

**MANAGEMENT LETTER**  
**AUD-FM-13-09**

To the Chief Financial Officer and Inspector General of the U.S. Department of State

Kearney & Company, P.C. (referred to as “we” hereafter), has audited the consolidated financial statements of the U.S. Department of State (Department) as of and for the year ended September 30, 2012, and has issued our report thereon dated November 15, 2012.<sup>1</sup> In planning and performing our audit of the Department’s consolidated financial statements, we considered the Department’s internal control over financial reporting and compliance in order to determine our auditing procedures for the purpose of expressing an opinion on the consolidated financial statements and not to provide assurance on internal control. Accordingly, we do not express an opinion on the effectiveness of the Department’s internal control related to financial reporting and compliance. We have not considered the Department’s internal control since the date of our report on the FY 2012 financial statements.

During our audit, we noted certain matters related to internal control over financial reporting and compliance that we considered to be material weaknesses or significant deficiencies under standards established by the American Institute of Certified Public Accountants. A material weakness is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity’s financial statements will not be prevented or detected and corrected on a timely basis. A significant deficiency is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness yet important enough to merit attention by those charged with governance.

Our report on internal control noted one material weakness related to financial reporting. Our report also described five matters related to internal control that we considered to be significant deficiencies: Foreign Service National after-employment benefits, property and equipment, budgetary accounting, unliquidated obligations, and information technology.

Our procedures were designed primarily to enable us to form an opinion on the Department’s consolidated financial statements and therefore may not have identified all internal control weaknesses that may exist. However, we would like to use the knowledge we gained during our audit of the financial statements to provide comments and suggestions that we hope can be useful to the Department.

Although not considered to be significant deficiencies, we noted certain other matters involving internal control and operations. These findings and recommendations, which are summarized in Appendix A, are intended to assist the Department in improving internal control or to result in

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<sup>1</sup> *Independent Auditor’s Report on the U. S. Department of State 2012 and 2011 Financial Statements* (AUD-FM-13-08, Nov. 2012).

other operating efficiencies. These findings and recommendations have been discussed with appropriate Department officials. Comments by Department management on this report are presented as Appendix B.

We appreciate the courteous and professional assistance provided by Department personnel during our audit. We would be pleased to discuss these comments and recommendations with the Department.

This letter is intended solely for the information and use of Department management, those charged with governance, and others within the Department and the Office of Inspector General and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in blue ink that reads "Kearney & Company". The signature is written in a cursive, flowing style.

March 5, 2013  
Alexandria, Virginia

## MANAGEMENT LETTER COMMENTS

### COMMENTS REPEATED FROM PRIOR YEAR

During the audit of the U.S. Department of State's (Department) FY 2011 financial statements, Kearney & Company, P.C. (referred to as "we" hereafter), identified matters that we reported in an internal control report<sup>1</sup> and a management letter.<sup>2</sup> The severity of one issue reported in the FY 2011 internal control report, calculation of voluntary contributions, had decreased sufficiently during FY 2012 for us to include the issue in this management letter rather than the FY 2012 report on internal control. The other findings included in this section were reported in the FY 2011 management letter. These findings remain open and were updated with information obtained during the audit of the Department's FY 2012 financial statements.

#### I. General Issue

##### Untimely Responses to Audit Requests

As part of the financial statement audit, we made requests for data and documentation in order to validate and substantiate account balances and transactions that support the Department's financial statements. In general, the data we requested should have been an integral component of the Department's internal control structure and therefore should have been readily available.

The Department did not always provide documentation in a timely manner. As of October 31, 2012, we had issued 1,035 audit requests with due dates prior to November 1, 2012. Of the total requests, 11 responses had not been received by October 31, 2012. Table 1 provides an overall summary of the response times for the 1,024 items that had been received.

**Table 1. Response Times for Audit Requests**

	Total Items Received as of 10/31/2012	Received by Due Date*	Received One Week or Less After Due Date*	Received Between One and Two Weeks After Due Date*	Received Between Two and Three Weeks After Due Date*	Received More Than Three Weeks After Due Date*
<b>Audit Requests</b>	1,024	693	170	58	46	57
<b>Percent</b>	100	68	17	6	4	5

\*We considered one week to be five business days.

