

**REPORT ON THE  
FEDERAL COMMUNICATIONS COMMISSION  
FISCAL YEAR 2000  
FINANCIAL STATEMENTS**

**00-AUD-09-52**

**June 27, 2001**



**Office of Inspector General**

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**Federal Communications Commission**



## OFFICE OF INSPECTOR GENERAL

### MEMORANDUM

**DATE:** June 27, 2001

**TO:** Chairman  
Managing Director  
Chief Financial Officer

**FROM:** Inspector General

**SUBJECT:** Audit of the Federal Communications Commission's  
Fiscal Year (FY) 2000 Financial Statements

This letter transmits Clifton Gunderson LLP's (hereafter referred to as "CG-LLP") report on its FY 2000 financial statement audit of the Federal Communications Commission (FCC) and the results of the Office of Inspector General's (OIG) review thereon.

At the direction of the Department of the Treasury, FCC prepared consolidated financial statements in accordance with Office of Management and Budget (OMB) Bulletin No. 97-01, *Form and Content of Agency Financial Statements*, as amended, and subjected them to audit. The Chief Financial Officers Act of 1990 (Public Law 101-576 referred to as the "CFO Act"), amended, requires the FCC OIG, or an independent external auditor as determined by the Inspector General, to audit agency financial statements in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States. Under a contract monitored by the OIG, CG-LLP, an independent public accounting firm, performed the audit of FCC's FY 2000 financial statements.

#### **OIG Evaluation of CG-LLP's Audit Performance**

To fulfill our audit responsibilities under the CFO Act for ensuring the quality of the audit work performed, we conducted a review of CG-LLP's audit of FCC's FY 2000 financial statements in accordance with *Government Auditing Standards* and OMB Bulletin No. 01-02, *Audit Requirements for Federal Financial Statements*.

Specifically, we:

- reviewed CG-LLP's approach and planning of the audit
- evaluated the qualifications and independence of its auditors
- monitored progress of the audit at key points
- examined working papers and audit documents to evaluate compliance with *Government Auditing Standards*
- reviewed CG-LLP's audit reports to ensure compliance with *Government Auditing Standards* and OMB Bulletin No. 01-02, and
- performed other procedures we deemed necessary.

Based on the results of our review, we determined CG-LLP planned, executed, and reported the results of its audit of FCC's FY 2000 financial statements in accordance with applicable auditing standards. Therefore, in our opinion, CG-LLP's work provides a reliable basis for the firm's opinion on FCC's FY 2000 financial statements. Based on our review of the audit, we concur with CG-LLP's finding of reportable conditions related to internal control and instances of noncompliance with applicable laws and regulations. Accordingly, we concur with its reports thereon.

### **Opinion on the Financial Statements**

CG-LLP issued an unqualified opinion on FCC's FY 2000 Consolidated Financial Statements. CG-LLP opined, the Principal Statements and related notes present fairly, in all material respects, in conformity with U. S. generally accepted accounting principles, FCC's assets, liabilities, and net position; net cost; changes in net position; budgetary resources; reconciliation of net cost to budgetary obligations; and custodial activity as of September 30, 2000 and for the year then ended.

### **Matters Pertaining to Effectiveness of Internal Control Identified During the Audit**

In performing its internal control testing of controls necessary to achieve the objectives in OMB Bulletin No. 01-02, CG-LLP identified matters relating to significant deficiencies in the design or operation of FCC's internal control that, in its judgement, could adversely affect FCC's ability to record, process, summarize, and report financial data consistent with the assertions by management in the financial statements. Specifically, these matters were categorized as material weaknesses and reportable conditions per definitions of the American Institute of Certified Public Accountants.

Material weaknesses are reportable conditions in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relating to the financial statements may

occur and not be detected within timely period by the employees in the normal course of performing their assigned functions. CG-LLP identified material weaknesses in the areas of:

- Financial Reporting
- Cost Accounting System
- Universal Service Fund and Telecommunication Relay Service Fund Financial Reporting
- Loans Receivable and Related Accounts, and
- Information Technology.

CG-LLP identified additional reportable conditions not considered to be material weaknesses. Other reportable conditions include:

- Review and Finalize Written Internal Control Documentation for Financial and Administrative Operations
- Improve Internal Controls over Certain Accounts Receivable
- Improve Supporting Documentation and Controls over Property and Equipment
- Improve Controls over Accounts Payable
- Performance Goals and Results, and
- OMB Circulars No. A-127 and A-130 Reviews.

## **Results of Tests of Compliance with Laws and Regulations**

FCC management is responsible for complying with laws and regulations applicable to the agency. To obtain reasonable assurance about whether FCC's financial statements are free of material misstatements, CG-LLP performed tests of compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of financial statement amounts and certain other laws and regulations specified in OMB Bulletin No. 01-02, including the requirements referred to in the Federal Financial Management Improvement Act of 1996. As appropriate, CG-LLP limited its tests of compliance to these provisions and it did not test compliance with all laws and regulations applicable to FCC.

CG-LLP's tests disclosed instances of noncompliance with specific laws and regulations required to be reported under *Government Auditing Standards* and OMB Bulletin No. 01-02 as follows:

- Chief Financial Officers Act of 1990
- Debt Collection Improvement Act of 1996
- Government Performance and Results Act of 1993, and
- Federal Financial Management Improvement Act of 1996.

In accordance with generally accepted government auditing standards, the Reports of the Independent Auditor prepared by CG-LLP are dated February 9, 2001, the last day of audit fieldwork.

Should you or your staff have any questions, please contact me or Thomas Bennett, Assistant Inspector General for Audit, on (202) 418-0470. We appreciate the courtesies and cooperation extended to Clifton Gunderson LLP and to the OIG staff during the conduct of the audit and review.

H. Walker Feaster, III  
Inspector General

Attachment

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**SECTION I**

**INDEPENDENT AUDITOR'S REPORT**



### Independent Auditor's Report

To the Inspector General of the  
Federal Communications Commission

We have audited the accompanying consolidated balance sheet of the Federal Communications Commission (FCC) as of September 30, 2000, and the related consolidated statements of net cost, changes in net position, budgetary resources, financing, and custodial activity for the year then ended (collectively the Principal Statements). These Principal Statements are the responsibility of FCC's management. Our responsibility is to express an opinion on these Principal Statements based on our audit.

We conducted our audit in accordance with the U. S. generally accepted auditing standards; the standards applicable to the financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin 01-02, *Audit Requirements for Federal Financial Statements*. These standards require that we plan and perform the audit to obtain reasonable assurance about whether the Principal Statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the Principal Statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall Principal Statements' presentation. We believe our audit provides a reasonable basis for our opinion.

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In our opinion, the Principal Statements and related notes present fairly, in all material respects, in conformity with U. S. generally accepted accounting principles, FCC's assets, liabilities, and net position; net cost; changes in net position; budgetary resources; reconciliation of net cost to budgetary obligations; and custodial activity as of September 30, 2000 and for the year then ended.

In accordance with *Government Auditing Standards*, we have also issued our reports dated February 9, 2001 on our consideration of FCC's internal control over financial reporting, and on our tests of FCC's compliance with certain provisions of laws and regulations. These reports are an integral part of our audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Our audit was made for the purpose of forming an opinion on the basic Principal Statements taken as a whole. The Management Discussion and Analysis and Required Supplemental Information are not a required part of the Principal Statements but are supplementary information required by OMB Bulletin No. 97-01, *Form and Content of Agency Financial Statements*. The other Accompanying Information is presented for the purposes of additional analysis and is not a required part of the Principal Statements. Such information contains a wide range of data, some of which are not directly related to the Principal Statements. We have applied certain limited procedures, which consisted principally of comparing this information for consistency with the Principal Statements and discussing the methods of measurement and presentation with FCC management. However, we did not audit the information and express no opinion on it.

*Clifton Gunderson LLP*

Calverton, Maryland  
February 9, 2001

**SECTION II**

**INDEPENDENT AUDITOR'S REPORT  
ON INTERNAL CONTROL**



### Independent Auditor's Report on Internal Control

To the Inspector General of the  
Federal Communications Commission

We have audited the Principal Statements (hereinafter referred to as "financial statements") of the Federal Communications Commission (FCC) as of and for the year ended September 30, 2000, and have issued our report thereon dated February 9, 2001. We conducted our audit in accordance with U. S. generally accepted auditing standards; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 01-02, *Audit Requirements for Federal Financial Statements*.

In planning and performing our audit, we considered FCC's internal control over financial reporting by obtaining an understanding of FCC's internal controls, determined whether internal controls had been placed in operation, assessed control risk, and performed tests of controls in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements. We limited our internal control testing to those controls necessary to achieve the objectives described in OMB Bulletin No. 01-02. We did not test all internal controls relevant to operating objectives as broadly defined by the Federal Managers' Financial Integrity Act (31 U.S.C. 3512), such as those controls relevant to ensuring efficient operations. The objective of our audit was not to provide assurance on internal control. Consequently, we do not provide an opinion on internal control.

Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be reportable conditions. Under standards issued by the American Institute of Certified

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Public Accountants, reportable conditions are matters coming to our attention relating to significant deficiencies in the design or operation of the internal control that, in our judgment, could adversely affect the agency's ability to record, process, summarize, and report financial data consistent with the assertions by management in the financial statements. Material weaknesses are reportable conditions in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Because of inherent limitations in internal controls, misstatements, losses, or noncompliance may nevertheless occur and not be detected. However, we noted certain matters discussed in the following paragraphs involving the internal control and its operation that we consider to be reportable conditions and material weaknesses.

In addition, with respect to internal controls related to performance measures reported in FCC's Management Discussion and Analysis (MD&A), we obtained an understanding of the design of significant internal controls relating to the existence and completeness assertions, as required by OMB Bulletin No. 01-02. Our procedures were not designed to provide assurance on internal controls over reported performance measures, and, accordingly, we do not provide an opinion on such controls. However, we noted certain significant deficiencies in internal control over reported performance measures discussed in the following paragraphs that, in our judgment, could adversely affect the agency's ability to collect, process, record, and summarize performance information and report performance measures in accordance with management criteria.

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**MATERIAL WEAKNESSES**

**I.        Financial Reporting (Repeat Condition)**

The Chief Financial Officers (CFO) Act of 1990 assigned responsibility for developing and operating financial management systems to each Federal agency. OMB Bulletin No. 97-01, *Form and Content of Agency Financial Statements*, as amended (OMB Bulletin No. 97-01, as amended) defines the form and content of financial statements to be prepared by each agency. To accomplish the objective of complying with the CFO Act, the agency is required to develop a system to prepare a complete set of financial statements on a timely basis in accordance with generally accepted accounting principles. The statements are to result from an accounting system that is an integral part of a total financial management system containing sufficient structure, effective internal control, and reliable data. Financial reporting also consists of policies and procedures related to

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the processing and summarizing of accounting entries, and the preparation of financial statements.

FCC achieved an exceptional goal in preparing its first complete set of financial statements for fiscal year 2000; just one year after its first ever balance sheet and notes were prepared and audited. FCC staff, increasing cooperation and coordination among offices and bureaus, and services from external consultants, among others, were instrumental in achieving this goal. However, we believe that FCC's financial reporting process continues to need refinement. This refinement should allow FCC to prepare reliable financial statements in a more timely and efficient manner at the end of the fiscal year and interim periods throughout the year.

FCC's financial reporting weaknesses are detailed as follows:

**A. Develop an Integrated Financial Management System**

OMB Circular No. A-127, *Financial Management Systems* requires that each agency establish and maintain a single integrated financial management system. Without a single integrated financial management system to ensure timely and accurate financial data, poor policy decisions may occur, due to inaccurate or untimely information. Managers are less likely to be able to report accurately to the President, Congress, and the public on Government operations on a timely manner. And, scarce resources are more likely to be directed toward the collection of information rather than to delivery of the intended programs.

Having a single, integrated financial management system does not necessarily mean having only one software application within each agency covering all financial management system needs. Also, it does not mean that all information is physically located in the same database. Rather, a single, integrated financial management system is a unified set of financial systems linked together electronically in an efficient and effective manner to provide agency-wide financial system support. Integration means that the user is able to have one view into systems such that, at whatever level the individual is using the system, he or she can obtain needed information efficiently and effectively through electronic means. Interfaces are acceptable as long as the supporting detail is maintained and accessible to managers. Interface linkages must be electronic unless the number of transactions is so small that it is not cost beneficial to automate the interface. Easy reconciliations between systems, where interface linkages are appropriate, must be maintained to ensure data accuracy.

FCC utilizes the Federal Financial System (FFS) as its general ledger and core financial management system. FFS is not capable of generating most data analysis

user reports on a real time basis. Users have to request reports which are generated by a software application whose operations are only known to some staff of Financial Operations (FO). Other financial management systems used at FCC include the property management system, loan database spreadsheets, license databases, collection system, cost system, commercial accounting software for fines and forfeitures, and various spreadsheet applications. None of these financial management systems are integrated.

**Management Comments:**

Management concurs. The effort to develop an integrated financial system has been ongoing since FY 1999. Current efforts involve implementation of the Revenue Accounting and Management Information System (RAMIS) as well as upgrading the cost accounting system and reconfiguring FFS. RAMIS has been partially implemented for FY 2001 and is integrated with the core financial accounting system. FCC hired a contractor to help develop the functional requirements applicable for the replacement of the current cost accounting system and has targeted FY 2002 for implementation of a new cost accounting system. FCC also contracted with the developer of FFS to explore the capabilities of this system.

FCC noted FFS is incapable of generating real time reports but can respond in real time to specific inquiries. Currently, the data warehouse utility is updated nightly to include previous day's transaction information. Using data warehouse capabilities, report information is frequently tailored to meet the needs of various users.

**B. Establish and Maintain an Adequate Audit Trail Used in Preparing the Financial Statements**

FCC employs spreadsheet applications to create, document, report, and support its financial statements. These spreadsheets are linked to several different files. The files were not provided to the auditors at the same time as the spreadsheets and receipt was after several requests. Numerous numbers in the spreadsheets are keyed numbers and could not be traced back to the trial balance. When audit trails were available, most of them were a series of numbers in a comment box without an explanation or clear explanation of the various Standard General Ledger (SGL) accounts comprising the total. In addition, adjusting entries were prepared as post closing entries resulting in some discrepancies in the Statement of Net Cost, Statement of Changes in Net Position, and the trial balance. Also, some adjusting entries were not reflected in all affected financial statements until they were brought to FCC's attention by the audit process.

Although the use of spreadsheet applications appears to be common practice in the preparation of financial statements throughout the Federal government, adequate audit trails are necessary for review verification and ultimately audit. Lack of adequate audit trails increases the risk of errors. FCC's process of preparing financial statements is manually intensive, time consuming, and lacks controls over the completeness of final data used to prepare the financial statements. The lack of control over the completeness of final data and inadequate audit trails was evidenced upon technical review of the financial statements. Additionally, entity personnel encountered the same difficulties when researching compiled numbers in response to audit inquiries.

