INSPECTOR GENERAL STATEMENT ON THE FEDERAL COMMUNICATIONS COMMISSION’S FISCAL YEAR 2003 MAJOR MANAGEMENT CHALLENGES

04-AUD-08-01 December 4, 2003

Office of Inspector General

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Federal Communications Commission
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INSPECTOR GENERAL STATEMENT ON THE FEDERAL COMMUNICATIONS COMMISSION’S MAJOR MANAGEMENT CHALLENGES
OFFICE OF INSPECTOR GENERAL

MEMORANDUM

DATE: December 4, 2003

TO: Chairman
    Managing Director

FROM: Inspector General

SUBJECT: Inspector General Statement on the Federal Communications Commission’s Major Management Challenges

In November 2000, the President signed the Reports Consolidation Act of 2000 (Public Law No. 106-531), which requires Inspectors General to provide a summary and assessment of the most serious management and performance challenges facing Federal agencies and the agencies’ progress in addressing them. To date, the Federal Communications Commission (FCC) Inspector General was not subject to this requirement since the Commission was not a covered agency per the Chief Financial Officers Act of 1990. With the enactment of the Accountability of Tax Dollars Act of 2002, the FCC is now subject to these provisions. This document responds to the requirements and provides the initial response to be included in the Consolidated Audit of the Federal Communications Commission Fiscal Year 2003 Financial Statements.

We identified the following seven significant management issues facing FCC for fiscal year 2003.

- Universal Service Fund Fraud
- Financial Reporting
- Loan Subsidiary Ledgers
- Information Technology and Information Systems Security
- Revenue Gap
- Reporting Components
- Physical Security and Protection of Personnel
The FCC continues to address these issues, many of which are of a long term nature and do not lend to themselves to quick fixes. Our assessment of the status of these challenges is enclosed.

The Reports Consolidation Act of 2000 permits agency comment to the Inspector General statements. To this effect, we request all comments or responses be received by my office by January 2, 2004.

H. Walker Feaster, III  
Inspector General

Attachment

Cc: Mark Reger, Chief Financial Officer
Universal Service Fund (USF) Fraud

Fraud is an inherent risk in the USF core business process: collection, certification, and disbursement of funds for advanced telecommunications services. As of fiscal year end 2003, 43 investigations have been initiated. Of those investigations, 35 are on-going and eight have been closed. Investigations have led to indictments as well as subsequent sentencing relating to fraudulent actions. To date, over $3.3 million in recoveries have been processed by the fund administrator with additional recoveries greater than $1.9 million sought.

FCC has taken action to address fraud in the USF business process however additional efforts are needed. FCC and the USF Administrator, in conjunction with the Office of Inspector General and the Department of Justice, have developed processes for suspected fraudulent activity monitoring, investigation, and referral. However, controls over management oversight and accountability for receipts of USF funds have been materially weak because of inadequate management controls, lack of a sufficient independent audit program to deter future fraudulent activity, and weaknesses in the structure of the program.

Financial Reporting

FCC does not maintain current and accurate financial data during the course of the year. As a result, FCC undertakes a massive effort to compile, analyze, and correct its financial data to prepare accurate financial statements quarterly and at fiscal year end. FCC can enhance both its processes and timing of financial reporting practices, improve its policies and procedures to ensure consistent accounting practices, and continue its endeavor for an updated, integrated financial management system entity-wide.

FCC has made progress in correcting financial management weaknesses. Recent improvements in its loan receivable and cost accounting processes resulted in FCC obtaining unqualified opinions. Despite these achievements, FCC needs to take additional steps to ensure proper financial management reporting. Specifically, it has not made the major changes needed to address a long-standing weakness in financial reporting. Significant elements of this weakness include the lack of:

- integrated financial management system(s) within FCC as well as its reporting components
- timely recording and analysis of financial activities for certain accounts
FEDERAL COMMUNICATIONS COMMISSION’S MAJOR MANAGEMENT CHALLENGES

- a cost accounting system that accounts for unit costs per generally accepted accounting principles,
- complete budgetary accounting for consolidated reporting components, and,
- a complete and thorough process for compiling the entity consolidated statements with minimum errors.

Loan Subsidiary Ledgers

Testing of loan ledger balances repeatedly identifies errors. FCC’s loan subsidiary ledger is comprised of loan models which are elaborate and complex spreadsheets documenting loan information and balances. In addition to the inherent limitations of the spreadsheet models, the applications utilized in the spreadsheet software are implemented to their maximum potential use which create more problems. Furthermore, FCC’s loan review process is manually intensive, therefore the risk of error is higher as a result of these conditions.

FCC is addressing its loan subsidiary ledger issue with the creation of the loan module in the Revenue Accounting and Management Information System and the outsourcing of its loan portfolio to a loan service provider. In October 2003, the loan service provider assumed service responsibility for FCC’s loan portfolio. For fiscal year 2004 financial reporting, FCC expects to discontinue use of the loan model spreadsheets as its system of record. Additional future challenges now exist in the management and oversight of the loan servicing contract.