We acknowledge the improvements made by the Department in providing documentation in a timely manner since FY 2011. Specifically, as of October 31, 2011, only 53 percent of audit requests had been received by the due date.

<sup>1</sup> *Independent Auditor's Report on the U.S. Department of State 2011 and 2010 Financial Statements* (AUD/FM-12-05, Nov. 2011).

<sup>2</sup> *Management Letter Related to the Audit of the U.S. Department of State FY 2011 Financial Statements* (AUD/FM-12-06, Mar. 2012).

We found that delays in providing documentation were caused by a number of factors. For instance, we noted that the Department sometimes had difficulties in obtaining information in a timely manner from overseas posts. We also found that the Department did not initiate action on requests with long lead times until the due date was approaching. In some cases, the Department did not respond to, or it provided inadequate responses to, our requests for information until formal notices of findings and recommendations were provided. Late responses may also be indicative of inaccurate or incomplete information. Additionally, the Department's records management practices were not standardized to properly store and maintain information for management review.

The inability to produce documentation supporting financial transactions can lengthen processing times for analyses and reconciliations, as well as increase the possibility of undetected errors. Delays in providing accurate financial information can lengthen financial reporting cycle times, which decreases the relevance of financial information to end users. Providing timely and accurate information to the financial statement auditors could potentially lead to cost savings in performing the audit.

This issue was initially reported in our FY 2010 management letter.

Recommendation:

We recommend that the Department

- Enhance its procedures to ensure that information is provided to the financial statement auditor in a timely manner.
- Ensure that standards for records management and retention are in place and are enforced.
- Proactively seek clarity on any unclear audit requests in order to facilitate the most efficient and effective means of gathering required documentation.

## **II. Fund Balance with Treasury**

### **Insufficient Fund Balance with Treasury Reconciliation Process**

Agencies are required to promptly reconcile Fund Balance with Treasury (FBWT) information in order to identify and resolve differences between the agency financial records and the Department of the Treasury (Treasury) fund balances. The Department maintains two cash reconciliation reports: the Global Financial Services-Charleston Cash Reconciliation Report and the Financial Reporting Analysis (FRA) Cash Reconciliation Report. These reports document final balances for each Treasury Account Fund Symbol for the applicable accounting period. Because of the disaggregated nature of the Department's operations, the FBWT reconciliation process involves the reconciliation of disbursements and collections processed both domestically and overseas as well as through third parties.

A suspense account is a temporary account used by agencies to record transactions with discrepancies until a determination is made on the proper disposition of the transaction. For

instance, the Department will record unreconciled differences identified during the FBWT reconciliation process in a suspense account until the discrepancies are resolved. Treasury allows entities with a justifiable business need to submit a request to use suspense accounts, which are only to be used as a temporary holding place for transactions that must be cleared within 60 days. The Department received a waiver from Treasury for continued use of its suspense accounts.

We obtained and reviewed the FRA Cash Reconciliation Report as of September 30, 2012, and identified 54 instances in which a variance existed between Treasury and Department fund balances. These variances amounted to a net difference of approximately \$12.7 million. However, when the absolute value of all variances was considered, the variance totaled approximately \$60.8 million.

We also found that the Department had balances in several suspense accounts that had not been researched and resolved within 60 days as required. Specifically, we identified 10 suspense accounts in which the balance remained unchanged during FY 2012.

The Department reconciled disbursements and collections at the transaction level monthly; however, the Department did not investigate and resolve all variances because the Department's policy required that variances be investigated only if the net aggregate variance was more than 2 percent of the total amount of FBWT. The Department did not consider the absolute value of the variances in this threshold. In addition, the Department did not have a complete history of transactions that it could compare with Treasury information, as data from previous financial systems were not available to the staff performing the reconciliations. These data restrictions continued to prevent the Department from fully reconciling the FBWT account. The Department also did not have appropriate controls in place to ensure all suspense activity was researched and resolved within the required 60 days.

Failure to implement timely and effective reconciliation processes could

- Increase the risk of fraud, waste, and mismanagement of funds.
- Affect the Government's ability to effectively monitor budget execution.
- Affect the Department's ability to accurately measure the full cost of its programs.
- Result in violations of the Antideficiency Act.
- Result in erroneous financial statements.

