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BY THE U.S. GENERAL ACCOUNTING OFFICE

Report To The Secretary Of Transportation

Transportation's First-Year Implementation Of The Federal Managers' Financial Integrity Act

GAO reviewed the processes used by 22 federal agencies to implement the Federal Managers' Financial Integrity Act of 1982. The act was intended to help reduce fraud, waste, and abuse across the spectrum of federal government operations by requiring agencies to assess and annually report on the adequacy of their internal controls and accounting systems.

This report highlights the progress and problems encountered by the Department of Transportation in its first year of experience with this new act. The report focuses on Transportation's evaluation of internal controls and reviews of accounting systems and the improvements being made as a result of identified problems. Transportation agreed with GAO's proposals to improve its efforts to implement the act.



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

RESOURCES, COMMUNITY,
AND ECONOMIC DEVELOPMENT
DIVISION

B-202205

The Honorable Elizabeth H. Dole
The Secretary of Transportation

Dear Madam Secretary:

This report presents the results of our review of the processes used by the Department of Transportation to implement the Federal Managers' Financial Integrity Act (FMFIA) of 1982. Transportation was one of 22 agencies we reviewed to assess governmentwide compliance with the act during its first year.

The act establishes a governmentwide framework for improving and monitoring the effectiveness of financial management in executive agencies. Section 2 of the act requires each agency to conduct evaluations of its systems of internal controls in accordance with guidelines issued by the Office of Management and Budget (OMB) and to report annually in a statement to the Congress and the President on whether internal controls comply with standards prescribed by the Comptroller General.

The act also added requirements for federal agencies to operate effective accounting systems. Under section 4 of the act each agency is required to include in the above annual statement a report on whether its accounting systems conform to the principles and standards for accounting developed by the Comptroller General.

The following summarizes the results of our review. Appendix I contains details of our work.

INTERNAL CONTROL EVALUATION EFFORTS

Concerning section 2 of the act, your December 23, 1983, statement to the President and the Congress disclosed that Transportation's system of internal control, taken as a whole, provides reasonable assurance that overall internal control objectives were met. The statement identified various material weaknesses, including two Department-wide material internal control weaknesses in the automated data processing area dealing with security and risk analysis of facilities. The statement

also identified material weaknesses at various administrations-- Urban Mass Transportation, Federal Aviation, Federal Highway, Federal Railroad, Maritime, and Coast Guard--including weaknesses in the grants program and grantee control areas and management and maintenance of electronic systems. (See app. II.)

OMB guidelines outline the following basic approach to evaluate, improve, and report on internal controls: (1) organizing the internal control evaluation process, (2) segmenting the agency to create an inventory of assessable units, (3) conducting vulnerability assessments, (4) reviewing internal controls, (5) taking corrective actions, and (6) reporting on the adequacy of internal controls and plans for corrective action.

Transportation has made progress in complying with OMB's guidelines considering the scope and divergent nature of its programs and activities. Aspects of the Department's implementation efforts were noteworthy, including top management support and some efforts by individual administrations.

In implementing the FMFIA process, Transportation delegated FMFIA authority to the Assistant Secretary of Transportation for Administration. The Director of the Office of Management and Planning was later delegated direct responsibility for implementing the internal control requirements. Subsequently, responsibility for the process was further delegated to the secretarial officers and the various administrators--Federal Aviation, Urban Mass Transportation, Federal Highway, Federal Railroad, Maritime, St. Lawrence Seaway Development Corporation, National Highway Traffic Safety, Coast Guard, and Research and Special Programs. OMB guidelines and GAO standards were distributed, and a planning guide was developed on internal control responsibilities for administrators and program managers. Workshops were held in July and August 1983.

Each administration identified assessable units. Segmenting was done based on existing organization structures and programs. In some cases the process was done wholly at headquarters, and in others the field offices were included. Responsible officials and program managers generally completed vulnerability assessments.

Although Transportation's offices and administrations developed their own processes for evaluating internal controls, they generally followed OMB guidance. Headquarters developed a pamphlet and questionnaires to assist the offices and administrations in conducting internal control reviews and is developing a process for tracking corrective actions. The Office of

Inspector General (OIG) provided technical assistance and guidance, participated in workshops dealing with the process, and completed two audits of the process.

Notwithstanding the above progress, our review showed that Transportation could improve its FMFIA efforts by providing better central direction of the internal controls evaluation process. We recognize that the Department operates in a decentralized manner and that it has delegated responsibility for the program to the secretarial offices and administrations. However, we found that:

- The Department has not developed written procedures regarding the internal control process prescribed by section 2 of the act. The Department issued a basic implementing order delegating responsibility for the process to the Transportation offices and administrations and distributed available OMB guidance and GAO standards requirements. The offices and administrations have not developed adequate written procedures of their own.
- While the Department has acknowledged the need to better document the vulnerability assessment process it has not prescribed specific procedures on what documentation is needed. The result has been a general lack of and inconsistency in documentation which precludes comparison of the effectiveness of the assessments made by the Transportation offices and administrations and the need for corrective action. The Department has stated that there is a need for specific guidance from OMB on how to adequately document the evaluation process.
- Vulnerability assessments completed by the offices and administrations could not be readily related to internal control reviews or other corrective actions taken or planned, since they often did not cover the same program and organizational segments.
- FMFIA training was provided after the Department's first-year segmenting and vulnerability assessment process was almost entirely completed and dealt primarily with internal control reviews. Not all staff members who should have been trained participated.
- A systematic process for reporting internal control review results and following up on corrective actions had not been established by the Department at the time of our review. However, the Department plans to establish a reporting and tracking system and is considering where it

will be operated--at Transportation headquarters or at each of the offices and administrations.

- The Department identified major weaknesses in its first internal controls year-end statement. Other major weaknesses may not have been included, however, because (1) what should be considered a material weakness was not adequately defined by the Department in accordance with OMB guidance and (2) the assessments that were completed did not cover all of the Department's organizations and functions.
- The Office of Inspector General's role at the Department with regard to FMFIA was to provide technical assistance and guidance in the process. During the Department's first-year internal control effort, that role had been primarily as an advisor. Details of the Office of Inspector General's functional responsibilities with regard to internal controls requirements are not defined in separate instructions to the offices and administrations. A better definition of the Office of Inspector General's role with regard to the internal control process would assist the offices and administrations in outlining their own responsibilities for the process.