Maintaining an adequate audit trail enhances the quality of the agency report, reduces the risk of errors through an organized systematic process, and allows a person to independently review the report data accumulation process. Additionally, adequate audit trails facilitate the financial statement compilation process and helps ensure completeness of data upon review by management.

**Management Comments:**

Management concurs. Fiscal year 2000 was the first year FCC prepared all required financial statements to audit. As part of our effort to identify early audit issues, interim statements were prepared; however, parts of the preparation process were not fully established at fiscal year-end. FCC is formalizing policies and procedures specifically related to financial reporting with planned implementation by the close of FY 2001. In addition, FCC reviewed the spreadsheets used to prepare FY 2000 financial statements and made revisions that include using the updated OMB Bulletin No. 97-01, as amended crosswalks to prepare the Statement of Financing and the Statement of Custodial Activity.

**C. Correct and Update Federal Financial System Setup and Posting Model Definitions (Modified Repeat Condition)**

Last year's material weakness in the reporting process noted incorrect accounting entries associated with the transaction codes set up in FFS. FCC had not updated its FFS system setup and posting model definitions for many years. As SGL numbers, definitions, and standard accounting entries were updated and revised by the Department of the Treasury, Financial Management Service (FMS) over the years, and as FCC accounting activities became more complex, the FCC general ledger system set-up remained unchanged.

In response to the weakness noted, FCC management reviewed and updated, as a start, the auction and credit reform related transaction codes and accounting entries

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during the current fiscal year. In preparing the annual financial statements, however, FCC identified additional FFS year-end closing process errors. FCC hired a contractor to provide guidance in implementing recommended changes to the FCC's current configuration of the FFS tables and posting models. This system's deficiencies impair the quality and the reliability of the financial management information. A summary of the contractor's posting analysis findings are as follows:

- Incorrect debit/credit postings, inconsistencies between certain tables, and inaccurate closing accounts;
- Current value of funds rate in a table has not been updated;
- Report reference tables are out-of-date and will require significant changes in order for the FCC to facilitate Federal Agencies' Centralized Trial Balance System (FACTS) I and II reporting and to generate SF-133, Report on Budget Execution, and FMS 2108, Year-End Closing Statement. FCC, however, has not used the external reporting capabilities of FFS;
- Out-dated SGL accounts, account titles, and cross-references, plus inaccurate natural balances;
- Several of the reports reference tables are no longer required; and
- The report reference tables are out-of-date related to referencing the SF-133 and FMS-2108 in several areas, including formatting, balance indicators, and account references.

The contractor made detailed recommendations to enhance compliance with the SGL and facilitate use of external reporting capabilities of FFS.

**Management Comments:**

Management concurs. Prior to the FY 2000 closing, FCC was aware the FFS posting model contained incorrect definitions and had taken steps to contract with the FFS developer to identify and correct deficiencies. The contractor has since completed its evaluation and reviewed recommendations have been corrected in FFS. In conjunction with the FFS review, FCC also worked with the contractor to update the reporting tables needed to prepare the SF-133 and FMS 2108 from FFS. FCC continues to explore modifications to FFS to improve its financial reports.

**D. Improve Analysis of Budgetary Accounts**

In preparing the Statement of Budgetary Resources and Statement of Financing, FCC encountered a great deal of difficulty due to erroneous balances accumulating in the accounting system over time that remained unadjusted. Although FCC explained that most of the variances we identified are due to beginning balances and the FFS closing

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process system deficiencies as explained above, the process of correction and procedural changes at year-end resulted in time consuming analysis and delays in preparing these statements.

**Management Comments:**

Management concurs. FCC addressed some of the budgetary issues by modifying current transaction codes and will continue to address improper budgetary balances as identified. The preparation of quarterly financial statements, FACTS II quarterly reporting, update of the SF-133 and 2108 reporting module, and monthly reconciliations in FY 2001 will help to eliminate issues created by prior period transactions.

**E. Record Activities Timely and Prepare and Analyze Financial Activity (Modified Repeat Condition)**

Although FCC prepared its interim financial statements (except for the Statement of Financing) at June 30, 2000, the interim statements did not reflect current accounting activities for certain areas and there was no evidence of adequate management review. Interim financial statements are supposed to reflect the current financial condition and operations to allow management to analyze data and make decisions based on reported information. We noted that activities were not being recorded timely. For example,

- All interim regulatory fee sampled items (4 of 4) examined were not recorded in FFS for more than three months between the date of an authorized transaction and the entry into FFS;
- All interim fines and forfeitures receivable sampled items (4 of 4) reviewed were not recorded in FFS quarterly and the amount recorded was the total net balance of the activities; and
- Loan collection transaction activity was not recorded in FFS during the year but only applied to principal, interest, and other accounts at year-end.

Not recording or delays in recording transactions make data on the interim financial statements unreliable and unusable for management decision purposes. *Standards for Internal Control in the Federal Government*, issued by the General Accounting Office (GAO) in November 1999, page 15 states that "Transactions should be promptly recorded to maintain their relevance and value to management in controlling operations and making decisions."

Account analyses and reconciliations for accounts such as Loans Receivable; Interest Receivable; Accounts Payable; Accounts Receivable; and Property, Plant, and

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Equipment were not periodically performed during the entire fiscal year, and for most accounts, analyses were performed only once at fiscal year-end in preparation for financial statement reporting. As a result, significant journal vouchers prepared as part of a general account "clean-up" for the year-end were identified and posted. Regular financial statement preparation and analysis on a monthly or quarterly basis may eliminate the need for many of these adjustments during the year-end closing process and reduce the risk that material errors or irregularities in general ledger accounts remain undetected until after the end of the fiscal year.

**Management Comments:**

Management concurs. Beginning with second quarter FY 2001 balances, all principal statements and related footnotes are prepared on a quarterly basis. In addition, the Financial Operations Center has added six additional positions to improve the timeliness and completeness of the financial statement reconciliation effort and recommended reviews. FCC analyzed current reconciliations to identify monthly reconciliations not in place and established procedures for performing those reconciliations.

FCC is improving the recordation of its loan receivable and interest receivable transactions via RAMIS. This system will receive a download from the bank and create FFS transactions within 24 hours of receipt of payment by the bank. This will enhance FCC's ability to routinely reconcile balances and ensure current, accurate management information on the status of its portfolio. Until the system is fully implemented, FCC continues to rely on the loan model prepared by its contractor recognizing the associated delays inherent in the process.

FCC agrees additional steps are needed to improve the completeness of interim statements. FY 2001 will show considerable progress towards this goal.

**F. Formalize Financial Reporting Processes and Responsibilities in the Preparation of Financial Statements (Modified Repeat Condition)**

Preparation of the annual financial statements is the responsibility of the agency's management. In carrying out this responsibility, each agency CFO should prepare a policy memorandum that guides fiscal management personnel in the preparation of the annual financial statements. FCC does not have a formalized financial reporting process nor does it have written documentation that provides an integrated view of the procedures, personnel, and systems employed in preparation of the financial statements. Moreover, FCC did not have a process for identification of transactions requiring elimination at the consolidated level. Although FCC management told us that formalized financial reporting policy and guidelines have been drafted, a copy

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has not been provided for review as part of the audit process. The existence of written procedures will provide structure to the preparation and review process.

The FMS, Financial Standards and Reporting Division issued the *Accounting Policies and Procedures Guide for Federal Intragovernmental Transactions*. Although the guide is for intragovernmental transactions, it provides guidance related to elimination within an entity in preparing consolidated financial statements. This guide provides government-wide policies and procedures to account for and reconcile transactions occurring within and between each entity. In page 18 of this guide, it states "Each agency should develop and implement procedures to provide for the preparation of financial reports in accordance with the policies and procedures in this guide. Amounts reported in the basic financial statements, supplemental information, and in the footnotes should be supported by schedules summarizing and documenting the combination of SGL accounts comprising each total on the financial statements. Elimination entries should be supported with schedules summarizing the SGL accounts that are combined to total the amounts eliminated." It also states in page 17 that "Consolidated financial statements present an agency's financial information as a single entity. Elimination entries remove redundant activity and account balances within the consolidated statements. Each agency should have procedures for capturing this activity and balances within the agency to facilitate elimination process. Elimination entries should be performed at the consolidated level. Agencies should implement policies and procedures providing guidance within the agency for the identification of transactions requiring elimination at the consolidated level to facilitate financial statement preparation."

**Management Comments:**

Management concurs. FCC established a separate Financial Statements and Policy Group within its Financial Operations Center to address both financial statement preparation and financial policies and procedures. The group was established in FY 2000. The group's first priority is the completion of the policies and procedures manual begun in FY 2000. Currently, six of the eight chapters are in final draft status. Upon completion, the manual will be available to all employees via the FCC Intranet and an agency initiated training program.

**G. Inadequate Discussion in Management's Discussion and Analysis**

FCC's MD&A did not adequately discuss the requirements of the Federal Accounting Standards Advisory Board's (FASAB), Statement of Federal Financial Accounting Standards (SFFAS) No. 15, *Management's Discussion and Analysis* pertaining to the future effects on the entity of existing, currently known demands, risks, uncertainties, events, conditions, and trends.

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MD&A should describe important existing, currently-known demands, conditions, risks, uncertainties, events, conditions and trends (current factors) – both favorable and unfavorable – that affect the amounts reported in the financial statements and supplementary information. The discussion of these current factors should go beyond a mere description of existing conditions to include a discussion of the possible future effect of those factors.

**Management Comments:**

Management concurs. The FY 2000 financial statement compilation efforts focused on the principal statements and related footnotes. In addressing the MD&A section, management chose to focus its efforts on the establishment of performance measures where performance reporting was established or could be modified to meet reporting requirements. In FY 2001, FCC plans to incorporate a section to address future effects and consider other areas where improvements can be made.

**H. Combination of Reportable Conditions May Materially Impact Financial Statements (Repeat Condition)**

Reportable conditions noted in this report are internal control weakness relating to reconciliation procedures which could collectively have a material impact on FCC's ability to produce reliable financial statements in an efficient and timely manner and to comply with the intent of the CFO Act.

**Management Comments:**

While acknowledging conditions exist, management does not feel they impact the financial statements as evidenced by the audit opinion.

**Recommendations:**

We believe that FCC's continued efforts to meet its commitment to excellence in financial reporting have resulted in many positive changes in this year's financial reporting process. We still believe, however, that strong oversight from key financial and operational offices such as the CFO, Information Technology Center (ITC), and Administrative Office (AO), is needed to ensure that financial statements are prepared accurately and timely. We recommend the following:

1. Conduct an overall assessment of the financial management systems in use and the degree of integration needed. Prepare a plan outlining what the steps are (i.e., processes, data stewardship, management information, systems

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architecture, internal control), the timelines for completion, and the estimated cost to implement and maintain an integrated system.

**Management Comments:**

Management concurs. FCC reviewed several of its financial management systems and are at various stages of implementation. RAMIS will integrate with FFS for loans, fines and forfeitures, and eventually all receivables of the FCC. In addition, during FY 2001 FCC will review potential cost accounting systems which also will integrate with FFS.

2. Train FFS users to use the application software currently employed to ensure users can generate common widely-used reports (except for special reports) that are needed for account analysis without having to request the report be generated by another user (i.e., obtain the information needed efficiently and effectively through electronic means).

**Management Comments:**

Management concurs. FCC requested additional licenses to FFS data warehouse in order to provide broader access to report and query tools. Additional training classes for users will be conducted in FY 2001.

3. Establish and maintain an adequate audit trail used in preparing the financial statements. Modify as deemed appropriate and apply commonly used SGL crosswalks in preparing the principal financial statements.

**Management Comments:**

Management concurs. The crosswalks for FY 2001 were updated to incorporate the FY 2001 OMB crosswalks. In addition, financial reporting policies and procedures will be completed and implemented prior to FY 2001 close.

4. Identify and document in the accounting policies and procedures the transactions requiring elimination at the consolidated level and provide pro-forma eliminating entries.

**Management Comments:**

Management concurs. A section will be incorporated into the financial reporting policies and procedures that addresses elimination entries.

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5. For intragovernmental transactions, accumulate the detail and summary information for each activity by trading partner by employing the following:
  - a) Incorporate the trading partner code as part of the account coding classification.
  - b) Incorporate the trading partner code in the customer/vendor identification code in accounts receivable/accounts payable systems.
  - c) Incorporate the trading partner code into data captured when transactions are entered into accounting systems.

**Management Comment:**

Management concurs and noted elements of this information is captured within FFS.

6. Update and correct FFS to comply with the transaction posting models consistent with SGL guidance and policies when recording and classifying transactions. Ensure that changes made to FFS are tested and accepted before they go into live production.

**Management Comments:**

Management concurs. FCC hired the developer of FFS to perform a review of the posting model and provide recommendations. Recommendations were received and many have been enacted in the system. All changes are tested and accepted prior to implementation.

7. Review all frequently used transaction types and transaction codes to ensure that the accounting entries (budgetary and proprietary) are correct.

**Management Comments:**

Management concurs and stated this type of review is now a part of the ongoing reconciliation process.

8. Record transactions on a timely basis. Proper cut-off should be implemented when preparing interim financial statements.

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**Management Comments:**

Management concurs. As the quarterly financial preparation becomes more familiar, management believes cut-off procedures also will become better defined. As RAMIS and the new cost system are implemented, recordation times will improve.

9. Update and circulate to appropriate employees the Financial Coding Handbook. Ensure that appropriate employees receive adequate training.

**Management Comments:**

Management concurs and noted FCC currently distributes to all appropriate staff an updated version of the coding handbook at the beginning of each fiscal year. Additional training classes are being held in FY 2001.

10. Ensure compliance with the standards required in preparing MD&A as outlined in SFFAS 15. Specifically, discussions related to the future effects on the entity of existing, currently known demands, risks, uncertainties, events, conditions and trends should be included or expanded.

**Management Comments:**

Management concurs. FCC will review the MD&A standards again as part of the FY 2001 financial preparation procedures.

11. Finalize written policies and procedures on the financial reporting processes. The written policies should provide sufficient guidance for the year-end closing of the general ledger as well as interim and annual financial statements' preparation and analysis. The procedures should at least address the following issues:
  - a) Prepare and review a complete set of financial statements in accordance with generally accepted accounting principles at least quarterly.
  - b) Establish milestones by setting dates for critical phases such as general ledger closing, preparation of statements, notes, and accountability report, quality control review, etc.
  - c) Collect common closing and adjusting entries in a formal listing, which is used when the general ledger is closed and financial statements are prepared.

