INSPECTOR GENERAL STATEMENT ON THE FEDERAL COMMUNICATIONS COMMISSION'S FISCAL YEAR 2004 MAJOR MANAGEMENT CHALLENGES

04-AUD-06-27 October 15, 2004

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: October 15, 2004

TO: Chairman
Managing Director

FROM: Inspector General

SUBJECT: Inspector General Statement on the Federal Communications Commission's (FCC) 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. This document responds to the requirements and provides the fiscal year 2004 submission to include in the Fiscal Year 2004 FCC Performance and Accountability Report.

We identified six significant management issues facing FCC for fiscal year 2004.

- Reporting Component Investigations and Fraud
- Financial Reporting
- Reporting Components
- Information Technology and Information Systems Security
- Revenue Gap
- 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 November 14, 2004.

H. Walker Feaster, III
Inspector General

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Inspector General

Attachment

Cc: Mark Reger, Chief Financial Officer

Reporting Component Investigations and Fraud

Fraud is an inherent risk in the Universal Service Fund (USF) core business process: collection, certification, and disbursement of funds for advanced telecommunications services. As of fiscal year end 2004, 55 investigations have been initiated. Of those investigations, 37 are on-going and 18 are closed. Investigations have led to indictments as well as subsequent sentencing relating to fraudulent actions. To date, five indicted individuals and one indicted corporation have accepted plea agreements in four separate investigations. Additionally, five individuals have been indicted in another case that is currently scheduled for trial. 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, developed processes for suspected fraudulent activity monitoring, investigation, and referral.

In addition to law enforcement activities, audits conducted of the E-Rate program disclosed significant potential recoveries. Currently, these recoveries are in excess of $20 million. FCC has taken action to improve oversight of the E-Rate program; however, additional efforts are needed. Controls over management oversight and accountability for receipts of USF funds by program beneficiaries 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.

Additionally, the Office of Inspector General is aware of an ongoing investigation of the Telecommunications Relay Service (TRS) Fund. FCC informed the Office of Inspector General there is the possibility of settlement for monetary recovery of disbursed funds. The TRS Fund compensates providers for the reasonable costs of providing interstate telephone transmission services that enable a person with a hearing or speech disability to use such services to communicate with a person without hearing or speech disabilities.

Financial Reporting

FCC does not maintain current and accurate financial data during the course of the year. As a result, FCC undertakes a massive, manually intensive 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 given the resources available. Recent improvements in its loan receivable and cost accounting processes addressed this challenge. Additionally in fiscal year 2004, FCC fully outsourced its loan portfolio operations and instituted a new cost accounting system which greatly improved its costing for performance. 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 need for:

- integrated financial management system(s) within FCC as well as its reporting components,
- timely recording and analysis of financial activities for certain accounts,
- a cost accounting system that accounts for unit costs per generally accepted accounting principles, provides information for performance measurement, and routinely provides this information to program managers,
- complete budgetary accounting for consolidating reporting components,
- a complete and thorough process for compiling the entity consolidated statements with minimum errors, and
- expanded oversight of component accounting activities.

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.

In fiscal year 2003, FCC adopted Commission Order FCC 03-232, the first of what was expected to be a series of Orders defining the applicability of certain laws and regulations to these organizations and components. Although the Order defined applicability of certain requirements for two of three current financial reporting components, it did not address the remaining component. Additionally, the scope of the new requirements was fairly ambiguous as to which relevant provisions of Federal financial management and reporting statutes and laws it applied. To date, FCC has not issued similar Orders addressing this issue or clarified the relevancy of the other existing provisions. Thus, the applicability of key provisions of Federal financial management and reporting statutes and laws, as well as some in their entirety, remains undecided.

During fiscal year 2004, the reporting components addressed by the aforementioned Order progressed toward meeting the October 1, 2004 effective date. Near fiscal year end 2004, component management informed FCC it would not meet the implementation date for key elements. To the best of our knowledge, no temporary, interim, or corrective actions to mitigate this challenge have been provided to or by FCC management.

