



OIG HIGHLIGHTS

View Report AUD-FM-15-40.

What OIG Audited

In response to a request from the Bureau of International Security and Nonproliferation, Nonproliferation and Disarmament Fund (NDF) management, Kearney & Company, P.C. (Kearney), an independent auditing firm acting under OIG direction, audited selected NDF controls. The objective of this audit was to determine the extent to which NDF internal controls relating to the management activities and the budget and finance activities listed in the Department of State Management Controls Checklist have been designed and implemented effectively. NDF management also requested that Kearney perform focused audit procedures over the budget and finance controls and contracting processes related to NDF's work in Egypt.

What OIG Recommends

OIG made seven recommendations to NDF to strengthen the design and operation of management, budget and finance, and contracting controls. Based on the response received from NDF, OIG considers the recommendations resolved pending further action. Management responses and OIG replies are presented after each recommendation in the Audit Results section of this report. NDF's response has been reprinted as Appendix C.

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September 2015
OFFICE OF AUDITS
Financial Management Division

Audit of Selected Nonproliferation and Disarmament Fund Management Controls

What OIG Reported

NDF's role is to supplement U.S. diplomatic efforts to promote bilateral and multilateral nonproliferation and disarmament activities through the development, execution, and implementation of carefully selected projects. Federal regulations and guidance require that agency management develop and maintain effective internal control and evaluate and report on the overall adequacy and effectiveness of internal control.

Kearney found that most of NDF's controls related to management activities were designed and implemented effectively. However, control improvements are needed. Specifically, NDF did not have a process to periodically review its organizational structure to ensure appropriate supervision and authority exists; did not have a formal process for preparing and approving language in Memorandums of Understanding relating to NDF projects; did not identify and document the specific provisions for which it used its "notwithstanding authority"; and did not have processes to evaluate the cost effectiveness of using contractors to perform project management and administrative functions.

Kearney also found that, although most controls related to budget and finance activities were designed and implemented effectively, some controls needed improvement. Specifically, NDF did not always enter final obligation amounts in its Project and Information Management System; project managers did not include the required information in their certifications of the receipt of goods and services; NDF did not always record expenses in the NDF system; and NDF did not have a formal process for developing and documenting its annual budget request.

Further, Kearney found that controls relating to contract initiations and contract modifications were not implemented effectively for the Egypt project. Specifically, NDF did not maintain the contract initiation documentation for one contract and did not prepare an acquisition plan for one contract. In addition, NDF did not prepare and maintain the documentation or obtain the approvals required for contract modifications.



OIG

Office of Inspector General

U.S. Department of State • Broadcasting Board of Governors

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FINANCIAL MANAGEMENT DIVISION

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Audit of Selected Nonproliferation and Disarmament Fund Management Controls

Office of Inspector General
U.S. Department of State
Washington, D.C.

Kearney & Company, P.C. (Kearney) has performed an audit of management controls within the Nonproliferation and Disarmament Fund. This performance audit, performed under Contract No. SAQMMA14A0050, was designed to meet the objective identified in the report section titled "Objectives" and further defined in Appendix A, "Scope and Methodology," of the report.

Kearney conducted this performance audit from January through April 2015 in accordance with *Government Auditing Standards*, 2011 Revision, issued by the Comptroller General of the United States. The purpose of this report is to communicate the results of Kearney's performance audit.

Kearney appreciates the cooperation provided by Nonproliferation and Disarmament Fund personnel during the audit.



Kearney & Company, P.C.
Alexandria, Virginia
August 12, 2015

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OBJECTIVE

In response to a request from the Bureau of International Security and Nonproliferation (ISN), Nonproliferation and Disarmament Fund (NDF) management, Kearney & Company, P.C. (Kearney) performed this audit to determine the extent to which NDF internal controls relating to the management activities and the budget and finance activities listed in the Department of State (Department) Management Controls Checklist¹ have been designed and implemented effectively. NDF management also requested that Kearney perform focused audit procedures over the budget and finance controls and contracting processes related to NDF's work in Egypt for which NDF plans to substantially increase the amount of funding.

BACKGROUND

ISN is responsible for managing a broad range of U.S. nonproliferation policies, programs, agreements, and initiatives. ISN has three major programs: Nuclear Affairs, Non-Nuclear and Counter-Proliferation, and Nonproliferation Programs. NDF, one of ISN's Nonproliferation Programs offices, was established to provide a means for the U.S. Government to respond rapidly to nonproliferation and disarmament opportunities, circumstances, or conditions that are unanticipated or unusually difficult but of high priority. NDF's role is to supplement U.S. diplomatic efforts to promote bilateral and multilateral nonproliferation and disarmament activities through the development, execution, and implementation of carefully selected projects. When an office within the Department or other U.S. Government agency, such as the U.S. Department of Energy, identifies a nonproliferation opportunity that was not anticipated or budgeted, the office or agency submits a project proposal to NDF. NDF funds and executes the approved projects in coordination with these other offices and agencies.

NDF is a small organization comprised of Department personnel and contractors, including personal services contractors. NDF staff includes a Director, a Deputy Director, a Comptroller, finance officers, project managers (PM), policy officers, a contract advisor, and project support specialists. Excluding the Director, there are three PMs who negotiate, manage, and implement NDF projects. Most PMs are former senior officials from military and diplomatic missions with a significant amount of experience and knowledge in nonproliferation activities.

NDF is funded each year by the Nonproliferation, Anti-terrorism, Demining, and Related Programs appropriation. Since its creation in 1994 through the end of FY 2014, NDF has received \$654 million in appropriated funds. NDF received \$30 million in appropriated funds during FY 2014. NDF funds are available until they are expended to permit maximum flexibility

¹ The management activities and the budget and finance activities from the Management Controls Checklist that were included in this audit are listed in Appendix A. The Bureau of the Comptroller and Global Financial Services annually distributes the checklist via email.

in project implementation. Despite the indefinite availability of the appropriated funds, the funds must be aligned to a project before they can be spent. The Under Secretary for Arms Control and International Security must approve all projects. Furthermore, NDF must formally notify Congress of the projects it plans to implement through a Congressional Notification. NDF cannot exceed the amount of funding included in the Congressional Notification for each project. If additional funds are necessary to achieve an objective, a new project is created.

NDF funding is provided “notwithstanding any other provision of law.”² “Notwithstanding authority” is an extraordinary authority granted to NDF by Congress that allows it to override portions of laws and regulations in special circumstances.³ For example, despite Federal Acquisition Regulation requirements that Government offices “Buy America,” NDF is permitted to obtain goods or services from foreign contractors. NDF may also award contracts without complying with Federal Acquisition Regulation requirements relating to competition.

To track its funds and manage its projects, NDF developed and implemented a Project and Information Management System⁴ (PIMS). PIMS’ primary purpose is to ensure that funds expended for a project do not exceed the amount in the Congressional Notification. NDF records in PIMS the funds received through appropriations and the amount in the Congressional Notification, amount obligated, and amount spent for each project. PIMS is used only by NDF and does not interface with the Department’s official financial system of record, the Global Financial Management System (GFMS). Therefore, NDF must manually record financial data in PIMS and perform manual reconciliations to ensure that the information in PIMS is consistent with the information in GFMS for budget execution and financial reporting purposes.

The Egypt Project

In 2009 NDF initiated a project in Egypt with the primary goal of stopping illegal trade in conventional weapons across borders in order to “enhance peace, security, and stability in the Middle East.”⁵ Since its initiation, the project has encountered a number of delays due in part to the revolution that occurred in Egypt in January 2011. Despite the delays, NDF management stated that a great deal of progress on the project was made during the latter half of 2014. As a result, NDF plans to obtain additional funds to further enhance border security in Egypt.

² Consolidated Appropriations Act, 2014, Pub. L. No. 113-76, and prior year appropriation legislation.

³ Although there are no specific restrictions on NDF’s use of “notwithstanding authority,” the authority is not absolute. For example, a Government Accountability Office opinion (*Architect of the Capital-Payment of Fringe Benefits to Temporary Employees*, B-303961, Dec. 6, 2004) concluded that the Architect of the Capital could not use “notwithstanding authority” to waive the Antideficiency Act. NDF has stated that its practice is to follow all laws, regulations, and Department guidance and to limit the use of “notwithstanding authority” to circumstances in which overriding certain provisions in laws and regulations is necessary to meet project-specific needs.

⁴ NDF renamed the system in 2014 from Financial Information Management System to Project and Information Management System. There were no significant changes made to the system related to this name change.

⁵ NDF submitted a second Congressional Notification in 2010 to obtain additional funding for the work in Egypt. These additional funds were recorded in PIMS as a separate project. However, because the funds were for the same work, Kearney has considered the work in Egypt as one project throughout this report.

Statement of Assurance

According to Office of Management and Budget (OMB) Circular A-123, Revised, *Management's Responsibility for Internal Control*, management has a fundamental responsibility to develop and maintain effective internal control. Internal control includes the plans, methods, policies, and procedures adopted by management to provide reasonable assurance that the objectives of management are achieved and the integrity of programs is safeguarded. The three primary objectives of internal control are to ensure:

- the effectiveness and efficiency of operations,
- the reliability of financial reporting, and
- compliance with regulations and applicable laws.

The Federal Managers' Financial Integrity Act of 1982⁶ requires agencies to establish and maintain internal control. The Act also requires the agency head to annually evaluate and provide to the President and the Congress a Statement of Assurance on the overall adequacy and effectiveness of internal control within the agency.

To prepare the Secretary of State's annual Statement of Assurance, the Department requires that chiefs of mission, Assistant Secretaries, and office heads prepare an annual assurance statement concerning the effectiveness of internal controls in their respective operations. Specifically, senior Department management must provide assurance that they have carried out the management control⁷ responsibilities assigned to them, as specified in the *Foreign Affairs Manual* (FAM).⁸ They must also provide a listing of the reviews conducted that support their assurance statement as well as a listing of any management control material weaknesses or significant deficiencies identified during the reviews. Additionally, senior Department management must provide a plan and schedule for correcting the weaknesses identified and an updated corrective action plan for weaknesses reported in the prior year.

The Bureau of the Comptroller and Global Financial Services (CGFS) provides guidance to senior Department management to assist them in preparing their assurance statements. The guidance includes a Management Controls Checklist, which, although not required, is provided as a tool to help identify management control gaps as well as to identify reviews that management might have performed. The Checklist includes a list of control activities organized into 16 categories, such as Management and Budget/Finance.⁹

⁶ Pub. L. No. 97-255, 31 U.S.C. § 65 note.

⁷ Internal control is also referred to as management control. The Department uses the term management control.

⁸ 2 FAM 020, "Management Controls."

⁹ In addition to the Management and Budget/Finance categories, the Checklist includes control activities for the following categories: Human Resources; Post Management; Contracts and Grants; Physical Security; Information Technology Security; Programs; Property and Inventory; Post Interagency Housing Board, Safety; Health and Environmental Management Program; Government Owned Residential Properties; Property Leasing Program; Real Property Application; Repairs and Improvements; and Heritage Assets.

The Assistant Secretary for ISN requires that each of the Directors in ISN, including the NDF Director, prepare an assurance statement regarding management control in their office, which the Assistant Secretary relies upon to support the ISN assurance statement. Within NDF, the Director and the Deputy Director complete the Management Controls Checklist provided by CGFS to assess NDF controls and provide the basis for the NDF assurance statement.

Prior Audit Reports

2012 Audit Report

In 2012, the Office of Inspector General (OIG) reported on the sufficiency of NDF controls over its contracting and project management processes and on whether the integrity of the data in NDF's internal financial and project management system was sufficient to prepare auditable financial reports for external users.¹⁰ During this audit, Kearney found that NDF's controls over the contracting process were sufficient to meet many objectives but needed improvement. Specifically, controls over contract initiation and modification, invoice approval, and contract closeout were well designed but were not consistently executed. In addition, NDF did not have sufficient controls over unliquidated obligations (ULO), a control to close out contracts in a timely manner, or a process to document the projects for which NDF's "notwithstanding authority" was used. Without sufficient controls related to contracting, there could be delays in contract initiation and modification, improper payments to contractors, and delays in project implementation and execution, among other things.

Kearney also found that NDF executed projects to achieve nonproliferation goals around the world, and the PMs effectively managed the status of their projects. However, PMs did not manage projects consistently and did not always use the project management functionality of PIMS. Without consistent project management practices, NDF could not ensure that it carried out its mission in the most effective and efficient manner.

Further, PIMS contained accurate and complete information on funds received as well as the amounts in the Congressional Notification for each project. However, obligations and expenses in the system were not always accurate, complete, or entered in a timely manner; and the system lacked key reporting functionality. Additionally, although NDF had some controls to protect the data in the system, NDF had not implemented certain application level controls. For example, NDF did not have a comprehensive application security plan and had not formally approved or implemented its draft contingency plan. Because of the data inaccuracies in PIMS and the limitations of its reporting capabilities, Kearney concluded that in its current state PIMS would be unable to produce auditable financial reports.

¹⁰ *Audit of Nonproliferation and Disarmament Fund Controls Over Contracting and Project Management and Integrity of Financial Data* (AUD-FM-13-17, Dec. 2012).

OIG recommended that NDF take actions to improve its controls over contracting and project management and improve the reliability of the data in its financial and project management system.