Because the Department performed its reconciliation based on net value rather than absolute value, the Department could significantly understate the total outstanding FBWT variance. In addition, by not resolving suspense account activity within the required 60 days, the Department was not in compliance with Treasury requirements.

This issue was initially reported in our FY 2009 management letter.

Recommendation:

We recommend that the Department enhance its Fund Balance with Treasury (FBWT) reconciliation process by

- Identifying older reconciling items and taking the appropriate actions to clear these items.
- Modifying its internal reconciliation policy to require that the absolute value of variances be considered rather than the net value and applying the 2 percent threshold for investigating variances at individual fund levels rather than at the FBWT level.
- Researching and resolving all balances in suspense accounts within 60 days.

### **III. Accounts Payable**

#### **Inaccurate Liability Calculation for Certain Voluntary Contributions**

The Department provides discretionary financial assistance, called voluntary contributions, to foreign countries, public international organizations, international societies, commissions, and other international organizations. The Bureaus of International Organization Affairs and Population, Refugees and Migration are responsible for the majority of voluntary contributions within the Department.

Federal agencies should record a liability for all amounts owed as of the financial statement date, including amounts owed for voluntary contributions. In addition, Federal agencies should record an advance for all funds provided for voluntary contributions that have not been expended by the recipient.

During FY 2012, the Department implemented a process to identify advances or liabilities related to voluntary contributions. We reviewed disbursements made during October 2012 and concluded that the liability estimate was reasonable. However, the Department did not recognize funds that had been advanced to one of the Department's largest recipients of voluntary contributions, the United Nations High Commissioner for Refugees (UNHCR). During our analysis of supporting documentation received from UNHCR, the organization indicated that it maintained a 1- to 2-month surplus of funds. Based on this information, the Department should have recorded an advance amount.

The majority of voluntary contributions are made to a small number of international organizations. The Department reviewed agreements and disbursement patterns over the previous three fiscal years and requested additional information from selected organizations to determine an amount to record for advances and liabilities related to voluntary contributions. The Department concluded that because UNHCR had stated that the payments received were used only for immediate needs, neither a liability nor an advance existed as of the end of the fiscal year. However, UNHCR also stated that it had maintained a surplus of funds. The Department did not follow up with the organization to determine whether an advance should have been estimated and recorded for UNHCR.

Based on the results of our audit, the Department made an adjustment of approximately \$67 million to correct the amount of voluntary contributions that was not recorded as an advance in its financial statements.

This issue was initially reported in our FY 2011 Report on Internal Controls.

**Recommendation:**

We recommend that the Department continue to strengthen its voluntary contribution estimation process. Specifically, the Department should

- Ensure that recipients of voluntary contributions understand the requests for information made by the Department to determine a liability or advance, such as clearly explaining key terms such as disbursement, expense, and immediate need.
- Validate the estimation methodology annually using actual data to confirm the predictive reliability of the methodology.
- Document and maintain support for the data and assumptions used to develop the voluntary contributions liability or advance estimate. The documentation should be sufficient and available to facilitate a review of the Department's assumptions and conclusions.

**IV. Payroll****Inadequate Control Over Personnel Records and Actions**

The Department has almost 30,000 full-time employees located domestically and overseas, including Civil Service, Foreign Service, and Foreign Service National (FSN) staff. Civil Service and Foreign Service employees are paid according to standard Federal Government pay scales using the Consolidated American Payroll Processing System (CAPPS). FSN employees are generally paid in local currency, and their salary and benefits are based on local prevailing practice, which is documented in each post's local compensation plan. FSN employees are paid using the FSN Payroll system.

Ensuring the sufficiency of controls over personnel-related activities is a key responsibility of managers. We identified control deficiencies related to maintaining personnel records, processing personnel actions and calculating benefits, and processing employee separations. This issue was initially reported in our FY 2009 management letter.