Accordingly, in a draft of this report we proposed that the Secretary direct the Assistant Secretary for Administration to assert a stronger central role over the Department's offices and administrations in their FMFIA internal controls implementation efforts and

- develop written procedures for the FMFIA processes, including suggested standard forms, criteria, and documentation requirements;
- provide for additional staff development and training in implementing FMFIA requirements;
- establish a Department-wide corrective actions follow-up system; and
- in accordance with OMB guidance, develop criteria for determining what material internal control weaknesses reported to the Department by the offices and administrations should be included in the Secretary's year-end statement to the Congress and the President.

We also proposed that the Secretary of Transportation work with the Office of Inspector General to more specifically define OIG's role in the internal control process.

ACCOUNTING SYSTEMS' COMPLIANCE EFFORTS

In contrast to the act's section 2 internal control requirements for which the Office of Management and Budget furnished guidelines, no specific guidance was provided to federal agencies regarding the steps necessary to determine their accounting systems' compliance with the Comptroller General's Accounting Principles and Standards. Transportation developed a checklist based on these principles and standards which was used as the basis for determining the systems' compliance. The Department's efforts, in our view, represent a good faith first-year effort to comply with the act's section 4 requirements.

In your December 23, 1983, annual statement, you reported that Transportation's accounting systems conformed to the Comptroller General's principles and standards except as follows:

- Twelve systems were conforming generally to the principles and standards but had some "principal" instances of nonconformity.
- Two systems were reported as being in overall nonconformity with the principles and standards.

Most reported material deviations from the principles and standards were common to several administrations and offices and related to (1) accountability over property, (2) accrual of expenditures, (3) accounting systems documentation, and (4) internal financial reporting. (See app. II.)

With respect to the process used to comply with section 4 of the act, we found that the Department did not

- incorporate testing procedures into its systems compliance evaluations or
- develop specific procedures and guidance for consolidating the administrations' reports into the Department's overall statement and for ensuring that the results of all section 2 and section 4 work are fully considered for reporting.

As a result, in our draft of this report we proposed that the Secretary direct the Assistant Secretary for Administration to (1) require the administrations to incorporate system testing into Transportation's compliance evaluation procedures and ensure that all accounting systems are documented, and (2) strengthen guidance and procedures for consolidating individual administration reports into Transportation's overall

annual statement and ensure that the results of all section 2 and section 4 work are considered for inclusion in the annual statement.

AGENCY COMMENTS AND OUR EVALUATION

In its June 4, 1984, comments on a draft of this report (see app. III), Transportation concurred with our proposed corrective actions and stated that it is making efforts to improve its internal control and accounting programs in accordance with our findings and proposals.

We are pleased with Transportation's response to our proposals and believe Transportation's comments show a strong commitment to the effective implementation of the act. Because of the Department's responsiveness, we have not included any recommendations in this report. We plan to monitor the Department's progress as part of our continuing reviews of federal agencies' implementation of FMFIA.

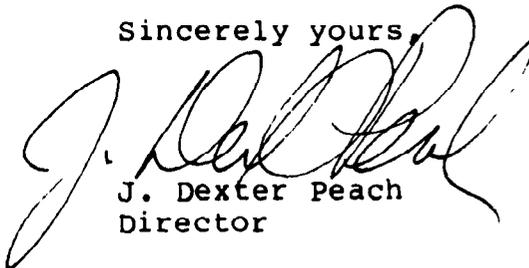
As Transportation makes additional progress in implementing the internal control and accounting system requirements of the act and in correcting known weaknesses, and as it makes the improvements it has planned in response to our proposals, it should have a more meaningful basis for determining whether its internal controls and accounting systems meet the objectives of the act.

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We are sending a copy of this report to appropriate congressional committees; the Director, Office of Management and Budget; and other interested parties.

We appreciate the cooperation extended to our staff during our work and look forward to the same spirit of cooperation in subsequent review efforts.

Sincerely yours,



J. Dexter Peach
Director

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ABBREVIATIONS

ADP	automated data processing
AMTRAK	National Railroad Passenger Corporation
CG	Coast Guard
DOT	Department of Transportation
FAA	Federal Aviation Administration
FHWA	Federal Highway Administration
FMFIA	Federal Managers' Financial Integrity Act
FRA	Federal Railroad Administration
GAO	General Accounting Office
ICR	internal control review
OIG	Office of Inspector General
MARAD	Maritime Administration
NHTSA	National Highway Traffic Safety Administration
OFM	Office of Financial Management
OMB	Office of Management and Budget
RSPA	Research and Special Programs Administration
SLSDC	Saint Lawrence Seaway Development Corporation
UMTA	Urban Mass Transportation Administration

TRANSPORTATION'S FIRST-YEAR IMPLEMENTATION OF THE
FEDERAL MANAGERS' FINANCIAL INTEGRITY ACT OF 1982

INTRODUCTION

Responding to continuing disclosures of fraud, waste, and abuse across a wide spectrum of government operations, which were largely attributable to serious weaknesses in agencies' internal controls, the Congress in 1982 enacted the Federal Managers' Financial Integrity Act (FMFIA) (31 U.S.C. 3512(b) and (c)). The act strengthens the existing requirement of the Accounting and Auditing Act of 1950 that executive agencies establish and maintain systems of accounting and internal control in order to provide effective control over, and accountability for, all funds, property, and other assets for which the agency is responsible (31 U.S.C. 3512(a)(3)).

GAO believes that full implementation of the act will enable the heads of federal departments and agencies to identify their major internal control and accounting problems and improve controls essential to the development of an effective management control system and a sound financial management structure for their agencies.