2014 Audit Report

In 2014, OIG reported on the results of a follow-up audit to assess NDF's progress in addressing the control deficiencies identified in 2012.¹¹ Kearney found that NDF had strengthened controls over contract initiation and modification, and these controls were operating effectively. In addition, NDF developed a process to monitor its ULOs that identified and facilitated the deobligation of invalid ULOs. NDF also implemented contract closeout controls and made progress in remediating the backlog of contracts requiring closure. Although NDF made significant progress, Kearney identified the need for additional improvements. NDF strengthened its controls over invoice approvals, but the control over the certification of receipt of goods or services was not consistently executed. NDF also developed a policy for documenting the use of its authority to waive Federal requirements, but the policy did not align with actual practice and did not require that NDF document the use of the authority at a sufficient level of detail.

NDF had also improved its controls over project management; however, PMs did not consistently follow policies relating to managing project scope and project risk in PIMS because of the lack of sufficient training in PIMS functionality. In addition, NDF's control for maintaining project schedules in PIMS was complex, and PMs did not enter the information necessary to monitor project schedules. Similarly, PMs did not consistently maintain project-related documents in PIMS according to newly established document management guidelines because NDF had multiple locations where the documents could be stored. Further, although NDF had established a timeframe for closing projects, some projects in the closeout process were not closed timely because of the lack of timeframes for all project closeout tasks.

NDF had improved significantly the integrity of the data in PIMS. Kearney identified fewer obligations and expenses that were not recorded accurately, timely, or completely than were identified in 2012. The exceptions identified occurred because NDF did not develop or execute sufficient reconciliations of the information in PIMS with the information in GFMS. NDF also improved PIMS reporting capabilities to fulfill requirements for reliable and complete financial reports. However, the reliability of the reports was limited by the accuracy, timeliness, and completeness of the data in PIMS.

NDF improved PIMS application level controls by preparing and finalizing comprehensive system security and contingency plans. NDF also strengthened its processes to ensure that only approved changes to PIMS were made and developed a user access matrix to ensure that all

¹¹ *Follow-up Audit of Nonproliferation and Disarmament Fund Controls Over Contracting and Project Management and Integrity of Financial Data* (AUD-FM-15-18, Dec. 2014).

PIMS users had the appropriate level of access. However, one user profile was not included in the matrix, and the system administrator profiles allowed system administrators to change key financial data.

OIG made 11 recommendations for NDF to continue to take actions to improve its controls over contracting and project management and improve the reliability of the data in its financial and project management system.

AUDIT RESULTS

Finding A: Most Management-Related Controls Were Designed and Implemented Effectively, but Areas for Improvement Exist

Kearney found that most of NDF's controls related to the management activities listed in the Management Controls Checklist were designed and implemented effectively. Specifically, NDF had effectively designed and implemented controls to review and update information in the FAM; ensure continuous communication; eliminate unnecessary duplication; assess risk; ensure business class travel is approved based on an appropriate, documented justification; ensure that purchase and travel cards are used appropriately; manage the costs related to conferences and training; and address and close external review recommendations.

Although most management-related controls were designed and implemented effectively, Kearney identified instances in which control improvements are needed. Specifically, NDF did not have a process to periodically review its organizational structure to ensure appropriate supervision and authority exist. Such a review has not been implemented because of the small size of the organization. Although Kearney found that appropriate supervision and authority existed within NDF's organizational structure, without a process for periodic reviews, conditions may change and the existing lines of authority and supervision may no longer be appropriate.

Control improvements are also needed to ensure compliance with laws and regulations. Kearney found that NDF had effective controls to ensure that a Congressional Notification is made before projects are initiated. However, NDF did not have a formal process for preparing and approving the language in the Memorandums of Understanding (MOU) relating to those projects. As a result, language in the MOU could be modified after key NDF personnel reviewed the MOU in a manner that may put NDF at risk for noncompliance with the FREEDOM Support Act¹² or other laws and regulations. Additionally, as noted during the 2014 audit, NDF did not identify and document the specific provisions for which it used its "notwithstanding authority". As a result, NDF did not have sufficient documentation to support its use of this authority to Congress and other stakeholders.

¹² Pub. L. No. 102-511 (1992); 22 U.S.C. §§ 5801, et. seq.

Further, Kearney found that NDF lacked processes to evaluate the cost effectiveness of using contractors, including personal services contractors (PSC), to perform project management and administrative functions within NDF. Approximately 33 percent of NDF's employees are contractors. However, NDF had not performed a formal cost-benefit analysis to determine whether its use of contractors was, in fact, more cost effective than hiring full-time employees.

Controls Ensuring FAM Updates Were Operating Effectively

Management Control Activity: *Has management conducted reviews of the FAM and Foreign Affairs Handbook (FAH) sections that you are responsible for maintaining, to ensure that the information is up to date?*

NDF controls to ensure that the information in the FAM is up to date were properly designed and operating effectively. On an annual basis, the Bureau of Administration sends an email to all Executive Directors asking them to work with their program offices to review and update their sections of the FAM and FAH. Instructions on how to complete the review, as well as a spreadsheet listing the sections of the FAM and FAH each Executive Director is responsible for reviewing, are attached to the email. ISN is responsible for updating 1 FAM 450.¹³ The ISN Executive Office (ISN/EX) forwards the Bureau of Administration's email, as well as a copy of 1 FAM 450, to all ISN offices, including NDF, and requests that each office review its sections of the FAM and provide updates to ISN/EX, if necessary.

To ensure that the necessary updates are made, the NDF Deputy Director assigns to the NDF Policy Officer the responsibility of preparing NDF's response to ISN/EX. The NDF Policy Officer solicits input from NDF staff and informs the NDF Director and Deputy Director of the necessary FAM updates. The Deputy Director submits the updates to ISN/EX. ISN/EX informs ISN offices when the changes have been made. Upon receipt of this notification, the NDF Director confirms that NDF's proposed changes were made.

Kearney obtained and reviewed documentation relating to the process for updating the FAM and FAH in 2014. Specifically, Kearney reviewed the ISN/EX request, NDF emails relating to the request including the NDF response to ISN/EX, and the ISN/EX notification of the FAM or FAH changes made. Based on its review of this documentation, Kearney confirmed that the NDF Deputy Director assigned the responsibility of responding to ISN/EX's request to the Policy Officer, the Policy Officer solicited input from all NDF staff, and NDF provided suggested FAM updates to ISN/EX. In addition, the NDF Director notified NDF staff of the FAM changes made upon receipt of the notification from ISN/EX.

Controls Ensuring Continuous Communication Were Operating Effectively

Management Control Activity: *Are managers ensuring continuous communication exists between management and personnel and external entities?*

¹³ "Bureau of International Security and Nonproliferation (ISN)."

Overall, the three NDF controls related to communication that Kearney tested were designed and implemented sufficiently for Kearney to conclude that NDF controls ensuring continuous communication were effective. NDF controls to ensure that continuous communication exists between management and personnel, as well as between management and external entities, were designed and generally implemented effectively. For example, to ensure continuous communication within NDF, NDF holds weekly staff meetings. NDF's Deputy Director attends weekly ISN staff meetings. Immediately following the ISN meeting, the Deputy Director meets with NDF staff to brief them on the information obtained during the ISN meeting. NDF staff has the opportunity to discuss issues or concerns relating to NDF operations and projects at these meetings. During Kearney's fieldwork at the NDF office in February and March 2014, Kearney observed that the staff meetings occurred on a regular basis each week.

NDF also uses the functionality of PIMS to help ensure continuous communication about NDF projects between NDF personnel and management. Specifically, PMs maintain information on their projects' status in PIMS. The Deputy Director provides monthly PIMS Project Implementation Status Reports to the NDF Director. These reports include project status and the planned "next actions." Next actions are the actions required to keep the project moving, such as site visits, or to close the project. Although Kearney found that this control is designed effectively, Kearney found that it was not always implemented fully. During the 2014 audit, Kearney found that PMs did not consistently update next actions in PIMS, which limited the amount of information reported in the Project Implementation Status Report. Specifically, PMs had not entered next actions for 6 of 41 active projects (14.6 percent). During this audit, Kearney reassessed NDF's use of next actions. Specifically, Kearney reviewed the December 2014 Project Implementation Status Report and found that 22 of the 24 active projects included next actions. Only 2 of 24 active projects (8.3 percent) did not include next actions. In the 2014 report, OIG recommended that NDF train staff on the functionality of PIMS and develop a control to demonstrate that PMs monitor and document project progress timely.¹⁴ These recommendations remain open.

Additionally, NDF Review Panel meetings enable NDF to communicate on a regular basis with Department bureaus and offices outside NDF and with other Federal agencies. The NDF Review Panel consists of Assistant Secretaries and Deputy Assistant Secretaries from four bureaus within the Department as well the Assistant Secretary-level equivalents from other Federal agencies, such as the Departments of Commerce, Defense, Energy, and Homeland Security. The Panel was established to review project proposals submitted to NDF by various U.S. Government agencies and offices. The NDF Review Panel meets or exchanges emails at least quarterly and holds additional meetings as needed. The Review Panel determines, among other things, whether the proposed project is worth pursuing, if NDF is capable of executing the project, and if NDF can control the costs. A majority of the Department members of the Review Panel must vote to approve a proposal before the project can be initiated. Once a project proposal is approved or rejected by the Review Panel, an NDF Program Analyst prepares a Decision Memorandum, which

¹⁴ AUD-FM-15-18, Recommendations 3 and 4.

summarizes the project objectives, costs, and risks, and includes the Review Panel's recommendation to initiate, postpone, or reject the project. The Review Panel provides its recommendation to the Under Secretary of State for Arms Control and International Security who makes the final decision to initiate a project.

Kearney obtained and reviewed the meeting minutes for the Review Panel meeting held in August 2014. Kearney confirmed that representatives from all member agencies attended the meeting, and that the Panel reviewed newly proposed project proposals.

Controls Ensuring Unnecessary Duplication Is Identified and Eliminated Were Operating Effectively

Management Control Activity: *Is management eliminating unnecessary duplication within operations overseas among the different Mission elements and domestically among the bureaus and offices?*

NDF controls to identify and eliminate unnecessary duplication were designed and implemented effectively. Specifically, the NDF Review Panel meetings, which are attended by individuals from across the Department and government, enable NDF management to identify and eliminate potential duplication of NDF project activities before a project is approved.

Kearney selected a random sample of 3 of the 11 projects proposed during 2013 and 2014 and reviewed the Review Panel Decision Memoranda for the proposed projects.¹⁵ For one of the three projects, the Review Panel identified areas in which the project could overlap with work being performed by another government agency. NDF provided a justification to the Review Panel to support the need for the NDF project, and the Review Panel approved the project.

Controls To Assess Risk Were Operating Effectively

Management Control Activity: *Has management conducted a bureau/post risk assessment?*

NDF controls to assess risk were designed and implemented effectively. The FAM requires that Chiefs of Mission and bureau and office heads perform a risk assessment "of each assessable unit within their organization as frequently as circumstances warrant, but not less frequently than every 5 years."¹⁶

To assess risk, the NDF Director has contracted for external audits of NDF controls since 2012. Specifically, in 2012 the NDF Director requested an audit of controls over NDF's mission-critical processes – contracting and project management – and the integrity of data in PIMS. In 2014, the Director requested an audit to follow up on NDF's progress in addressing the control deficiencies identified during the 2012 audit. The NDF Director also requested this 2015 audit of

¹⁵ Details on the selection of this and other samples can be found in Appendix B, Scope and Methodology.

¹⁶ 2 FAM 022.7(3), "Bureau and Office Heads and Chiefs of Mission."

management and budget and finance controls, with specific audit procedures performed over the budget and finance controls and contracting processes relating to the NDF project in Egypt.

In addition to the external audits, NDF performs risk assessments on controls relating to specific projects. For example, because of the size of the NDF project in Egypt, the NDF Director has assigned a finance officer to travel with the PM on certain project site visits to ensure that financial controls are being followed and that the finance staff in NDF is aware of developments related to the project. NDF also assesses project risks through the NDF Review Panel process. During the review of the Decision Memoranda for 3 of the 11 projects proposed during 2013 and 2014, Kearney noted that the Review Panel considered project risks for all 3 projects.

Controls Over Business Class Travel Were Operating Effectively

Management Control Activity: *Are reviews performed to ensure that approval of business class travel includes an appropriate justification and is documented on DS-4087?*

Management Control Activity: *Are management control reviews conducted for ensuring that business class travel is authorized and approved by an appropriate official, which [sic] is not subordinate to the traveler?*

NDF controls to ensure that business class travel includes an appropriate justification and is authorized by an appropriate official were designed and operating effectively. The FAM requires that employees complete an *Authorization Request for Premium Class Air Travel* (Form DS-4087) for all business class air travel. The form must include the justification for business class and be authorized by an approving official not subordinate to the traveler.¹⁷ Employees are allowed business class travel 1) when coach-class air accommodations are not available, 2) when there is no space available in coach class, 3) for travel by an individual with a disability or special need, 4) under security or exceptional circumstances, 5) when foreign-carrier coach-class air accommodations are inadequate, 6) when such accommodations result in overall cost savings, 7) when required to meet the agency mission, 8) when using frequent traveler benefits, 9) when the transportation is paid in full by a non-Federal source if otherwise authorized by law or regulation, and 10) for travel in excess of 14 hours for temporary duty travel or medical evacuation travel with certain exceptions.

NDF requires that NDF staff submit their initial request for travel to the NDF Finance Office. The Finance Office sends an email to the NDF Director or Deputy Director listing the expenses related to the trip and stating the reason the traveler is requesting business class. The Director or Deputy Director approves or denies the request via email. If the traveler receives an initial approval from the Director or Deputy Director, the traveler, or a finance officer on the traveler's behalf, submits a formal travel request through the Department's travel system. The travel system automatically routes the authorization for NDF business class air travel to ISN/EX for final approval.

