

Office of Inspector General

FY 2011 Financial Statements
Management Letter

A12-01A



March 2012

FEDERAL MARITIME COMMISSION



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

March 5, 2012

Office of Inspector General

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

FROM: Inspector General

SUBJECT: Transmittal of the FY 2011 Management Letter

When performing an audit of an agency's major financial systems and accounting processes, auditors often detect deficiencies in internal controls that do not rise to a level of seriousness to be reported in the auditor's opinion. These findings are communicated to the auditee in a management letter. Attached is a copy of the FY 2011 Financial Statement Management Letter that reports on such findings.

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

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

The OIG will continue to review areas vulnerable to accounting error and report any findings in next year's management letter. I am available to discuss the letter at your convenience.

Attachment

/Adam R. Trzeciak/

March 2, 2012

Federal Maritime Commission
Washington, D.C.

In planning and performing our audit of the financial statements of the **Federal Maritime Commission (FMC)** as of **September 30, 2011**, in accordance with auditing standards generally accepted in the United States of America and Government Auditing Standards, issued by the Comptroller General of the United States, we considered the FMC's internal control over financial reporting as a basis for designing our auditing procedures for the purposes of expressing our opinion on the financial statements, and not for the purpose of expressing an opinion on the effectiveness of the agency's internal control. However, based on our audit, we are providing the following findings and recommendations.

Prior Year Findings - Updated

Finding 1. Close out procedures on contracts need improvement

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

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

We reviewed 10 undelivered orders to ensure payables were properly recorded. During this review, we identified one FY 2008 undelivered order for \$155,850 where services were completed and the amount remained in undelivered orders at September 30, 2009. The amount was deobligated in FY 2010 and returned to Treasury after identification by the auditor. While it did not appear that these funds could have been used for other unmet agency needs because the

order was issued in FY 2008 and services were provided in FY 2009, the discipline to deobligate funds timely, i.e., within the fiscal year the funds are obligated, will provide the agency the flexibility to use funds where they are needed.

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

FY 2010 Follow-up: We noticed improvements in the close out procedures during the year, however, we identified two information technology contracts, totaling \$21,000, that were completed but not closed out and deobligated.

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

FY 2011 Follow-up: We noted that close out procedures improved and old information technology contracts were deobligated.

We consider this comment closed.

Finding 2. Formal procedures needed to account for internal use software

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

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

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

FY 2010 Follow-up: The OIG identified several software projects that needed to be capitalized by the agency. The OIG worked with OBF to ensure that approximately \$298,000 of

improvements to the phone and teleconferencing system were capitalized and \$180,000 of software in development was capitalized during fiscal year 2010.

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

FY 2011 Follow-up: On February 28, 2011, OBF updated the operational and administrative program for capitalized assets to include procedures to address the acquisition of internally developed software.

We consider this comment closed.

Finding 3. Agency program officials risk unauthorized commitments and anti-deficiency violations when purchase orders are signed after services begin

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

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

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

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

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

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

- A vendor provided keycard monitoring and maintenance services to the agency beginning on October 1, 2008. The contracting officer signed the order for these services on November 18, 2008.

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

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

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

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

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

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

Regardless of managers' intent to spend funds cautiously during CR funding, it is important to have purchase orders in place at the beginning of the period of performance because the purchase

order obligates funds for the activity. This ensures that funds will be available to pay for services received, regardless of when the agency is billed.

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

FY 2009 Recommendation: We recommend that the Managing Director establish a procedure to notify CORs when funding on purchase orders is about to expire to assist them to submit timely purchase requests to continue funding.

FY 2010 Follow-up: The Office of the Managing Director anticipates having these procedures written and completed by January 31, 2011. The new procedures will include a requirement for CORs to ensure that purchase documents are issued prior to commencement of performance and comply with appropriation requirements. The procedures will also include a mechanism to assist CORs to submit timely purchase requests to continue funding. We will follow-up on this finding during next year's audit.

FY 2011 Follow-up: In a memorandum to the OIG dated April 26, 2011, the managing director stated that the responsibility for maintaining adequate funding for purchase orders lies with each COR and his/her respective supervisor, explaining his decision to forgo new procedures and instead directed this responsibility be memorialized in each CORs performance standards.