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- d) Identify the individuals who will be involved in the financial reporting process and establishing clearly defined roles and responsibilities for the staff involved in the preparation of interim and year-end financial statements.
- e) Prepare and retain all journal entries in sufficient detail with supporting documentation, and post all journal vouchers in the general ledger.
- f) Retain all documentation supporting the request, purpose and approval of all object class designations. Also, a listing of all current object codes including a statement of the purpose of each code should be maintained and provided to all personnel with the responsibility to initiate, prepare, and approve accounting transactions to ensure that object codes are used appropriately.
- g) Require supervisory review for all entries posted to the general ledger and consolidating financial statements. A supervisor should review revisions to previously approved entries and revised financial statements. All entries and review should be evidenced in writing.
- h) Prepare and analyze formal monthly reconciliations of subsidiary and summary account balances. FCC should also consider a "formal closing" of all accounts at an interim date(s), which will reduce the level of accounting activity and analysis required at year-end. This "formal closing" entails ensuring that all transactions are recorded in the proper period through the month-end. With complete and timely transaction recording, analysis of all major accounts can be performed effectively.
- i) Utilize established tools (i.e., checklists, implementation guides, etc.) available for assistance in financial statement compilation and review.
- j) Prepare and retain a comprehensive set of files, working papers and other documentation in support of all information included in the financial statements. This documentation should be more self-explanatory than what has been retained in the past. The documentation should be at a supporting detail level where an accountant/auditor can utilize provided documentation for substantiation of reported data without extensive explanation or re-creation by the original preparer.

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**Management Comments:**

Management concurs noting policies and procedures for financial operations, which are being coordinated by a certified public accounting firm, will be implemented in FY 2001.

**II.      Cost Accounting System (Repeat Condition)**

FCC's cost accounting system has not been a fundamental part of the financial management system. Although cost reports are generated and distributed to various FCC bureaus and offices, the reliability of these reports is questionable due to the lack of review of the cost allocation methodology and formulas, and the lack of review of proper application of the cost accounting activity codes. The cost accounting system is so inadequate that FCC does not use its reports in preparing its financial statements or analyzing program costs. In addition, we do not believe that the employees from bureaus and offices outside of FO, who are responsible for financial-related activities fully understand the importance of properly coding the obligations/expenditures.

In order to prepare the Statement of Net Cost by program costs in fiscal year 2000, FCC downloaded program costs from its FFS into a spreadsheet application. Using the spreadsheets, the indirect costs were allocated to each of FCC's five programs proportionately to total direct costs. Although we believe that specific earned revenue should be matched against specific program costs in accordance with the program description in its budget submission to Congress, FCC also allocated earned revenue on the same basis used to allocate costs.

Additionally, FCC identified five responsibility segments for cost allocation purposes but it did not determine related outputs for its responsibility segments as part of its cost methodology. SFFAS No. 4, *Managerial Cost Accounting Standards*, states that management of each reporting entity should define and establish responsibility segments and managerial cost accounting should be performed to measure and report the costs of each segment's outputs. Reporting entities should report the full costs of outputs in general purpose financial reports. Specifically, for each segment, managerial cost accounting should:

- Define and accumulate outputs, and if feasible, quantify each type of output in units
- Accumulate costs and quantitative units of resources consumed in producing the outputs, and
- Assign costs to outputs, and calculate the cost per unit of each type of output.

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SFFAS No. 4 states that cost accounting information must rely on consistent and uniform terminology for concepts, practices and techniques to be useful. Reliable information on the costs of the Federal programs and activities is crucial for effective management of government operations. In managing Federal government programs, cost information is essential in (1) budgeting and cost control, (2) performance measurement, (3) determining reimbursement and setting fees and prices, (4) program evaluations, and (5) making economic choice decisions.

Although implementation of a cost accounting "system" is not necessarily a prerequisite for compliance with SFFAS No. 4, the agency's cost system or cost finding techniques should meet the required minimum level of cost accounting necessary to accomplish the many objectives associated with planning, decision-making, and reporting. This minimum level, in accordance with SFFAS 4 includes:

- Collecting cost information by responsibility segments,
- Measuring the full cost of outputs,
- Developing appropriate costing methodology,
- Providing information for performance measurement,
- Instituting a reporting frequency that is timely and on a regular basis,
- Integrating both managerial cost accounting and general financial accounting utilizing the SGL,
- Providing the appropriate precision of information (i.e., reliable and useful),
- Accommodating management's special cost information needs that may arise due to unusual or special situations or circumstances, and
- Documenting all managerial cost accounting activity, processes, and procedures (should outline applicable activities, provide instructions for procedures and practices followed, list the cost accounts and subsidiary accounts related to the SGL, and contain examples of forms and other documents used).

### **Management Comments:**

Management concurs. The current cost accounting system was designed before FCC faced meeting the requirements of SFFAS No. 4 and was designed to meet budgetary requirements and accounting requirements of the original regulatory fee and auctions program, not cost accounting requirements of the CFO Act. Realizing the need for a more comprehensive and integrated cost accounting system, FCC hired an outside contractor to develop the functional requirements for a new cost accounting system. Until a new system is implemented, FCC will rely on spreadsheet allocations to perform its cost allocation. Where possible, FCC will adjust its current methodology and review operations to identify associated outputs.

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**Recommendations:**

12. Review the propriety of the costing methodology and the matching of earned revenue against costs (costing methodologies).
13. Determine outputs for all responsibility segments as required.
14. Document the costing methodologies and process in a formal policy and procedures manual or handbook. Management should determine which cost objects to define, the costing methodology to use, the type of costs to include for each reporting or decision making purpose (i.e., full cost), and other items of a similar nature.

**Management Comments:**

Management concurs with Recommendations 12, 13 and 14. As part of its development of the Financial Reporting Policies and Procedures, FCC will review the current net cost methodology. The review will address responsibility segment outputs as well as earned revenue matching.

15. Evaluate the adequacy of the cost accounting system or other cost-finding techniques (cost systems) in accumulating and allocating costs, matching revenue, accounting, and generating financial information. The cost systems should meet the minimum requirements outlined in the Joint Financial Management Improvement Program (JFMIP) *System Requirements for Managerial Cost Accounting*.

**Management Comments:**

Management concurs. In the short-term, FCC is reviewing its net cost methodology to identify improvements. As a long-term solution, FCC hired an outside contractor to assist with the development of functional requirements for a new cost accounting system.

16. Ensure that appropriate employees of bureaus and offices fully understand the importance of properly classifying costs and are trained on the proper application of the activity codes.

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**Management Comments:**

Management concurs. The Financial System Operations Group annually updates and distributes to all appropriate staff a coding handbook identifying the proper codes for the fiscal year.

**III. Universal Service Fund and Telecommunication Relay Service Fund  
Financial Reporting (Modified Repeat Condition)**

The Universal Service Fund (USF), including the Telecommunication Relay Service Fund (TRS) is an additional reporting component FCC included in its consolidated financial statements. FCC management concluded in August 1999 that the USF was a reporting entity to be consolidated with FCC. This conclusion was based on criterion from the Statement of Federal Financial Accounting Concepts (SFFAC) No. 2, *Entity and Display* that USF appears in FCC's Federal budget section titled, *Federal Programs by Agency and Account*. FCC also included the TRS Fund in its fiscal year 2000 financial statements. The USF is administered by Universal Service Administrative Company (USAC), a not for profit corporation, which through a contract with the National Exchange Carrier Association (NECA), maintains the USF accounting records and sends reports to the Department of the Treasury. The TRS Fund is managed by the NECA, which reports the program's financial information directly to FCC.

FCC is in an on-going process of reviewing USF (and TRS) activities. At this time, FCC cannot assure that USF or TRS Fund activities were in compliance with all laws and regulations, as the issue of which laws and regulations were applicable to the USF and TRS Fund was still unresolved at the end of the audit. FCC management should provide direction regarding the laws and regulations with which USF and TRS Fund should comply as well as guidance regarding the form and content of information needed for financial statement reporting purposes (see our Report on Compliance with Laws and Regulations, CFO Act.)

In addition, FCC did not provide adequate direction to USAC or NECA for the financial reporting of USF and TRS Fund activities. The FCC financial statements were prepared by consolidating information provided by USAC and NECA into the FCC statements. FCC included this financial data into its financial statements with limited or no review of the reasonableness, accuracy, and propriety of these amounts. FCC had no employee assigned to review the processes and procedures used to gather and report the financial information submitted to FCC. The USAC officials responsible for providing this USF information were unsure, however, as to what information was required and whether their systems could provide that information. For example, USAC originally provided information for the Statement of Budgetary Resources and the Statement of Financing

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without assurance that the input was required, and since the USAC accounting system did not include budgetary information, the financial information provided was less reliable. In addition, the figures reported for Accounts Payable, Payable to Providers, and Property, Plant and Equipment had to be reclassified because of differences between FCC and USAC. These reclassifications took place after a series of draft financial statements had been submitted for audit contributing to delays in completing the audit.

FCC management is responsible for obtaining reasonable assurance on the completeness and the reliability of the USF and TRS Fund financial reporting and its compliance with laws and regulations before information is consolidated into the FCC statements. This assurance was not obtained.

**Management Comments:**

FCC and USAC expended considerable time and effort in assessing the applicability of Federal laws and regulations to the USF during FY 2000. The Office of General Counsel (OGC) provided analysis and USAC took required steps to comply with the applicable federal laws and regulations.

USAC management remains confident that USAC systems can provide whatever information is required. USAC's reported information was appropriately classified for the USF as a stand-alone entity. As part of the consolidation with FCC, reclassifications were expected and made. FCC and USAC will institute a formal financial reporting compilation process to ensure this process does not cause delay in subsequent years. USAC provided assurance to FCC on the completeness and reliability of the financial information provided as well as assurance USF is in compliance with applicable laws and regulations.

**Recommendations:**

FCC management is aware of the issue of oversight of USF and TRS Fund financial reporting. The following actions should be implemented early in fiscal year 2001 in order to avoid repeating the problems:

17. Document clearly the legal, financial, and operational boundaries of FCC, USF, TRS, USAC, and NECA. With the assistance of OGC, USAC, and NECA, FCC management needs to formally define in writing each financial management role and responsibility to avoid confusion and misunderstanding.

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**Management Comments:**

Management concurs noting the relationship between FCC, USF, and USAC is already defined in the extensive regulations and Commission orders governing the operations of USAC and the USF. USAC or NECA will continue to seek guidance and clarification as necessary from the Commission.

18. Obtain from the OGC a list of laws and regulations applicable to the financial activities of USF and TRS Fund and communicate this information to officials of USAC and NECA. Ensure that USF and TRS Fund financial activities are in compliance with these laws and regulations by reviewing these activities periodically.

**Management Comments:**

FCC and USAC will continue to review compliance with applicable laws and regulations on at least an annual basis.

19. Assign one or more staff from FO to obtain an in-depth understanding of USF and TRS Fund operations, including financial operations, and who will work in coordination with Common Carrier Bureau (CCB) to comprehensively review financial and operational information provided by USAC and NECA.

**Management Comments:**

Management concurs. Throughout FY 2000, FCC and USAC established a stronger working relationship as it relates to compilation of the financial statements and subsequent audit. To ensure the relationship fully develops, FCC assigned a member of the new Financial Statements and Policy Group to gain an in-depth understanding as recommended by the auditors. This staff member will work closely with USAC to provide guidance in the generation of quarterly and year-end financial statements and supporting documentation.

20. Review monthly financial reports provided by USAC and NECA. Request additional information from USAC and NECA as necessary to obtain reasonable assurance that the financial data is reliable.

**Management Comments:**

FCC started preparing quarterly statements during FY 2001 and has already contacted both USAC and NECA concerning the USF and TRS information needed for the statements.

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21. Develop a formal financial reporting compilation process that adequately addresses issues arising from its consolidating reporting components.

**Management Comments:**

Management concurs stating FCC is documenting its financial reporting process as part of a policies and procedures manual that will be implemented during FY 2001.

**IV.    Loans Receivable and Related Accounts (Modified Repeat Condition)**

FCC uses installment payment mechanisms to finance some of the spectrum sales to successful and qualifying bidders. These direct loans are accounted for in accordance with the Federal Credit Reform Act (FCRA) which requires that the cost of direct loans be estimated at present value for the budget. Loans servicing and collecting responsibilities were outsourced to FMS, until mid-1999 when FCC discontinued this arrangement and brought all aspects of the loan servicing in-house. Although FCC intended to transfer the loan servicing and collection responsibilities to a private contractor, it did not occur in fiscal year 2000.

In 1999, when the loan servicing was transferred in-house, FCC discontinued using the loan servicing system as its loan subsidiary system. However, the incumbent system continued to be used for other processes such as billings, collections, installment payment amounts and dates received. In 1999, FCC started using spreadsheet applications (loan models) developed by a public accounting firm (consultants) hired by FCC to verify that loan balances were valid, accurate, and auditable. These loan models were instituted as the loan subsidiary system. FCC planned to replace these loan models with RAMIS by September 30, 2000; however, this plan did not materialize according to the schedule. RAMIS is modified off-the-shelf software that will handle accounting for all collections and loan management within FCC and interfaces with other FCC financial systems. Consequently, FCC continued to use the loan models as its loan subsidiary system with the assistance of the consultants in maintaining the loan models during fiscal year 2000.

**A. FCC Current Loan Subsidiary Ledger System Is Inadequate (Modified Repeat Condition)**

FCC's loan subsidiary ledger system is comprised of the loan models, which are elaborate and complex spreadsheets with configuration settings and information for original and adjusted loan principal, daily earned interest, suspension interest, payment data, and application of payments, among other items. These loan models (1) document the loan terms as determined by FCC's rules and official loan

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documents; (2) recalculate loan balances for financial statement reporting purposes; and, (3) serve as the cash flow model data for the loan subsidy model calculator.

Our review of the loan models showed that improvements were made to enhance the usefulness of the spreadsheets. Additional information such as tracking of changes to the database and raw collection data were added. However, deficiencies noted in prior year remained uncorrected. These are as follows:

- Configuration settings are still easily changed manually. Alteration of relevant configuration settings used in loan balance calculation could produce significantly different results. Once one user alters a setting, it would be difficult for another user to know what changes were made unless the user is notified.
- The loan models and the spreadsheet process lacked documented and approved policies and procedures for its use and review of key input and output data.
- The loan models' formulas are not protected to prevent inadvertent or unintentional modifications nor is there assurance that enter/modify access to the spreadsheet process is limited to authorized staff. We believe FCC should take ownership of these critical loan systems and its staff should be trained to be able to independently use the loan models and to review the reports generated by the model to reduce reliance on the accountants.
- Continued heavy reliance is still placed on the consultants who are responsible for the complete process (i.e., from data entry/download, to adjustments, to review, and to report generation).
- FCC still does not physically maintain an official and back-up soft copy of the loan models, with updated information at least monthly, until a new system is implemented.

During the fiscal year, a processing file was incorrectly uploaded into the spreadsheet application subsidiary system requiring subsequent review and additional resources to correct the effects of the upload. A condition as such should have been detected by FCC's oversight of its consultants and/or its internal control of loan processing activities.

Throughout the fiscal year, FCC has been reviewing the loans and related account balances. Loan review, as defined by FCC, is a process performed by the consultants to correct data in the loan models as a result of discovery, review, and additional information obtained. Some of these reviews accounted for:

- Unallowed suspension interest – interest was suspended for certain debtors that were ineligible for the suspension of interest. FCC has to recalculate the interest

- earned before the loans went in default and adjust the interest (suspension vs. regular interest, overstated vs. understated amounts) as appropriate.
- Incorrect billings in the amounts and due date which caused debtors to pay less and/or later than they were scheduled incurring non-delinquent late fees.
  - Policy decisions finalized in fiscal year 2000 that affected the loan and related account balances.