Furthermore, bureau and offices which facilitate reporting component oversight are slow to address known problem areas and fundamental questions. This observation is not limited to those directly responsible for component oversight, but to other relative areas including: legal, planning, financial management, information technology, and general management. Identified issues and problem areas languish for multiple fiscal years with limited or no resolution. Although proposed solutions are discussed, many get diverted to address critical problems. This fact was highly evident in late fiscal year 2004 as FCC responded, and continues to respond, in what could be categorized as a reactive versus a proactive mode of oversight.

Information Technology and Information Systems Security

As technology advances and our reliance on technology increases, the need for a strong information technology infrastructure becomes 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. In the area of information systems security, the Information Technology Center has developed a disaster recovery plan for its information technology infrastructure and the Wireless Technology Bureau's Auctions Operation Branch has implemented a robust network intrusion detection system. Furthermore, the Commission has begun implementing its capital investment program.

Revenue Gap

Although FCC collects approximately $250 million in regulatory fees each year, FCC can not 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 fully 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. In fiscal year 2004, FCC billed 3,449 payees comprising $141.5 million in regulatory fee. As of fiscal year end, FCC received $136.8 million of the billed regulatory fee. FCC's ability to bill regulatory fee payees is significant progress relating to collection of known payees. However, since FCC does not have a complete universe of potential regulatory fee payees, it cannot determine the total regulatory fee subject to collection, and it does not have a complete universe to facilitate regulatory fee rate assessment in future years.

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. In the area of physical security, the Commission has significantly upgraded the security of its Gettysburg facility and has enhanced the physical access to the Portals II building with the addition of concrete barriers. 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

UNITED STATES GOVERNMENT

MEMORANDUM

DATE: November 15, 2004

TO: Inspector General

FROM: Chairman

SUBJECT: Response to the Inspector General's Statement on the Federal Communications Commission's Major Management Challenges

Thank you for the October 15, 2004 memorandum providing your office's assessment of the management challenges the Federal Communications Commission (FCC) is now facing. Progress has been made since receipt of your first report for FY 2003, and in FY 2004 improvements continued on each of these challenges. A summary of the progress and status of each challenge identified is attached. I remain committed to a complete and successful resolution of all these concerns.

Attachment

Management Responses to
Major Management Challenges
9/30/04

Reporting Component Investigations and Fraud

The Commission has taken numerous steps to improve Universal Service Fund (USF) oversight. To combat the risk of waste, fraud, and abuse in the USF program, the Commission took the following steps during Federal fiscal year (FY) 2004:

- Adopted new rules to revise the Commission's recovery approach such that recovery actions are now directed against any party or parties (including service providers and E-rate applicants) that have committed statutory or rule violations;

- Adopted new rules to strengthen audit and investigation processes, including the establishment of heightened scrutiny for applicants and service providers that have violated the statute or the Commission's rules in the past;

- Adopted and oversaw a targeted independent audit to address significant allegations of waste, fraud, and abuse concerning one Territorial Department of Education and its service providers;

- Ensured that USAC improved its own efforts to detect and deter waste, fraud, and abuse in the USF program. During FY 2004, USAC took steps to improve its oversight of the USF program, including: (a) developing a comprehensive plan to promote awareness of program rules in the E-rate community; (b) engaging an independent auditor to conduct 100 audits of E-rate program beneficiaries; (c) implementing an internal audit strategy focused on beneficiaries of all USF programs, as well as contributors to the USF; (d) working with the Commission's Office of Inspector General (OIG) to develop a plan for conducting hundreds of audits of USF beneficiaries; (e) initiating recovery of improperly disbursed funds; and (f) improving its review and processing of applications; and

- Improved its own managerial controls addressing USF oversight, including dedicating additional Commission staff to USF audit and oversight issues and revising the independent audit of USAC required by the Commission's rules to determine whether USAC is administering the program to prevent waste, fraud, and abuse.