¹⁷ 14 FAM 567.2-4, "Business-Class Travel."

Between October 1, 2013, and December 31, 2014, NDF staff used business class travel on four occasions. Kearney reviewed the travel request packages for the four trips. The *Authorization Request for Premium Class Air Travel* for all four trips included an appropriate justification. Three of the requests were justified based on temporary duty travel in excess of 14 hours, and one request was justified because coach-class accommodations were not available. Three of the four authorization requests were signed by the Director or Deputy Director. In one instance, the authorization request on file was not signed; however, NDF had email documentation showing that the NDF Director had approved the request. Additionally, Kearney confirmed that the ISN/EX Executive Director or Deputy Executive Director had approved the three business class requests that were for air travel; the fourth business class request was for travel by train, for which authorization by ISN/EX was not required.

Purchase Card and Travel Card Controls Were Operating Effectively

Management Control Activity: *Have reviews been conducted on credit card usage, i.e., purchase cards and travel cards?*

NDF controls to ensure that reviews over purchase and travel cards are conducted were designed and implemented effectively. One of the NDF finance officers holds a purchase card for the acquisition of supplies or services, the aggregated amount of which cannot exceed \$3,000. NDF has developed and implemented a *Purchase Card Request Form* to ensure that all purchases under \$3,000 are properly documented and approved. Any NDF employee can make a purchase request. The employee must include the product or service requested, the quantity, and the price on the *Purchase Card Request Form*. Purchase requests must be approved by both the NDF Director and the Comptroller. In addition, the finance officer maintains a log of all purchases made during the month and compares the information in the log to the information in the monthly credit card statement to ensure that the charges agree.

ISN also reviews NDF's purchase card usage. On a monthly basis, the NDF finance officer submits the credit card statement and all supporting invoices to the ISN/EX Project Coordinator for review and approval. ISN/EX also conducts an annual review of purchase card purchases. NDF and other ISN purchase card holders are required to submit all credit card records for the fiscal year to the ISN/EX Supervisory Support Services Specialist. The Supervisory Support Services Specialist reviews the records and prepares a report on the appropriateness of the charges.

Kearney selected a sample of 3 purchase card transactions totaling \$5,145 from the 26 purchase card transactions totaling \$21,795 made from April 1, 2014, to December 31, 2014.¹⁸ Kearney confirmed that the *Purchase Card Request Form* was properly completed for each transaction. Kearney also obtained the October 2014 credit card statement and the finance officer's purchase card log and confirmed the information from the statements agreed with the information

¹⁸ Kearney leveraged the sample of expenditures selected to test the accuracy of expenses for this procedure. Details on the selection of the sample can be found in Appendix B, Scope and Methodology.

maintained in the log. Additionally, Kearney confirmed with the ISN/EX Supervisory Support Services Specialist that NDF had submitted its FY 2014 records for the annual ISN/EX purchase card review.

Travel card purchases are not subject to the same level of review in NDF as purchase card charges because the traveler is responsible for paying his/her own bill. Only 5 of 21 NDF employees have travel cards. Travelers submit an expense report to the NDF Finance Office detailing all travel related costs incurred. The traveler must provide support for all travel costs in order to be reimbursed. NDF finance officers review the supporting documentation and ensure that the travel costs align with the approved travel authorization. They also confirm that the submitted expenses are eligible for reimbursement based on Department regulations. The ISN Bureau Program Coordinator along with CGFS staff monitor employee travel card purchases and limits. If CGFS identifies charges on the travel card that were not explicitly authorized in a travel authorization, the traveler will not be reimbursed for that expense. Department employees, including NDF staff, who fail to make timely payments on their travel card may be subject to garnishment of wages. When potential misuse is identified by CGFS, CGFS sends a Misuse Assessment Form to the ISN Bureau Program Coordinator. After two instances of potential misuse are identified, CGFS requests that the employee be counseled about the continued misuse of the travel card. Kearney confirmed with the ISN Bureau Program Coordinator that no NDF employee had delinquent payments or reports of travel card misuse.

Controls To Ensure Effective Management of Conference and Training Costs Were Operating Effectively

Management Control Activity: *Does management conduct reviews to effectively manage costs related to sponsoring and attending conferences, while still achieving the Department's mission?*

NDF controls to effectively manage costs related to sponsoring and attending conferences¹⁹ were designed and operating effectively. NDF funds employee development training and occasionally sponsors project-related training. NDF staff interested in obtaining training must submit a training request to the Director for approval. The request must include the description, cost, and benefit of the training.

Kearney reviewed all NDF administrative costs from April through December 2014 and identified the costs related to employee development, including travel costs. During this period, two NDF finance officers attended Executive Potential Program training. This training is a 1-year program offered by the Graduate School USA designed to help senior leaders understand and meet the challenges facing today's Federal workforce. The training requires a significant amount of travel.

¹⁹ OMB Memorandum M-12-12, "Promoting Efficient Spending to Support Agency Operations," May 11, 2012, requires agencies to exercise discretion and judgment in ensuring conference expenses are appropriate, necessary, and managed to minimize expense to taxpayers. The memorandum defines conferences as "[a] meeting, retreat, seminar, symposium or event that involves attendee travel. The term 'conference' also applies to training activities that are considered to be conferences under 5 CFR 410.404."

Kearney obtained and reviewed copies of the training requests. The requests included the description, cost, and benefit of the training and were approved by the NDF Director.

In some cases, NDF sponsors training events that are related to project execution. During its review of proposed projects, the Review Panel determines if the costs associated with the project, including the costs of training events, are reasonable. Kearney reviewed the Decision Memorandum for one project for which NDF sponsored training exercises for a Proliferation Security Initiative event. The cost of the training was included in the project proposal and reviewed by the Review Panel along with the costs of other project tasks. The Review Panel determined that the cost of the training was reasonable and that the objective of the training event aligned with NDF's and the Department's mission.

Controls Related To External Reviews Were Operating Effectively

Management Control Activity: *Does management take a proactive approach to ensuring that outstanding OIG, Government Accountability Office (GAO), or other external review recommendations are addressed and closed?*

NDF controls to ensure that external review recommendations are addressed and closed were designed and implemented effectively. When external reviews, including OIG and GAO audits, are performed and recommendations made to NDF, the NDF Director assigns a person on his staff to address the recommendations. For example, the NDF Director assigned one PM to respond to the recommendations contained in the reports on OIG's 2012 and 2014 audits and another PM to respond to the recommendations contained in a 2012 GAO report.²⁰

Kearney reviewed the NDF documentation relating to OIG's 2012 audit report. The report included 18 recommendations. NDF maintained a binder to track the progress of closing each recommendation. The binder included documentation of frequent communication between NDF and OIG regarding the status of the recommendations and of the actions taken by NDF to address and close the recommendations. To assess whether the actions taken sufficiently addressed the recommendations, NDF requested a follow-up audit in 2014. During the 2014 audit, Kearney determined that NDF had sufficiently addressed 8 of the 18 recommendations, and OIG closed these recommendations.²¹ During the 2014 audit, OIG reissued recommendations related to the remaining 10 recommendations from the 2012 audit. Although NDF was developing corrective actions to address the 10 recommendations, it had not completed implementing these items at the time of the audit.

²⁰ *Nonproliferation and Disarmament Fund: State Should Better Assure the Effective Use of Program Authorities* (GAO-13-83, Nov. 2012).

²¹ The Office of Audits' practice is to close recommendations from prior projects during follow-up audits and issue new recommendations if the issue has not been resolved. Appendix B in audit report AUD-FM-15-18 provides a crosswalk of the recommendations between the 2012 and 2014 report.

Kearney also obtained and reviewed documentation relating to GAO's 2012 audit of NDF. The documentation evidenced email communication between NDF and GAO throughout the audit and in response to the four GAO recommendations included in the report. Three of the four recommendations have been closed, and the documentation showed that ISN was taking action to address the fourth recommendation.

Controls Related to Organizational Reviews Should Be Developed

Management Control Activity: *Are organizational reviews performed to ensure appropriate supervision and authority exists [sic]?*

NDF does not have a control to periodically review its organizational structure to ensure that appropriate supervision and authority exist. The FAM states that "organizations should operate with the minimum number of organizational levels, with emphasis on delegation of authority to the lowest appropriate working levels" and that "organizations should minimize the number of deputy, assistant, and special assistant positions."²²

NDF is a small organization with 21 employees. NDF staff has well-defined roles and responsibilities. Specifically, the NDF Director, among other things, determines the proposals to pursue, provides policy and programmatic guidance, and ensures that project goals align with NDF's mission. The Deputy Director assigns projects to PMs, approves plans for project teams, reviews project reports, and provides the status of all projects to the Director. PMs oversee NDF projects, approve project-related tasks, and provide project status updates to the Deputy Director. The Comptroller approves all NDF funding. Finance officers report to the Comptroller and each is assigned responsibility for specific types of transactions, such as travel, payroll, or contracts; and back-up officers have been identified for each type of transaction.

Kearney assessed NDF's organization and determined that it complied with FAM guidelines. NDF has a functional structure and a certain amount of authority is delegated to all levels within NDF. In a functional organization, each portion of the organization is grouped according to its purpose. The functional structure works well for small organizations in which each department can rely on the talent and knowledge of its workers to support itself. Based upon NDF's size, Kearney concluded that NDF's existing structure is reasonable. However, conditions in an organization may change over time, and existing lines of authority and supervision may no longer be the most appropriate to enable an organization to meet its goals effectively and efficiently. Without periodic reviews of its organizational structure, NDF may not recognize and address changing needs or validate and reemphasize the lines of authority and supervision in its existing structure.

Recommendation 1: OIG recommends that the Nonproliferation and Disarmament Fund develop a control to periodically reevaluate its lines of authority, responsibility, and reporting to ensure that its organizational structure continues to meet its needs.

²² 3 FAM 2614 (d) and (e), "Policy."

Management Response and OIG Reply: NDF agreed with the recommendation, and OIG considers the recommendation resolved. The recommendation can be closed when OIG reviews and accepts documentation showing that NDF has developed a control to periodically reevaluate its lines of authority, responsibility, and reporting.

Controls Ensuring Compliance with Laws and Regulations Need Improvement

Management Control Activity: *Does management ensure compliance with laws and regulations pertaining to the work of their areas of responsibilities as specified in 1 FAM 000 thru 1 FAM 600, "Authority, Responsibility and Organization?"*

Kearney found that controls ensuring NDF's adherence with laws and regulations could be improved. NDF operates under numerous laws and regulations. Based on the scope of this audit, Kearney did not assess NDF's compliance with all applicable laws and regulations; instead, Kearney focused its review on the legislation underpinning NDF's existence – the FREEDOM Support Act²³ and the Department of State, Foreign Operations, and Related Programs Appropriations Act.²⁴

The FREEDOM Support Act requires that no less than 15 days before NDF obligates funds to a project, a report on the proposed project should be submitted to the Speaker of the House of Representatives, the President pro tempore of the Senate, and the appropriate congressional committees.²⁵ Once NDF notifies Congress of the proposed project, a 15-day timeline is initiated during which Congress has the opportunity to reject the proposal. If the 15-day limit elapses without rejection, NDF may begin to execute the project. To ensure compliance with this aspect of the FREEDOM Support Act, NDF's Project Management Guide requires that a copy of the Congressional Notification be obtained from the Bureau of Legislative Affairs prior to creating a project in PIMS. Kearney identified one new project that had been initiated since the 2014 audit and confirmed that NDF obtained a copy of the Congressional Notification from the Bureau of Legislative Affairs prior to initiating the project.

NDF must spend project funds in accordance with the specific purposes included in the Congressional Notification. During this audit, NDF informed Kearney of an instance in which an MOU allowed a PM to reprogram unused funds. Specifically, the MOU states, "any NDF funds remaining ... are to be returned to NDF **unless otherwise directed in writing by the NDF PM** [emphasis added]." If the international organization did not expend all funds on the MOU, this language provides the PM the authority to direct the organization to spend the funds for a purpose outside the original scope of the project.

NDF management and finance officers review and approve MOUs before they are executed. However, NDF did not have a formal policy requiring this approval or addressing the

²³ Pub. L. No. 102-511 (1992).

²⁴ Consolidated and Further Continuing Appropriations Act, 2015, Pub. L. No. 113-235.

²⁵ Pub. L. No. 102-511, § 508; 22 U.S.C. § 5858(a).

circumstances in which changes to an MOU may be made or the process for making such changes. In this case, NDF personnel stated that the language may have been added after NDF management and finance officers reviewed and approved the MOU.

A PM's ability to instruct an international organization on how to use excess funds would be reasonable if the planned use of the excess funds is approved by the Assistant Secretary and fits within the project description approved by the Under Secretary for Arms Control and International Security and Congress notified. However, as the MOU is currently written, the PM could instruct that the international organization to use the excess funds for expenditures in violation of the FREEDOM Support Act or other laws and regulations. In this instance, the PM did not exercise the authority provided in the MOU, and the excess funds were returned to NDF. The Department of State, Foreign Operations, and Related Programs Appropriations Act provides NDF with "notwithstanding authority." The use of NDF's "notwithstanding authority" is governed by the Department's Office of the Legal Advisor. Kearney considers this to be an effective control in ensuring that "notwithstanding authority" is used only when appropriate. However, during the 2014 audit, Kearney found that, although NDF had improved its control over the use of "notwithstanding authority," NDF did not document the specific provisions within the laws or regulations for which the authority was used. In the 2014 report, OIG recommended that NDF update its policy to require that these provisions be identified and documented.²⁶ This recommendation remains open.