As a result of these reviews, interest receivable of at least \$180 million was adjusted downward in fiscal year 2000.

Our audit disclosed that loan models have not been fully updated to reflect changes from the loan review made during the year, resulting in inconsistencies of loan data among the loan model, subledger, and the cash flow model used in the subsidy calculation. To illustrate, a loan on the loan model reflects a default date of 10/30/98, which is the default date as if the loan was eligible for suspension interest after non-payment of the first payment due date of 7/31/98. These dates were incorrect since the loan was later identified as ineligible for suspension of interest. The subledger and the cash flow model shows the correct default date of 8/28/97, after the non-payment of the first payment due date of 2/28/97. FCC explained these inconsistencies were due to inherent limitations with using the spreadsheet application as the loan subsidiary system.

Also, the limitations of the spreadsheet application loan models required FCC to create separate subsidiary ledgers to account for the interest receivable earned but not yet billed. Interest receivable earned includes interest receivable on defaulted loans after the last billing date but before the next billing date. The loan models were not developed to calculate the interest earned as of a cut-off date if it differed from the billing date.

Generally, the reviewing process was manually intensive requiring FCC to apply collections manually to correct situations (i.e., recalculating correct interest and creating/setting a temporary credit to adjust late fees charged mistakenly in the loan models). The risk of error in this temporary solution (loan models) is higher as a result of the aforementioned conditions.

**Management Comments:**

Management concurs. As stated in FY 1999, FCC hired a public accounting firm to ensure installment loan balances were valid, accurate, and auditable. Technical security concerns did not allow FCC to implement RAMIS in FY 2000 as planned. To meet the obligation to provide sound, reportable, and auditable financial data, FCC extended a contractual engagement with the same firm to continue to provide

information until such time as FCC was able to bring RAMIS on-line. Currently, FCC operates both systems and plans to migrate fully to RAMIS in time for FY 2001 close. FCC intends to transfer the loan portfolio to an outside loan servicer who is required to provide timely financial data to FCC and ensure proper billing, collection, and reporting of loans.

The \$180 million interest adjustment was a combination of correcting interest reported as revenue in FY 1999 to FY 2000 and an accrual for FY 2000. Since FCC did not prepare a Statement of Net Cost for FY 1999, only a balance sheet adjustment was provided. The adjustment had a zero net effect to the FY 2000 financial statements.

**B. Reconcile General Ledger to the Subsidiary Ledger Balances (Modified Repeat Condition)**

A major objective of internal control is to ensure the integrity of the underlying accounting data supporting the financial statements. An important control in this regard is the reconciliation of FCC accounting records. An adequate reconciliation provides the assurance that processed transactions are properly and timely recorded in the accounting records and financial statements, which then allows management the ability to analyze its financial condition and results of operations on a routine basis.

FCC does not reconcile its loans and related account balances in the general ledger to the subsidiary records. At year-end, entries are made to recognize the effects of the subsidiary records in the general ledger accounts. To record and track credit reform collections received throughout the year in fiscal year 2000, FCC established an SGL Account 2402, Unapplied Collections. Balances in SGL 2402 were then reallocated at year-end to principal, interest, late fees, etc. based on the application of payments made in the loan models. At September 30, 2000, FCC had approximately \$12 million still remaining in this account.

**Management Comments:**

Management concurs. Loan collection activity is currently processed from a lockbox at a Federally insured bank and downloaded to FCC nightly. From this download, two identical files are produced. One file updates the cash balance in the Financing account and the duplicate file is fed into a subsidiary system that updates individual loan balances. Segregated reconciled balances are entered into FFS to decrease the unapplied collections and update other categories. Finalization of this process and reconciled balances were not completed for FY 2000 until year-end.

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The \$12 million outstanding in unapplied collections represents identified amounts that could not be applied at year-end due to insufficient payor supplied information. This is less than 3% of \$650 million collected in FY 2000 and remains a consistent payment application issue for this dynamic portfolio. As the portfolio is transferred to RAMIS and the loan servicer, additional steps will be implemented to lessen the unapplied balance.

**C. Implement Direct Loan System to Account for All Events in a Loan Cycle (Repeat Condition)**

FCC's plan of implementing RAMIS did not materialize in fiscal year 2000 as explained above. During the fiscal year, FCC continued to rely on various systems and spreadsheet applications to account and report direct loan transactions. As a result, there is a higher risk of human error resulting in inconsistent and/or disparate data in various systems and programs. *Direct Loan System Requirements* issued by JFMIP states that a direct loan system must interact with the core financial system to perform fund control checks, initiate or record payments, record the results of other direct loan-related financial transactions, and acknowledge receipt of financial information exchange. It must be able to perform automatic system balancing to ensure that direct loan partners are able to agree on transaction number and dollar values passed, processed and rejected. This automated balancing includes cumulative subsidiary account balancing to the general ledger. It should be able to support managerial accounting. These internal management information requirements are those required to establish credit management and financial reporting systems that are in compliance with standards provided in OMB Circulars No. A-34, *Instructions on Budget Execution*; A-123, *Management Accountability and Control*; A-127, *Financial Management Systems*; and A-129, *Managing Federal Credit Programs*. See Auditor's Report on Compliance with Laws and Regulations.

**Management Comments:**

Management concurs. FCC recognized RAMIS would not be implemented by the close of FY 2000 and contracted with a major public accounting firm to provide loan accounting activities until RAMIS was implemented. During FY 2001 FCC's loan portfolio will transfer to a loan servicing financial institution; however, FCC will maintain both RAMIS and the public accounting firm through September 30, 2001 as backup.

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**D. Loan Documentation Needs Improvement (Repeat Condition)**

In managing the Federal government's receivables, OMB Circular No. A-129, *Managing Federal Credit Programs* identified documentation as one of the loan servicing requirements. It states that approved loan files (or other systems of records) shall contain adequate and up-to-date information reflecting terms and conditions of the loan, payment history, including occurrences of delinquencies and defaults, and any subsequent loan actions which result in payment deferrals, refinancing, or rescheduling. Accurate and complete documentation is critical to providing proper servicing to the debtor and pursuing collection of delinquent debt.

Our review disclosed that FCC's loan file documentation is still inconsistent and incomplete. For instance, 29 of 45 (64%) loan files reviewed do not have a series of the FCC Form 175, "Application to Participate in an FCC Auction"; one (2%) loan file contains an installment payment plan note without signature; three (7%) loan files do not have Installment Payment Plan notes; one (2%) file under an assignee name was not updated upon an exchange of the Security Agreement. Also, FCC discontinued updating payment history on that loan file.

The issue of loan file documentation needing improvement needs to be addressed as FCC changes its environment regarding loan business practices. The criticality of the issue increases as FCC progresses to outsourcing its loan servicing business practices and migrates to the new loan subsidiary system aforementioned.

**Management Comments:**

Management concurs. Over the past two years, FCC has been involved in ongoing efforts to fully document and update loan histories to ensure that loan balances are fully supported. Where information gaps are identified, FCC continues efforts to ensure completeness.

**Recommendations:**

Although FCC management has implemented controls since it took over the loan servicing operations, controls need to be fully implemented for effective and efficient loan management. Also, while expert consultants were hired to assist in the credit reform program, the accuracy, reliability, and reasonableness of source data is still FCC management's responsibility.

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We recommend the following:

22. While RAMIS is not operational and FCC uses the loan models, it should:
- a) Ensure that access to the loan models is limited to authorized staff.
  - b) Train FCC employees to have adequate knowledge in using and reviewing the loan models. If consultants are responsible for updating and analyzing the loan models, FCC employees should review, at least monthly, the configuration settings and formulas of the loan models to ensure they were not changed. In addition, FCC employees should review the outputs of the spreadsheets.
  - c) Develop written policies and procedures for the use and review of the loan models and related output.
  - d) Hardcode or lock cells with formulas in the loan models to prevent inadvertent or unintentional changes.

**Management Comments:**

Management concurs with Recommendations 22a, 22b, 22c, and 22d noting FCC initiated steps to ensure that agency personnel have copies of contractor's data models and reviews and comparisons are performed routinely.

- e) Physically obtain and keep an official copy of the loan models updated at least monthly since these are FCC's subsidiary records and are maintained by consultants outside of FCC financial management systems. A back-up copy should also be maintained.

**Management Comments:**

Management concurs noting FCC receives and maintains two backup copies of the models quarterly. As needed, FCC requests and receives monthly updates.

23. Ensure that the loan subsidiary system being developed and tested (RAMIS) is capable of interfacing with other financial management systems.

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**Management Comments:**

Management concurs noting RAMIS testing is ongoing for all phases of implementation to ensure proper integration.

24. Ensure that RAMIS meets all the applicable requirements for a direct loan system in the Federal Financial Management System Requirements (FFMSR) issued by JFMIP. One of these requirements is to ensure that the direct loan system can support the following functions:
- Loan extension
  - Account servicing
  - Department of the Treasury cross-servicing
  - Portfolio management
  - Delinquent debt collection
  - Other reporting requirements

**Management Comments:**

Management concurs and states RAMIS is in compliance with all FFMSR and JFMIP requirements. Management added the new loan servicer is also contractually bound to meet these requirements.

25. Record loan activities promptly to maintain their relevance and value to management in controlling operations and making decisions.

**Management Comments:**

Management concurs noting, as aforementioned, it expects complete SGL compliance at the transaction level within 24 hours of receipt of funds.

26. Reconcile general ledger balances to the subsidiary records on a monthly basis.
27. Ensure all loan files are kept up-to-date, have consistent information, and contain relevant loan and other documents necessary to conform to private sector standards.
28. Establish effective controls for transfer of loan data files to the new loan system, and ultimately, to a loan servicer , if employed.

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**Management Comments:**

Management concurs with Recommendations 26, 27, and 28 stating controls are in place to ensure proper transfer and FCC will have an independent, public accounting firm verify the balance.

**V.      Information Technology**

Our review and testing of controls related to Information Technology identified the following conditions (see our Report on Compliance with Laws and Regulations, Federal Financial Management Improvement Act):

**A. FCC Is Not In Compliance with OMB Circular No. A-130 Requirement for a Comprehensive Security Plan (Modified Repeat Condition)**

Some of the key components of an entity-wide security program are the performance of risk assessments and the development of a comprehensive security plan. Each organization needs a set of management procedures for identifying and assessing risks, and deciding what policies and controls are needed to achieve effective security controls.

OMB Circular No. A-130, *Management of Federal Information Resources*, Appendix III, "Security of Federal Automated Information Resources," as revised in February 1996, established a minimum set of controls for federal agencies, including risk assessments, assigning responsibility for security, security planning, periodic review of security controls, and management authorization of systems to process information.

Deficiencies in security controls that, in our view, significantly impact FCC's ability to protect its sensitive or critical resources include:

- FCC lacks a comprehensive and integrated security management structure. In such an environment, responsibilities could be unclear leading to the possibility of applying security controls inconsistently throughout the agency. As a result, certain vulnerabilities may be overlooked. In addition, monitoring the effectiveness of procedures for security controls throughout the agency will be ineffective.
- FCC has not performed risk assessments for its major application systems and its mission-critical general support system. FCC did perform vulnerability assessments for several of its major applications and general support systems in

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- fiscal year 2000, but has not completed risk assessments as prescribed by OMB Circular No. A-123, *Management Accountability and Control*.
- FCC does not have security plans for any of its major application systems and mission-critical general support systems. FCC plans to complete a template for its security plans by fiscal year 2001.
  - There is no periodic review of security controls over FCC's systems. In addition, FCC has not performed any formal certification and accreditation of its systems. FCC plans to conduct initial security reviews over a two-year period ending in fiscal year 2002. FCC plans to make these reviews part of its internal control review process.

**Management Comments:**

Management concurs. FCC developed a comprehensive and integrated security management structure. The basis for this structure was the creation and distribution of FCC Instruction 1479.1, *FCC Computer Security Program Directive*. The directive provides the framework for the Computer Security Program and assigns responsibilities for managing and using FCC computer resources and provides a framework to ensure an adequate level of protection to Commission computer-based systems.

FCC performed vulnerability assessments of several of the Commission's major applications during FYs 2000 and 2001 and contracted for the services required to complete necessary reviews. Also, FCC completed a risk assessment of its network in November 2000. In addition, the process for conducting such reviews was modified to ensure the inclusion of OMB Circular No. A-123, *Management Accountability and Control* issues. The process used by the assessment team includes the framework described in the National Information Assurance Certification and Accreditation Process (NIACAP).

FCC contracted services required to develop security plans for both its general support systems and major applications, as required by OMB Circular No. A-130, *Management of Federal Information Resources*, Appendix III. FCC's general support system security plan has been developed and is being reviewed by management. Several major application security plans are being developed and reviewed at this time and all remaining plans have been scheduled for development in FYs 2001 or 2002.

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**B. FCC Needs Improved Controls to Protect Its Information (Modified Repeat Condition)**

For a computerized-dependent organization like FCC, achieving an adequate level of information protection is highly dependent upon maintaining consistently effective access controls and system software controls. Access controls should limit and monitor access to computer resources (i.e., data files, application programs, and computer-related facilities and equipment) to the extent necessary to provide reasonable assurance that these resources are protected against waste, loss, unauthorized modification, disclosure, or misappropriation. Such controls include logical/technical controls, for example, security software programs designed to prevent or detect unauthorized access to sensitive data. Similarly, system software controls should limit and monitor access to powerful programs and sensitive files that control computer processing and secure the application and data supported by the system.

Our limited internal controls testing identified information protection-related weaknesses in FCC's information systems environment. Impacted areas included FCC's distributed computer system as well as its mainframe computers. These vulnerabilities expose FCC and its computer systems to risks of external and internal intrusion, subject sensitive FCC information related to its major applications to potential unauthorized access, modification, and/or disclosure, and increase the risks of fraud, waste and abuse.

Rights and privileges granted to users of the Collections System are undefined. The system administrator is not aware of what access rights are granted to each level or class of access. The system has no password history file, and does not conform to Federal Information Processing Standards (FIPS) Publication 112 "Password Usage." Incompatible duties are not adequately segregated, with application programmers having access to production data sets and performing functions in the production environment. Audit logging has also not been activated and there is no monitoring of access activities.

FCC has not assessed the risk of not protecting sensitive and mission critical files. No written criteria have been established to guide security personnel in monitoring and restricting access to production data and program files. FCC does not have an entity-wide security program in place; it does not sufficiently address mainframe components of its computing environment.

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**Management Comments:**

Management concurs. FCC continually works to improve the posture and effectiveness of the computer security program. In addition, the Computer Security Officer is working with application custodians and application level security representatives to ensure required and adequate levels of protection are provided and required tasks addressed. The most recent initiatives include implementing system risk assessments, certification and accreditation, security test and evaluations, and the preparation of system level security plans. While the referenced mainframe computer is not managed by FCC, management will work with the custodial Federal agency to mitigate noted issues.