The act requires that:

- Each agency establish and maintain its internal controls in accordance with the standards prescribed by the Comptroller General,¹ so as to reasonably assure that (1) obligations and costs comply with applicable law, (2) all funds, property, and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation, and (3) revenues and expenditures applicable to agency operations are recorded and properly accounted for.
- Each agency evaluate and report annually on internal control systems. The report is to state whether agency systems of internal control comply with the objectives of internal controls set forth in the act and with the standards prescribed by the Comptroller General. Where systems do not comply, the act also provides for agency statements to identify the material weaknesses involved and describe the plans for corrective action.
- Each agency, as part of its annual statement, include a separate report on whether the agency's accounting systems conform to the principles, standards, and related requirements prescribed by the Comptroller General.

¹The Comptroller General issued Standards for Internal Controls in the Federal Government in June 1983.

--The Office of Management and Budget (OMB) issue guidelines for federal departments and agencies to use in evaluating their internal control systems. These guidelines were issued in December 1982.

OMB's internal control guidelines outline a phased approach to be used by agencies for evaluating, improving, and reporting on their internal controls:

1. Organize the internal control evaluation process, including overall planning and direction, assigning responsibilities, and developing an information system to monitor and track the status of evaluations and corrective actions.
2. Segment the agency into organizational units, programs, and functions.
3. Assess the vulnerability of the individual segments (assessable units) to fraud, waste, and abuse and decide which segments are most vulnerable.
4. Review the internal controls for the selected activities and develop recommendations to correct identified weaknesses.
5. Take corrective actions to improve the internal controls.
6. Prepare the required annual statement to the President and the Congress on the status of the agency's system of internal control.

This report on the Department of Transportation (DOT) is one of 22 reports on the processes used by executive agencies to implement the act.

BACKGROUND ON DOT AND ITS INTERNAL
CONTROL AND ACCOUNTING SYSTEMS
COMPLIANCE EVALUATION PROCESSES

DOT was established in 1966. Its mission is to develop national transportation policies and programs conducive to fast, safe, efficient, and convenient land, air, and water transportation at the lowest cost. Organizationally it is made up of the Office of the Secretary of Transportation and related staff organizations, five assistant secretaries of transportation, and nine semi-autonomous administrations--Federal Aviation Administration (FAA), Coast Guard (CG), Urban Mass Transportation Administration (UMTA), Federal Highway Administration (FHWA), Federal Railroad Administration (FRA), Maritime Administration (MARAD), Saint Lawrence Seaway Development Corporation (SLSDC), National Highway Traffic Safety Administration (NHTSA), and Research and Special Programs Administration (RSPA). For fiscal year 1984, DOT has estimated civilian and military positions at about 101,000. Its fiscal year 1984 budget authority is estimated at about \$28.6 billion.

How DOT implemented internal controls requirements

By separate orders (DOT Order 5100.4, dated March 31, 1982, and DOT Order 5100.4a, dated November 7, 1983), responsibility for the internal control process was delegated to the DOT offices and administrations, which were also later provided copies of OMB's guidelines, the GAO standards, and a DOT planning guide on completing internal control reviews. Earlier, in February 1982, prior to the enactment of FMFIA, DOT initiated OMB circular A-123 internal control requirements, including conducting vulnerability assessments and internal control reviews. Using various methods, each of the offices and administrations independently divided their organizations into segments and assessable units.

DOT provided general guidance on how to complete the vulnerability assessment process. The offices and administrations then developed their own forms, questionnaires, rating systems, and quality assurance procedures. Generally OMB guidance was followed, but the approaches used varied. Most vulnerability assessments² were done by program managers or by others with knowledge of the functional areas being assessed. Individuals we interviewed had some knowledge of internal controls and related requirements. Staff training, dealing primarily with internal control reviews (ICRs), was provided in July and August 1983. DOT's Office of Inspector General (OIG) was available to provide technical assistance when requested and also commented on DOT guidance as it was developed and participated in training sessions.

DOT prepared a guide and sample questionnaires to assist in developing ICRs. Some administrations issued separate ICR implementing orders. The results of the vulnerability assessments, GAO and OIG audits, other DOT studies and reviews, and the general background knowledge of responsible officials were used in selecting areas to receive ICRs. DOT has estimated that it will perform about 130 ICRs. DOT is developing a process for tracking corrective actions resulting from ICRs.

DOT'S accounting systems compliance evaluations

The Director, Office of Financial Management (OFM), under the Assistant Secretary for Administration, organized and directed DOT's accounting systems compliance evaluations. The

²DOT did not develop an agencywide inventory of assessable units and their vulnerability ratings. About 300 highly vulnerable assessable units were identified for "further review."

Director's office prepared written guidelines for the evaluations, assigned responsibilities, consolidated and summarized evaluation results, and included senior accounting officials throughout the process. The process required senior accounting officials to develop an inventory of accounting systems along with systems background data.

Accounting officials were responsible for evaluating each accounting system under their control for compliance with the Comptroller General's principles and standards. The accounting officials and other senior financial management personnel applied their personal knowledge of each accounting system to a checklist of GAO's accounting principles and standards. Deviations disclosed were listed along with planned corrective actions and a schedule for their implementation. DOT is developing a followup system to track corrective actions.

Year-end statement

To develop its year-end statement, DOT required all offices and administrations to submit a list of both uncorrected and corrected material internal control weaknesses. The material weaknesses were identified based on the vulnerability assessments and ICRs done and previous OIG and GAO audit reports as well as other evaluations and management's general awareness of weaknesses. The Office of the Assistant Secretary for Administration in conjunction with OIG then assessed the information reported to decide what to include in the Secretary's statement. Many of the reported material weaknesses were determined to be minor or not representative and were not included in the Secretary's statement. In the December 23, 1983, statement, the Secretary reported that the DOT-wide evaluation of systems of internal controls was accomplished in accordance with both OMB guidelines and GAO standards and that DOT's system of internal control, taken as a whole, provides reasonable assurance that overall control objectives were met and that all material weaknesses had been identified and reported.

The Secretary's statement identified two DOT-wide material weaknesses for which corrective actions are planned. Both are in the automated data processing (ADP) area, dealing with (1) inventories of security-sensitive ADP uses and applications and (2) risk analyses of computer facilities. The statement also identified corrective actions which had been taken on material weaknesses at five of the administrations in the financial management, property, ADP, and accounting areas as well as planned corrective actions to be taken (see app. II). Planned corrective actions, as reported in the Secretary's year-end statement, include

--management and maintenance of electronic systems and marine response fund operations,

- guidance for use in certification of disadvantaged businesses for preferential consideration on government contracts and state employment of consultants,
- grants program management and grantee controls over real property and buses,
- repair contracts on schoolships, and
- the energy conservation program.