The new language meant, in part, to address the funding lapses we observed, states that the COR:

(s)erves as a COR advising the FMC and/or BPD contracting officer (CO) for administering all aspects of assigned contracts. Provides appropriate and effective technical liaison between the Government and the contractor and between the end user and the CO. Ensures that any changes and modifications required are authorized and formally processed through the CO and communicates effectively with all parties to ensure the contractor fulfills each contract and that the contract is managed properly to meet mission requirements.

We could not conclude that any CORs reading the new performance standard would grasp that funding of a contract is a focal point of their COR duties. In short, the language is too generic.

We agree that CORs should be directly reviewed by their supervisors. However, when a contract is not funded timely the agency may commit funds for which there is no budget authority and potentially commit an Anti-Deficiency Act violation. An Anti-Deficiency Act violation can be very embarrassing for the agency and could lead to the COR being personally responsible for the payment of these services. During our review of contract files we noted one contract for health services in which services began on October 1, 2010; however the contract was not signed until August 30, 2011. If management prefers to include instructions in the CORs performance plan, then we recommend that the language more specifically address funding concerns as stated in management's initial response to the recommendation. Given management's response we cannot close this recommendation.

FY 2011 Recommendation #1: The Office of the Managing Director include specific language in the COR's performance plan addressing funding lapses that occur when funding runs out before a new purchase order has been approved.

Finding 4. Formal Procedures Needed to Track Civil Penalties

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

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

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

As a hedge against staff losing track of individual penalties assigned to it to monitor (due to reassignments, departures or the press of daily business), and to enhance controls over civil penalty receivables, OGC should centrally track all penalties assigned, noting the attorney assigned, the judgment amount, amounts paid, balance owed, and due date. The due date is important to ensure that the agency complies with the requirements of Debt Collection Improvement Act of 1996.²

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

FY 2011 Follow-Up: According to FMC management, a Managing Directive has been drafted that addresses debt collection agency wide, including civil penalties, transfers to treasury, and

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

maintenance of an accounts receivable report. It is currently being circulated for review and will be sent to the OIG when it has been finalized.

We noted that our initial recommendation would have required only a few hours to set up and perhaps one hour per month to monitor. While it is management's prerogative to develop a debt collection system, it has delayed addressing the vulnerability we identified in our prior year letter by one year. We will continue to monitor management's progress and we will opine on the effectiveness of the new system in our FY 2012 letter.

Finding 5. Senior Executive Service Candidate Training Obligations and Bona Fide Needs

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

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

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

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

According to GAO, bona fide needs questions frequently involve transactions that cover more than one fiscal year. In a typical situation, a contract (or purchase order) is made in one fiscal year with performance and payment to extend, at least in part, into the following fiscal year. In one decision,³ GAO has opined that "*training that began on the first day of the fiscal year 1990 was held chargeable to 1989 appropriations where the training had been identified as a need for*

³ See 70 Comp. Gen. 296 (1991)

1989, scheduling was beyond the agency’s control, and the time between procurement and performance was not excessive.” (Emphasis added.)

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

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

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

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

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

FY 2011 Follow-up: Management agrees that last minute purchase decisions can be problematic. However, according to management’s response to the recommendation the SES CDP was not a last minute afterthought, but an effort by the Commission to implement an important career development program. The CDP extends over multiple years and requires at least eighteen months for each candidate to complete, once selected. Further, management believes that the internal controls established in Commission Order 112 are adequate. The Managing Director or the Chairman already approves virtually all obligations made during the fiscal year, including non-routine, year-end procurements.

Management provided documentation to support that plans were being made early in the fiscal year to implement a SES training program. We also noted this year that obligations in general are approved by the managing director's office. Due to the frequency of purchases made at the end of the fiscal year, we will continue to monitor controls over spending and approvals in subsequent audits.

We consider this comment closed.

Finding 6. Human Resources Contractor Evaluation did not Follow FAR Requirements

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

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

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

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

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

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

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

FY 2011 Follow-up: In management's response to the FY 2010 management letter, the managing director has asked OMS to revise Commission Order 112 (CO 112), *Procurement*, to adopt a "Procurement Checklist of Required Actions Prior to & After Award", and to develop a form to document justification of sole source procurements by September 2011. We noted that CO 112 has not been updated and the procurement checklist has not been completed. We will follow-up on this finding in next year's audit.

Finding 7. Sole Source Contract Issued to Non-GSA Vendor Without Performing Market Research

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

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

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

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

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

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

schedule and is considered to be an “open market” source by the FAR. Open market sources are to be the last option considered by federal agencies when selecting vendors.