Recommendation 2: OIG recommends that the Nonproliferation and Disarmament Fund (NDF) develop and implement a standard process for developing Memorandums of Understanding (MOU). This process should require the approval of the final MOU by, at a minimum, the NDF Director and Comptroller as well as controls to ensure that no changes can be made to the MOU without approval by these individuals.

Management Response and OIG Reply: NDF agreed with the recommendation, and OIG considers the recommendation resolved. The recommendation can be closed when OIG reviews and accepts documentation showing that NDF has developed and implemented a standard process for developing MOUs.

Controls To Ensure Cost Effectiveness of Outsourcing Need To Be Developed

Management Control Activity: *Has management performed reviews to evaluate the cost-effectiveness and appropriateness of either insourcing or outsourcing functions that are not inherently governmental?*

NDF does not have a control to evaluate the cost effectiveness and appropriateness of insourcing or outsourcing functions that are not inherently governmental. The FAM states that

²⁶ AUD-FM-15-18, Recommendation 2.

“Organization heads must manage organization and position structures like they would monetary resources” and that “Positions should be carefully planned and staffed to make the most effective use of human resources at the lowest practical expenditure to accomplish assigned missions.”²⁷ Additionally, OMB guidance relating to managing the multi-sector workforce states that “agencies should perform a cost analysis that addresses the full costs of government and private sector performance and provides ‘like comparisons’ of costs that are of a sufficient magnitude to influence the final decision on the most cost effective source of support for the organization.”²⁸

Currently, 7 of NDF’s 21 staff are contractors, including 5 PSCs and 2 other contractors. However, NDF has not performed a formal, documented comparison of the costs of employing contractors to the costs of employing full-time employees. NDF management stated that using PSCs as PMs is more cost-effective than hiring full-time employees because a personal services contract can be terminated or suspended when a project ends and no other projects are beginning. Full-time employees would remain on the payroll even when there is no work available.

Kearney determined the number of years that each PSC had been employed with NDF. The three PSCs who work as PMs have been employed by NDF for 6 to 8 years continuously. The two PSCs who perform ongoing internal operations have worked for NDF for 6 and 11 years, respectively. The remaining two contractors have worked for NDF 1 and 5 years, respectively.

Without a formal, documented cost analysis, NDF cannot determine whether its use of contractors is, in fact, more cost effective than hiring full-time employees. Kearney recognizes the unique and specialized skills and experience of the PSCs filling the PM positions and notes that a cost analysis would need to take into consideration the level of expertise needed to execute project management responsibilities as well as the cost of benefits provided to full-time employees.

Recommendation 3: OIG recommends that the Nonproliferation and Disarmament Fund perform a comparison of the cost of employing contractors to the cost of equivalent Federal positions.

Management Response and OIG Reply: NDF agreed with the recommendation, and OIG considers the recommendation resolved. The recommendation can be closed when OIG reviews and accepts documentation showing that NDF performed the cost comparison.

²⁷ 3 FAM 2614 (a) and (c), “Policy.”

²⁸ OMB Memorandum M-09-26, *Managing the Multi-Sector Workforce*, July 29, 2009.

Finding B: Most Budget and Finance Management Controls Were Designed and Implemented Effectively, But Some Controls Need Improvement

Kearney found that most of NDF's controls related to the budget and finance activities listed in the Management Controls checklist were designed and implemented effectively. Specifically, NDF effectively designed and implemented controls to systematically and timely identify ULOs in need of deobligation and to ensure that contracts and grants are closed out in a manner to prevent invalid ULOs. In addition, NDF has effective controls to ensure the collection of unspent project funds provided to other government agencies and international organizations. However, Kearney identified one instance in which a PM did not document issues related to confirming that all NDF funds were expended. The lack of documentation may limit NDF's ability to ensure that all excess funds have been returned to NDF or to prevent similar issues from occurring during future projects.

Kearney found that the NDF controls to ensure segregation of duties in the requisition, purchasing, and receiving functions and to ensure that obligations supporting disbursements were properly authorized were operating effectively. However, other disbursement controls need improvement. Specifically, final obligation amounts were not always entered into PIMS accurately because NDF's reconciliation process was not effective. In addition, the control to ensure that invoices are properly approved was not operating as designed because PMs did not use the correct certification form. As a result, payments may be made for goods and services not received. Although the current processes ensured that expense amounts were accurately recorded, not all expenses were recorded in PIMS in a timely manner because of the ineffective reconciliation process. When information is not recorded in PIMS timely, NDF management and PMs may not have the information they need to properly approve disbursements and manage NDF projects.

Kearney also found that NDF did not have a formal process for developing and documenting its annual budget request because, in part, of the unforeseen nature of NDF projects. Additionally, NDF did not have an effective process to determine the amount of funding required for administrative purposes. As a result, funds may not be available for NDF projects when needed.

Unliquidated Obligations Monitoring Control Was Operating Effectively

Budget and Finance Control Activity: Are review procedures in place to systematically and timely identify ULOs in need of deobligation?

The NDF control to systematically and timely identify ULOs in need of deobligation was designed and implemented effectively. PMs are responsible for ensuring that the ULOs related

to their projects are valid; that is, the balances on the obligations are still needed.²⁹ The Comptroller and finance officers are responsible for ensuring that the ULOs for administrative costs, such as the costs to provide cellular phone service, are valid. Each month, PIMS automatically produces a ULO report, which is provided to the PMs and finance officers to review and determine whether the ULOs are still valid. If a PM or finance officer identifies a ULO that is no longer valid and should be deobligated, the PM or finance officer prepares a memorandum requesting deobligation.

Kearney reviewed all 51 NDF ULOs, amounting to \$27 million, in GFMS at December 31, 2014. Of 51 ULOs, Kearney identified 6 ULOs with balances amounting to \$5 million that had no expenditures since June 2014. For these six ULOs, NDF personnel provided reasonable explanations for the continued need for the ULO.

As shown in Table 1, the results of this review are consistent with the results of Kearney's review of ULOs during the 2014 audit, indicating that NDF's process has continued to operate effectively.

Table 1. Results of Invalid ULO Tests in 2015 and 2014

Audit Year	ULOs Identified Without Activity in 6 Months	Invalid ULOs
2015	6	0
2014	13	0

Source: Prepared by Kearney based on its reviews of ULOs during the 2014 and 2015 audits.

Kearney also analyzed the deobligations processed in PIMS from April 2014 through December 2014. This analysis showed that, although the number of deobligations varied each month, the deobligation of ULOs that were no longer needed occurred on a consistent, regular basis.

Table 2. Deobligation Activity, April 2014 through December 2014

Month	Number of Obligations Deobligated in PIMS
April	9
May	11
June	14
July	9
August	16
September	19
October	6
November	7

²⁹ The U.S. Standard General Ledger defines a ULO as "the amount of goods and/or services ordered that have not been ... received and for which amounts have not been prepaid or advanced."

Month	Number of Obligations Deobligated in PIMS
December	12
Total	103

Source: Prepared by Kearney based on its review of the Deobligations from April 2014 – January 2015 Report from PIMS.

Contract Closeout Controls Were Operating Effectively

Budget and Finance Control Activity: *Are contracts/grants being closed out timely to mitigate the risk of having ULOs?*

NDF controls to close contracts and grants³⁰ timely to mitigate the risk of having ULOs were designed and operating effectively. During the 2014 audit, Kearney found that NDF had developed and implemented a formal process to close out contracts in a timely manner. Specifically, NDF requires that its employees close out contracts in a manner consistent with Federal and Department acquisition regulations. In addition, NDF requires that the PMs complete a Contracting Officer's Representative (COR) Contract Closeout Checklist to ensure that all contractual and funding actions required under each contract are complete to facilitate the contract closeout process.

Based on the positive results of the tests of the NDF control to identify and deobligate ULOs, which included all contract and grant ULOs, Kearney concluded that the contract and grant closeout controls are operating effectively.

Controls To Ensure the Collection of Unspent Advances Were Designed and Implemented Effectively But Need Improvement

Budget and Finance Control Activity: *Are reviews performed on the Bureau's cash management and collection process?*

NDF controls to ensure that NDF collects the funds provided to government agencies and international organizations that remain unspent at the completion of a project were designed and implemented effectively but need improvement. The FAM states that the management, financial management, or program officer is responsible for "determining whether a debt exists, and if so the amount owed" as well as "maintaining records of the debt and monitoring uncollected debts."³¹

³⁰ Since April 1, 2014, NDF has not issued any grants, and only 1 of the 51 ULOs outstanding on December 31, 2014, was for a grant. Because it does not generally issue grants, NDF does not have a formal closeout process for grants.

³¹ 4 FAM 492.1, a(1) and (3), "Debt Determinations."

NDF advances funds to government agencies and international organizations to complete project objectives, such as the removal of chemical weapons from a country, under the terms of an Inter-Agency Agreement (IAA), Memorandum of Discussion (MOD), or MOU. At the end of each project, PMs are required to prepare a *Project Closeout Checklist*, which lists 12 tasks that the PM must complete before closing a project. One of the 12 tasks is to provide assurance that the funds provided to other government agencies and international organizations were used as stated in the IAA, MOD, or MOU, and that remaining funds were returned to NDF. The completed Checklist must be signed by the PM and approved by the NDF Director.

Kearney reviewed the project files for all eight projects with a status of "Closing Projects – Financial Review Complete" in PIMS. This status means that the project is ready to be closed, and that a review of project funding has occurred. Of the eight projects, NDF provided funding through an IAA, MOD, or MOU for six of the projects. Kearney obtained a copy of the *Project Closeout Checklist* for each of the six projects and confirmed that the Checklist was signed by the PM and approved by the NDF Director.

Kearney also reviewed the documentation supporting the PM's response in the Checklist that funds were returned or there were no excess funds requiring return. For four of the six projects, Kearney determined that the documentation included sufficient information to support the PM's response. For the remaining two projects, both of which related to one MOU with the Department of Energy, the documentation stated that the funding provided by NDF was spent in exact accordance with the budget, with no remaining funds. Upon further review, Kearney learned that NDF funds were commingled with Department of Energy funds. Because the funds were commingled, the Department of Energy was unable to provide a report showing that the NDF funds were fully expended, as required by the MOU. Other documentation, including emails and budget reports, evidenced that the PM researched this issue and concluded that there were no excess funds because the project went over budget, and the Department of Energy had provided additional funds to the project to make up the shortfall. However, the PM did not document this information in the *Project Closeout Checklist*.

According to NDF finance officers, the PM did not understand the importance of documenting these issues in the *Project Closeout Checklist*. No financial impact resulted from the commingling of funds or the lack of documentation in this case. However, without adequate documentation supporting the conclusions reached by PMs during project closeouts, NDF management may not have the information necessary to confirm that all excess funds have been returned to NDF or the information needed to prevent similar issues from occurring during future projects.

Recommendation 4: OIG recommends that the Nonproliferation and Disarmament Fund modify the *Project Closeout Checklist* to include an area where project managers can document any issues encountered when completing the checklist and formally notify project managers of the requirement to document issues.

Management Response and OIG Reply: NDF agreed with the recommendation, and OIG considers the recommendation resolved. The recommendation can be closed when OIG reviews and accepts documentation showing that NDF has modified the *Project Closeout Checklist* to include an area where project managers can document any issues encountered when completing the checklist and formally notify project managers of the requirement to document issues.

Controls To Ensure Segregation of Duties Were Operating Effectively

Budget and Finance Control Activity: *Are reviews being conducted to verify that segregation of duties exists between requisition, purchasing, and receiving functions?*

NDF controls to ensure that segregation of duties exists were designed and implemented effectively. The FAH requires certain operations be separated “to reduce the risk of error, waste, and wrongful acts.” For example, purchasing goods and services, recording receipt of goods and services, and examining invoices should be separated. If overlaps are necessary, management should implement checks and balances to ensure that responsibilities are carried out properly.³²

NDF assignment of responsibilities and NDF processes incorporate segregation of duties controls for initiating, approving, and recording transactions. For example, for NDF projects, the NDF Director and other agencies propose projects, the NDF Review Panel recommends projects, and the Under Secretary for Arms Control and International Security approves projects. Depending on the project, the Bureau of Administration contracting officers execute the related contracts or the NDF Director approves the related IAAs, MODs, and MOUs. The NDF Comptroller approves the obligation of funds, and the NDF finance officers record the obligation transactions. PMs certify the receipt of goods and services, the NDF Comptroller approves payment, and the NDF finance officers record the expense transactions.

To test segregation of duties, Kearney selected two samples. The first sample of 46 transactions, amounting to \$7.5 million, were selected from 538 expense transactions, amounting to \$8.8 million, that were recorded in PIMS from April 1, 2014, through December 31, 2014, for all projects except the project in Egypt. The second sample of 18 transactions, amounting to \$8.6 million, were selected from 572 expense transactions, amounting to \$46.6 million, that were recorded in PIMS from January 1, 2009, through December 31, 2014, for the project in Egypt.³³

Kearney reviewed the purchase, receiving, and invoice documentation for the selected transactions and determined that all of the transactions tested were initiated, approved, recorded, and otherwise handled in accordance with NDF segregation of duties controls.

³² 4 FAH-3 H-413.5 (a) and (b)(1) through (3), “Separation of Duties.”