In the year-end statement the Secretary also stated that in the future DOT will (1) maintain a more centralized oversight of the assessments and reviews to be conducted and (2) implement a more consistent segmentation and analysis methodology.

In early November 1983, the nine administrations and offices reported the results of their accounting system compliance evaluation work. Based on this, the Secretary reported in the annual statement that accounting systems in place as of December 31, 1983, generally conform in all material respects to the Comptroller General's principles and standards except as follows:

- Twelve systems were conforming generally to the principles and standards but had some "principal" instances of nonconformity.
- Two systems were reported as being in overall nonconformance with the Comptroller General's principles and standards.

Most reported material deviations from the principles and standards were common to several administrations and related to (1) accountability over property, (2) accrual of expenditures, (3) accounting systems documentation, and (4) internal financial reporting. The reports described each case of nonconformity and usually specified the principle or standard involved. Each administration's report described actions planned to correct identified deviations from the principles and standards.

OFM consolidated the administrations' reports into the Secretary's overall statement on DOT's conformity to the Comptroller General's principles and standards. The overall statement was consistent with the conclusions of the administrations' separate reports.

OBJECTIVES, SCOPE, AND METHODOLOGY

Our review objective was to assess DOT processes for evaluating internal control and accounting systems for purposes of reporting under the act. Our work was done primarily at DOT headquarters, Office of the Assistant Secretary for Administration, and at the headquarters offices of FAA, CG, FHWA, UMTA,

MARAD, NHTSA, RSPA, and FRA. To broaden the scope of our coverage, field work was completed on FAA in the Chicago, New York, and Boston regions; FHWA in the Kansas City and Albany regions and division offices in Albany, Trenton, Providence and Topeka; UMTA in the Boston, New York, and Chicago regions; and RSPA at the Transportation Systems Center in Cambridge, Massachusetts. Our review work was conducted from June 1983 through February 1984.

Because our first-year review was limited to an evaluation of the implementation process, we did not attempt to independently determine the status of DOT's internal control system or the extent to which DOT's accounting systems comply with the Comptroller General's principles and standards.

We obtained and reviewed documentation developed by DOT and the various administrations, including copies of vulnerability assessments, ICRs, and accounting system compliance evaluation results. We reviewed OMB files accumulated during its monitoring of DOT's progress in meeting the act's requirements as well as copies and extracts of past GAO and OIG reports, special studies, and congressional reports on DOT actions covering the last 2 fiscal years.

We interviewed officials responsible for coordinating the FMFIA process at their respective organizations, staff who carried out the evaluations, and representatives of the Office of Inspector General. We discussed the methodologies employed and guidance provided in performing the evaluations. We also reviewed written instructions made available to the office or the operating unit where the evaluations were completed and examined supporting documentation and other available records substantiating the review work done.

We also reviewed DOT's efforts to evaluate controls relating to ADP operations because of ADP's integral role in DOT activities. We reviewed DOT's ADP control efforts at DOT headquarters and at CG, FAA, and UMTA headquarters.

We conducted our work in accordance with generally accepted government auditing standards.

**BETTER CENTRAL GUIDANCE AND DIRECTION
IN EVALUATING INTERNAL CONTROLS IS NEEDED**

We found that the various DOT offices and administrations were not consistent in how they carried out their evaluations of internal controls. The lack of consistency made it difficult for DOT to assess the condition of its internal controls and the need for corrective actions. We recognize that DOT's offices and administrations are semi-autonomous and that the Assistant Secretary for Administration who has responsibility for the FMFIA process has little line authority over them. However, we

believe that, to effectively implement the act, strong central direction is needed.

Based on our review, we believe certain areas in the internal control evaluation process merit further attention by DOT. More specifically, there is a need for written procedures and guidance in carrying out the internal control evaluation process, vulnerability assessments need to be fully documented, and internal control reviews need to be directed at the more vulnerable organizational units or functions.

Our work also showed that DOT (1) needs to better develop staff skills on internal control activities, (2) work with the Office of Inspector General to better define the Office of Inspector General's role, (3) develop a followup and tracking system, and (4) establish criteria on including material weaknesses in its year-end statement.

Need for written procedures and guidance

DOT did not develop written procedures regarding the internal control evaluation process. DOT's basic implementing orders delegated full responsibility for the process to the offices and administrations, yet no detailed guidance was provided. Similarly, the offices and administrations did not develop adequate written procedures. Nor did DOT provide an adequate definition of an assessable unit. The definitions applied by the administrations were inconsistent. MARAD for example, defined an assessable unit as a program, administrative function, or subdivision which is the subject of a vulnerability assessment, while FHWA considered an assessable unit as an organizational component with a potential for more than low inherent risk. The result was that not all organizational and functional activities of the offices and administrations were included in the inventories of assessable units.

OMB guidelines provide for coverage of all agency activities and functions in the segmenting and vulnerability assessment process. DOT, however, did not describe how the offices and administrations were to segment their programs, functions, and administrative activities. Each administration independently embarked on the segmenting process and the identification of assessable units. In some cases segmenting was done at headquarters, as was the case at CG, and in other cases the field offices were included, as at FHWA.

At FAA, FRA, and MARAD, organizational components identified on the administration's basic organizational chart were considered segments, resulting in excessively large and unmanageable segments. NHTSA, though using its basic organizational chart, omitted from coverage in its segmenting process 7 of 10 regional offices and did not cover two of its field research offices. NHTSA did not always include grant program

activities in its assessable units inventory and did not establish assessable units at the seven regional offices and two field research offices which were omitted in the segmenting process. At our request, NHTSA reconciled its assessable units to its approximately \$200 million budget and identified about \$113 million of program activity not included in its assessable units inventory.

At one FHWA regional office, only one of four division offices was segmented, even though each division office covered individual statewide operations. FRA took each of its basic organizations and considered them to be assessable units. The result was that FRA evaluated as single assessable units \$780 million in grants to the AMTRAK passenger train corporation made in fiscal year 1983, and the billion dollar northeast corridor railroad improvement program.