**Insufficient, Inconsistent, or Incorrect Personnel Record Documentation**

The Office of Personnel Management requires agencies, including the Department, to maintain up-to-date, complete, and correct personnel records for each employee. These personnel folders should include all benefit election forms, as well as any elections resulting in deductions to an employee's pay. In addition, the Department is required to review time and attendance (T&A) submissions for accuracy. Maintaining up-to-date personnel folders and reviewing T&A submissions for accuracy help ensure that employees are compensated only for actual hours worked and benefits earned.

To verify the accuracy of Civil Service and Foreign Service employee salaries and benefits, we assessed the completeness of personnel records for a sample of 78 employees. We noted the following discrepancies during our testing:



- Five employee timesheets were not provided.
- Four Request for Leave or Approved Absence Forms (Standard Form [SF]-71) were not provided.
- Four Life Insurance Election Forms (SF-2817) were not provided.
- Two Health Benefits Election Forms (SF-2809) were not provided.
- Seven Thrift Savings Plan election forms were not provided.
- In one instance, the sick leave hours reported on the SF-71 did not match the employee's sick leave hours on the Earnings and Leave Statement.
- In two instances, the Federal Employees' Group Life Insurance election selected on the SF-2817 did not match the election on the employee's Notification of Personnel Action (SF-50).
- In one instance, the election selected on the Thrift Savings Plan election form did not match the election on the employee's Earnings and Leave Statement.

As part of our contractual agreement with OIG, we chose an additional 35 employees for testing to assist the Office of Personnel Management in its financial statement audit. We noted the following discrepancies during our testing:

- Three SF-2817s were not provided.
- In two instances, the optional Federal Employees' Group Life Insurance elections on the SF-2817 did not match the elections on the SF-50.

The Department did not sufficiently oversee and review the documentation maintained in personnel files and T&A reports. Poor administrative control over the payroll cycle and lack of sufficient and updated supporting documentation in the Official Personnel File may lead to errors in employee pay, improper benefit elections, or increased benefit costs. Incomplete personnel records prevent the timely receipt of sufficient and accurate documentation when requested and hinder the prompt identification and remediation of errors.

#### Improper and Untimely Processing of Personnel Actions and Incorrect Benefit Calculations

The Department processes personnel actions when an employee is hired by the Department or an existing employee has a change in personnel status. These personnel actions are documented either on the SF-50 or on the Joint Form (JF) 62A (Personal Services Contracting Action). In addition, each pay period employees accrue leave benefits based on guidance issued by the Department or post.

We selected a sample of 78 payroll disbursements and 45 new hire personnel actions from CAPPS and 80 payroll disbursements and 50 new hire personnel actions from FSN Payroll to test controls over T&A, personnel actions, and hiring. For each of the sample items selected, we reviewed the SF-50 for proper and timely approvals. Additionally, for the sample items selected for T&A testing, we reviewed timesheets for proper approval and accurate processing. We also verified that the pay and benefit amounts were properly calculated and accrued.



During our testing of the CAPPs transactions, we noted the following:

- Eleven of 78 personnel actions in our payroll disbursement sample were not approved in the pay period following the effective date on the personnel action.
- One of 78 employees in our payroll disbursement sample elected health benefits using the SF-2809; however, no amounts were deducted or withheld from the employee's pay.
- Eight of 45 personnel actions in our new hire sample were not approved in the pay period following the effective date on the personnel action.

During our testing of the FSN Payroll transactions, we noted the following:

- Seventeen of 80 personnel actions in our payroll disbursement sample were not approved in the pay period following the effective date on the personnel action.
- One of 80 personnel actions in our payroll disbursement sample did not contain the date that the Human Resource Officer approved the personnel action. As such, we were unable to verify that the approval occurred prior to the effective date.
- Eight of 80 employees in our payroll disbursement sample were accruing annual or sick leave benefits at a rate inconsistent with the local compensation plan.
- One of 50 personnel actions in our new hire sample was not approved in the pay period following the effective date on the personnel action.

Each bureau and post had been delegated the authority to approve personnel actions and enter the information into the personnel system. We found that bureaus and posts were processing personnel actions inconsistently. The Department did not have a centralized process to ensure that bureaus and posts were approving employee actions and entering the information into the personnel system in a timely manner.