**C. FCC Needs to Accelerate Efforts to Develop and Test its Contingency Plans (Repeat Condition)**

Losing the capability to process, and protect information maintained on FCC's computer systems can significantly impact FCC's ability to accomplish its mission to serve the public. The purpose of service continuity controls is to ensure that, when unexpected events occur, critical operations continue without interruption or are promptly resumed. To achieve this objective FCC should have (1) procedures in place to protect information resources and minimize the risk of unplanned interruptions and (2) a plan to recover critical operations should interruptions occur. These plans should consider activities performed at FCC's general support facilities, as well as the activities performed by users of specific applications. To determine whether the disaster recovery plans will work as intended, FCC should establish and periodically test the capability to perform its functions in disaster simulation exercises.

Our review of FCC service continuity controls identified deficiencies that could affect FCC's ability to respond to a disruption in business operations as a result of a disaster or other long-term emergency. The deficiencies were as follows:

- FCC has not formally identified and prioritized all critical data and operations on its major applications and the resources needed to recover them if there is a major interruption or disaster.
- FCC has not formally identified and prioritized all critical data and operations on its networks and the resources needed to recover them if there is a major interruption or disaster. In addition, we could not determine whether FCC had established emergency processing priorities that will help manage disaster situations more effectively for the network.
- FCC has not integrated the contingency plans of its data centers, networks and telecommunication facilities in a comprehensive disaster recovery plan.

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FCC is in the process of developing a comprehensive contingency plan. FCC plans to complete this effort by the end of fiscal year 2001.

**Management Comments:**

Management concurs. FCC plans to fund the development a Commission-wide Contingency of Operations Plan (COOP) in a multi-phased approach. The first phase includes the conduct of a business impact analysis to formally identify and prioritize all critical data and operations on major applications and the resources needed to recover if there is a major interruption or disaster. Upon completion, critical aspects of the COOP will be developed and tested.

**Recommendations:**

29. Establish a comprehensive and integrated security management structure to ensure that FCC's security policy is consistently applied.

**Management Comments:**

Management concurs stating FCC recently updated its computer security policy to reflect current computer and information security concerns and countermeasures. All computer security related policies are provided to each level of system level management to ensure consistency.

30. Conduct risk assessments for the FCC general support systems and major applications.

**Management Comments:**

Management concurs. FCC completed a risk assessment of its general support systems and its network in Fall 2000.

31. Develop and implement security plans for FCC's major application systems and mission-critical general support systems.

**Management Comments:**

Management concurs. FCC contracted for the required services to develop and implement security plans for its major application systems and mission-critical general support systems. Plans are being developed, using the guidance offered by National Institute of Standards and Technology (NIST), Special Publication

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800-18, *Guidance on the Development of Security Plans*, to ensure compliance with OMB Circular No. A-130, Appendix III. The expected completion time frame of the plans is by second quarter FY 2002.

32. Certify and accredit FCC's major applications and general support systems, based on the security plans developed and implemented.

**Management Comments:**

Management concurs. FCC contracted for the required services to certify and accredit FCC's major applications and general support systems. These reviews are being conducted to ensure compliance with OMB Circulars No. A-123, A-127 and A-130, Appendix III. NIACAP is being used as the required model to support this effort. The expected completion time frame of the reviews is by fourth quarter FY 2002.

33. Establish a system to periodically review security controls over FCC's computer systems in accordance with OMB Circular No. A-130, *Management of Federal Information Resources*, Appendix III.

**Management Comments:**

Management concurs noting major application and general support system certification and accreditation review processes currently underway will allow for periodic review of these systems, as required by OMB Circular No. A-130, Appendix III.

34. Strengthen controls over access to protect all mainframe and client server-based resources.
35. Address inadequacies and inconsistencies in the mainframe and network access request process.

**Management Comments:**

Management concurs with Recommendations 34 and 35. FCC's Computer Security Officer will work directly with the administrators of the mainframe system, including network access request processes, to ensure adequate controls are implemented and test these processes.

36. Require periodic review of user privileges to ensure that capabilities are in line with job responsibilities.

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**Management Comments:**

Management concurs. FCC's Computer Security Officer will develop a process to ensure Commission-wide compliance to require periodic review of user privileges to ensure capabilities coincide with job functions. The expected completion time frame for this effort is by second quarter FY 2002.

37. Enhance audit trail facility utilization and review.

**Management Comments:**

Management concurs. FCC's Computer Security Officer will develop and distribute a Commission-wide policy to make mandatory the use and review of appropriate system audit trail facilities within FCC, both at the general support and major application levels. The expected completion time frame of the plan is by first quarter FY 2002.

38. Develop and implement a FCC-wide security plan as prescribed by OMB Circular No. A-130, *Management of Federal Information Resources*.

**Management Comments:**

Management concurs. FCC contracted required services to develop and implement FCC-wide security plans for major application systems and mission-critical general support systems. These plans are being developed to ensure compliance with OMB Circular No. A-130, Appendix III and are being prepared using the guidance offered by NIST Special Publication 800-18, *Guidance on the Development of Security Plans*.

39. Develop and test contingency plans for FCC's major applications, networks, and telecommunications facilities.

**Management Comments:**

Management concurs. FCC noted the aforementioned COOP will address the recommendation.

40. Obtain written documentation from FCC's data centers of developed and tested contingency plans and participate in the scheduled tests of the plans.

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**Management Comments:**

Management concurs. FCC's Computer Security Officer will obtain written documentation from its data centers of developed and tested contingency plans and request that FCC be able to participate in the scheduled future tests of the plans. The expected time frame for the completion of these plans is by the second quarter FY 2002.

41. Immediately develop a comprehensive contingency plan that integrates the individual plans of its data centers, networks, and telecommunications facilities.

**Management Comments:**

Management concurs and stated the contingency plan development team will factor in the integration of the FCC plan with those plans for non-FCC individual support data centers, networks, and telecommunications facilities.

**REPORTABLE CONDITIONS**

**VI. Review and Finalize Written Internal Control Documentation for Financial and Administrative Operations (Modified Repeat Condition)**

In response to last year's internal control report, FCC started to document its accounting policies and procedures related to various financial and administrative operations such as auctions; accounts receivable; property, plant, and equipment; accounts payable; payroll; and budget. All of the documents mentioned, except for the property, plant, and equipment and payroll, have not been finalized and require management review before finalization.

FCC's *Property Management Policies and Procedures* (manual), although finalized, has certain disconnects in definitions, policies, and procedures of property described in the manual versus the property items shown in the financial statements. The categories of personal property listed in the manual are Equipment, Software, Bulk Purchases, and Sensitive Property, while the note to the financial statements showed the categories as Furniture, Non-Computer Equipment, Computer Equipment, Bulk Purchases, Vehicle Systems, Broadcast Stations, Equipment, ADP Software, and ADP Software-In-Process. In addition, while reported separately as property in the notes of the financial statements, furniture is not mentioned in the manual as part of any category of property, nor is its inventory and valuation method, useful life, and disposal method described. These disconnects could result in confusion, misunderstanding, and inconsistencies in implementation of the policies and procedures.

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Documented internal control and financial policies and procedures are a major part of managing an agency. These comprise the plans, methods, and procedures used to meet missions, goals, and objectives and in, doing so, support performance-based management. Internal control serves as the first line of defense in safeguarding assets and preventing and detecting errors and fraud. Documentation of control policies and procedures reduces the risk of misunderstanding, confusion, and inconsistent actions taken.

**Management Comments:**

Management concurs noting FCC has been developing a comprehensive policy and procedures manual. Upon completion, the manual will be placed on the FCC Intranet to provide easy access for staff. Additionally, management will conduct training sessions to familiarize staff with the new policies and procedures.

**Recommendations:**

We recommend that FCC:

42. Perform a global assessment of the financial and administrative operations that will require a written internal control policies and procedures manual. Consolidate all financial policies and procedures in a manual that is updated through controlled memoranda during the year. Update the manual for the memoranda changes annually or as necessary.

**Management Comments:**

Management concurs stating a global assessment was performed to identify sections to include in the manual under development. The procedures will include change procedures that control how and when policies and procedures are updated.

43. Perform an in-depth review of the draft and final written internal control policies and procedures manual to ensure that information is accurate, current as to the Federal internal control environment, and consistent with related documentation.

**Management Comments:**

Management concurs. Policies and procedures are being developed and are subject to management review throughout the process.

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44. Ensure that FCC employees responsible for internal controls are provided with a copy of the internal control policies and procedures manual and are knowledgeable of the contents.

**Management Comments:**

Management concurs. As mentioned above, once completed the policies and procedures will be available via Intranet access.

45. Upon finalization of internal control policies and procedures manuals, conduct sufficient training of Commission personnel.

**Management Comments:**

Management concurs. A training plan will be developed to disseminate the information contained in the new manual.

**VII. Improve Internal Controls over Certain Accounts Receivable (Modified Repeat Condition)**

**A. Regulatory Fees**

The Omnibus Budget Reconciliation Act of 1993 requires FCC to collect regulatory fees to offset certain costs incurred in regulating its industry. The legislation also gives FCC the authority to review the regulatory fees and adjust the fees to reflect changes in its appropriation from year to year. It also authorizes FCC to charge a late payment penalty and to dismiss applications or revoke licenses for non-payment of the fees, and waive, reduce, or defer payment of a fee for good cause.

FCC's fee collection database is not linked to its licensing databases, making it difficult for FCC to perform routine automated checks on whether all licensees have paid their regulatory fee. In response to this weakness identified in the prior year report<sup>1</sup> and the GAO report<sup>2</sup>, FCC implemented the Commission Registration System (CORES), a commercial off-the-shelf software that will assign a specific FCC Registration Number (FRN) to a licensee to track all transactions related to that licensee. The FRN will be populated in RAMIS, and eventually linked to all the licensee databases in each bureau or office within FCC. Unfortunately, RAMIS was

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<sup>1</sup> OIG Report titled, *Report on the Federal Communications Commission Fiscal Year 1999 Financial Statements* (00-AUD-01-01) dated, July 7, 2000.

<sup>2</sup> GAO report titled, *Telecommunications: FCC Does Not Know If All Required Fees Are Collected* (RCED-99-216) dated, August 31, 1999.

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not operational during fiscal year 2000. In addition, CORES was not implemented until July 2000. The success of CORES as a complete database is yet to be evaluated due to the newness of the process and especially when registration in CORES is encouraged, not required.

To close the loop on the potential revenue gap from non-paying licensees, FCC instituted a new process for fiscal year 2000 collection after the regulatory fee payment deadline elapsed. The process requires FO (1) to send a list of entities that paid fees, along with the amount and other relevant data to the appropriate bureaus and (2) to request that each bureau sends its lists of licensee/entities subject to the fee. A billing statement is then sent to licensees that were identified through this process. This process was labor intensive since FCC's organizational structure is decentralized with each bureau (program operation) still maintaining its own licensee database. These databases do not interface with each other or with the financial management system. In addition, the bureaus' databases do not always have the current status of a licensee.

In our review of the regulatory fees that were collected where there was a difference between the FCC estimated fee and the fee calculated by the licensee, we noted that FCC processed the licensee's lower amount without question or request for back-up documentation. While FCC stated that any differences are reviewed for further action, we found no evidence of this review in the files. Also, FCC believes that since its data is estimated based on historical data, the licensees' data will be more accurate. We believe that FCC, in order to assure itself that it is collecting appropriate amounts and its collection process is fair to all licensees, should review the basis of licensees' calculations when they differ substantially from the original estimate. This process will also assist FCC in estimating future regulatory fees. When discussed with management, FCC stated that it would now require the licensee to submit worksheets supporting their payment calculations.

### **B. Application-Processing Fees**

As authorized under Section 8 of the Communications Act of 1934, as amended, FCC collects application processing fees from applicants applying for certain licenses. Applicants submit a completed FCC application form with a "Remittance Advice" to a specific bank lockbox. The bank stamps the documentation with a received date, assigns a fee control number, deposits the payment with the Department of the Treasury, enters data from application into the fee collection database, and forwards the application documentation, and copies of proof of payments to FO. FO, without opening the application documentation package, forwards the package to the bureaus for processing.

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As noted in our report last year and in the GAO report noted above, adequate documentation from the bureaus did not exist to show that application fees were paid. In addition, the bureaus' lack of access (read-only), whenever needed, to the fee collection database made it more difficult for them to verify proper payment of fees. FCC, in its responses, indicated that this weakness will be corrected by the implementation of RAMIS and CORES in fiscal year 2000. Unfortunately, as aforementioned, RAMIS was not operational, CORES was operational as of July 2000 and registration in CORES is voluntary, not mandatory.

Although FO noted that it has had requests for access to the Collections System from the bureaus to verify that proper payments were received and recorded in the system, the implementation of this verification process was not in effect for most of the fiscal year. Moreover, we do not believe that all bureaus requiring application-processing fees implemented this verification process.

In both the regulatory fee and the application-processing fee, there is a higher risk that fees required by legislation are not recorded and collected. Therefore, the conditions for a potential revenue gap still exist.

Internal controls, as used in OMB Circular No. A-123, *Management Accountability and Control* covers all aspects of an agency's operations (programmatic, financial, and compliance). Without integrated database systems accessible to all, and with the bureaus maintaining the customer database while FO maintains the collections data, the need for the bureaus (program) and the FO (financial) to coordinate and communicate in establishing and maintaining internal controls is mandatory.

### **Management Comments:**

Management concurs. FCC noted deficiencies in the fee collection programs in 1998 and initiated comprehensive steps to fundamentally re-engineer the automated systems. FCC initiated steps to resolve issues originally identified in the GAO report. One major initiative is the implementation of two new systems, RAMIS and CORES. CORES assigns a specific FRN to a licensee that will be used to track all transactions related to that licensee. The FRN will be populated in RAMIS, and eventually linked to all the licensee databases in each bureau or office within FCC. Once RAMIS is operational, each phase of collections, whether it is the application fees or the yearly regulatory fees, will be processed through RAMIS. This will be extremely beneficial for the yearly regulatory fees because it will allow management to generate a record of each collection to be used as a basis for bill generation in subsequent years.

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**Recommendations:**

FCC has initiated several manual processes and controls and has started implementing information technology systems to improve management of its account receivable. We recommend the following:

46. Ensure that RAMIS and CORES, when fully operational, address and provide solutions to weaknesses noted in our findings.

**Management Comments:**

Management concurs. FCC believes the systems will resolve the weakness.

47. Continue with the alternative procedures used to ensure that all fees are collected while the new systems are not fully operational. Improve on the procedures by evaluating the results of this year's manual processes used in identifying unpaid regulatory fees and maintain a historical record of the percentage of collections. Use this statistical information to determine how close actual payments are to FCC's estimate and adjust future estimates, if necessary.

**Management Comments:**

Management concurs. FCC plans to continue manually calculating unpaid regulatory fees until an automated system is implemented.

48. Document and implement standard procedures for bureaus to review payment of fees prior to processing an application. Verify compliance with the internal controls documented in the procedure manual.