The OIG raised similar concerns in a FY 2007 report on a contract for consulting services⁶; specifically that a sole source contract was used to improperly used to justify not seeking a competitive bid on needed services.

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

FY 2011 Follow-up: In management’s response to the FY 2010 management letter, the managing director has asked OMS to revise Commission Order 112, *Procurement*, to adopt a “Procurement Checklist of Required Actions Prior to & After Award”, and to develop a form to document justification of sole source procurements by September 2011. We noted that CO 112 has not been updated and the procurement checklist has not been completed. We will follow-up on this finding in next year’s audit.

⁶ See A07-02, *Audit of Contracts*.

Current Year Comments

Finding 8. Conflict Management: Needs Assessment and Training

According to Commission Order 112, *Procurement*, all procurement transactions, whether by sealed bids or by negotiation and without regard to dollar value, shall be conducted in a manner that provides for, and promotes, to the maximum extent practicable, full and open competition as expressed in the FAR.

In August 2011, the FMC identified a requirement for a conflict resolution seminar for FMC managers. FMC procurement staff performed market research by meeting with one potential vendor (Vendor #1). A proposal was prepared, dated August 2011, by Vendor #1 to address this requirement. On September 21, 2011, the agency provided three vendors, including Vendor #1, with a Statement of Objectives (SOO) that described the training requirement (objectives) as follows:

The workshop shall provide participants with an understanding of the dynamics of conflict and how to resolve conflict effectively with individuals or with groups. The emphasis of the workshop should be on developing skills and tools to understand the causes of conflict and to reach satisfactory outcomes.

This workshop provides (sic) participants with skills and tools to resolve conflicts with individuals and with groups, both internally with a working group, with peers and bosses, across departments and divisions, as well as outside individuals or groups with interests and concerns.

A purchase request to fund this requirement was prepared on September 23, 2011, in the amount of \$4,000,⁷ the estimated cost submitted by Vendor #1. According to the requisition, the training would be provided over two days for 24 agency employees.

According to FAR 37.602, *Performance Work Statement (PWS)*, a PWS may be prepared by the Government or result from an SOO prepared by the Government where the offeror proposes the PWS. The requests for proposal that were provided to the three vendors requested a PWS, including an agenda of content and activities.

Commission Order (CO) 112, *Procurement*, requires that each technical proposal include instructions for the preparation and evaluation of technical and cost proposals. The weights assigned to the factors are to be established on a case-by-case basis. Examples of evaluation criteria include: (1) the prospective contractor's understanding of the statement of work as shown by its proposed technical approach; (2) the availability and experience of technical personnel to be employed on the project; (3) relevant experience of the organization (e.g., size and dollar value of similar projects); and (4) prospective contractor's proposed method of assuring the achievement of timely and acceptable performance of the work, as proposed.

⁷ On November 17, 2011, the task amount was increased by \$6,000 to a total of \$10,000.

In its request for proposal, the agency notified vendors in the SOO that the “Government will award a contract... based on the best overall value, to the responsible offeror whose offer confirming to the solicitation will be the most advantageous to the Government, price and other factors considered.” The SOO did not identify what “other factors” would be considered.

Three proposals were received on September 26 and 27. A technical evaluation was performed on September 28 by the FMC training coordinator, indicating that all proposals were technically acceptable. Once this determination was made, price became the determining factor. The vendor the agency met with in August 2011 was the lowest bidder and was selected.

Analysis

We believe that this requirement lacked “competition, to the maximum extent possible” as required by CO 112. We believe further that the winning vendor had a competitive advantage over the two other proposals for reasons discussed below.

The FMC met with Vendor #1 in August 2011. Although we do not have minutes of the meeting, we found a proposal in the file, dated August 2011, for a two day seminar in conflict resolution. The agency used the meeting as an opportunity to perform market research, according to the CO, to learn about vendor offerings. The meeting and resulting proposal, in themselves, are not necessarily problematic.

Rather, we are concerned that language describing the agency’s conflict resolution workshop requirement in its request for proposal was copied, almost verbatim, from Vendor #1’s August 2011 proposal. For example, the first two paragraphs in Vendor #1’s proposal read as follows:

This workshop is designed to provide participants with an understanding of the dynamics of conflict and how to resolve conflict effectively with individuals or with groups. The emphasis of the workshop is on developing skills and tools to understand the causes of conflict and to reach satisfactory outcomes, even when emotions are high.