In addition, each post had been delegated authority to establish annual and sick leave policies for FSN employees. These policies were documented in the post-specific local compensation plan. We found that data used to process leave accruals was not always input into the FSN Payroll system correctly at the Department's Financial Service Centers. In addition, controls were not consistently in place at posts to ensure that the proper leave accrual rate was being applied.

The potential for improper payments exists if personnel actions are not processed properly or timely, and the potential for improper leave accruals exists when incorrect rates are entered into the payroll system. In addition, the lack of proper oversight of personnel actions may result in errors remaining undetected and uncorrected for long periods of time. Untimely personnel actions are often processed retroactively, leading to supplemental payments being processed manually and increasing the risk of human error and decreasing efficiency.

#### Improper and Untimely Processing of Separation Personnel Actions

When an employee separates from the Department because of resignation, retirement, or death, the Department processes personnel actions to document the employee's personnel status. These personnel actions are documented either on the SF-50 or on the JF-62A.

We selected a sample of 45 personnel actions for separations from CAPPS and 35 personnel actions for separations from FSN Payroll to determine whether the employees were removed from payroll, T&A, and personnel systems in a timely manner. We also verified that the personnel action was approved by the pay period following the proposed separation effective date.

During our testing of CAPPS transactions, we noted that

- 16 of 45 employees were not deactivated in the personnel system in the pay period following the separation effective date on the personnel action.
  - 3 of 16 employees not deactivated timely were paid incorrectly after the separation effective date on the personnel action.
- 15 of 45 personnel actions were approved after the pay period following the proposed separation effective date.

During our testing of FSN Payroll transactions, we noted that

- 6 of 35 personnel actions were approved subsequent to their effective dates.

Each bureau and post had been delegated the authority to approve personnel actions and enter the information into the personnel system. We found that bureaus and posts were processing personnel actions inconsistently. The Department did not have a centralized process to ensure that bureaus and posts were approving employee separations and entering the information into the personnel system in a timely manner.

The potential for improper payments exists if personnel actions are not processed properly or in a timely manner. We noted that three of the employees we tested were paid incorrectly after their separation dates. In addition, the lack of proper oversight of personnel actions may result in errors remaining undetected and uncorrected for long periods of time. Untimely personnel actions are often processed retroactively, which increases the risk of human error and decreases efficiency.

Recommendation:

We recommend that the Department strengthen controls over personnel records and actions. Specifically, the Department should

- Strengthen monitoring procedures that will ensure bureaus and posts are complying with policies for timely processing and appropriately approving personnel actions, including periodic reviews of documentation.
- Develop procedures to monitor employees' biweekly benefit amounts and ensure that the data used to calculate these amounts are accurate.
- Develop a process to conduct periodic reviews over personnel records.
- Institute mandatory training sessions on controls over personnel records for employees who process personnel actions and increase accountability for employees who process personnel actions at the bureaus and posts.

## V. Accounts Receivable

### Lack of Validation and Monitoring Controls Over Aged Unbilled Federal Accounts Receivable

Unbilled accounts receivable (AR) arise as revenue is recognized for services rendered that exceed the amounts that have been billed. The Department enters into reimbursable agreements with other Federal entities to agree to terms, conditions, and costs for services to be provided. Unbilled Federal AR transactions are created through the normal course of business when administrative timing issues exist; however, these transactions are also generated when necessary billing information is unavailable or when the cost of services exceeds the reimbursable agreement and the customer is not willing or is unable to cover those costs. According to Department policy, receivables over 90 days old are considered past due and should be escalated for further review.

We identified unbilled Federal AR amounting to \$593 million on the Department's September 30, 2012, trial balance. Although the Department's policy is to process undisputed bills for payment within 15 business days or resolve disputes within 30 days, we found that \$77.9 million of the \$593 million in unbilled Federal AR was over 6 months old, as shown in Table 2.

**Table 2. Aging of Unbilled Federal Accounts Receivable Over 6 Months Old**

Time Period	Number of Transactions	Amount (in millions)
Over 3 years	440	\$33.9
Between 2 and 3 years	91	5.0
Between 1 and 2 years	173	15.5
Between 6 months and 1 year	126	23.5
<b>Total Over 6 Months</b>	<b>830</b>	<b>\$77.9</b>

These transactions, some of which date back to FY 2002, were identified either as being collectible or as pending further research by the Department.