During Federal fiscal year 2004, the Commission ensured that the Universal Service Administrative Company (USAC) conducted audits of USF beneficiaries, including audits performed by an independent auditor of $311,591,578 in USF monies provided to 79 randomly-selected Schools and Libraries Support Mechanism (E-rate) program beneficiaries. The 79 independent audits during Federal fiscal year 2004 resulted in recommended recovery of $8,899,897, or 2.86 percent of the total audited amount. To date, USAC, an independent auditor, or the Commission's Office of Inspector General (OIG) has issued a total of 198 audit reports of the E-rate program addressing a combined $1,141,400,629 in disbursements of E-rate program USF monies, or 13.3 percent of the total E-rate program USF monies disbursed since 1998. The 198 audits have resulted in a total recommended recovery amount of $43,949,362, or 3.85 percent of the $1.14 billion in E-rate program USF monies that were audited.

Safeguarding the USF program from the risk of waste, fraud, and abuse is an ongoing process that we continue to strive to improve. In this regard, the Commission continues to work on other measures intended to further safeguard the USF, including on-going rulemaking proceedings that address the appropriate amount of USF monies that should be disbursed in the program, the competitive bidding process, and mandatory independent audits of program beneficiaries. The Commission anticipates taking additional policy and program management steps in these areas during FY 2005.

With regard to the ongoing investigation of the Telecommunications Relay Service Fund, a settlement agreement between the defendant and the US Attorney's Office was signed as of September 30, 2004, and is currently awaiting approval by the court.

Financial Reporting

Major strides have been made by the FCC over the past several years in financial reporting. During FY 2004, a new cost accounting system was implemented that provides both budgetary and financial reporting of the goals included in the FCC's Strategic Plan. This is the first system that has allowed us to report on our results of operations as they correspond to our performance measurements. In addition, we implemented an additional module in our subsidiary revenue system that allows us to account for all the financial transactions relative to the auctions held by the FCC. Our previous manual process documented only by spreadsheets now resides in an automated financial system. Another major accomplishment is the completed outsourcing of loans operations to a service provider. The provider has been operational for the entire year and has provided monthly, quarterly and year-end reports to support our loan activity and balances.

Of course, we still have more to achieve in the financial reporting arena. The FCC has initiated a review for a replacement of our existing automated financial accounting system, which would integrate more of the systems than currently linked. Expected completion of that review is during FY 2005. In addition, a final module in our subsidiary revenue and accounting system will be implemented fully. This final module will account for all International Telecommunications Settlements. And finally, we continue to work on the consolidation of financial information of the FCC and its reporting components. This process remained fully manual for FY 2004, however with the implementation of GovGAAP by the components, consistency of financial transactions and data will allow a more expeditious consolidation of financial data on a monthly, quarterly and year-end basis to generate the required financial reports.

Reporting Components

The establishment and utilization of the reporting components by the Commission has been instrumental in accomplishing critical strategic objectives. They play a key part in carrying out the Commission's direction and provide an avenue for the Commission to accomplish its goals.

During FY 2004, the Commission took significant steps towards strengthening oversight of the Universal Service Administrative Company. In particular, the Commission implemented the following measures:

- Established an inter-bureau and office working group to more effectively coordinate oversight issues affecting the Universal Service Fund and USAC;

- Monitored USAC's efforts to ensure compliance with the Commission's Debt Collection Implementation Act (DCIA) rules adopted in April 2004;

- Reviewed and approved USAC's quarterly administrative expense filings and projected program demand;

- Responded to USAC's request for guidance pertaining to Federal budgetary accounting requirements. This process involved gaining an understanding of the legal, policy, and accounting issues related to USAC's transition to Government accounting standards, coordinating with other agencies within the Federal Government, and providing written instructions to USAC in less than eight weeks after these issues were raised to senior Commission staff; and

- Improved its own managerial controls addressing USF oversight, including dedicating additional Commission staff to USF audit and oversight issues, revising the independent audit of USAC's administration of the USF, attending USAC's quarterly meetings of its Board of Directors, and implementing a tracking system to assist in identifying and resolving policy and program management issues. In addition, the Commission initiated regular coordination meetings between senior and mid-level staff of USAC and the Commission.