This workshop provides participants with skills and tools to resolve conflicts with individuals and with groups, both internally with a working group, with peers and bosses, across departments and divisions, as well as outside individuals or groups with interests and concerns.

A comparison with the two paragraphs identifying FMC’s training requirement near the beginning of this finding (see previous page) shows a very strong correlation between the first paragraphs, and, in the second paragraph, a verbatim relationship.

Vendor #2 and Vendor #3 were not given a clear understanding in the SOO as to how their proposals would be evaluated. “(P)rice and other factors” do not enable these vendors to tailor their proposals to what the FMC considered to be important, whereas the first vendor knew, or was in a better position to know, based on an August 2011 meeting with FMC staff, what the agency was looking for. Vendor #1’s bid was tailored to the FMC’s specific needs. The FMC’s contracting officer pointed out that he spoke with the two vendors prior to soliciting a proposal

from them. While this mitigates some of the disparity, we believe it best to provide all vendors with the same opportunity to discuss the requirement. In this instance, the vendor who visited the FMC and provided a description of the requirement that was used in the SOO would, at least in appearance, have a competitive advantage.

According to one contracting officer we spoke with from a sister agency, allowing vendors to propose the PWS leaves the door open for numerous evaluation inconsistencies since the content of proposals could range from one end of the spectrum to the other. As such, evaluation documentation and award justification for this type of procurement is extremely important to guard against potential challenges by unsuccessful bidders.

The technical evaluation panel consisted of one agency staff. Her results indicated that “all proposals met the performance criteria.” No additional information about the relative strengths or weaknesses of the approaches, past experience or technical merit was included in the technical evaluation. A price analysis by the CO and contract specialist followed the technical evaluation. As previously stated, the lowest bid was chosen.

The agency did not adequately plan to meet this requirement. Sending out proposals on September 21, with a one week turnaround, provides vendors with little time to prepare a comprehensive proposal and the agency even less time to follow an evaluation plan to review for technical content – given the September 30 fiscal year end. The agency simply ran out of time. If price was the overriding factor, the agency could have adopted a “low price, technically acceptable” approach, where each proposal is reviewed, one at a time, beginning with the lowest price proposal. Once an acceptable technical proposal is found, the evaluation concludes and that proposal is accepted. A “best value” approach is generally far more time consuming and involves the assignment of points to evaluation factors. Only after these technical scores are considered is price considered. The FMC did not assign evaluation points to any proposal.

With an agency the size of the FMC, with most of its appropriation going to salaries, it is sometimes necessary to delay many procurements until near the end of the year to ensure that basic requirements are addressed. In this particular instance, however, the agency was aware of this need in August but chose to wait until September 21.

FY 2011 Recommendation #2: OMS adhere to FAR and CO 112, *Procurement*, principles of full and open competition and provide all prospective vendors with equal opportunities to compete. Specifically, if one vendor is asked to meet with agency procurement staff, all vendors should have this opportunity.

Finding 9. Accounts Payable is understated

Accounts payable (or payables) represent amounts owed for purchases of goods or services. During the year, payables are recorded when an invoice, packing slip or receiving report is received by the agency. The Office of Management Services (OMS) reviews all obligations at year-end and establishes an accrual for all services and goods received by year-end (e.g., to recognize that money is owed in the period that the goods were received). For example, an

invoice for computer monitors that were delivered on September 15th (FY 2011) may not be sent by the manufacturer until October 10th (FY 2012). The expense should be recorded on the FY 2011 books because the monitors were received in FY 2011.

We reviewed accounts payable at year-end to ensure that all expenses for goods and services were properly recorded in the appropriate period. During our review, we identified approximately \$150,000 in additional FY 2011 payables that were not recorded by the agency in FY 2011. Since the adjustments were not made the agency's payables and expenses for FY 2011 were understated on the agency's financial statements.

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

OMS has established a standard operating procedure which reviews all procurements over \$10,000 at year end with the COR to determine any amounts that should be accrued. This process is normally performed by sending an e-mail to the COR requesting a statement as to whether any of the goods or services in the open obligation have been received as of September 30th. If services or goods have been received the COR will then provide an estimate of these items to be accrued. The audit team noted that, due to transition in OMS staff members, CORs were not contacted and no accruals were established.