Similarly, since no written procedures had been prescribed, the administrations took differing approaches on ADP coverage. CG, for example, performed all of its ADP related reviews at headquarters and did not include in the segmenting-assessable units process 46 different ADP systems located at 28 of its major field locations.

Need for documenting vulnerability assessments

While DOT has acknowledged the need for documenting its vulnerability assessments, it has not prescribed what documentation it considers necessary. The result is a general lack of and inconsistency in the documentation of the process among the DOT offices and administrations, and an inability on the part of DOT management to review the effectiveness of assessments made.

OMB guidelines on documentation were general, stating that the FMFIA processes should be documented. In its internal control guidance, DOT stated that the objectives, control techniques, and accountability for the resources involved for all transactions and operations being assessed should be documented and that the risks to be guarded against and the objectives to be accomplished by the control techniques should be identified. Suggested vulnerability assessment forms included with the OMB guidelines were to be adapted to facilitate an adequate documentation process. The guidance and materials provided were offered as assistance to the program managers and administrators.

Each of the administrations followed its own documentation criteria in completing its vulnerability assessments. The following describes the extent of documentation associated with vulnerability assessments at three of the largest DOT administrations.

Federal Aviation Administration

FAA developed a vulnerability assessment form but made its use optional. FAA's instructions provided that any reasonable method for completing and documenting the assessments would be acceptable. Further, FAA headquarters did not require the various offices to submit copies of completed assessments. Each organization was to submit a narrative report to the administrator on the assessments completed. The report was to provide a brief summary of assessment coverage and results and identify functions and programs having highest vulnerability. The resulting reports received at FAA headquarters were varied and often brief. Some FAA offices such as Civil Rights, General Counsel, and Public Affairs did not report the results of the assessments they completed.

Coast Guard

The assessments completed at CG were documented using a standard form. All that was required to complete the form was an overall numerical score. No backup or support materials documenting the basis for the scores was required. All of the forms were completed at CG headquarters, and the completed forms were accepted by the internal control coordinator after the mathematics were verified.

Federal Highway Administration

FHWA used a standard form to document the assessment process which took place largely at the region and division office level. Managers completed the forms, but no criteria were provided as to how various vulnerability ratings should be documented. The documentation in support of the ratings which accompanied the forms and which were forwarded to FHWA headquarters did not adequately explain the basis for the ratings.

Internal control reviews should be directed at vulnerable areas

OMB guidance states that agencies should consider performing ICRs of assessable units that have been rated as having a high or medium vulnerability or consider other alternatives such as planning corrective actions or scheduling other type audits and special studies. At DOT, the ICRs or other alternatives planned, could not be readily related to the assessable units considered to have a high or medium vulnerability. This occurred because ICRs were not always scheduled to cover assessable units for the same program elements and organizational segments on which the vulnerability assessment had been completed.

Each of the offices and administrations individually decided where the ICRs should be completed and what programs and

functions would be covered. Of the four largest administrations at DOT, FHWA appeared best to schedule its ICRs or other alternative actions in areas that were identified as highly vulnerable.

At UMTA, based on our review of past GAO and IG reports, areas we noted as vulnerable which were not scheduled for ICRs or other alternative actions included (1) the contracting, grants awards, and grant monitoring areas, (2) controls over contractor and grantee costs, and (3) followup to corrective actions identified as necessary based on past reviews.

In the case of CG, we noted from past GAO and IG reports vulnerable areas not scheduled for ICRs or other actions, including (1) fund controls and (2) inventory and supply management.

At FAA, officials said that 9 ICRs of a planned total of 35 were complete. FAA earlier had identified over 160 high and medium vulnerability areas which were to be considered for ICRs or other corrective actions.

Need for additional internal controls staff development

DOT's internal controls staff development training program had weaknesses, including a lack of timeliness, comprehensiveness, and attendance by those needing training. Training was scheduled after the segmenting and vulnerability assessment processes had been completed by the offices and administrations, and the training primarily dealt with the internal control review process. While DOT's training program established a good awareness of the internal control program, many staff members doing the assessments were not trained. For greater effectiveness in future assessment periods, DOT needs to expand its staff development, especially in the areas of segmenting and the completion of vulnerability assessments.

Under the direction of the Office of the Assistant Secretary for Administration, DOT had completed an internal control training program for DOT managers and administrative staff. The program was presented to some 800 employees in 19 workshops held at headquarters and at 11 field offices nationwide. The workshops were conducted cooperatively by the Office of the Assistant Secretary for Administration and the Office of the Inspector General. These training sessions dealt primarily with internal control reviews and the need for systematic corrective action and a reporting process.

Staff members attending these sessions in many cases were not those who performed the vulnerability assessments. At UMTA headquarters, for example, of 18 staff members we contacted who completed vulnerability assessments, 5 received training. At

the three UMTA regions we visited, none of the nine assessors received training. At FHWA, 424 vulnerability assessments were completed, and 119 FHWA staff members attended training sessions.³ At CG, the assessments covered 225 assessable units, and 69 staff members received training. Of nine CG assessors we contacted, none received training.

DOT officials have acknowledged that additional staff development in the FMFIA internal control process is necessary. DOT is considering plans for additional training in the process.

Inspector General's role
should be better defined

The Office of Inspector General's role in DOT's internal control process has not been adequately defined. Formally defining OIG's role would clarify for the secretarial offices and administrations their responsibilities under the act, in relation to OIG, thus eliminating possible confusion. During DOT's first-year implementation efforts, OIG has acted primarily as an advisor.

OMB guidelines state that the OIG normally reviews internal control documentation and systems. DOT orders dealing with the act generally describe OIG participation but do not explicitly define OIG's role. DOT Order 5100.4a, dated November 7, 1983, which superseded DOT order 5100.4, dated March 31, 1982, states that the Office of the Inspector General provides "technical assistance" to the DOT offices and administrations in implementing internal control requirements prescribed by OMB Circular A-123⁴ and the act and "coordinates" on internal control control criteria and guidelines developed by the Assistant Secretary for Administration. No further definition of the OIG role has been developed.