**Management Comments:**

Management concurs. FO is working with the bureaus and offices to update its policies and procedures to ensure verification of payment of fees prior to processing an application or granting a right.

49. Increase communication and coordination between FO and the bureaus. Ensure that authorized bureau staff have at least read-only access to financial information relevant to their operations. The bureaus and FO should be proactive to the process instead of reactive.

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**Management Comments:**

Management concurs. FO has taken a proactive approach to working with bureaus and offices on outstanding regulatory fee items and application fee issues.

50. Consider using CORES as a mandatory customer registration mechanism to ensure completeness of the database and consistent implementation of the registration procedures.

**Management Comments:**

Management concurs. FCC is currently addressing the full utilization of the FRN and CORES.

**VIII. Improve Supporting Documentation and Controls on Property and Equipment**

An agency must establish physical control to secure and safeguard vulnerable assets. Such assets should be periodically counted and compared to control records. Internal control and all transactions and other significant events need to be clearly documented, and the documentation should be readily available for examination. In addition, control activities help ensure that all transactions are completely and accurately recorded.

Although we were ultimately able to apply audit procedures to audit property and equipment, our review of property and equipment disclosed several internal control deficiencies as follows:

**A. Inadequate Supporting Documentation**

- Documentation supporting 11 of 18 (61%) property sample items described in the property management system did not agree to the description on the property management system. The specific part and serial number on the supporting documentation was different from what was in the property management system.
- Three of eighteen (17%) sample items did not have receiving reports or packing slips to provide evidence of receipt.
- One of eighteen (6%) sample items did not have an invoice.
- One of eighteen (6%) sample items did not have an appropriate payment authorization.
- Two of eighteen (11%) sample items did not have a proof of payment such as an FFS disbursement document that ties to the property.

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- Four of eighteen (22%) sample items did not have a required review/approval signature on one or more documents supporting the sample item.

**B. Incorrect Dollar Values in the Property Records**

Six of eighteen (33%) sample items had incorrect dollar values in the property management records, requiring changes to be made when brought to the attention of FCC management.

**C. Some Capitalized Costs Not Distinguished from Non-Capitalized Costs**

In reviewing accounting entries related to acquisition of certain equipment, we noted that the use of wrong budget object codes (BOC) resulted in capitalized costs not distinguished from non-capitalized costs. Specifically, ADP equipment acquisition was charged to BOC 3120, ADP Equipment, a BOC that is not to be used at the transaction level. FCC's *Financial Coding Handbook* (Fiscal Year 2000 edition) states BOC 3120 is to be used for budget allocation and operational transactions are not to be posted to it. Transactions are to be posted in FFS to either capitalized ADP equipment (BOC 3121) or non-capitalized ADP equipment (BOC 3122.) As a result, capitalized costs could not be distinguished from non-capitalized costs without a detailed account analysis.

**Management Comments:**

Management concurs. FCC developed new processes and communications channels to improve property management and financial practices. Nevertheless, it recognized there is room for further advancement. FCC believes the shortcomings identified during the FY 2000 inventory/audit were directly related to insufficient personnel with the required training and experience in government asset management. To resolve the situation we have created four new positions to be filled in FY 2001: Inventory Operations Program Manager, Financial Audit Coordinator, Inventory Management Specialist, and Data Entry Clerk.

**D. Property Reconciliations Not Performed for Most of Fiscal Year 2000**

Property reconciliations were not performed for most of fiscal year 2000. We requested to see monthly reconciliations but were provided only with the June, July and September 2000 reconciliations.

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**Management Comments:**

Management concurs recognizing property reconciliations were not performed for the entire year. FCC began addressing this issue as soon as the FY 1999 audit was completed; however, at that point several months had lapsed in FY 2000. In FY 2001, all months have and will be reconciled.

Our review of software acquisitions for completed and in-process transactions disclosed the following:

**E. Documentation Was Not Readily Available for Examination**

Overall, it took two months for FCC to obtain supporting documentation needed to vouch payments under multiple purchase orders to their respective software systems. Additionally, this documentation was provided after FCC performed an extensive review and search of software acquisitions. Audit procedures revealed that supporting documentation kept in files was disorganized, incomplete and not conducive to substantiation review. Information needed to compare specific purchase orders and payments with the software asset was not provided until after multiple requests and discussion.

**Management Comments:**

Management concurs. Capitalization of software was one of the final capital asset categories to be addressed, partly due to its complexity. FCC now has a system in place for identifying system costs as they are incurred and will be able to provide stronger and more timely support for FY 2001 balances.

**F. Documentation Did Not Demonstrate that Software Maintenance is Accurately Identified and Expensed**

FCC reports software as in process until it is certified for operation and classified as capitalized software subject to depreciation. FCC has been developing several software systems and each software system development life cycle can span for several years and involve multiple purchase orders. When purchase orders are originally prepared, they identify an accounting "string" of codes to be charged including the fund, SGL account, organization, BOC, etc. Since numerous payments may be made under the same purchase order, the payments are usually charged to the originally established accounting string, which may not be correct.

In our audit, the back up files for one of the capitalized software sample items included approximately \$40 thousand in payments that FO instructed ITC not to

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include in the cost of the asset because they were for software maintenance. We did not receive supporting documentation to assure ourselves that these payments were properly recorded.

Correct BOC classification has been an issue for FCC because often staff who enter BOC information in FFS are not knowledgeable of the differences in accounting for expenditures, (i.e., capitalized vs. non-capitalized, depreciable or expensed). The tendency is to charge the amount to the BOC already listed on the purchase order or invoice. Thus, if a purchase order is originally coded to capitalized software, and a payment relates to maintenance, it will normally be charged to the BOC originally coded on the purchase order or invoice.

**Management Comments:**

Management concurs. The referenced asset for \$40,623, when researched by FCC staff with specific payment vouchers, was charged against BOC 2520, Contract Services – Non Federal, which is not a capitalized code. The BOC for this entry should have been 2572, ADP Software Maintenance. Neither of these BOCs represent capital expenses, therefore, the amount was properly expensed.

ITC will advise staff to pay close attention to the correct BOC usage. As part of the data collection activities underway for FY 2001, ITC has instituted necessary steps to ensure BOCs used are consistent with the ADP services provided. The Planning and Support Group (PSG) is reviewing all ITC-related service requests for proper BOC entries.

**Recommendations:**

51. Include in the AO's procedures requirements that:
- a) The receiving unit prepares a receiving report when a packing slip is not included in the shipment.
  - b) The receiving unit records all relevant asset information such as asset number, serial numbers and purchase order on the supporting documentation (order, receipt, and payment) to facilitate tracking and reconciliation of an asset in the property management system, in FFS, and the supporting documentation.
  - c) Request assistance from the ordering office before assigning an asset number if there is any question as to how to assign asset and serial numbers to items received.

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- d) For complex orders with multiple parts and lines in the purchase order, such as purchases of computer equipment or software, require the ordering office to provide instructions on the purchase order or other document sent to the warehouse or receiving unit as to how costs and assets are to be recorded in the master property record.

**Management Comments:**

Management concurs. FCC recognized the *Property Management Policies and Procedures* have certain “disconnects” in the definitions, policies, and procedures of property currently described. During the past year, FCC discovered many changes/updates which need to be incorporated into policies and procedures. FCC will ensure all financial policies and procedures and administrative requirements are captured in a revised edition.

- 52. Determine which office, FO or AO, is responsible for maintaining the completeness of supporting documentation. Consider including a checklist of relevant documentation that should be in an asset file to ensure completeness of supporting documentation.
- 53. To improve the accuracy of cost data in the management property record and the FFS, we recommend that FO:
  - a) Reconcile on a monthly basis the management property record and the FFS for capitalized assets and at least annually for non-capitalized assets.
  - b) Review FFS entries to ensure use of proper accounting BOC.
  - c) Restrict the use of budgetary BOC in FFS and train employees on the proper accounting entries.

**Management Comments:**

Management concurs with Recommendations 52 and 53 noting FCC has already acted on the recommendations.

- 54. To provide assurance that software maintenance costs are classified appropriately, we recommend that FO, working closely with ITC to:
  - a) Review capitalized software and software maintenance costs on a periodic basis.

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- b) Establish a formal mechanism to ensure that personnel responsible for knowing which costs are maintenance and which costs are developmental provide correct BOC guidance to personnel entering the information in FFS.
- c) Provide training to appropriate personnel on proper allocation of costs to BOCs.

**Management Comments:**

Management concurs. Data is now being gathered and reviewed on a quarterly basis. Management noted it has collected the software inventory for the first quarter of FY 2001 and requested second quarter information. Management provided guidance to Customer Service Representatives (CSR), Bureau and Office Contracting Officer Technical Representatives, and system owners on how to code maintenance versus development cost entries. The capture of data quarterly on software maintenance and development was formalized in September 2000 and is operational. All CSRs and PSG staff have been trained on the proper usage and data entry of both the procurement system and FFS and have been given documentation on the appropriate BOC definitions.

- 55. Ensure that software and systems' owners certify the transfer of a software system from development to operations (in-service) in order for the proper classification and proper depreciation of the asset.

**Management Comments:**

Management concurs stating FCC requires self-certifications quarterly from all system owners for their systems that have moved from development to production.

**IX. Improve Controls Over Accounts Payable (Modified Repeat Condition)**

FCC did not analyze its accounts payable on a routine basis to determine accuracy, reasonableness, and proper classification. Also, the accounts payable general ledger balance was not being reconciled to subsidiary records. Upon analysis of the subsidiary records, we noted vendors' accounts beginning with a Z code with a total of approximately \$15 million debit balances shown as outstanding accounts payable at September 30, 2000. A "Z" code is a vendor code in FFS that starts with the prefix Z. FCC could not initially explain the nature of the debit balances and had to research the issue. Eventually, FCC determined the debit balances were substantially due to auction up-front payments refunded to losing bidders from prior years activity dating back to at

**SECTION II                      INDEPENDENT AUDITOR'S  
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least 1996. When refunds were made, FCC debited accounts payable even though an accounts payable was not originally established.

FFS allows vendor accounts to be paid even without a payable being established, thus creating debit account balances. Although a correcting entry to reverse (or establish) an accounts payable was made when this error was discovered, the correcting entry was not matched with the vendor codes with debit balances. In addition, we noted numerous outstanding balances in the subsidiary ledger schedule being identified by a journal voucher, not by a vendor. We have identified at least 38 journal vouchers prepared to correct balances; most of these vouchers were not matched against a specific vendor balances. Also, FCC does not require all critical accounts payable fields such as the vendor balance field in FFS to be completed.

Standards for internal controls state that transactions are to be properly classified. Account balances should be analyzed on a periodic basis to ensure their propriety, accuracy, and timely detection of errors.

**Management Comments:**

Management concurs. FCC is aware of the issues identified with respect to accounts payable and has been working in FY 2001 to address the problems. Management affected several changes to the accounts payable subsidiary listing and a monthly reconciliation was established. FCC made a pointed effort to work with its fund managers in reviewing and eliminating stale accounts payable and unliquidated obligation balances during FY 2000. Management intends to continue improving this area for FY 2001.

**Recommendations:**

56. Review vendor account balances within the accounts payable subsidiary ledger.

**Management Comments:**

Management concurs. FCC added the vendor name to the monthly subsidiary listing so that vendor balances can be more easily identified. FCC will continue to work with its fund managers to conduct quarterly reviews of both accounts payable and unliquidated obligation balances.

57. Perform periodic reconciliation of the general ledger and the subsidiary ledger balances. Analyze the balances in the accounts periodically (monthly).

**SECTION II                      INDEPENDENT AUDITOR'S  
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58. Activate user access controls and data entry field requirements to ensure that only appropriate activity is recorded in the accounts payable subsidiary ledger.

**Management Comments:**

Management concurs with Recommendations 57 and 58 and established a monthly reconciliation format and began reconciling accounts payable balances in FY 2001.

59. Minimize the use of journal vouchers. If a journal voucher has to be prepared, ensure that the appropriate subsidiary ledger is adjusted for the effect of the journal voucher.

**Management Comments:**

Management concurs stating wherever possible it will attempt to use transaction codes in order to establish and liquidate accounts payable.

60. Consider using a sub-SGL account (i.e., SGL 2110.1) to account for auction related payables. This will allow management to perform an effective and efficient review of the accounts payable and the auction-related transactions.

**Management Comments:**

Management concurs stating it will consider a sub-SGL account in its general ledger structure.

**X. Performance Goals and Results (Repeat Condition)**

The Government Performance and Results Act of 1993 (GPRA) places management expectations and requirements on federal agencies by creating a framework for more effective planning, budgeting, program evaluation, and fiscal accountability for federal programs. The intent of the GPRA is to improve public confidence in Federal agency performance, by holding agencies accountable for achieving program results, and to improve congressional decision-making by clarifying and stating program performance goals, measures, and costs "up front." The annual financial statements is one medium for reporting performance goals and results.

In fiscal year 1999, FCC did not report performance goals and results in its MD&A. FCC explained that it was due to a problem in incorporating the provisions of GPRA into its annual financial statements, not due to lack of processes for identifying, assembling,

## SECTION II INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL

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analyzing, and reporting performance data, which we reported. In fiscal year 2000, FCC did include performance goals and results in its MD&A. These goals and results, however, could not be linked to the input (costs) as reported in the Statement of Net Cost. In addition, this information did not become available for our review until December 2000. There was no global list of performance goals and results (annual performance plans) where we could verify whether appropriate management and performance information was obtained at each level of organization. We could not verify the process where global performance goals and results are evaluated to determine the most significant activities and indicators for financial reporting purposes.

Goals and performance measures must be used in day-to-day management and built into the performance appraisal system to develop an understanding of the relationships between strategic goals and individual work assignments. GPRA's objective is to manage for results. It offers a framework to integrate key management processes in order to provide policy and decision-makers with better information on program results and costs. Without timely feedback on the goals, results, and costs of a program, responsible managers are not able to use the valuable information to take action. As a result, GPRA becomes a useless paperwork exercise.

The FCC strategic plan provided to us was in draft and management intends to finalize it after the end of the audit. The reported measures of program and financial performance were consistent with information on major goals and objectives from the draft strategic plan but again, could not be linked to the program and costs featured in the Statement of Net Cost. The costs in the Statement of Net Costs are quantitative data for use in assessing or measuring the outputs and outcomes of specific performance indicators. As noted in item II of this report, FCC does not have adequate cost accounting systems to measure and report the costs of each segment's outputs.

We believe that increased coordination and communication is still needed among the Performance Evaluation and Results Management Office (PERM - GPRA lead responsibility office), budget office, program offices (bureaus), and the fiscal accountability office (CFO's office) to ensure integration and consistency of processes, shared financial and operational information, and to promote understanding of the performance measurement system throughout the organization.

### **Management Comments:**

Management concurs agreeing the goals and results reported in the MD&A section of the financial statements need to be linked to the Statement of Net Cost.