The Department had implemented a quarterly process to review significantly aged unbilled AR, which the Department defined as any unbilled AR more than 1 year old. Each quarter, staff in the Bureau of Budget and Planning assessed whether the significantly aged unbilled AR were valid and communicated this information to the Bureau of the Comptroller and Global Financial Services. The Bureau of the Comptroller and Global Financial Services should write off any transaction identified as invalid. However, we found that the majority of the AR reviewed during this process were identified as "pending further research." Although the Department had a process in place, the control was not being executed effectively, and as a result, aged AR were not being resolved in a timely manner. Further, Department officials were hesitant to write off aged AR, even aged AR from years in which the funding had expired, as the officials believed these AR may still be able to be collected.

In addition to the review process, the Department planned to take other actions to address the significantly aged unbilled AR. For instance, the Department anticipated including local guard services at post in the International Cooperative Administrative Support Services agreements with other agencies at posts by FY 2013. Because the local guard agreements are a common category of unbilled AR, this arrangement should decrease the number of unbilled AR in the future.

We also found that some of the unbilled AR occurred because the Department did not have the correct billing information for other agencies. The Department planned to review new reimbursable agreements, which have the potential to result in unbilled AR, and coordinate with the respective agency to ensure that accurate fiscal information for submitting bills is obtained prior to executing the agreement. In addition, the Department planned to write off unbilled AR from before 2007 once additional research was completed. As of September 30, 2012, the Department had not fully implemented these corrective actions.

The collection of outstanding AR represents a source of funds for an organization. By not managing aged unbilled AR in a timely and effective manner and not ensuring that new agreements contained the correct billing information, the Department was not collecting funds from other Federal agencies that it could use for Department priorities. The chance of collecting a receivable decreases the longer the receivable remains outstanding. Additional administrative efforts are needed to track and validate the items that have remained outstanding for a long period. In addition, by not identifying which unbilled AR items are uncollectible, the Department is overstating its assets in its financial statements.

This issue was initially reported in our FY 2011 management letter.

**Recommendation:**

We recommend that the Department continue to strengthen controls to ensure unbilled accounts receivable are valid and resolved in a timely manner. Specifically, the Department should

- Research and resolve all aged unbilled accounts receivable that are deemed “pending further research.”
- Develop a process to ensure reimbursable agreements are not executed without correct fiscal billing information.
- Take action to either collect aged unbilled accounts receivable or write off items that are not collectible.

**VI. Revenue**

**Inadequate Controls Over Machine Readable Visa Fee Analysis**

The Bureau of Consular Affairs (CA) is responsible for issuing non-immigrant visas, referred to as Machine Readable Visas (MRV), to foreign nationals at embassies and consulates. CA encourages posts to collect the MRV fees offsite to limit the Department’s cash collection responsibilities. Posts must maintain proper internal controls to ensure that the offsite locations

properly execute their duties on behalf of the Department by collecting fees when issuing MRV fee receipts and remitting all fees collected to the Department. To achieve this objective, CA directs each post to perform, at least weekly, an MRV fee analysis by comparing the fees collected with the number and type of services provided, as identified by records other than the fee receipts. The MRV fee analysis should ensure the cumulative amount of fees collected by the offsite location meets or exceeds the cumulative number of MRV applications processed by the post. The collections made at offsite locations directly affect revenue reported by the Department.

We tested the operating effectiveness of the weekly MRV fee analysis during FY 2012 at eight posts and noted exceptions at six posts. Specifically, as of May 2012, Embassy Seoul, Korea, had not completed its MRV fee analysis for March or April 2012. We also found that while a supervisory review was being conducted at this post, the review was not documented or evidenced on the weekly analysis. In addition, we noted instances of cumulative deficits at five other posts tested (Ottawa, Canada; Tokyo, Japan; Lima, Peru; Kingston, Jamaica; and Tel Aviv, Israel). Cumulative deficits occur when the cumulative number of fees collected is less than the cumulative number of visa applications processed. As of June 30, 2012, Embassy Ottawa had 22 weeks of cumulative deficits, and Embassy Lima had 13 weeks of cumulative deficits.