³³ The period tested for the Egypt project is different from the period tested for all other projects. Kearney tested Egypt project expenses from August 1, 2009, when the Egypt project was initiated, through December 31, 2014. Kearney tested all other project expenses from April 1, 2014, through December 31, 2014.

Controls Relating To Disbursements Need Improvement

Budget and Finance Control Activity: *Are reviews performed to verify disbursements are properly authorized and supporting documentation and records are maintained?*

NDF controls to verify that disbursements are properly authorized and supporting documentation and records are maintained need improvement. For a disbursement to be properly authorized, it must be supported by a valid obligating document, the obligation must be properly recorded in PIMS, the invoice must be properly approved, and the expense must be properly recorded in PIMS.

We found that two controls surrounding NDF's disbursing process were properly designed and operating effectively. However, we also found that two controls were ineffectively designed and another one control was operating ineffectively, despite having effective control design. Specifically, the NDF control to ensure that obligations were recorded in PIMS prior to the processing of an invoice was designed and operating effectively. However, the NDF control to ensure that final obligation amounts are entered into PIMS accurately, based upon a signed contract or other obligating documents, was not designed effectively. In addition, the NDF control to ensure that the receipt of goods and services are verified before a payment is made was designed effectively but not operating effectively. Despite ineffective control over receipt of goods and services, the control to ensure the NDF Comptroller certified invoices before they were paid was both designed and operating effectively. Finally, although NDF controls ensured that expense amounts were accurately recorded, not all expenses were recorded in PIMS due to ineffectively designed manual processes.

Obligations

To make a disbursement, the FAH states that "supporting documentation is required to ensure that all payments are authorized, accurate, legal, correct, and that the goods were actually received or services actually performed."³⁴ Supporting documentation includes a proper obligating document, such as a purchase order or contract.³⁵ Table 3 presents the NDF approvals required for different obligating document types.

Table 3. NDF Obligation Approvals

Obligation Type	Required Approvals
Vender Contracts	Contracting Officer
Grants	NDF Director and Grants Officer
IAAs, MODs, MOUs, and Reimbursable Agreements	NDF Comptroller, NDF Director, and Assistant Secretary for ISN
PSC Contracts	NDF Comptroller and Contracting Officer

³⁴ 4 FAH-3 H-423.5, "Supporting Documentation."

³⁵ 4 FAH-3 H-433.2, "Verifying Information Accuracy."

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Travel	NDF Comptroller or NDF Finance Officer
Purchase Cards	
Requisition	NDF Finance Officer and NDF Comptroller
Purchase Card Request Form	NDF Comptroller and NDF Director

Source: Prepared by Kearney based upon review of NDF policies and procedures.

Kearney reviewed the obligating documents for the 64 selected expense transactions selected for testing, amounting to \$16 million, to determine whether the transactions had been properly approved. Kearney found that all 64 transactions had valid obligating documents that were approved in accordance with the required approvals listed in Table 3. Table 4 presents the breakdown of the expenses tested by project category.

Table 4. Tested Expenses With Appropriate Obligating Documents and Approvals

Project Category*	Number Tested	Number with Approved Obligation	Invoice Amount
Egypt Project	18	18	\$8,587,488
All Other Projects	46	46	\$7,494,709
Total	64	64	\$16,082,197

* The scope period of the testing performed on the Egypt project is different from the scope of the testing performed on all other projects. The scope of period of testing of Egypt expenses is from August 1, 2009, to December 31, 2014, while the scope of the period of testing for all other project expenses is April 1, 2014, to December 31, 2014.

Source: Prepared by Kearney based upon the PIMS Transactions Report January 2009 – December 2014 and the results of expense testing.

Because NDF relies on obligation amounts in PIMS when approving disbursements, NDF controls must ensure that the obligations are accurately recorded in PIMS; otherwise, a disbursement may be inappropriately rejected. NDF records obligation estimates in PIMS based upon procurement requests. These obligations are identified as estimates by the use of an estimate indicator “flag” in PIMS. When NDF establishes a formal obligation, such as a contract or purchase order, NDF records the obligation in GFMS, enters the actual amount of the obligation in PIMS, and removes the estimate “flag.”

GAO Standards for Internal Control in the Federal Government states that “transactions [should be] promptly recorded to maintain their relevance and value to management in controlling operations and making decisions.”³⁶ Additionally, NDF policies and procedures require that the estimate “flag” be unchecked in PIMS when the obligations are entered into GFMS and become binding.

In the 2014 audit report, OIG recommended that NDF develop and implement an automated process to reconcile financial data in PIMS, including obligations, to the financial data in GFMS

³⁶ *Standards for Internal Control in the Federal Government*, GAO-14-704G (September 2014).

or a manual process that captures all transactions in both systems over a period of time. An automated process was not developed, but NDF indicated that the manual processes were improved. To determine whether the manual processes were sufficiently improved to ensure that all NDF obligations were recorded in PIMS, Kearney reconciled the ULOs in PIMS to the ULOs in GFMS as of December 31, 2014. The 62 ULOs in PIMS matched the 51 corresponding obligations in GFMS.³⁷

To further test whether obligation amounts were accurately recorded in PIMS and supporting documentation was maintained, Kearney selected a sample of obligations. From a population of 124 obligations totaling \$71 million, Kearney selected 19 obligations totaling \$67 million, of which 12 obligations amounting to \$65 million were related to the project in Egypt. Kearney obtained supporting documentation for each obligation and compared this documentation to the final amount recorded in PIMS.³⁸ Of 19 obligations, 4 were not properly recorded. Specifically, the final amount of the obligation in PIMS did not agree to the final amount of the obligation in the executed contract. Table 5 provides the results of testing the accuracy of obligations.

Table 5. Results of Testing the Accuracy of Obligations

Project Category	Number Tested	PIMS Amount Sampled	Amount in PIMS when the Estimate Flag Was Unchecked	Amount per Executed Obligation	Number of Exceptions	Amount of Exceptions
Egypt Project	12	\$65,291,198	\$65,291,198	\$64,049,693	2	(\$1,241,505)
All Other Projects	7	1,588,813	6,935,063	\$3,359,970	2	(3,575,093)
Total	19	\$66,880,011	\$72,226,261	\$67,409,663	4	(\$4,816,598)

Source: Prepared by Kearney based on the results of testing the accuracy of obligations.

The two exceptions related to the Egypt project were executed in 2009, but the obligation amounts in PIMS were not corrected until Kearney informed NDF personnel of the discrepancy during this audit. The amount in PIMS for one of the exceptions for the other projects was not updated to match the final amount funded in the contract until 65 working days after the contract was executed, which was 35 working days after the estimate flag was removed in PIMS. Another obligation was corrected to match the executed contract amount 12 working days after the contract was executed.

³⁷ There is not an exact match of ULOs between the two systems because of differences in the format of the PIMS Obligations Report and GFMS Obligations Report.

³⁸ Kearney considered the amount in PIMS to be final when the estimate flag was removed.

NDF personnel stated that the errors and lack of timely identification of these errors occurred because NDF's processes to reconcile transactions in PIMS with the transactions in GFMS are manual and labor intensive. Additionally, NDF finance officers indicated that contracting officers did not always provide NDF the final contracts in a timely manner. When accurate and complete financial information is not recorded in PIMS or is not recorded timely, NDF management and PMs may not have the information they need to properly manage NDF projects.

Based upon this testing, Kearney has concluded that NDF controls to ensure that obligations were recorded in PIMS prior to the processing of an invoice were designed and operating effectively. However, the NDF control to ensure that final obligation amounts are entered into PIMS accurately, based upon a signed contract or other obligating documents, was not designed effectively. Therefore, the recommendation from the prior report remains open.³⁹

Invoice Authorization

In addition to a proper obligating document, the FAH states that documentation supporting a payment must include a proper receiving document, such as a receiving report or annotation of receipt on the invoice.⁴⁰ The FAH further states that "the COR should review [invoices] to determine the validity of costs claimed and relate total expenditures to the physical progress of the contract."⁴¹ Further, NDF requires that the PMs complete the "PM/COR Invoice Certification of Deliverables and/or Services Form" for each invoice relating to their projects. The PM must indicate on this form whether "(A) the COR inspected and accepted the deliverables described in the voucher, or (B) a third party inspected and accepted the deliverables." Additionally, the PM must indicate whether the items on the invoice have been fully or partially received or indicate that the items were not received. To document their review and approval of the invoice, PMs must sign the form. In addition, the NDF Comptroller must review the invoice and supporting documentation and certify the invoice for payment.

Of 64 expense transactions selected for testing, totaling \$16 million, 29 expense transactions, amounting to \$5.5 million, related to a vendor invoice. Kearney reviewed the receiving documentation and invoices for the 29 transactions and determined that the NDF Comptroller certified the 29 transactions for payment. However, the PM did not indicate whether the COR or a third party inspected and accepted the deliverables on the "PM/COR Invoice Certification of Deliverables and/or Services Form" for all 29 sampled transactions. The number and dollar amount of invoices without a proper PM/COR certification for the project in Egypt and for all other projects are presented in Table 6.

³⁹ AUD-FM-15-18, Recommendation 9.

⁴⁰ 4 FAH-3 H-433.2, "Verifying Information Accuracy."

⁴¹ 14 FAH-2 H-522.4, "Reviewing Vouchers."

Table 6. Invoices Tested That Did Not Have PM/COR Certification

Project Category	Invoices Tested	Invoices Without PM/COR	
		Certification	Invoice Amount
Egypt Project	8	8	\$2,829,599
All Other Projects	21	21	2,683,442
Total	29	29	\$5,513,041

Source: Prepared by Kearney based on the results of PM/COR certification testing.

The NDF Comptroller stated that PMs were not using the correct “PM/COR Invoice Certification of Deliverables and/or Services Form” because they were in the habit of using an older form. Additionally, finance officers did not reject invoices that were submitted by PMs with the wrong form. Without proper certification by an individual who has direct knowledge of the goods or services, payments may be made for goods or services that NDF does not receive.

In the 2014 report, OIG recommended that NDF provide the CORs a written notification of the requirement to complete the PM/COR Invoice Certification of Deliverables and/or Services Form.⁴² This recommendation remains open.

Expenses

The PMs use the expense information in PIMS when reviewing and approving invoices and managing project progress. NDF finance personnel have a number of manual processes at the transaction or project level to ensure that expense amounts are properly recorded in PIMS. For example, an NDF finance officer created an application to track vendor invoices as they are received by NDF, entered into GFMS, and subsequently paid. Similarly, to ensure PSC payments are entered correctly into GFMS and PIMS, NDF finance officers review the bi-weekly “Advice of Charge” report that lists payroll transactions for PSCs in GFMS and compare the charges to the amounts PSCs should be paid. Additionally, the Finance Office has a filing system to ensure that supporting documentation for all amounts recorded in PIMS is maintained.

In the 2014 audit report, OIG recommended that NDF develop and implement an automated process to reconcile financial data in PIMS, including obligations, to the financial data in GFMS or a manual process that captures all transactions in both systems over a period of time.⁴³ An automated process was not developed, but NDF indicated that the manual processes were improved. To test whether the manual processes were sufficiently improved to ensure expense amounts were properly recorded in PIMS and supporting documentation was maintained, Kearney reviewed the documentation for the sample of 64 expense transactions, totaling \$16 million. All 64 transactions were accurately recorded in PIMS and valid supporting documentation was maintained, as shown in Table 7.

⁴² AUD-FM-15-18, Recommendation 1.

⁴³ AUD-FM-15-18, Recommendation 9.

Table 7. Results of Testing the Accuracy of Expenses

Project Category	Expenses Tested	Expenses Accurately Reported	Expense Amount
Egypt Project	18	18	\$8,587,488
All Other Projects	46	46	7,494,709
Total	64	64	\$16,082,197

Source: Prepared by Kearney based on the results of expense testing.

To further test whether the current manual processes were effectively designed to ensure all expenses were recorded in PIMS, Kearney performed a reconciliation of expenses recorded in PIMS with expenses recorded in GFMS. Of the 736 expense transactions, amounting to approximately \$14.8 million, recorded in PIMS between April 1, 2014, and December 31, 2014, Kearney identified 730 transactions, amounting to \$14.8 million, that were recorded in GFMS during the scope period or within 1 month of the scope period, which Kearney considered to be reasonable. However, Kearney identified six transactions, amounting to approximately \$11,000, that were recorded in GFMS more than 1 month before entry into PIMS, which Kearney considered to be an exception.

In addition to the transactions included in PIMS, Kearney identified 15 transactions totaling approximately \$47,000 that were recorded in GFMS but were not recorded in PIMS during the scope period. Kearney found that 8 of the 15 transactions, amounting to \$46,000, were recorded in PIMS within 1 month of the scope period, which Kearney considered to be reasonable. However, seven transactions, amounting to less than \$2,000, were recorded in GFMS but were not recorded in PIMS within 1 month after the end of the scope period, which Kearney considered to be an exception.

