target date of February 28, 2011.

**Management Letter Recommendation 3. (Finding 6)** The OIG recommends that the OGC maintain a database of all civil monetary penalties assessed by the agency, and suggestss that the database contain the date of the penalty, the defendant's name, the monetary penalty amount, and the date when collection of the penalty was received. The OIG recommends that OGC provide OBF with a spreadsheet containing the information recorded in the database each time there is a modification to the account to enable OBF to record collections against the judgment and timely refer past due amounts to Treasury for collection with the Debt Collection Improvement Act of 1996.

**OMD Response:** This finding notes a flaw in communications from OGC to OBF, indicating that OGC does not always notify OBF when an assessment has been made and payment should be collected. We will correct that problem. OGC will notify OBF of existing assessments due and change its notification system by June 30, 2011.

**Management Letter Recommendation 4. (Finding 7)** The OIG recommends that controls over year-end procurements be established in order to avoid last minute purchase decisions. Additionally, the OIG recommends that all obligations made during the final week of the fiscal year (with the exception of routine year end subscription renewals) should have documented reasons for delay and be approved by the Managing Director.

**OMD Response:** As the OIG correctly states in its finding, a *bona fide* need existed for training that was part of the Commission's SES candidate development program (CDP). The SES CDP is an eighteen month to two year career development program, which requires various components, including but not limited to: execution of an IDP, mentoring, developmental assignments, and external training components. See 5 C.F.R. § 412.104; Commission Order 119. Completion of the entire program is required before the agency can benefit from candidates being qualified for appointment to vacant SES positions within the agency. Thus, the program is nonseverable and the Commission's appropriation of funds in FY 2010 was permissible and consistent with a determination made by the Comptroller General in *EEOC- Payment for Training of Management Interns,* B-257977 (1995).

Documentation was provided to the OIG demonstrating that vendors for external training were indentified prior to the close of FY 2010. We also note that the establishment and execution of the SES CDP was an intensive endeavor requiring the coordination of several agency offices over a period of several months. The Commission initially announced its intent to initiate the SES CDP during FY 2010 in its 2009 Human Capital Management Report dated December 15, 2009. Subsequent to that announcement, the Director of the Executive Resources Board and the Managing Director coordinated with OBF, OHR, and OMS to: identify and budget for suitable external vendors based upon past agency SES CDP classes; undertake the candidate application process; select candidates; notify candidates; and coordinate with candidates regarding IDP and course registration. As the OIG notes in its finding, candidates were notified of selection on September 27, 2010. On September 30, 2010 the agency issued purchase orders to Citibank for external training.

In preparing training procurement documentation, OMS' long-standing practice is to make payment for training courses via credit card. Training institutions prefer this method, and it is a much simpler and more cost effective means of payment. To accomplish this, purchase orders are issued to the credit card company (i.e., Citibank). Further, this practice is consistent with Commission Order 112, Section (e), which states that the "Government-wide commercial purchase card (VISA/Mastercard) may be used for making purchases under the simplified acquisition threshold of up to $100,000 to the maximum extent practicable."

In addressing the OIG's recommendation for this finding, the OMD is not sure of the OIG's intent. As discussed above, the SES CDP required a collaborative approach among several offices that transpired over several months. Within three days of notifying candidates of selection, OMS prepared the requisite training documentation. Subsequent to being accepted to the SES CDP, candidates applied for and were accepted to their respective external training courses and OMS registered and paid for courses.

Management agrees that last minute purchase decisions can be problematic. However, the SES CDP was not a last minute afterthought, but an effort by the Commission to implement an important career development program. The CDP extends over multiple years and requires at least eighteen months for each candidate to complete, once selected. Further, management believes that the internal controls established in Commission Order 112 are adequate. The Managing Director or the Chairman already approves virtually all obligations made during the fiscal year, including non-routine, year-end procurements.

**Management Letter Recommendation 5. (Finding 8)** The OIG recommends that OMS require program offices to follow the FAR and prepare work statements, including deliverables and timeframes, for all service requirements, and that evaluations be performed by two or more employees based on the written responses of the vendors.

**Management Letter Recommendation 6. (Finding 9)** The OIG recommends that all future sole source actions are properly documented with market research results following FAR-required sources of services (FAR Parts 10 & 8, respectively).

**OMD Response to Recommendations 5 and 6:** The Managing Director believes that the cited actions have complied with the FAR, although better documentation should have existed. Therefore, in response to Recommendations 5 and 6, the OMS has been directed to revise the agency's procurement directives, including Commission Order 112, *Procurement*. This Order will delineate and restate the proper procedures to be followed for developing agency acquisition packages at different dollar thresholds and ensure documented compliance with the appropriate FAR provisions. To assist staff in the future, OMS will adopt a "*Procurement Checklist of Required Actions Prior to & After Award."* In addition, OMS will develop a form to document justification for sole source procurements. It is anticipated that the revised Commission Order and forms will be issued by the end of September 2011.

If you have any questions regarding the above responses, please let me know.

/Ronald D. Murphy/

cc: Directors OBF and OMS
General Counsel