During FY 2012, CA took steps to improve the MRV fee analysis performed at posts by establishing and implementing a centralized review within its Office of the Comptroller. In July 2012, CA implemented a Sharepoint site in which posts would submit their weekly MRV fee analysis. The centralized review ensured that posts were completing the analysis and reviewing deficit balances. However, prior to implementing this centralized review, CA had no control in place to ensure that posts were completing the analyses accurately and in a timely manner.

While the centralized review procedures have improved the oversight of the fee analysis, control design issues have contributed to the cumulative deficits at posts. The Consular Consolidated Database tracked the visa workload counts for each post and was the source of the workload data for completing the analysis. However, the Consular Consolidated Database reports were neither standardized nor consistent across each post. CA officials stated that the reports used by posts for workload counts may have included the same visa applicant multiple times because of temporary visa application refusals. Although visa applicants paid the fee once, they were potentially included in the workload reports each time an application refusal was processed.

Without proper controls, cash collected at offsite locations could be misappropriated and not be deposited into the Department's accounts. In addition, the Department may not be able to detect inaccuracies in the amounts recorded for MRV fee collections.

This issue was initially reported in our FY 2011 management letter.

**Recommendation:**

We recommend that the Department

- Continue monitoring the Machine Readable Visa fee analyses prepared by posts and investigating the sources of cumulative deficits.
- Develop standardized Consular Consolidated Database reports that properly identify unique applicants.

**NEWLY IDENTIFIED COMMENTS**

During the audit of the Department's FY 2012 financial statements, some additional matters came to our attention that had not been reported in the FY 2011 internal control report or management letter.

**VII. Parent/Child Transactions****Insufficient Oversight of Financial Information Provided by the U.S. Agency for International Development**

The Department receives funds through appropriation legislation. In some cases, these appropriated funds are required to be transferred to another agency for programmatic execution. Despite transferring these funds, referred to as "child funds," to another agency, the Department maintains responsibility for reporting on their use and status in its annual financial statements. The U.S. Agency for International Development (USAID) receives a significant amount of child funds from the Department. Each quarter, USAID provides the Department with balances from its general ledger for inclusion in the Department's financial statements.

USAID's OIG has reported a longstanding material weakness related to the reconciliation of FBWT, which would include the child funds from the Department. Specifically, USAID has been unable to successfully reconcile the FBWT amount in the general ledger with the fund balance amount reported by Treasury or to its own subsidiary ledger. In FY 2012, USAID performed an analysis to quantify the differences between the three amounts and recorded adjustments so the Treasury and general ledger amounts equaled the amount recorded in USAID's subsidiary ledger. USAID also analyzed differences between the Advance amounts recorded in the general ledger and subsidiary ledger and adjusted the general ledger amounts to match the subsidiary ledger. The impact these adjustments would have had on the Department's financial statements is shown in Table 3.

**Table 3. Impact of Adjustments From the U.S. Agency for International Development on the Department's Financial Statements**

Financial Statement	Line Item	Adjustments (in Millions)
Balance Sheet	FBWT	\$(95.3)
	Advances	167.0
	Unexpended Appropriations	(71.7)
Statement of Budgetary Resources	Outlays	96.3
	Unpaid Obligations	(96.3)
Statement of Net Costs	Expenses	(72)
	Revenues	\$72

USAID was unable to identify the specific transactions that caused the differences or to determine the root cause of the unreconciled items. In November 2012, USAID informed the Department that it had identified an issue with the methodology it used to calculate the adjustments and stated that the adjustments might be reduced once it had an opportunity to refine its process.

The Department relied on USAID to report accurate balances; however, the amounts provided by USAID included adjustments that were not supported. The Department did not have an effective, routine process to ensure that amounts reported by USAID were complete and accurate. The Department did not have an effective way to communicate with USAID to obtain information regarding the amounts reported.

USAID may have recorded inaccurate or unsupported adjustments that went undetected by the Department. Inaccurate adjustments could result in a material misstatement in the Department's financial statements. The Department reversed the USAID adjustments during the preparation of its FY 2012 financial statements.