When information is not recorded in PIMS timely, NDF management and PMs may not have the information they need to properly approve disbursements and manage NDF projects. Based upon this testing, Kearney has concluded that NDF controls to ensure that expenses were recorded in PIMS accurately were not designed effectively. Therefore, the recommendation from the prior report remains open.⁴⁴

Controls Related to the Budgeting Process Should Be Developed

Budget and Finance Control Activity: *Does management review the Bureau/Post budgeting process to ensure the necessary controls are in place?*

NDF did not have a formal, documented process to develop the NDF annual budget request. NDF is a contingency fund; that is, NDF is provided funding that will be used to cover unforeseen future project expenses. Since budgets are typically developed 2 to 3 years before

⁴⁴ AUD-FM-15-18, Recommendation 9.

projects are identified and proposed, it is difficult for NDF to determine its project funding needs. According to the NDF Director, NDF requests a minimum of \$25 million in funding on an annual basis to maintain available funds of approximately \$30 to \$40 million to execute future projects, based on current project levels and needs. The calculation of needed funds and the NDF Director's approval of the amount requested have not been formally documented in the past because NDF is a small organization, and the calculation is straightforward. However, without documentation of the calculation of the amount requested and a formal approval of this amount within NDF, decisions regarding the planned use of available funds are not apparent and NDF may not have sufficient funds to respond to nonproliferation needs without obtaining a supplemental appropriation from Congress.

In addition, NDF did not have a process for determining the amount of funds to allocate for administrative purposes. Unlike project costs, NDF's administrative costs are relatively consistent and predictable from year to year. NDF has actual prior year annual costs for contractor support, training, credit card purchases, travel, phone bills, the operations and maintenance of PIMS, as well as the estimated costs for other contracts that NDF plans to execute. However, NDF has not used this information to determine the amount of funds to allocate for administrative purposes. Instead, NDF historically allocated 5 percent of its annual appropriation to administrative purposes.

From FYs 2013 through 2015, NDF did not allocate any funds for administrative purposes because excess administrative funds remained from earlier years. At the time of this audit, NDF had not spent all of the funds that it allocated for administrative purposes in 2009, 2010, and 2011. Additionally, NDF had not begun to obligate or spend amounts allocated for administrative purposes in 2012. Table 8 provides the details on the availability of funds previously allotted for administrative purposes.

Table 8. Amount Committed for NDF Administrative Purposes by Fiscal Year

FY Funding Was Received	Amount Allotted from Funds Received	Amount Obligated, Unpaid from Funds Received	Amount Spent from Funds Received*	Amount Available from Funds Received
2015	\$0	\$0	\$0	\$0
2014	\$0	\$0	\$0	\$0
2013	\$0	\$0	\$0	\$0
2012	\$1,500,000	\$0	\$0	\$1,500,000
2011	\$2,663,150	\$1,239,413	\$51,705	\$1,372,032
2010	\$1,250,000	\$573,044	\$668,167	\$8,789
2009	\$2,050,000	\$101,569	\$1,768,465	\$179,966

* This is the amount spent to date. As there is an available balance and NDF funds are available until expended, NDF is still making payments using 2009 administrative funds.

Source: Prepared by Kearney based on its review of December 2014 PIMS Reports.

According to one NDF finance officer, allocating 5 percent of the annual appropriation for administrative purposes has been NDF's standard practice for a number of years. By allocating a standard percentage of the appropriation rather than calculating administrative costs on an annual basis, NDF has allocated more funding for administrative purposes than necessary. As a result, less funding was available for NDF projects.

Recommendation 5: OIG recommends that the Nonproliferation and Disarmament Fund develop a formal, documented annual budgeting process. The process should include a method for determining the amount of funding needed for administrative purposes.

Management Response and OIG Reply: NDF agreed with the recommendation, and OIG considers the recommendation resolved. The recommendation can be closed when OIG reviews and accepts documentation showing that NDF has developed a formal, documented annual budgeting process.

Finding C: Contracting Controls Were Not Effectively Implemented for the Egypt Project

Kearney found that some controls related to contract initiation were not properly implemented for the Egypt project. Specifically, NDF did not maintain contract documentation, as required. In addition, Kearney identified one instance in which the PM did not prepare an acquisition plan when required. The lack of required documentation and an acquisition plan to guide contract administration increases the risk of noncompliance with laws and regulations related to acquisitions and may limit NDF's ability to identify and address contract administration issues.

Kearney also found that NDF did not prepare and maintain the documentation required or obtain the approvals required for contract modifications because NDF's policy was unclear. Without clear policies, a significant modification may be made without the knowledge or approval of the NDF Director.

Contract Initiations

The *Department of State Acquisition Regulation* states that it is mandatory to document procurement requests on the *Domestic Procurement Request* form (Form DS-1969) for domestic contracting activities exceeding the simplified acquisition threshold.⁴⁵ The *Department of State Acquisition Regulation* also requires that domestic offices develop a formal, written acquisition plan for all acquisitions exceeding \$5 million, including the base period plus all option years.⁴⁶ The purpose of completing an acquisition plan is to ensure that the agency meets its needs in

⁴⁵ *Department of State Acquisition Regulation*, Part 653.204-70 (a)(1), "DOS forms."

⁴⁶ *Department of State Acquisition Regulation*, Part 607.103 (d), "Agency-head responsibilities."

an effective, economical, and timely manner.⁴⁷ In June 2013, NDF updated and clarified its policies to include these requirements. The NDF policies also require that both the COR and the NDF Director sign the *Domestic Procurement Request* to certify that all required documents, such as the statement of work and the independent government cost estimate, are included in procurement request packages.

NDF did not have documentation, including a *Domestic Procurement Request* or an acquisition plan, for one of the two contracts related to the Egypt project.⁴⁸ This contract was executed in 2009, and the PM responsible for the project when the contract was executed no longer works for NDF. However, the Department requires that documentation supporting executed contracts be maintained until 6 years and 3 months after final payment or cancellation of the contract.⁴⁹ In the 2014 report, OIG recommended that NDF update its policy to require that documentation retention policies are consistently followed.⁵⁰ This recommendation remains open.

Kearney found that documentation for the second contract related to the Egypt project included the *Domestic Procurement Request* to support the initiation of the contract. The *Request* was completed and signed by the COR and the NDF Director, as required. However, NDF had not developed an acquisition plan for this contract. The initial cost estimate for the contract, a sole-source contract with an Egyptian construction company, was \$5 million. Since the cost estimate did not exceed \$5 million, an acquisition plan was not required and was not prepared. The contract was for construction and site preparation at three locations. However, NDF planned to have this construction company perform the same work at multiple other locations, which were not included in the original contract. Six months after execution of the contract, NDF submitted a procurement request to increase the contract by \$2.1 million for construction and site preparation at another location. Had the work for all locations been included in the original contract, an acquisition plan would have been required.⁵¹

This occurred because the PM did not consider the costs related to all anticipated work that drove the cost well over \$5 million when determining whether an acquisition plan was needed. The lack of a formal acquisition plan for large dollar contract actions increases the risk of noncompliance with laws and regulations related to acquisitions. Additionally, the lack of an acquisition plan may limit NDF's ability to identify and address contract administration issues.

⁴⁷ *Federal Acquisition Regulation*, 7.102, "Policy."

⁴⁸ This contract was initially awarded for \$39 million.

⁴⁹ General Records Schedule, "Routine Procurement Files." This requirement applies only to procurements that exceeded the simplified acquisition threshold of \$25,000 and all construction contracts exceeding \$2,000. Additionally, the reference is to the guidance in place in 2009. This guidance was superseded by Domestic Records Disposition Schedules A-06-004-03, "Executed Contracts."

⁵⁰ AUD-FM-15-18, Recommendation 7.

⁵¹ During the 2014 audit, Kearney tested four contract initiations for projects unrelated to the Egypt project. One of the four contract initiations required an acquisition plan, and the plan was properly prepared.

Specifically, NDF may not have the controls in place to identify projects that are not meeting their cost, schedule, and performance goals and to develop appropriate corrective actions.

Recommendation 6: OIG recommends that the Nonproliferation and Disarmament Fund formally notify personnel of the costs that should be considered when determining whether to prepare an acquisition plan.

Management Response and OIG Reply: NDF agreed with the recommendation, and OIG considers the recommendation resolved. The recommendation can be closed when OIG reviews and accepts documentation showing that NDF has formally notified personnel of the costs that should be considered when determining whether to prepare an acquisition plan.

Contract Modifications

The FAH states that when a modification is necessary, the COR must prepare a procurement request.⁵² The COR can use the *Domestic Procurement Request* or the Integrated Logistics Management System Ariba requisitioning electronic format to document the request. The NDF policy issued in June 2013 requires that the reasons for modifying contracts be clearly documented on the *Domestic Procurement Request*, and that both the COR and the NDF Director sign contract modification requests to document that the requests are appropriate.

NDF processed 14 modifications for 1 of the 2 contracts related to the Egypt project.⁵³ Three of the modifications were initiated after the June 2013 policy was issued. The documentation did not include a completed *Domestic Procurement Request* for any of the 14 modifications, including the 3 modifications initiated after June 2013. In addition, Kearney reviewed the available documentation for the 14 modifications including the Ariba requisition, the revised statement of work, and other relevant documentation. Of 14 modifications, 5 modifications lacked evidence of PM and Director approval; 2 modifications were approved by the PM but not the Director; and 5 modifications were approved by the Director but not the PM. Only two modifications were approved by both the PM and the Director.⁵⁴ The results of Kearney's tests for contract modification approvals are shown in Table 9.

⁵² 14 FAH-2 H-534, "Processing Contract Modifications."

⁵³ No contract modifications had been processed for the second contract related to the Egypt project as of December 31, 2014.

⁵⁴ During the 2014 audit, Kearney tested eight contract modifications for projects unrelated to the Egypt project. All eight modifications had the required approvals.

Table 9: Contract Modification Approvals

Results	No. of Modifications	Modifications Initiated After June 12, 2013
Modifications without evidence of PM or Director approval	5	0
Modifications approved by PM but without evidence of Director approval	2	0
Modification approved by the Director without evidence of PM approval	5	3
Modifications approved by both PM and Director	2	0
Total	14	3

Source: Prepared by Kearney based on the results of contract modification testing.

In some cases, contract modifications were initiated by the NDF Director because the PM was overseas or otherwise unavailable. NDF policy does not provide guidance regarding who should initiate a contract modification when the primary PM is unavailable. Additionally, when Kearney inquired about the modifications that were not approved by the NDF Director, the Director stated that he does not need to approve no-cost contract modifications. However, the policy memorandum does not provide for instances in which the Director would not approve contract modification requests. Although a modification may not require increased funding, a no-cost modification could result in significant changes related to project execution or project deadlines.

Modification documentation and approvals were not consistent with NDF policy because the policies and procedures were not clear. NDF finance officers stated that PMs provide the *Domestic Procurement Request* only for contract initiations, not for modifications. Additionally, NDF had developed an internal form, titled "Request for Contract Modification," which includes a location for both the PM and the NDF Director to approve the modification request. However, although the "Request for Contract Modification" is made available to PMs, it is not referenced in the June 2013 policy memorandum.

Without clear policies and procedures regarding contract modifications, a significant modification to a statement of work may be made by a PM without the knowledge or approval of the NDF Director.

Recommendation 7: OIG recommends that the Nonproliferation and Disarmament Fund revise its policy and procedures for contract modification to clarify documentation and approval requirements.

Management Response: NDF agreed with the recommendation, and in its response included the initial requirements, which were provided to NDF staff in May 2015. NDF's response indicated that the requirements would be further developed and detailed.

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OIG Reply: Based on NDF's response, OIG considers the recommendation resolved. Because NDF's response indicated that the documentation provided was its initial requirements, the recommendation can be closed when OIG reviews and accepts additional documentation that shows the fully developed and detailed policy and procedures for contract modifications.

RECOMMENDATIONS

Recommendation 1: OIG recommends that the Nonproliferation and Disarmament Fund develop a control to periodically reevaluate its lines of authority, responsibility, and reporting to ensure that its organizational structure continues to meet its needs.

Recommendation 2: OIG recommends that the Nonproliferation and Disarmament Fund (NDF) develop and implement a standard process for developing Memorandums of Understanding (MOU). This process should require the approval of the final MOU by, at a minimum, the NDF Director and Comptroller as well as controls to ensure that no changes can be made to the MOU without approval by these individuals.

Recommendation 3: OIG recommends that the Nonproliferation and Disarmament Fund perform a comparison of the cost of employing contractors to the cost of equivalent Federal positions.

Recommendation 4: OIG recommends that the Nonproliferation and Disarmament Fund modify the *Project Closeout Checklist* to include an area where project managers can document any issues encountered when completing the checklist and formally notify project managers of the requirement to document issues.

Recommendation 5: OIG recommends that the Nonproliferation and Disarmament Fund develop a formal, documented annual budgeting process. The process should include a method for determining the amount of funding needed for administrative purposes.

Recommendation 6: OIG recommends that the Nonproliferation and Disarmament Fund formally notify personnel of the costs that should be considered when determining whether to prepare an acquisition plan.

Recommendation 7: OIG recommends that the Nonproliferation and Disarmament Fund revise its policy and procedures for contract modification to clarify documentation and approval requirements.