Information Technology and Information Systems Security

As technology advances and our reliance on technology increases, the need for a strong information technology infrastructure becomes even more important. FCC’s operations have become increasingly more reliant on automated systems and further integration of FCC data and services with external users via the internet is escalating. Along with explosive growth in computer connectivity comes the ability to disrupt or sabotage critical operations, read or copy sensitive data, and tamper with critical processes.

FCC’s information technology control environment and systems security need to be enhanced. FCC is noncompliant with a number of Federal statutes and policies. Commission systems have been susceptible to malicious attacks via viruses and worms, and unauthorized access. Inadequacies and inconsistencies exist in the mainframe and network access request process and efforts to develop and test FCC’s contingency plans
have been slow. Additionally, FCC lacks a viable capital asset plan, needs to further enhance its audit trail facility utilization and review, and strengthen its password access controls.

FCC has taken steps to address its information technology and information systems security vulnerabilities. FCC developed its agency-wide security plan and is working toward compliance with required Federal policies and statutes; however, completion dates for key items to address this challenge have repeatedly been revised.

**Revenue Gap**

Although FCC collects approximately $250 million in regulatory fees each year, FCC cannot determine if all required fees are collected. The difference between what is collected, an amount subject to Congressional determination, and what should have been collected if all regulated parties paid their fees, is deemed a revenue gap.

Recent systems development and the mandatory use of the FCC Registration Number provide the Commission with a record of each collection which facilitates bill generation to non-payees. However, FCC does not have a complete universe of potential regulatory fee payees, it can not determine the total regulatory fee subject to collection, and it does not have a complete universe to facilitate regulatory fee rate assessment for future years.

**Reporting Components**

Throughout its history, FCC created subsidiary organizations and administrative components, subject to various levels of FCC oversight, to conduct Commission business and meet the agency mission. Fundamentally, these organizations were created without a complete assessment or determination of how component functions or responsibilities would comply with Federal laws and regulations, policy, or concepts. This issue exists to date and creates considerable confusion.

Until recently, FCC addressed questions arising from this issue on an individual basis resulting in a legal interpretation. At the close of fiscal year 2003, FCC adopted the first of what is expected to be a series of Commission Orders defining the applicability of certain laws and regulations to these organizations and components.
Physical Security and Protection of Personnel

This challenge is not unique to FCC. Since September 11, 2001, physical security and protection of personnel have been critical issues in the Federal government and the United States in general.

The FCC has taken steps to identify and implement security measures to protect FCC personnel and its physical infrastructure. Specifically, FCC created a program to inform personnel regarding potential threats and threat management, prepared measures to address potential catastrophic events, and made security enhancements to FCC facilities.

Despite these efforts, the Commission has related personnel and physical infrastructure issues to complete. For example, the FCC has not completed a Commission-wide continuity of operations plan. Security and protection enhancements to some facilities have not been completed. And, recommendations regarding work place violence need to be addressed by an appointed task force.
SECTION II

CHAIRMAN’S RESPONSE TO INSPECTOR GENERAL STATEMENT ON THE FEDERAL COMMUNICATIONS COMMISSION’S MAJOR MANAGEMENT CHALLENGES
Federal Communications Commission
Washington, D.C.

January 12, 2004

Walker Feaster III
Inspector General
Federal Communications Commission
445 12th Street, S.W.
Washington, D.C. 20554

Dear Mr. Feaster:

Thank you for the December 4, 2003 memorandum, providing your office’s assessment of the management challenges the Federal Communications Commission (FCC) is now facing. The items identified in the memo are long-standing concerns which have required, and received, attention over multiple fiscal years. Significant progress was made on each item in FY 2003, with two of the issues mentioned (Loan Subsidy Ledgers and Physical Security) at completion points barring further actions, and efforts are underway to further mitigate, if not resolve, the remaining items. Attached is a summary of the progress made toward meeting the remaining challenges, and where appropriate, a description of the additional steps to be taken. I remain committed to the successful resolution of all these concerns.

Sincerely,

Michael K. Powell

Attachment
Management Responses to
Major Management Challenges

Universal Service Fund Fraud
Significant progress has been made toward strengthening the internal controls over the USF. Improvements include the development of an internal audit staff at USAC including a certified fraud investigator, recruitment of a full-time Chief Financial Officer and migration of their entire accounting system from a vendor to USAC control. However, there is much more that must be done.