**Recommendation:**

We recommend that the Department

- Work collaboratively with the U.S. Agency for International Development (USAID) to determine what, if any, adjustments are needed to resolve the differences in Fund Balance with Treasury and Advances between the Department of the Treasury and USAID's general and subsidiary ledgers and adjust the balances as appropriate.
- Expand the process used to perform analytical procedures over the balances reported by USAID and inquire about significant changes to account balances.
- Develop a communication protocol for obtaining accounting information for child funds from USAID, including a requirement that USAID should provide supporting documentation for adjustments to Department funds over an agreed-upon materiality threshold, and specific documentation standards for adjustments recorded to Department funds.



**VIII. Required Supplementary Information****Inadequate Process To Identify and Measure Deferred Maintenance**

The Department occupies government-owned or long-term leased real properties at more than 270 overseas locations. The Department also owns several pieces of domestic real property, including the National Foreign Affairs Training Center in Arlington, Virginia; the International Center in Washington, D.C.; the Financial Services Center in Charleston, South Carolina; the Information Management Center in Beltsville, Maryland; and the Florida Regional Center in Ft. Lauderdale, Florida. The Department also owns consular centers in Charleston; Portsmouth, New Hampshire; and Williamsburg, Kentucky.

The Department did not have a process in place to measure and report deferred maintenance for domestic properties. Although the Department used a condition assessment survey to evaluate property conditions and determine the repair and maintenance requirements for its overseas buildings, we identified over 50 overseas deferred maintenance items, amounting to approximately \$9 million (12 percent of the amount reported by the Department for deferred maintenance), that did not, according to the items' descriptions, meet the definition of deferred maintenance. For instance, the description of some of the items appeared to relate to improvements or upgrades rather than to maintenance.

According to Department officials, the Department receives sufficient funding for domestic maintenance and repairs. The officials did not believe that any domestic deferred maintenance could exist. Although the Bureau of Overseas Buildings Operations had developed a process to identify maintenance and repair needs overseas, the process did not always adequately differentiate maintenance and repairs from upgrades.

Without a process to review the condition of domestic real properties and sufficiently estimate deferred maintenance and repairs for overseas properties, the information in the Department's Agency Financial Report may be incomplete or inaccurate.

**Recommendation:**

We recommend that the Department strengthen controls to ensure that deferred maintenance is accurately identified and measured. Specifically, the Department should

- Develop and implement a process to measure and report on deferred maintenance for domestic properties.
- Improve the process for identifying deferred maintenance for overseas properties to ensure that only deferred maintenance items are reported.




United States Department of State  
*Comptroller*  
1969 Dyess Avenue  
Charleston, SC 29405

**FEB 20 2013**

UNCLASSIFIED

**MEMORANDUM**

TO:           OIG – Harry W. Geisel

FROM:       CGFS – James L. Millette 

SUBJECT:   Draft Management Letter Related to the Audit of the Department of State's Fiscal  
Year (FY) 2012 Financial Statements

This is in response to your request for comments on the Independent Auditor's Draft Management Letter (Letter) related to the audit of the Department of State's (Department) FY 2012 Financial Statements.

The Department concurs in concept with the Letter's recommendations. We believe the Letter identifies areas where processes and internal controls can be strengthened to improve the Department's financial reporting and operations. We will work collaboratively and constructively with your office and Kearney & Company on the recommendations identified in the Letter to implement improvements and address these matters. As we work with Kearney to identify the needed corrective actions, we may propose alternative means to address the spirit of the recommendations versus the specific recommendations proposed in the Letter. We may also identify situations where the cost to implement a specific part of a recommendation may exceed the projected benefit. Regardless, we are committed to build on the progress made over the last year.

We thank you for the opportunity to comment on the draft Letter. We would also like to extend our appreciation to your staff and to Kearney & Company for the professional and collaborative manner in which they conducted the audit. We believe considerable progress was made over the past year, especially related to the Department's financial reporting of after-employment benefits for LES we employ around the world, as a result of the collaborative manner in which the audit was conducted.

cc:    M – U/S Patrick F. Kennedy  
      OIG/AUD – Ms. Evelyn Klemstine  
      Kearney & Company, P.C. – Mr. Jeffrey W. Green  
      CGFSDCFO – Christopher H. Flaggs  
      CGFS/EX – Phillip J. Schlatter

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