APPENDIX A: MANAGEMENT CONTROL CHECKLIST ITEMS AND CONTROLS

Table A.1: List of Controls From the Management Controls Checklist for the Management Section and Results of Testing

Question	NDF Control	Designed Effectively?	Operating Effectively?
Has management conducted reviews of the Foreign Affairs Manual (FAM) and Foreign Affairs Handbook (FAH) sections that you are responsible for maintaining, to ensure that information is up to date?	Assignment of responsibility Review processes	Yes	Yes
Are managers ensuring continuous communication exists between management and personnel and external entities?	Weekly NDF staff meetings	Yes	Yes
	Project Implementation Status Reports	Yes	Yes
	NDF Review Panel meetings	Yes	Yes
Is management eliminating unnecessary duplication within operations overseas among the different Mission elements and domestically among the bureaus and offices?	NDF Review Panel project proposal review	Yes	Yes
Has management conducted a bureau/post risk assessment?	External audits and internal reviews	Yes	Yes
	NDF Review Panel reviews	Yes	Yes
Are reviews performed to ensure the approval of business class travel includes an appropriate justification and is documented on DS-4087?	NDF Travel Request review and approval Bureau of International Security and Nonproliferation (ISN), Executive Office review and approval	Yes	Yes
Are management controls reviews conducted for ensuring that business class travel is authorized and approved by an			

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Question	NDF Control	Designed Effectively?	Operating Effectively?
appropriate official, which is not subordinate to traveler?	Purchase Card Request Form. Finance Office reconciliation ISN, Executive Office reviews	Yes	Yes
Have reviews been conducted on credit card usage, i.e., purchase cards and travel cards?	Bureau of the Comptroller and Global Financial Services reviews	Not Applicable*	Not Applicable*
Does management conduct reviews to effectively manage costs related to sponsoring and attending conferences, while still achieving the Department's mission?	NDF Director approval of employee training requests NDF Review Panel review of training event costs in project proposals	Yes	Yes
Does management take a proactive approach to ensuring that outstanding OIG, GAO (OBO/RM/FM, OPS/FIR, OPS/SHEM for posts) or other external review recommendations are addressed and closed?	Assignment of responsibility	Yes	Yes
Are organizational reviews performed to ensure appropriate supervision and authority exists <i>[sic]</i> ?	No formal control	No	Not Applicable
Does management ensure compliance with laws and regulations pertaining to work of their areas of responsibilities as specified in 1 FAM 000 thru 1 FAM 600 <u>Authority, Responsibility and Organization</u> ?	Nonproliferation and Disarmament Fund (NDF) Project Management Guide requirement that a copy of the Congressional Notification be obtained from the Bureau of Legislative Affairs prior to creating a project in its Project and Information Management System (PIMS)	Yes	Yes
	No formal control relating to preparation and approval of Memorandums of Understanding	No	Not Applicable
	Lack of documentation of the specific provisions of laws or regulations the "notwithstanding authority" was used to override	No	Not Applicable
Has management performed reviews to evaluate the cost-effectiveness and	No evaluation of cost effectiveness of using contractors	No	Not Applicable

Question	NDF Control	Designed Effectively?	Operating Effectively?
appropriateness of either insourcing or outsourcing functions that are not inherently governmental?	NDF identified this control as “applicable” in the Statement of Work. However, NDF identified this control as “not applicable” in the Management Controls Checklist completed in September 2014. Additionally, NDF has fewer than 25 staff. Therefore, Kearney did not perform any procedures related to this control.		
Is management ensuring that proposals to host or attend conferences, meetings, or workshops requiring travel of 25 or more Department participants have been pre-approved by the Under Secretary for Management?	NDF identified this control as “applicable” in the Statement of Work. However, NDF identified this control as “not applicable” in the Management Controls Checklist completed in September 2014. Additionally, NDF has fewer than 25 staff. Therefore, Kearney did not perform any procedures related to this control.		
Are reviews and evaluations conducted on travel advances to determine if vouchers are reimbursed appropriately upon return of personnel from work-related travel?	NDF identified this control as “applicable” in the Statement of Work. However, Kearney confirmed, through discussions with NDF personnel and review of expenditure information, NDF staff did not use travel advances. Therefore, Kearney did not perform any additional procedures related to this control.		
Has post considered using regional and U.S.-based support in lieu of additional Mission staffing?	NDF identified this control as “not applicable” in the Statement of Work. Kearney did not perform any procedures related to this control.		
Has post determined if locally-employed staff are fully utilized in order to carry out the Mission’s strategic goals?	NDF identified this control as “not applicable” in the Statement of Work. Kearney did not perform any procedures related to this control.		
Is post using the Collaborative Management Initiative’s e-services dashboard to measure delivery of administrative services?	NDF identified this control as “not applicable” in the Statement of Work. Kearney did not perform any procedures related to this control.		

Question	NDF Control	Designed Effectively?	Operating Effectively?
Is management/post ensuring that NSDD-38 procedures are being followed when establishing or abolishing positions overseas?	NDF identified this control as “not applicable” in the Statement of Work. Kearney did not perform any procedures related to this control.		

* This control is a Department-wide control, not an NDF-specific control, so Kearney did not test this control.

Source: Prepared by Kearney based on the Bureau of the Comptroller and Global Financial Services Management Controls Checklist and the results of control assessment and testing. The Checklist has been reorganized to match the order in which items are discussed in the report.

Table A.2: List of Controls From the Management Controls Checklist for the Budget/Finance Section and Results of Testing

Question	Control Tested	Designed Effectively?	Operating Effectively?
Are review procedures in place to systematically and timely identify ULOs in need of de-obligation?	Monthly unliquidated obligation review	Yes	Yes
Are contracts/grants being closed out timely to mitigate risk of having ULOs?	Contract closeout procedures	Yes	Yes
Are reviews performed on the Bureau’s cash management and collection process?	Project Closeout Checklist	Yes	Yes
	Documentation requirements	No	Not Applicable
Are reviews being conducted to verify that segregation of duties exists between requisition, purchasing, and receiving functions?	Assignment of responsibility Standard processes	Yes	Yes
Are reviews performed to verify disbursements are properly authorized and supporting documentation and records are maintained?	Obligation review and approval	Yes	Yes
	Manual processes to record final obligation amounts in PIMS	No	Not Applicable
	Project Manager and/or Contracting Officer’s Representatives Certification of Deliverables and/or Services	Yes	No
	NDF Comptroller certification of invoices	Yes	Yes
	Manual processes at the transaction or project level to ensure that expense amounts are properly recorded in PIMS	No	Not Applicable

Question	Control Tested	Designed Effectively?	Operating Effectively?
Does management review the bureau/post budgeting process to ensure the necessary controls are in place?	No formal documented process for annual budget requests	No	Not Applicable
	No formal documented process for determining the amount of funding to allocate for administrative purposes	No	Not Applicable
Are ULOs quarterly reviews being documented and maintained at posts?	NDF identified this control as "not applicable" in the Statement of Work. Kearney did not perform any procedures related to this control.		
Does management ensure that posts use the standardized guidance provided to Financial Management Officers for the review and evaluation of ULOs, for targeted areas such as secured procurements, grants, travel, and transportation?	NDF identified this control as "not applicable" in the Statement of Work. Kearney did not perform any procedures related to this control.		

Source: Prepared by Kearney based on the Bureau of the Comptroller and Global Financial Services Management Controls Checklist and the results of control assessment and testing. The Checklist has been reorganized to match the order in which items are discussed in the report.

APPENDIX B: SCOPE AND METHODOLOGY

In December 2014, the Nonproliferation and Disarmament Fund (NDF) requested a performance audit to determine the extent to which NDF internal controls relating to the management activities and the budget and finance activities listed in the Department of State (Department) Management Control Checklist have been designed and implemented effectively. NDF management also requested that focused audit procedures be performed over the budget and finance controls and contracting processes related to an NDF project in Egypt for which NDF plans to substantially increase the amount of funding. An external audit firm, Kearney & Company, P.C. (Kearney), acting on behalf of the Office of Inspector General (OIG), performed this audit.

Kearney conducted this performance audit from January to April 2015 in Washington, D.C. Kearney planned and performed the audit in accordance with performance audit requirements in the Government Accountability Office's *Government Auditing Standards*, 2011 revision. These standards required Kearney to obtain sufficient, appropriate evidence to provide a reasonable basis for findings and conclusions. The sufficiency and appropriateness of evidence needed and tests of evidence related directly to the objectives and scope of the audit. Kearney believes that the evidence obtained provides a reasonable basis for its findings and conclusions based on the audit objectives.

To obtain background information for this audit, Kearney researched and reviewed the *Foreign Affairs Handbook*, *Foreign Affairs Manual*, Federal Acquisition Regulation, the Department of State Acquisition Regulation, and Federal appropriations law. Kearney also reviewed Office of Management and Budget Circular A-123, Management's Responsibility for Internal Control, and Office of Personnel Management guidance regarding personnel development and planning.

Kearney leveraged information obtained during the 2012¹ and 2014² audits of NDF and documentation provided by NDF to OIG in response to the recommendations included in the 2012 audit report.³ Kearney also met with NDF personnel and contractors to obtain additional details regarding NDF's processes related to both management control activities and budget and finance control activities. Kearney met with personnel from Acumen, the vendor responsible for designing and maintaining the NDF Project and Information Management System (PIMS), to obtain an understanding of the status of NDF's efforts to reconcile the information in PIMS to

¹ *Audit of Nonproliferation and Disarmament Fund Controls Over Contracting and Project Management and Integrity of Financial Data* (AUD-FM-13-17, Dec. 2012).

² *Follow-up Audit of Nonproliferation and Disarmament Fund Controls Over Contracting and Project Management and Integrity of Financial Data* (AUD-FM-15-18, Dec. 2014).

³ The Statement of Work for this audit did not require Kearney to perform audit work on all recommendations in the 2012 report. Therefore, Kearney only assessed the status of the 2012 recommendations that related to the controls addressed in this audit.

the information in the Department's official accounting system of record, the Global Financial Management System (GFMS).

Kearney structured its review of management controls using the framework of the 12 activities listed in the Management section of the Management Controls Checklist that were deemed applicable by NDF.⁴ Kearney identified the risks associated with each of these 12 activities and the controls in place to address those risks. To assess the design and operating effectiveness of these controls, Kearney obtained relevant supporting documentation as detailed in the Audit Results section of this report.

Kearney structured its review of budget and finance controls using the framework of the six activities listed in the Budget and Finance section of the Management Controls Checklist that were deemed applicable by NDF.⁵ Kearney identified the risks associated with each of these six activities and the controls in place to address those risks. Kearney performed procedures to test and verify the validity of obligations and expenses in PIMS. Kearney also performed specific procedures related to NDF projects in Egypt. These procedures included verifying the validity of obligations and expenses and assessing the controls over the contracting process. Kearney obtained reports listing all obligations and expense activity recorded in PIMS for the period of April 2014 to December 2014⁶ and all obligations and expense activity recorded in PIMS related to projects in Egypt. (See the Detailed Testing Methodology section in this appendix for additional information on sample selection.) Kearney also used reports from PIMS to identify projects that closed and deobligations that occurred during the scope period.

Work Related to Internal Controls

Kearney performed steps to assess the adequacy of internal controls related to the areas audited. Specifically, Kearney gained an understanding of and assessed the design effectiveness of the NDF controls related to the control activities listed in the Management section and the Budget and Finance section of the Department's Management Controls Checklist. Work performed on internal controls during the audit is detailed in the Audit Results section of the report.

⁴ The Management section of the Management Controls Checklist includes 18 activities. NDF identified 4 of the 18 activities as "not applicable" to NDF operations. Two additional activities were identified as "applicable." However, after initial fieldwork, Kearney determined that these activities were not significant to NDF operations and, therefore, did not perform audit procedures for the two activities.

⁵ The Budget and Finance section of the Management Controls Checklist includes eight activities. NDF identified two of the eight activities as "not applicable" to NDF operations.

⁶ The statement of work identified the scope of the audit to include transactions executed between April 2014 and December 2014.

Use of Computer-Processed Data

Kearney used computer-processed data from the Department during this audit. Kearney obtained listings of projects, obligations, deobligations, expenses, and unliquidated obligations (ULO) from PIMS. Kearney used these populations to select samples for testing. Kearney performed analysis of the list of projects, ensuring that changes since the prior audit were properly accounted for and aligned to a project, to confirm reliability. Additional procedures performed throughout the audit were to assess the reliability of the information in the PIMS reports. Issues identified are detailed in the Audit Results section, Findings A, B, and C. Additionally, Kearney obtained expense information from GFMS for the period April 2014 to December 2014, a listing of ULOs from the GFMS reporting tool Data Warehouse, and obligation and expense data for specific transactions from PIMS. The Department has controls in place to ensure that the expenses recorded in GFMS are accurate and complete. Kearney is comfortable using GFMS to obtain populations of transactions for sampling. Kearney performed procedures to evaluate the listing of ULOs obtained from the GFMS Data Warehouse as part of the audit of the Department's FY 2014 Financial Statements and concluded that the listing was sufficiently reliable for sample selection purposes.

Detailed Sampling Methodology

The sampling testing objectives were to determine the effectiveness of the controls that ensure:

- duplication between NDF projects and other government efforts is eliminated;
- project risks are assessed;
- ULOs are valid;
- duties are segregated;
- expense data recorded in PIMS, including expenses related to the Egypt project, is accurate;
- invoices are properly approved;
- expense data recorded in PIMS is complete;
- obligation data recorded in PIMS is accurate;
- obligation data in PIMS is complete;
- excess project funding that should be returned to NDF is identified;
- contracting controls for NDF projects in Egypt operate effectively; and
- obligation data recorded in PIMS for the Egypt project is accurate.

Projects

Kearney obtained a listing of all 11 project proposals submitted in 2013 and 2014 from PIMS (Projects 296 through 306). Kearney selected a random sample⁷ of three projects to test whether duplication was assessed and risks were assessed before the projects were approved.⁸

Unliquidated Obligations

To test the effectiveness of ULO monitoring controls, Kearney reviewed all 51 NDF ULOs, amounting to \$27 million, in GFMS as of December 31, 2014. Kearney identified six ULOs without activity since June 2014 and obtained and reviewed the supporting documentation for these six ULOs. Table B.1 provides information on ULOs recorded in GFMS that had no activity for more than 6 months.