In FY 2004 USAC will complete audits on seventy-nine (79) USF beneficiaries, providing the detailed results for OIG review. These audits are likely to show that more routine information must be gathered on prospective beneficiaries and some results may trigger additional OIG investigations. The audits will also provide valuable information to be used in tightening internal controls. The audit vigilance applied to the Schools and Libraries Program will also be extended to the other USF programs to ensure they are operating in accordance with all statutory requirements. For FY 2004 our goal is to implement the September 26, 2003 Commission order which mandates that the USF be maintained in accordance with all federal financial requirements and be subject to all federal financial audit rules. USAC will convert their existing accounting system into a fully compliant federal budgetary accounting system by October 1, 2004. This alone will not solve the myriad of reporting problems we are experiencing with beneficiaries but it will bring the record-keeping into compliance with existing federal statutes. Simultaneously we have initiated efforts to bring USF computer systems into compliance with the associated federal statutes. Finally, we plan to establish a verification process to determine that the USF is charging suitable and accurate administrative costs for management of the fund. Currently the agency’s appropriated funds are assuming this burden and we recognize that that is inappropriate. As we gain knowledge, programmatic and administrative improvements will continue until all the current issues are resolved.
Financial Reporting

The FCC has obtained unqualified audit opinions for FYs 2000, 2002 and 2003. These are unparalleled achievements for a small agency. Although the financial records of the agency remain based primarily on the requirements of budgetary accounting, we continue to make modifications in processing and procedures in order to move towards a system which would reflect the financial statement position of the agency. This is a 10 year process for most large federal agencies but at the FCC size and strong centralization should lessen the time frames.

The agency does continue to remain wholly dependent on a small number of highly skilled federal employees with the unique technical knowledge necessary to convert the budgetary financial data into the annual financial statement format. This is a significant improvement from two years ago when the FCC was dependent on a contractor to prepare the statements.

This same FCC team is responsible for other improvements such as implementation of a new cost accounting system and the establishment of Chase Manhattan Bank as the system of record for the loan portfolio on October 1, 2003.

Our next tasks include full integration of our financial reporting activities components; the improvement of posting timeframes on non-routine transactions, and the increased ability to use this new information to make better financial decisions.

Loan Subsidiary Ledgers

The FCC transitioned the Auctions Loan Portfolio record-keeping process to Chase Manhattan Bank on October 1, 2003. This was a major accomplishment and reflects the dedication and effort of many offices within the FCC and their ability to work together towards a common goal. The FCC still lacks sufficient staff to monitor the portfolio performance and will rely on the work of an outside contractor to verify the accuracy of the
new process. Since the Commission does not currently anticipate issuing any new loans this will remain the resolution for the time being.

Information Technology and Information Systems Security

The explosive growth in the communication industry and the FCC’s heavy dependence on information technology to meet our mission needs means that a strong, secure technology infrastructure guided by sound business processes is more important than ever. The FCC’s business operations are almost totally dependent on automated systems that provide the public unprecedented web access to FCC data and services. This customer-oriented environment also brings with it the potential for disruption or sabotage of critical operations, exposure/loss of sensitive data, and impacted critical processes.

One challenge we face is that our internal systems security needs to be improved to meet the ever present security threats and must be compliant with Federal statutes and policies. At this time we must acknowledge that inconsistencies exist in the procedures granting access to our external hosted (mainframe) sites and local network access and that these need to be corrected. Also, efforts towards the development and testing of the FCC’s IT Disaster Recovery Plan have been slow but are proceeding and are expected to result in the required infrastructure at the FCC contingency site later this fiscal year.

While the FCC is taking proactive steps to address its information technology infrastructure and information systems security vulnerabilities, such as by developing an agency-wide security plan and working towards compliance with all required Federal policies and statutes, completion dates for some key milestones have repeatedly been revised due to resource constraints.

Another challenge the FCC faces is how to better manage our information technology investment portfolio and meet all applicable Federal policies, such as OMB Circular A-130
and the Clinger-Cohen Act. The FCC should implement a formal, documented information technology Capital Planning and Investment Control (CPIC) process and procedures with defined criteria for the selection, control, and evaluation of investments. Efforts are already underway this fiscal year to formalize and implement such a CPIC process.

**Revenue Information Gap**

The FCC is not currently able to determine if all required fees are collected because of insufficient licensing information. As a result, we cannot either identify potential payers or accurately anticipate the volumes of activity. Both these elements are necessary to accurately predict the payment amounts and to project rates. While this information gap has resulted in an under-collection of revenue only twice in the ten (10) year history of the regulatory fee program, there is an on-going need for structural improvement in the regulatory fee process. The FCC is in the midst of redefining internal roles and responsibilities, focusing on Bureau and Office involvement in estimating payment units and providing assistance in collection activities after the filing period closes. Adoption of the Debt Collection Improvement Act by the Commission in FY 2004 will be an important tool to aid our collection efforts.

**Reporting Components**

The current reporting components of the FCC include the Universal Service Fund, (USF), Telecommunications Relay Service, (TRS), and the North American Numbering Plan (NANP). Significant reporting improvement was achieved when the agency adopted an Order in October, 2003, requiring the components of the USF, which include USF and TRS, to transition to government accounting rules effective as of October 1, 2004. Additional Orders and/or a detailed contract are needed to bring the same level of oversight to NANP. The FCC will need to increase scrutiny of these reporting components in the program and financial areas to ensure compliance with these statutes. Following this, we must identify disciplined and structured processes to review and verify the financial information provided by the components to ensure accuracy and consistency in reporting between all units.
Physical Security and Protection of Personnel

While there has been significant progress on physical security enhancements, the FCC is unable to complete certain additional security improvements without the concurrence of building lessors. The FCC will continue to work on completing the outstanding enhancements where possible.