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**Recommendations:**

61. Enhance communication and information sharing to achieve better results. Ensure that staff throughout FCC is aware of and managers are involved in setting organizational goals and objectives, regularly assessing progress, and making needed changes to help ensure success.
62. Use goals and performance measures in day-to-day management and build them into performance appraisal system to develop an understanding of the relationships between strategic goals and individual work assignments.
63. Increase coordination and communication among the PERM, budget office, program offices, and the CFO office. The CFO office should provide costs input in achieving the outputs and/or outcomes of performance goals.
64. Link objectives and performance measures to the strategic plan and the annual financial statements.

**Management Comments:**

Management concurs with Recommendations 61, 62, 63, and 64. Management noted there was continued and close coordination between all offices, bureaus, Budget Office, and Office of CFO. Any integration issues were the result of inadequate cost data, not inadequate coordination. As aforementioned, the CFO has begun work on designing a new cost accounting system.

**XI.    OMB Circulars No. A-127 and A-130 Reviews (Repeat Condition)**

FCC has recently identified its major financial applications and general support systems, and established a timetable for meeting the requirements of OMB Circulars No. A-127, *Financial Management Systems* and A-130, *Management of Federal Information Resources* reviews of these applications. FCC plans to begin conducting OMB Circulars No. A-127 and A-130 reviews in Fiscal Year 2002. Until these reviews are performed and completed, FCC cannot determine compliance with these Circulars to include in its annual Federal Managers' Financial Integrity Act (FMFIA) report and ensure substantial compliance with Federal Financial Management Improvement Act (FFMIA).

**Recommendations:**

65. Institute a program for conducting periodic reviews in accordance with OMB Circulars No. A-127 and A-130.

**SECTION II                      INDEPENDENT AUDITOR'S  
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**Management's Comments:**

Management concurs noting it contracted the required services to certify and accredit FCC's major applications and general support systems. These reviews are being conducted to ensure compliance with OMB Circulars No. A-123, A-127, and A-130, Appendix III.

- 66. Include the results of OMB Circulars No. A-127 and A-130 reviews as part of Section 4 reporting in FCC's annual FFMIA report.

**Management's Comments:**

Management concurs adding ITC staff will coordinate with FO staff to ensure summaries of financial application level reviews performed to comply with OMB Circulars No. A-127 and A-130 are included in FFMIA reports.

\*\*\*\*\*

In addition to the reportable conditions described above, we noted certain matters involving internal control and its operation that we reported to the management of FCC in a separate letter dated February 9, 2001.

This report is intended solely for the information and use of the management of FCC, FCC Office of Inspector General, OMB, and Congress, and is not intended to be, and should not be, used by anyone other than these specified parties. We caution that misstatements, losses, and noncompliance may occur and not be detected by the testing performed and that such testing may not be sufficient for other purposes.

*Clifton Gunderson LLP*

Calverton, Maryland  
February 9, 2001

**SECTION III**

**INDEPENDENT AUDITOR'S REPORT  
ON COMPLIANCE WITH LAWS AND REGULATIONS**



### Independent Auditor's Report on Compliance with Laws and Regulations

To the Inspector General of the  
Federal Communications Commission

We have audited the Principal Statements (hereinafter referred to as "financial statements") of the Federal Communications Commission (FCC) as of September 30, 2000 and have issued our report thereon dated February 9, 2001. We conducted our audit in accordance with U. S. generally accepted auditing standards; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 01-02, *Audit Requirements for Federal Financial Statements*.

The management of FCC is responsible for complying with laws and regulations applicable to FCC. As part of obtaining reasonable assurance about whether FCC's financial statements are free of material misstatements, we performed tests of its compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of financial statements amounts, and certain other laws and regulations specified in OMB Bulletin No. 01-02, including the requirements referred to in the Federal Financial Management Improvement Act of 1996 (FFMIA). We limited our tests of compliance to these provisions and we did not test compliance with all laws and regulations applicable to FCC.

The results of our tests of compliance with laws and regulations described in the preceding paragraph, exclusive of FFMIA, disclosed instances of noncompliance with the following laws and regulations that are required to be reported under *Government Auditing Standards* and OMB Bulletin No. 01-02, which are described below.

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### **SECTION III            INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH LAWS AND REGULATIONS**

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#### **Chief Financial Officers Act of 1990 (CFO Act)**

The Government Management Reform Act of 1994 (GMRA) amended the requirements of the CFO Act by requiring, among other things, the annual preparation and audit of organization-wide financial statements of 24 executive departments and agencies. Although FCC is not listed in OMB Bulletin No. 01-02, as one of the agencies required to comply with these requirements, management has voluntarily elected compliance and as such is being evaluated accordingly.

The government has a responsibility to use timely, reliable, and comprehensive financial information when making decisions, which has an impact on citizens' lives and livelihood. To meet this responsibility, the CFO Act establishes a leadership structure, provides for long-range planning, requires audited financial statements, and strengthens accountability reporting.

Specifically, the CFO Act establishes the authority, functions and responsibilities of a CFO. These include, among others, that a CFO:

- Develop and maintain an integrated accounting and financial management system that complies with applicable accounting principles, standards, and requirements; internal control standards; and requirements of OMB, the Department of the Treasury, and others;
- Direct, manage, and provide policy guidance and oversight of all agency financial management personnel, activities, and operations;
- Implement agency asset management systems, including systems for cash management, credit management, debt collection, and property and inventory management and controls.

FCC does not meet the above criteria as explained in more detail in our Report on Internal Control, items I through V. The key items we identified include:

- FCC was not able to prepare reliable and timely financial management information efficiently for managing current operations.
- FCC's financial management systems do not comply with certain accounting standards and requirements, and internal control standards.

### **SECTION III INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH LAWS AND REGULATIONS**

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- FCC's financial information system is not fully integrated and relies on data from various subsystems and spreadsheet programs for the accounting, preparing, and reporting of financial statements.
- Policy guidance for financial management personnel, activities, and operations are not formalized in writing, not updated, or not practiced effectively.
- Direction, policy guidance and oversight of Universal Service Fund (USF) financial operations are inadequate.

In addition, FCCINST 1102.3, a FCC internal controls directive that assigns management responsibility and procedures for establishing, maintaining, evaluating, and reporting on internal controls expired in May 2000. There was no directive in effect after the expiration date.

#### **Debt Collection Improvement Act of 1996 (DCIA)**

DCIA requires agencies to notify the Department of the Treasury of all debts that are delinquent for more than 180 days for offset and for referral to the Department of the Treasury for cross-servicing debt collection. In FCC's "Treasury's Report on Receivable Due From The Public" (TROR) for administrative receivables submitted to the Department of the Treasury as of September 30, 2000, it reported \$20 million as the amount eligible for referral for offset, however, only \$109,000 of the \$20 million was referred to Department of the Treasury for cross-servicing. When this discrepancy was brought to FCC management's attention, FCC reviewed the debt eligible and actually referred to the Department of the Treasury and determined that \$18 million of the \$20 million should be referred for cross servicing.

Also, FCC is responsible for reporting receivable due from public for the USF and Telecommunication Relay Service Fund (TRS.) FCC has not been submitting the TROR for USF and TRS until September 30, 2000, the first time it has submitted the reports. We were not provided with the September 30, 2000 TROR report for USF and TRS and therefore were not able to review the reports for compliance.

#### **Government Performance and Results Act of 1993 (GPRA)**

The GPRA requires federal agencies to submit to OMB a strategic plan and annual performance plans that set goals with measurable target levels of performance; and annual program performance reports that compare actual performance to annual goals. Although FCC officials informed us that they had completed their annual performance

### SECTION III INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH LAWS AND REGULATIONS

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plan and their annual program performance report, they did not provide copies of these reports to us. FCC officials indicated to us that these reports were either not released outside the agency or were still under management review as of the end of our fieldwork.

Our review of these GPRA reports is required by OMB Bulletin No. 01-02. Without having access to these reports, we cannot assess FCC's compliance with certain provisions of GPRA.

#### **Recommendation**

We recommend that FCC comply with the provisions of GPRA and provide copies of these documents for our review as part of future financial statement audit.

#### **Federal Financial Management Improvement Act of 1996 (FFMIA)**

Under FFMIA, we are required to report whether the agency's financial management systems substantially comply with the Federal financial management systems requirements, applicable Federal accounting standards, and the United States Government Standard General Ledger (SGL) at the transaction level. To meet this requirement, we performed tests of compliance with FFMIA section 803(a) requirements.

The results of our tests disclosed instances, described below, where FCC's financial management systems did not substantially comply with certain requirements referenced in the preceding paragraph. The following instances of noncompliance have been identified and such matters are described in more detail in our Report on Internal Control.

#### Federal Financial Management Systems

Agency financial management systems shall comply with the Integrated Financial Management Systems as discussed in further detail in OMB Circular No. A-127, *Financial Management Systems*, Section 7. As described in more detail in our Report on Internal Control, items I, II, IV, and V,

- Integrated Financial Management Systems - FCC's core financial system (Federal Financial System) and feeder systems (direct loans systems and spreadsheets, cost systems, property management system, license database, collection systems, certain accounts receivable systems, procurement systems and various spreadsheets) are not integrated or electronically interfaced. A user is not able to have one view into systems such that, at whatever level the individual is using the system, he or she can obtain the information needed efficiently and effectively through electronic means. The primary reason of the noncompliance is due to FCC management's lack of

### SECTION III INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH LAWS AND REGULATIONS

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priority for financial management systems' enhancements until recently. In the last two years, FCC has developed a long-term plan for the full implementation of enhancements and/or integration of its financial management systems.

- Financial Reporting – FCC was not able to provide timely and reliable financial information for managing current government operations. The primary reason of the non-compliance is that financial activities are not recorded, prepared and analyzed timely.
- Security – During our review of the Information Technology controls, we identified several weaknesses, which are collectively considered a material weakness and are described in more detail in our Report on Internal Control, item V. The weaknesses include lack of compliance with OMB Circular No. A-130's, *Management of Federal Information Resources*, requirement for a comprehensive security plan, lack of necessary controls to protect information, and lack of a fully developed and tested contingency plan. The primary reason for the noncompliance is due to FCC management's lack of review of its compliance requirements for financial management systems. FCC has developed a corrective action plan to achieve compliance with OMB Circular No. A-130 requirements by fiscal year 2001.

#### Accounting Standards

Due to the lack of an adequate cost accounting system, FCC was not able to produce managerial cost information consistent with standards in Statement of Federal Financial Accounting Standard No. 4, *Managerial Cost Accounting Standards*, as described in our Report on Internal Control, item II.

#### Standard General Ledger at the Transaction Level

Implementing the SGL at the transaction level requires transactions be recorded in full compliance with the SGL Chart of Account's descriptions and posting models/attributes that demonstrate how the SGL is to be used for recording transactions of the Federal government accounting process. As described in detail in our Report on Internal Control, item I, FFS was not in substantial compliance with the SGL at the transaction level. Some of FFS's deficiencies include: out-dated SGL accounts, account titles, and cross-references; inaccurate natural balances; incorrect debit/credit postings; inconsistencies between certain FFS tables and posting models; and inaccurate closing accounts. The primary cause of this non-compliance is FCC's lack of review of its FFS system setup and posting model definitions for many years.

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**Management Comments:**

Management concurs. The aforementioned laws and regulations are addressed within the findings on the Independent Auditor's Report on Internal Control. As FCC corrects and resolves identified issues, the occurrences of non-compliance will reduce.

\*\*\*\*\*

Providing an opinion on compliance with certain provisions of laws and regulations was not an objective of our audit and, accordingly, we do not express such an opinion.

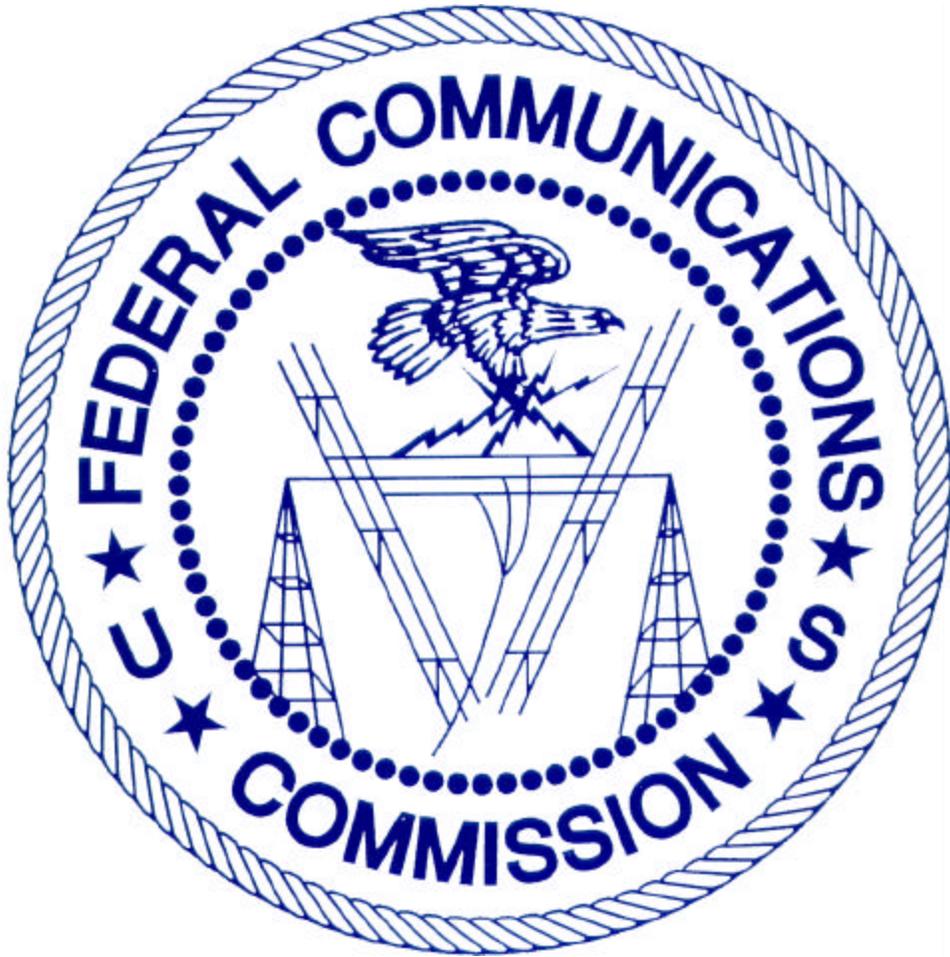
This report is intended solely for the information and use of the management of FCC, FCC OIG, OMB and Congress, and is not intended to be and should not be used by anyone other than these specified parties. We caution that non-compliance may occur and not be detected by the tests performed and that such testing may not be sufficient for other purposes.