To date, OIG involvement in the process has been as follows. In July and August 1983, OIG assisted in the instruction at internal control workshops held for DOT managers and administrative staff given by DOT. OIG also offered comments on guidance and instructional materials and was available to answer questions raised by the offices and administrations.

In December 1982, OIG issued an audit report on the status of DOT's implementation of the policies and standards prescribed by OMB Circular A-123. In addition, OIG issued a draft report on the Department's FMFIA implementation process in December 1983. These reports and OIG's general background knowledge of

³Generally, at FHWA each assessor completed one vulnerability assessment.

⁴This circular, which preceded the act, describes agencies' internal control responsibilities.

the internal control process were the basis for OIG's assessment of the 1983 year-end statement by the Secretary on the adequacy of internal controls. OIG issued a final audit report on March 30, 1984.

OIG has stated that in the future it will schedule audits of the vulnerability assessment and ICR processes and that OIG staff may do some ICRs.

A DOT-wide followup system should be established

DOT has not established a systematic process for following up on FMFIA activities. While DOT is establishing such a system, it has not decided how it will work and who--DOT headquarters or individual offices and administrations--will operate it.

Followup systems are prescribed by the OMB guidelines in order for the agencies to monitor the completion and effectiveness of corrective actions taken. To date, DOT has developed an initial inventory of internal control weaknesses. Also by memorandum request and through personal contact, DOT compiled a list of internal control corrective actions which had been taken. These efforts, however, are not part of a continuing, systematic followup effort.

DOT has acknowledged that a centralized oversight of future assessments and reviews is desirable and stated that a followup process will be initiated in 1984. DOT told us that it is obtaining a microcomputer to help establish a centralized followup system for corrective actions.

Improvements in year-end reporting needed

DOT did not establish criteria for defining what constituted a material weakness to be included in its year-end report. As a result it may not have identified and included all known material weaknesses, including all uncorrected weaknesses reported as material by the offices and administrations.

OMB guidance requires full disclosure by agencies of all material internal control weaknesses in the year-end statement. However, DOT had no procedures, guidance, or criteria to govern the process of consolidating the offices' and administrations' reports into DOT's overall statement. In making its decision on which material weaknesses to include in the year-end statement, DOT stated that it based its judgment on whether or not the weakness warranted Presidential and Congressional attention.

DOT also stated that for it to develop additional criteria for use by the offices and administrations in the development of

the Secretary's year-end statement, OMB should provide additional guidance on what it considers a material weakness.

DOT included two Department-wide and various administration-specific material weaknesses in its year-end statement. DOT excluded from its statement various weaknesses reported to it by the administrations and subsequently determined by DOT as not being material or not representing an overall DOT or administration problem.

For example, CG reported to DOT 24 uncorrected weaknesses in specific functional areas that included security of personnel records and files, fund management, sensitive information collection and dissemination, electronic systems management and maintenance, and financial management and supply issues. DOT included in the year-end statement 16 of the 24 uncorrected weaknesses in the categories of financial and fund management and electronics systems management and maintenance. DOT omitted the remaining eight from its year-end statement. Also, while CG reported 12 corrected weaknesses to DOT, including such issues as procurement, officer personnel recordkeeping, ADP security, management of small arms, and fuel management, DOT included only 1 of the 12 material weaknesses, ADP security, in its year-end statement.

Similarly, UMTA reported 26 material weaknesses that required corrective actions, including property management; time and attendance procedures; monitoring grantee activities; usefulness of ADP reports, specifically the automated grant information system; and followup of audit reports. DOT included nine of the uncorrected material weaknesses reported. It grouped them into the issues of grants management, project property management, and a bus management program. UMTA also reported 18 material weaknesses it said were totally corrected. These weaknesses included such areas as cash management, cost controls on construction contracts, and grant award procedures. DOT included in the year-end statement 5 of the 18 weaknesses which it grouped into the overall material weakness issue of financial management.

Similarly, although FHWA reported 21 uncorrected weaknesses, DOT included 2 in its year-end statement--employment of consultants on highway projects and increasing minority business contracts. Also, of the 18 material weaknesses FHWA reported corrected--including weaknesses in property management and equipment security, time and attendance procedures, change orders on the highway construction inspection program, and ADP procedures--DOT listed 2 in its year-end statement.

FAA reported one uncorrected material weakness: ADP acquisition procedures. DOT included it in the Secretary's year-end statement as a corrected weakness. FAA also reported 13 material weaknesses that were corrected. These were in such

areas as property transactions, construction monitoring procedures, purchasing procedures, control of operating inventory, documentation of internal controls, and long-range ADP information technology planning needs. DOT, in its year-end report, addressed 4 of the 13 reported weaknesses grouped into two categories, property and ADP management.

DOT officials in the Office of the Assistant Secretary for Administration have acknowledged the need for criteria as to which material weaknesses reported by the offices and administrations should be included in the Secretary's year-end statement. They also acknowledged the need for additional guidance in this area from OMB.

Conclusions

DOT has made progress this first year in establishing a process for evaluating its systems of internal controls. The process can be an important building block for assuring effective internal controls in the Department.

Notwithstanding this progress, our review showed that DOT needs a stronger headquarters central role over FMFIA implementation. To date, DOT offices and administrations have used various methods to implement the act so that DOT cannot compare the effectiveness of the efforts made or judge the adequacy of corrective actions undertaken. Agencywide direction is needed in such areas as (1) documenting the process, (2) establishing better staff development, (3) following up on corrective actions, and (4) establishing criteria for including material internal control weaknesses in the Secretary's annual statement. Also DOT's FMFIA process could be improved if the OIG defined its role in the process, particularly as it applies to the roles of the offices and administrations with regard to quality control of the FMFIA process.

As the Department progresses, strengthens and improves its internal control process, corrects known internal control weaknesses, and takes corrective action in the areas we identified, it should have a more meaningful basis for concluding whether its systems of internal controls meet the act's objectives.