FY 2011 Recommendation #3: We recommend that the Director of OMS review year-end procedures with his staff to ensure that all necessary accruals are made at year-end.

Finding 10. Procurement controls are needed for recurring services

The Bona Fide Needs rule is a fundamental principle of appropriations law. It states that a fiscal year appropriation may be obligated only to meet a legitimate or bona fide need arising in, or in some cases arising prior to but continuing to exist in, the fiscal year for which the appropriation was made. Recurring services are considered "severable" and are charged in the fiscal year in which the services are performed.

In August 2011 the agency procured \$5,000 for recurring shredding services for FY 2011. At the end of the year approximately \$300 of shredding services was used. In October 2011 this contract was modified to extend the period of performance to April 2012. Since shredding services are a recurring severable service FY 2011 funds should not be used for a FY 2012 need. This was discussed with director of OMS who agreed that shredding services was a severable service and that funds under this contract should be deobligated. In addition the director of OMS plans to establish a new FY 2012 obligation for shredding services.

FY 2011 Recommendation #4: We recommend that the director of OMS put procedures in place to identify the bona fide need of each contract and only approve obligations in the year that need exists.

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

Management comments to this letter are attached in their entirety.

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

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

Rockville, Maryland

Memorandum

TO : Inspector General

DATE: February 29, 2012

FROM : Managing Director

SUBJECT: FY 2011 Financial Statement Management Letter

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

Management Letter Recommendation 1. (Finding 3) The OIG recommends that specific language be included in the performance plans of Contracting Officer's Representatives (COR) to address funding lapses that occur when funding runs out before a new purchase order has been approved.

OMD Response: Management believes that the language in the CORs performance plan element is sufficient, considering that each COR is issued an Appointment Letter (copy attached) which outlines their responsibilities, including funding oversight, for the specific contract. Should there be a lapse of funding for any reason, the COR will have to perform a ratification to properly reinstate the contract. **This recommendation is considered closed.**

Management Letter Recommendation 2. (Finding 8) The OIG recommends that OMS adhere to FAR and C.O. 112, *Procurement*, principles of full and open competition and provide all prospective vendors with equal opportunities to compete. Specifically, if one vendor is asked to meet with agency procurement staff, all vendors should have this opportunity.

OMD Response: Management believes the Commission complied with the FAR and C.O. 112 in this procurement. Full and open competition was provided and equal opportunities were given to the required number of vendors. All bidders were contacted and afforded the same opportunity for meeting with procurement staff. Ultimately, the least cost alternative by far was selected.

Moreover, it is an accepted, common and necessary step when planning for procurements to research the market or at least some participants in the market to ascertain the type of services available that might suit the agency's needs and use that information in the development of the contract solicitation to ensure that bids are as closely related to the agency's needs as possible. In recognition of this, reference can be made to an Office of Federal Procurement Policy memo dated February 2, 2011*,

discussing “*Myth-Busting*”: *Addressing Misconceptions to Improve Communication with Industry during the Acquisition Process*. According to this memo:

While agencies do not have the resources, and are not required, to meet with every vendor at every step of the acquisition process, information gathered from industry sources plays an invaluable role in the acquisition process. For this reason, agencies must develop practices that will ensure early, frequent, and constructive communication during key phases of the process.

The OMS had constructive communication with all of the potential vendors during the key phases of this process. **This recommendation is considered closed.**

Management Letter Recommendation 3. (Finding 9) The OIG recommends that the Director, OMS, review year-end procedures with his staff to ensure that all necessary accruals are made at fiscal year-end.

OMD Response: The Director, OMS, met with his staff on February 27, 2012 to review and discuss current year-end procedures concerning accruals and how this function relates to the acquisition process. At the direction of the Managing Director, a review of the current procedures will be undertaken and procedures finalized before the end of this fiscal year.

Management Letter Recommendation 4. (Finding 10) The OIG recommends that the Director, OMS, put procedures in place to identify the bona fide need of each contract and only approve obligations in the year that need exists.

OMD Response: Procedures are in place to identify the *bona fide* need for each contract in the fiscal year that the need exists. With the previous hiring of the Contract Specialist within OMS and the commencement of the current fiscal year, additional internal controls were implemented to verify that each procurement is properly executed. **This recommendation is considered closed.**

/Ronald D. Murphy/

Attachment

cc: Directors OBF and OMS

*copy will be provided upon request of the OIG.