Table B.1: ULOs in GFMS with No Activity for More Than 6 Months as of 12/31/2014

Obligation Number	Last Activity Date	Amount
1054295224	8/17/2012	\$462,000
1054395134	2/21/2012	66,501
1054495243	1/29/2014	1,098,899
1054495260	3/20/2014	3,000,000
1054495263	4/2/2014	166,525
1054495238	4/14/2014	199,520
Total		\$4,993,445

Source: Prepared by Kearney based on information obtained from the Data Warehouse Unliquidated Obligations report as of December 31, 2014.

Expense Accuracy and Controls

To test the existence and accuracy of expense transactions in PIMS, Kearney ran a "Transaction" report in PIMS to isolate all transactions created between April 1, 2014, and December 31, 2014. Kearney then excluded certain types of transactions to arrive at the population from which a dual-purpose sample⁹ was selected. Those exclusions include removing from the population expense transactions with no transaction amount, expenses that related to NDF projects in Egypt (tested separately), expenses that netted to zero, and expenses with negative amounts (credits). From the adjusted population, Kearney selected a sample of 46 transactions. Specifically, Kearney selected all 20 transactions over \$69,421.77 and used monetary unit

⁷ When performing random sampling, each item in the population has the same probability of being selected.

⁸ This sample size is in accordance with American Institute of Certified Public Accountants guidelines for performing control tests over small populations.

⁹ A dual-purpose sample is selected to test both the amount recorded and the effectiveness of controls.

sampling¹⁰ to select the remaining transactions. The universe of expense transactions and the exclusions that were made are provided in Table B.2.

Table B.2: Universe of Expenses for Dual-Purpose Testing

	Number	Amount
All Expense Transactions Recorded in PIMS During the Scope Period	736	\$14,827,777
Less: Blank Transaction Amounts	9	0
Less: Expenses Related to NDF Projects in Egypt (tested separately)	160	6,556,682
Less: Net to Zero by GFMS Transaction No. and Transaction Amount	18	0
Less: Negative Amounts (tested separately)	11	(544,791)
Population for Dual-Purpose Sampling	538	\$8,815,886
Expenses Selected and Tested	46	\$7,494,709

Source: Prepared by Kearney based on information from the PIMS Transactions Report April 2014 – December 2014.

To evaluate the existence and accuracy of expense transactions related to the NDF project in Egypt, Kearney ran a "Transaction" report in PIMS to isolate all transactions created between January 1, 2009, and December 31, 2014, related to the project in Egypt, which is recorded in PIMS under two project numbers – 276 and 277. The project in Egypt was started in 2009; therefore, there were no expense transactions before 2009. Kearney excluded low risk expense transactions, such as expenses related to travel; Bureau of Administration, Office of Logistics Management, Office of Acquisitions Management fees; personal service contractor expenses; and expenses that netted to zero. Kearney then selected a random sample of 18 transactions for dual-purpose testing related to expense transactions for the Egypt project. The universe of expense transactions related to the project in Egypt and exclusions that were made are documented in Table B.3.

Table B.3: Universe of Expenses Related to Project in Egypt for Dual-Purpose Testing

	Number	Amount
All Expenses Recorded in PIMS Related to Project Numbers 276 and 277	575	\$46,603,251
Less: Expenses that Net to Zero	3	0
Subtotal	572	\$46,603,251
Less: Expenses Related to Travel (Low Risk)	209	177,921
Less: Office of Acquisitions Management Fees (Low Risk)	8	614,374
Less: Personal Service Contractor Expenses (Low Risk)	264	518,777
Population for Dual-Purpose Sampling	91	\$45,292,179
Expenses Selected and Tested	18	\$8,587,488

Source: Prepared by Kearney based on information from the PIMS Transactions Report January 2009 – December 2014.

¹⁰ Monetary unit sampling is a statistical sampling method. Using this method, each monetary unit (that is, dollar) is equally likely to be included in the sample. For example, a transaction for \$10,000 is ten times as likely to be sampled as a transaction for \$1,000.

Completeness of Expenses in PIMS

To test the completeness of expense transactions in PIMS, Kearney performed a reconciliation of expenses in PIMS to expenses in GFMS. Kearney obtained a listing of expense transactions in PIMS created between April 1, 2014, and December 31, 2014, by running a "Transaction" report in PIMS. Kearney also ran a Data Warehouse report to obtain a listing of all expense activity in NDF Treasury symbols¹¹ in GFMS with a transaction date between April 1, 2014, and December 31, 2014. Table B.4 lists the populations that were obtained to reconcile expenses in PIMS to expenses in GFMS.

Table B.4: PIMS to GFMS Expense Reconciliation

	Number	Amount
PIMS Expenses during scope period (4/1/2014 – 12/31/2014)	736	\$14,827,777
Less: Timing 1 – Entered in PIMS after 4/1/2014 but entered in GFMS before 4/1/2014. Transaction recorded in PIMS within 1 month of entry into GFMS.	20	22,517
Less: Timing 2 – Entered in PIMS before 12/31/2014 but entered in GFMS after 12/31/2014. Transaction recorded in PIMS within 1 month of entry into GFMS.	2	57,102
Less: Timing 3 – Entered in PIMS after 4/1/2014 but entered in GFMS before 4/1/2014. Transaction not recorded in PIMS within 1 month of entry into GFMS.	6	11,248
PIMS Expenses that Reconcile to GFMS Expenses	708	\$14,736,909
GFMS Expenses during scope period (4/1/2014 – 12/31/2014)	916	\$(13,136,497)
Less: Closing Entries, Journal Entries, and other Accounting Adjustments recorded in GFMS that do not represent true expenses and should not be recorded in PIMS.	67	(27,921,027)
Subtotal: GFMS Expenses during scope period (4/1/2014 – 12/31/2014) that should be recorded in PIMS.	849	14,784,529
Less: Interest Payments not included in PIMS Transaction Report but included in PIMS.	7	31
Timing 1 – Recorded in GFMS before 12/31/2014 but recorded in PIMS after 12/31/2014. Transaction recorded in GFMS within 1 month of entry into PIMS.	5	(1,293)
Timing 2 – Recorded in GFMS after 4/1/2014 but recorded in PIMS before 4/1/2014. Transaction recorded in GFMS within 1 month of entry into PIMS.	3	47,227
Error – Recorded in GFMS before 12/31/2014 but not recorded in PIMS as of 3/30/2015.	7	1,656

¹¹ The Department of the Treasury symbols 1911_X1075.0, 1911_X1075.D, and 1911_X1071.0, are unique to NDF. There were no expenses during this timeframe to X1071.0 between April 1, 2014, and December 31, 2014.

GFMS Expenses that Reconcile to PIMS Expenses	827	\$14,736,909
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Note: Numbers in this table may not add because of rounding.

Source: Prepared by Kearney based on information from the PIMS Transaction Report April 2014 – December 2014 and the Data Warehouse Report of expense activity in Fund X1075 April 2014 – December 2014.

Accuracy of Obligations in PIMS

To determine the existence and accuracy of obligations in PIMS, Kearney created an "Obligation" report in PIMS and isolated all obligations created between April 1, 2014, and December 31, 2014. Kearney identified 62 obligations created between April 1, 2014, and December 31, 2014. Of those 62 obligations, 21 related to the Egypt project. Seven obligations accounted for approximately 80 percent of the obligation balance. As shown in Table B.5, Kearney tested the existence and accuracy of those seven obligations.

Table B.5: Obligations Created in PIMS between April 1, 2014, and December 31, 2014

	Number	Amount
All Obligations Created in PIMS During Scope Period	62	\$9,750,683
Less: Obligations Related to NDF Projects in Egypt (tested separately)	21	7,743,977
Population Subject to Sampling	41	2,006,706
Obligations Selected and Tested	7	\$1,588,813

Source: Prepared by Kearney based on information obtained from the PIMS Obligations Report obtained on March 25, 2014.

To evaluate the existence and accuracy of obligation transactions related to the NDF project in Egypt, Kearney ran an obligation report in PIMS to isolate all obligations related to project numbers 276 and 277 (Egypt project numbers). As shown in Table B.6, Kearney selected eight obligations for contract control testing and leveraged the obligations related to these contracts for accuracy testing. Kearney then selected an additional sample of four transactions for accuracy testing. These transactions were selected because they were recorded in the scope period and brought the overall coverage of the testing of obligations created during the scope period to 95 percent.

Table B.6: Universe of Obligations Related to Project in Egypt

	Number	Amount
All Obligations Recorded in PIMS Related to Project Numbers 276 and 277	83	\$68,702,694
Contracts Tested for Control Purposes Leveraged for Accuracy Testing	8	62,103,894
Additional Obligations Sampled	4	3,187,304
Total Obligations Selected and Tested	12	\$65,291,198

Source: Prepared by Kearney based on information from the PIMS Obligation Reports for Project 276 and 277.

Return of Unspent Advanced NDF Funds

To evaluate the effectiveness of NDF's controls related to the collection of unused project funds, Kearney reviewed all projects that were recently closed to determine if there was unused funding that should be returned to NDF. To identify projects recently closed, Kearney obtained the December 2014 project status report from PIMS, and identified eight projects with a closing status of "Chart C - Closing Projects – Financial Review Complete." Kearney reviewed the Project Closeout Checklist and relevant supporting documentation for all eight projects.

Contracting Controls for NDF Projects in Egypt

To test controls over the contracting process related to NDF projects in Egypt, Kearney identified obligations related to the project in Egypt (PIMS project numbers 276 and 277). To identify obligations related to project numbers 276 and 277, Kearney used the universe of expense transactions obtained to test the existence and accuracy of expenses related to the project in Egypt after exclusions. Kearney summarized the 91 expense transactions by obligation number to identify contracts and contract modifications related to Egypt. Kearney then reviewed the December 2014 Projects ULO report to identify obligations related to the Egypt project that had no expenses recorded against them. Table B.7 lists the universe of obligations based upon contracts related to the project in Egypt.

Table B.7. Universe of Obligations Related to Egypt Project Numbers 276 and 277

Project Number	Number	Amount
NDF-276	7	\$57,627,847
NDF-277	1	4,476,047
Total Obligations Related to Contracts	8	\$62,103,894

Source: Prepared by Kearney based on information from PIMS.

After identifying obligations in PIMS that were for contracts related to project numbers 276 and 277, Kearney obtained the supporting documentation to identify the number of contract initiations and contract modifications that occurred. This was necessary because not every modification is entered as a separate obligation in PIMS and one modification might be recorded under multiple obligations in PIMS. As shown in Table B.8, Kearney determined that there were 2 contract initiations and 14 contract modifications related to project numbers 276 and 277.

Table B.8: Contract Initiations and Modifications Related to the Egypt Project

	Number	Amount
Contract Initiations	2	\$23,307,168
Contract Modifications	14	40,052,847
Total Contract Initiations and Modifications	16	\$63,360,015
Less: No-Cost Contract Modifications	8	\$0
Contracts	8	\$63,360,015

Source: Prepared by Kearney based on information from the PIMS Transaction Report January 2009 – December 2014.

Kearney identified a variance between the dollar amount of the obligations related to contracts documented in Table B.7 and the dollar amount of the executed contract and contract modifications documented in Table B.8. This difference was later corrected by NDF. Additional details are included in Finding B of the Audit Results section.

APPENDIX C: NONPROLIFERATION AND DISARMAMENT FUND RESPONSE



United States Department of State

*Bureau of International Security,
and Nonproliferation*

Washington, D.C. 20520

August 10, 2015

MEMORANDUM

TO: OIG/AUD – Norman Brown

FROM: ISN/NDF – Steven A. Saboe *SS*

SUBJECT: Draft Report on *Audit of Selected Nonproliferation and Disarmament Fund Management Controls*.

I would like to thank the audit team for their diligent work, thoughtful insights and continued professionalism while examining the Nonproliferation and Disarmament Fund's (NDF) management controls and Egypt-related budget and finance controls and contracting processes. I am pleased to know that most of the NDF's controls were designed and implemented effectively.

We agree with all 7 of the 2015 audit recommendations.

The NDF has already begun to revise procedures regarding contract modification documentation and approval requirements (recommendation 7). Initial requirements, which will be further developed and detailed, were provided to the NDF staff on May 12, 2015 by e-mail. The e-mail and memo are attached for your reference. Upon further review of current practices and requirements, the NDF will begin development and implementation of the remaining six recommendations soonest.

Attachment:

Guidance e-mail and memo regarding contract modification requests

Drafted: ISN/NDF: [REDACTED], ext. [Redacted] (b) (6)

Cleared: ISN/NDF: [Redacted] (b) (6) - OK

ABBREVIATIONS

CGFS	Bureau of the Comptroller and Global Financial Services
COR	contracting officer's representative
<i>FAH</i>	<i>Foreign Affairs Handbook</i>
<i>FAM</i>	<i>Foreign Affairs Manual</i>
GAO	Government Accountability Office
GFMS	Global Financial Management System
IAA	Inter-Agency Agreement
ISN	Bureau of International Security and Nonproliferation
ISN/EX	Bureau of International Security and Nonproliferation, Executive Office
MOD	Memorandum of Discussion
MOU	Memorandum of Understanding
NDF	Nonproliferation and Disarmament Fund
OIG	Office of Inspector General
OMB	Office of Management and Budget
PIMS	Project and Information Management System
PM	project manager
PSC	personal services contractor
ULO	unliquidated obligation

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