Ensuring proper oversight of USAC and the USF is an ongoing process that we continue to strive to improve. The Commission anticipates taking additional policy and program management steps to strengthen oversight of USAC and the USF during FY 2005, including both reevaluating the Commission's internal policies and procedures governing oversight of USAC and the USF and considering oversight issues in on-going rulemakings and other proceedings.

Information Technology and Information Systems Security

The FCC is taking proactive steps to address its information technology infrastructure and information systems security vulnerabilities, such as developing agency-wide security plans and working towards compliance with all required Federal policies and statutes. We recognize that completion dates for some key milestones have been revised due to resource and budget constraints.

One challenge we continually face is to sustain a secure and compliant IT infrastructure from internal and external threat. Our efforts towards the development and testing of the FCC's Information Technology Disaster Recovery Plan (IT DRP) were hampered by budgetary constraints, but we successfully completed and tested the Continuity of Operations Plan (COOP) and IT DRP during the first ever Federal Government-wide COOP test, Forward Challenge in May 2004. Additional work is underway to enhance COOP and IT DRP capabilities to include business applications and other related efforts.

We are also working 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. Efforts are already underway to formalize and implement a formal, documented information technology Capital Planning and Investment Control process, including procedures with defined criteria for the selection, control, and evaluation of investments. An IT Steering Committee (ITSC), comprised of representatives from the Bureaus and Offices, has been formally chartered by the Chairman and has been meeting monthly since March 2004. The purpose of the ITSC is to ensure an agency-wide approach to leveraging information technology in support of the mission critical activities of the FCC. In addition, the ITSC will prescribe policy and responsibilities for IT capital planning and investment processes throughout the FCC.

Revenue Gap

The FCC made substantial progress in the assessment and billing of regulatory fees. In particular, the Commission implemented the following measures: directly billed satellite licensees and interstate service providers (the largest fee category), instead of notifying them of charges through a general public notice; assessed fees on CMRS licensees and cable owners for the first time; and mailed postcards to media licensees and their legal representatives. We expect to directly bill the media licensees in FY 2005.

Based upon the agency's best current understanding of the universe of regulatory fee payers, we believe that the billing and assessment of interstate service providers, CMRS, cable, satellite and media licensees represents in excess of 94% of all regulatory fees owed. Specific recommendations for improving the agency's collection process are being considered in FY 2005.

Physical Security and Protection of Personnel

The COOP was developed and practiced in FY 2002, including a tabletop exercise involving about 50 FCC personnel at all levels. In FY 2003, the FCC's disaster recovery plan (DRP) was developed and initial information technology and telecommunications testing was conducted. During FY 2004, briefings for essential personnel were conducted in February, another tabletop exercise was conducted in March, and the FCC participated in the first-ever government-wide COOP exercise, Forward Challenge, in May. Forty-four agencies and 4,000 staff from across Government participated in that exercise, designed to further improve COOP and DRP execution. The FCC is planning to participate in Pinnacle 2005, an even larger-scale COOP exercise next May. Each time we conduct a COOP or DRP briefing, tabletop exercise, or actual deployment, the underlying documents and processes are revised based on lessons learned and best practices.

The FCC appointed a task force in January 2002 to address recommendations regarding workplace violence. The task force developed a zero tolerance policy, the FCC Policy Statement on the Prevention of Workplace Violence, and distributed this policy to all employees and contractors in June 2002. In addition, the FCC established and trained an advisory Threat Assessment Team. The agency is currently conducting workplace violence briefings for all supervisors, managers and Contracting Officer’s Technical Representatives. To date, 97% of FCC supervisors and managers have attended this training.