Proposals, agency comments, and our evaluation

In a draft of this report we proposed that the Secretary of Transportation direct the Assistant Secretary for Administration to assert a stronger central role over the DOT offices and administrations in their FMFIA implementation efforts and

- develop written procedures for the FMFIA processes, including suggested standard forms, criteria, and documentation requirements;

- provide for additional staff development and training in implementing FMFIA requirements;
- establish a DOT-wide corrective actions followup system; and
- in accordance with OMB guidance, develop criteria for determining what material internal control weaknesses reported to DOT by the offices and administrations should be included in the Secretary's year-end statement to the Congress and the President.

We also proposed that the Secretary of Transportation work with OIG to more specifically define OIG's role in the internal control process.

In its June 4, 1984, comments on a draft of this report, Transportation concurred with our proposed corrective actions and stated that it is making efforts to improve its internal control programs in accordance with our draft report's findings and proposals (see app. III). We are pleased with Transportation's response to our specific proposals and believe Transportation's comments show a strong commitment to the effective implementation of the act. Because of the Department's responsiveness, we have not included any recommendations in this report. We plan to monitor DOT's progress as part of our continuing reviews of federal agencies' implementation of FMFIA.

DOT EFFORTS TO DETERMINE ACCOUNTING SYSTEMS COMPLIANCE

DOT's initial efforts to comply with the act's requirements dealing with accounting systems conformity to the Comptroller General's standards accomplished much in the time available. The guidance developed by DOT's Office of Financial Management was detailed and generally facilitated the evaluation efforts. It provided the offices and administrations with a systematic approach for performing accounting system compliance evaluations and instituted standard reporting and documenting requirements. DOT can improve this process, however, by requiring additional documenting and testing of accounting systems and strengthening guidance for coordinating and consolidating the various office and administration reports into the Secretary's year-end statement.

Need to document and test accounting systems

Several DOT administrations' reports concluded that portions of their accounting systems documentation was incomplete or not current (DOT's guidance did not require that system documentation be updated). Additionally, none of the compliance evaluations we reviewed included tests of accounting systems in operation. DOT officials explained that time constraints in the act's first year precluded performing the necessary testing.

Accounting system documentation provides a clear and comprehensive description of such things as a system's objectives, methods of operations, established procedures, equipment used, operating locations, control features, special characteristics, and end products, such as accounting reports and financial statements. Documentation includes narrative descriptions, flow charts, procedures manuals, schedules, and charts in sufficient detail and logically organized to provide a ready understanding of a system's design, operations, and features.

Such information is needed to design the testing procedures necessary to determine if a system operates properly. However, there are many other advantages to properly documenting systems. For example, good documentation

- provides all employees with a consistent understanding of a system's operating procedures and requirements,
- facilitates familiarization and training of new employees,
- provides for a permanent record of changes made to equipment and operating procedures, and
- permits reviews by outside parties to be performed more quickly.

The Department's operating administrations have developed much of the information needed for documenting their accounting systems, but several concluded that documentation was either incomplete or out of date for portions of 8 of their 16 accounting systems. The administrations also reported plans for updating systems documentation where needed.

Concerning testing, the compliance evaluations we reviewed did not include standard tests of accounting systems to determine if they were operating in accordance with established policies and procedures. Evaluations were generally based on the reviewer's knowledge, experience, and observations.

Although we recognize that these individual's knowledge and judgment is invaluable to the review process, GAO's past audit work has frequently noted accounting systems operating differently from the manner specified in their design and even differently from the manner in which responsible officials believed them to be operating. Over time, accounting systems' operations change from their original design for various reasons, including (1) changes in the ADP equipment used, (2) turnover in personnel operating the systems, (3) control features being by-passed to save time, and (4) changes in the program activities serviced by the systems. Such changes are often gradual and can be overlooked by managers, especially when systems documentation is not kept up to date.

Effective testing can show whether systems are operating consistently, effectively, and in accordance with established policies and procedures. Generally, specific testing methods are developed based upon a system's particular design and features. To be economically feasible, the tests should be designed to focus on a system's key controls.

The need for system testing was illustrated by several instances noted during the Office of Inspector General's review of DOT's compliance evaluation process. The review, conducted at the completion of the process, noted that four of the administrations' accounting systems were not accruing certain expenditures as required by GAO's principles and standards. This fact was not recognized in the administrations' compliance reports to the Secretary. Subsequently, the reports were amended to disclose the lack of accruals.

We recognize that documenting and testing will require more resources. However, once a system has been properly documented, fewer resources should be required to keep the documentation current. By carefully developing and applying testing procedures selectively, managers can maximize potential benefits. Once the Department establishes procedures in these areas, it will need to advise and train its staff how to implement them.

Need to strengthen procedures and guidance for year-end reporting

DOT has not developed adequate written guidance and procedures for developing the Secretary's year-end statement. OFM coordinated the accounting system review work performed by the various operating administrations. It also developed the portion of DOT's year-end statement related to accounting systems, based largely on the results of the administrations' reviews. The annual statement reported that DOT's accounting systems generally conformed to the Comptroller General's principles and standards. The statement also included brief descriptions of areas in which individual accounting systems did not fully comply with specific principles or standards.

In preparing the annual statement, OFM evaluated each administration report on accounting systems review work and, exercising judgment, determined which instances of nonconformity were significant enough to consolidate into DOT's statement to the President and the Congress. As part of this process, the OFM also reviewed the operating administrations' reports on internal control evaluation for potential weaknesses related to accounting systems compliance.

The consolidation process required determining the relative significance of reported accounting weaknesses, rather than simply compiling the reported instances of nonconformity. Such judgments require considerable professional skill, as well as an

In-depth knowledge of an organization's operations and financial structure. DOT, however, has not developed written criteria for making such judgments on a department level basis.

In addition, DOT's procedures and guidance for coordinating the annual statement development process should be strengthened. The administrations' accounting systems review work may disclose potentially significant weaknesses related to internal control and vice versa. At DOT, the annual statement for these areas was developed by different organizations within the Office of the Secretary. Current DOT instructions, however, do not provide specifics to ensure all such weaknesses are considered for inclusion in the annual statement.

Conclusions

In a short time DOT developed and implemented guidance and a methodology for performing accounting system compliance evaluations, identified material system weaknesses, and reported results to the Congress and the President. DOT plans to correct weaknesses identified during its evaluation process and is developing a followup system.

DOT's efforts, in our view, represent a good faith first-year effort to comply with the act's accounting system compliance requirements. In future years, however, we believe it will also be necessary to (1) fully document accounting systems' design and control objectives and techniques, (2) test the systems' operations, including control techniques, to determine whether they are consistently operating as they should, and (3) strengthen the guidance and procedures for preparing year-end reports.

Proposals, agency comments, and our evaluation

In a draft of this report we proposed that the Secretary direct the Assistant Secretary for Administration to:

- Require the administrations to incorporate system testing into DOT's compliance evaluation procedures and ensure that all accounting systems are documented.
- Strengthen guidance and procedures for consolidating individual administration reports into DOT's overall annual statement and ensure that the results of all section 2 and section 4 work are considered for inclusion in the annual statement.

In commenting on a draft of this report, Transportation concurred with our proposed corrective actions and stated that it is making efforts to improve its accounting systems programs in accordance with our draft report's findings and proposals

(see app. III). Because of DOT's responsiveness, we have not included any recommendations in this report. We plan to monitor DOT's progress as part of our continuing reviews of federal agencies' implementation of FMFIA.

SUMMARY OF DEPARTMENT OF TRANSPORTATION'S
MATERIAL WEAKNESSES AS REPORTED IN THE SECRETARY'S
STATEMENT DATED, DECEMBER 23, 1983

FMFIA SECTION 2 INTERNAL CONTROLS

Corrective actions taken

URBAN MASS TRANSPORTATION ADMINISTRATION

--Centralized financial management system.

FEDERAL AVIATION ADMINISTRATION

--Property management responsibilities delegated to senior official.

SELECTED ADMINISTRATIONS

--ADP improvements in acquisitions (FAA), use (FHWA), and security (CG).

FEDERAL HIGHWAY ADMINISTRATION

--Cost change orders approval process strengthened.

FEDERAL RAILROAD ADMINISTRATION

--Strengthened accounting procedures on loans receivable.

Corrective actions planned

DEPARTMENT OF TRANSPORTATION

--Need for inventory of security sensitive ADP applications.

--Need for schedule of planned risk analyses of computer facilities.

COAST GUARD

--Plans for electronic systems data base and management-maintenance manual.

--Instructions to be provided for operations of marine environmental response fund.

--Plans for strengthened financial management, supply, and personal support programs

FEDERAL HIGHWAY ADMINISTRATION

- Study of disadvantaged business certification program processes.
- Possible revisions in guidance to states on employment of consultants on federal-aid highway projects.

URBAN MASS TRANSPORTATION ADMINISTRATION

- Study of automated grants management program
- Planned guideline changes on excess real property acquisitions by grantees.
- Planned guidance on improvements in grantee bus management programs.

MARITIME ADMINISTRATION

- Planned controls on contracts for repair of state schoolships.

FEDERAL AVIATION ADMINISTRATION

- Plans for improvement in energy conservation program

FMFIA SECTION 4 ACCOUNTING SYSTEMSSystems not in conformance

URBAN MASS TRANSPORTATION ADMINISTRATION

- New systems to be operational by September 1984.

COAST GUARD

- Plans for phased implementation of new system by 1988.

Systems in general conformity
with some areas of nonconformity

DOT's statement noted significant instances of nonconformity with principles and standards related to the following areas.

OFFICE OF THE SECRETARY ACCOUNTING SYSTEM

- Accountability over property, accrual of certain expenditures, and provision of an allowance for doubtful accounts.

FEDERAL AVIATION ADMINISTRATION ACCOUNTING SYSTEM

- Accountability over property and supplies, development of internal financial reports, recording letter of credit drawdowns, review of obligated grant funds, and the accrual of certain expenditures.

FEDERAL AVIATION ADMINISTRATION PAYROLL SYSTEM

- Development of internal financial reporting and coordination with the automated personnel information system.

UNITED STATES COAST GUARD FOUR PAYROLL SYSTEMS

- Systems documentation and reconciliation of allotment and payroll records.

FEDERAL HIGHWAY ADMINISTRATION ACCOUNTING SYSTEM

- Preparation of internal and external financial reports and accountability over property.

MARITIME ADMINISTRATION ACCOUNTING SYSTEM

- Documentation of procedures for developing cost information and valuation of donated and forfeited property.

MARITIME ADMINISTRATION PAYROLL SYSTEM

- Recognition of labor costs for reimbursable projects.

FEDERAL RAILROAD ADMINISTRATION ACCOUNTING SYSTEM

- Systems documentation, accountability over property, and accrual of certain expenditures.

FEDERAL RAILROAD ADMINISTRATION ACCOUNTING SYSTEM FOR THE ALASKA RAILROAD

- Development of internal financial reports, accrual of annual leave, and accountability over property.



U.S. Department of
Transportation

Assistant Secretary
for Administration

400 Seventh St. S.W.
Washington, D.C. 20590

JUN 4 1984

Mr. J. Dexter Peach
Director, Resources, Community and
Economic Development Division
U.S. General Accounting Office
Washington, D.C. 20548

Dear Mr. Peach:

This is in response to the General Accounting Office (GAO) draft report, "Transportation's First-Year Implementation of the Federal Managers' Financial Integrity Act," GAO/RCED-84-141, dated April 17, 1984.

As you are aware, the Department of Transportation (DOT) has held several meetings and discussions with your staff regarding this draft report. We have been pleased with the cooperative and responsive approach that has been taken by the GAO team in developing the proposed report. We feel that the implementation of the Federal Managers' Financial Integrity Act (FMFIA) is a very important Federal Government responsibility and that DOT's implementation program was a good first year effort. We are working toward improving our program in 1984 and beyond.

In regard to the draft report's recommendations contained on pages 6, 7, 8, and 9 of the draft letter to the Secretary, we concur in your recommendations. As we have discussed with your staff, we are making efforts to improve our internal control and accounting programs in accordance with your draft report's findings and recommendations.

Again, we appreciate the helpful and cooperative approach taken by your GAO internal control team. We strongly feel that the FMFIA program will benefit from a cooperative oversight and review process.

Sincerely,

A handwritten signature in cursive script, appearing to read "Robert L. Fairman".

Robert L. Fairman

(006107)



20/05

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