*Clifton Gunderson LLP*

Calverton, Maryland  
February 9, 2001

**SECTION IV**

**FEDERAL COMMUNICATIONS COMMISSION  
FISCAL YEAR 2000 ANNUAL FINANCIAL REPORT**



Fiscal Year 2000  
Annual Financial Report

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## **AUDIT OF THE FEDERAL COMMUNICATIONS COMMISSION FISCAL YEAR 2000 ANNUAL FINANCIAL REPORT**

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**FEDERAL COMMUNICATIONS COMMISSION**  
**Washington, D. C. 20554**

**OFFICE OF  
MANAGING DIRECTOR**

**A MESSAGE FROM THE MANAGING DIRECTOR**

I am pleased to present the Federal Communications Commission's (FCC) audited Financial Statements for fiscal year 2000. FY 2000 is the first year the FCC has generated fully OMB Bulletin 97-01, as amended, compliant, auditable financial statements and we are very pleased that our efforts have resulted in an Unqualified (clean) Opinion provided by the Office of Inspector General and their outside audit firm, Clifton Gunderson LLP.

The Chief Financial Officers Act of 1990 (CFO Act), as amended, did not identify the Commission as an agency subject to the Act's rigorous record keeping and reporting standards because of the small size of the agency's operating budget. However, because of the value and increasingly important Spectrum Auction Program and the associated Spectrum Auction Loan Portfolio, in September of 1998 the Department of the Treasury instructed the FCC to provide audit assurance of its FACTS data submitted for FY 1999 and subsequent years. While the Commission's annual budget is small, only \$209 million for FY 2000, its overall financial responsibilities have grown substantially since the passage of the CFO Act in 1990. In addition to its annual operating budget, the Commission is responsible financially for administering the Spectrum Auction Loan Program, the associated Installment Payment Program, and the Universal Service Fund. Since the auction program's inception in 1994, there have been over \$18.8 billion in received as of September 30, 2000. Auction income has become an increasingly important revenue source for the Federal Government. In FY 2001, Auction 35 was held and resulted in net high bids of over \$16.8 billion dollars. In addition, the Spectrum Auction Installment Payment program, comprised of both direct installments and outstanding loan obligations, had a net value in excess of \$9.6 billion on September 30, 2000. The Universal Service Fund maintained a portfolio balance in excess of \$2 billion at the close of the fiscal year, having collected in excess of \$4.5 billion for the year. The total assets under the agency's control were valued at slightly more than \$14.4 billion at the close of the reporting period.

The agencies that were required to adopt the standards of the Chief Financial Officers Act of 1990 have learned through 10 years of effort that changes to accounting practices come only through years of intensive efforts. The FCC accomplished remarkable success in FY 2000 creating a complete set of Financial Statements, Notes, and Required Supplementary Information that have received an unqualified opinion by the external auditors hired by the agency's Inspector General. This success is in no small part to the lessons learned by those much larger agencies over the past ten years. It is also a tribute to the outstanding level of cooperation which existed between the agency's financial and program staff and that of the Inspector General. Working as a team, with a single goal they have accomplished a goal not attained previously by a federal agency in the first year of a full scope audit.

We still have much work to do and the auditor's Internal Control report provides a clear road map. They correctly point out that we have not fully integrated the CFO Act's standard reporting into our daily operations. We are reviewing and replacing several major accounting systems, we have implemented a new inventory control system, we are outsourcing our loan processing activities and re-writing the entire accounting procedures manual for the agency. Implementing these many changes while maintaining the opinion obtained in FY 2000 represent our greatest challenge. Nonetheless, obtaining a "clean" opinion the very first year of effort is an accomplishment for which we are justifiably quite proud. We are committed to institutionalizing our financial improvements and to consistently providing reliable and timely financial information.



Andrew S. Fishel  
Managing Director

**Federal Communications Commission  
Washington**

Office of the  
Inspector General

**A MESSAGE FROM THE INSPECTOR GENERAL**

I am pleased to report that the Office of Inspector General has completed the audit of the Federal Communications Commission (Commission) Fiscal Year 2000 Consolidated Financial Statements. This was the second audit of the Commission's financial activity in accordance with OMB Bulletin No. 01-02, *Audit Requirements for Federal Financial Statements*, and the first audit that included all required principal statements. An expansion in reporting scope, spearheaded by the Chief Financial Officer and senior management, resulted in FCC compiling its first-ever financial statements that consolidated the financial activity of the Commission and the Universal Service Fund.

The audit results on the Commission's fiscal year (FY) 2000 financial statements reflect the dedication and effort FCC placed on achieving financial management initiatives. The expansion to full-scope reporting and receipt of an unqualified opinion on all principal statements for FY 2000 is commendable. Congratulations on a goal not easily obtained!

Although we issued an unqualified opinion on the FY 2000 financial statements, challenges remain for the Commission's financial management program. The Commission's financial reporting process requires automation and further integration into daily operations to ensure continued success. As the time frames and requirements of CFO Act reporting change, FCC needs to capitalize on its investments in financial management initiatives and efficiencies learned to timely meet future reporting **requirements**. Additionally, improved communication and data exchange between entity reporting components will be paramount to meet the Commission's financial management challenges and Governmentwide expectations.

Material weaknesses exist in the internal control of the Commission and our report cites instances of noncompliance with laws and regulations required to be reported in accordance with *Government Auditing Standards* and other authoritative guidance. Accordingly, we reported improvements in internal control noted throughout the conduct of the audit. As the Federal CFO and IG communities best know, the fundamental changes and system improvements to meet principals and standards require time for implementation and the rigors of an audit cycle to best assess their effect. The Commission has made fundamental changes and is in the process of transitioning to a more "CFO like" agency. Consequently, this transition arises in a period of heightened financial responsibility and increased revenue flows not experienced in the Commission's history.

I want to thank the Chairman, Managing Director, Chief Financial Officer, and Commission staff for their cooperation and efforts to make this achievement possible. Again, I congratulate the Commission on its success and I look forward to the challenges in the future as we partner to maintain the highest level of financial accountability across the Commission.

A handwritten signature in black ink, reading "H. Walker Feaster, III". The signature is written in a cursive style with a prominent flourish at the end.

H. Walker Feaster, III  
Inspector General

## **FEDERAL COMMUNICATIONS COMMISSION Fiscal Year 2000 Annual Financial Report**

### **Overview of FCC**

The Federal Communications Commission (FCC or Commission) is an independent United States government agency, directly responsible to Congress. The FCC was established by the Communications Act of 1934 and is charged with regulating interstate and international communications by radio, television, wire, satellite and cable. The FCC's Headquarters is located in Washington, DC, and it has field locations throughout the nation. The FCC's jurisdiction covers the 50 states, the District of Columbia, and U.S. possessions.

The FCC is directed by five Commissioners appointed by the President and confirmed by the Senate for 5-year terms, except when filling an unexpired term. The President designates one of the Commissioners to serve as Chairperson. Only three Commissioners may be members of the same political party. Commissioners cannot have a financial interest in any FCC-related business.

This document contains information about the FCC's principal financial statements for fiscal year 2000, including a consolidated balance sheet, a statement of net cost, a statement of changes in net position, a statement of budgetary resources, a statement of financing, and a statement of custodial activity, and notes to the principal statements. It also serves as a guide to key FCC initiatives and activities taking place during fiscal year 2000 or planned for future years that demonstrate the breadth of the Commission's work.

### **Mission Statement**

*“The Federal Communications Commission’s (FCC’s) primary goals are to promote competition in communications, protect consumers, and support access for every American to existing and advanced communications systems.”*

*Mission Statement  
“A New FCC for the 21<sup>st</sup> Century”*

### **Vision Statement**

*“A Vigorous Competitive Communications Market Providing Universal Access to all American*

This vision synthesizes the FCC's goals to promote competition in communications, protect consumers, and support access for every American to existing and advanced communications services.

The FCC's vision must be executed in a rapidly changing communications environment, which many consider a "communications revolution." In five years, the U.S. communications markets will be characterized predominantly by:

- Vigorous competition that will greatly reduce the need for direct regulation.
- The advent of Internet-based and other new technology-driven communications services that will continue to erode the traditional regulatory distinctions between different sectors of the communications industry.

The enactment of the Telecommunications Act of 1996 -- and the establishment of a new pro-competitive, deregulatory model for communications policy -- necessitates a reassessment of our core policy functions, structure, and processes. New competitors and technological innovation are currently transforming communications markets, but history has shown that markets that have been highly monopolistic often do not naturally become fully competitive. History has also shown that domestic markets that have been protected from foreign competition do not naturally open to global competition.

As a result, in the upcoming years, the FCC must wisely manage the transition from an industry regulator to a market facilitator. The FCC will be very different in both structure and mission from what we know it as today. As a result, fiscal year 2000 was characterized by extensive planning and research in support of our strategic plan.

The Commission's primary goals of promoting competition in communications, protecting consumers, and supporting access for every American to existing and advanced communications services will continue. Our strategic plan for the next five years recognizes that what will change are the means and mix of resources necessary to achieve these goals in an environment marked by greater competition and convergence of technology and industry sectors.

Therefore, during this crucial period of transition, the overall strategic objective of the FCC must be to continue to promote competition, open markets, and technological innovation, while also continuing to protect and empower consumers as they navigate the new world of communications.

At the same time, the Commission must significantly revamp its functions, processes, and structure agency-wide to meet the challenges of a rapidly progressing global information-age economy and an evolving global communications market. Pursuing these strategic objectives will require the identification of clear goals and the execution of year-by-year action plans. As we accomplish our transition goals, we set the stage for a competitive environment in which communications markets look and function like other competitive industries.

## **FCC Organization and Mandate to Harness the Communications Revolution**

The FCC is organized by function. We have seven operating Bureaus and ten Offices. The Bureaus' responsibilities include: processing applications for licenses and other filings; analyzing complaints; conducting investigations; developing and implementing regulatory programs; and taking part in hearings. Our Offices provide support services. Even though the Bureaus and Offices have their individual functions, they regularly join forces and share expertise in addressing Commission issues.

### **The Bureaus**

*Cable Services Bureau (CSB)* - serves as the single point-of-contact for consumers, community officials, and the industry for cable-related issues.

*Common Carrier Bureau (CCB)* - responsible for rules and policies concerning telephone companies that provide interstate, and under certain circumstances intrastate, telecommunications services to the public through the use of wire-based transmission facilities (i.e., corded/cordless telephones).

*Consumer Information Bureau (CIB)* - communicates information to the public regarding Commission policies, programs, and activities. This Bureau is also charged with overseeing disability mandates.

*Enforcement Bureau (EB)* - enforces the Communications Act, as well as the Commission's rules, orders, and authorizations.

*International Bureau (IB)* - represents the Commission in satellite and international matters.

*Mass Media Bureau (MMB)* - regulates AM, FM radio and television broadcast stations, as well as Multipoint Distribution (i.e., cable and satellite) and Instructional Television Fixed Services.

*Wireless Telecommunications Bureau (WTB)* - oversees cellular and PCS phones, pagers and two-way radios. This Bureau also regulates the use of radio spectrum to fulfill the communications needs of businesses, local and state governments, public safety service providers, aircraft and ship operators, and individuals.

### **The Staff Offices**

*Office of Administrative Law Judges (OALJ)* – presides over hearings and issues Initial Decisions.

*Office of Communications Business Opportunities (OCBO)* - provides advice to the Commission on issues and policies concerning opportunities for ownership and contracting by small, minority, and women-owned communications businesses.

*Office of Engineering And Technology (OET)* - allocates spectrum for non-Government use and provides expert advice on technical issues before the Commission.

*Office of the General Counsel (OGC)* - serves as chief legal advisor to the Commission's various Bureaus and Offices.

*Office of Inspector General (OIG)* - conducts and supervises audits and investigations relating to the operations of the Commission.

*Office of Legislative and Intergovernmental Affairs (OLIA)* - is the Commission's main point of contact with Congress and other governmental entities.

*Office of the Managing Director (OMD)* - functions as a chief operating official, serving under the direction and supervision of the Chairman.

*Office of Media Relations (OMR)* - informs the news media of FCC decisions and serves as the Commission's main point of contact with the media.

*Office of Plans And Policy (OPP)* - serves as the Commission's chief economic policy advisor.

*Office of Workplace Diversity (OWD)* - advises the Commission on all issues related to workforce diversity, affirmative recruitment, and equal employment opportunity.

### **The Universal Service Fund**

*Universal Service Fund (USF)* --- A significant program of the FCC, as designated in the U.S. Budget, is the Universal Service Fund (USF). USF consists of five elements, four of which are the universal service support mechanisms and the fifth being the Telecommunications Relay Service (TRS) Fund. The universal service support mechanisms were established pursuant to Section 254 of the Communications Act of 1934, as amended. The TRS Fund was established pursuant to Section 225 of the Communications Act of 1934, as amended. TRS fund compensates TRS providers for the reasonable costs of providing interstate telephone transmission services that enable persons with hearing or speech disabilities to use wireline or wireless telecommunications services.

The universal service support mechanisms are funded through mandatory contributions from all U.S. telecommunications companies, including local and long distance phone companies, wireless and paging companies, and payphone providers. There are four universal service support mechanisms: high cost, low income, rural health care, and schools and libraries. The High Cost Support Mechanism provides support to telephone companies that serve high cost areas. The Low Income Support Mechanism assists low-income consumers by helping to pay for service connection charges as well as monthly charges. The Rural Health Care Support Mechanism allows rural health care providers to pay the same for telecommunications services as their urban counterparts. The Schools and Libraries Support Mechanism provides discounted Internet access and telecommunications

service to schools and libraries. While consumers benefit from the support mechanisms, only service providers may receive money directly from the support mechanisms, which defray the cost of delivering services to customers.

*The Universal Service Administrative Company (USAC)* – administers the USF under the direction of the FCC.

*The National Exchange Carriers Association (NECA)* – administers TRS funds under the directions of the FCC.

The most current organizational chart for the FCC, dated January 22, 2001, is included on the following page.

# FEDERAL COMMUNICATIONS COMMISSION

## COMMISSIONERS

Michael K. Powell, Chairman

Susan Ness  
Harold W. Furchtgott-Roth

Vacant  
Gloria Tristani

### OFFICE OF INSPECTOR GENERAL

### OFFICE OF GENERAL COUNSEL

Administrative Law Div.  
Litigation Div.

### OFFICE OF MANAGING DIRECTOR

Human Resources Mgmt.  
Information Technology  
Center  
Financial Operations  
Administrative Operations  
Performance Evaluation &  
Records Management  
Secretary

### OFFICE OF MEDIA RELATIONS

Media Services Staff  
Internet Services Staff

### OFFICE OF PLANS &

POLICY

### OFFICE OF COMMUNICATIONS BUSINESS

OPPORTUNITIES

### OFFICE OF WORKPLACE DIVERSITY

### OFFICE OF LEGISLATIVE & INTERGOVERNMENTAL AFFAIRS

### WIRELESS TELECOMMUNICATIONS BUREAU

Auctions & Industry  
Analysis Div.  
Commercial Wireless Div.  
Public Safety & Private  
Wireless Div.  
Policy Div.  
Planning & Management  
Staff

### MASS MEDIA BUREAU

Audio Services Div.  
Policy & Rules Div.  
Video Services Div.  
Equal Employment  
Opportunity Staff  
Administration & Mgmt.

### CONSUMER INFORMATION BUREAU

Consumer Information  
Network Div.  
Reference Information Center  
Consumer Education Office  
Strategic Information Office  
Disabilities Rights Office  
Systems Support Office  
Staff

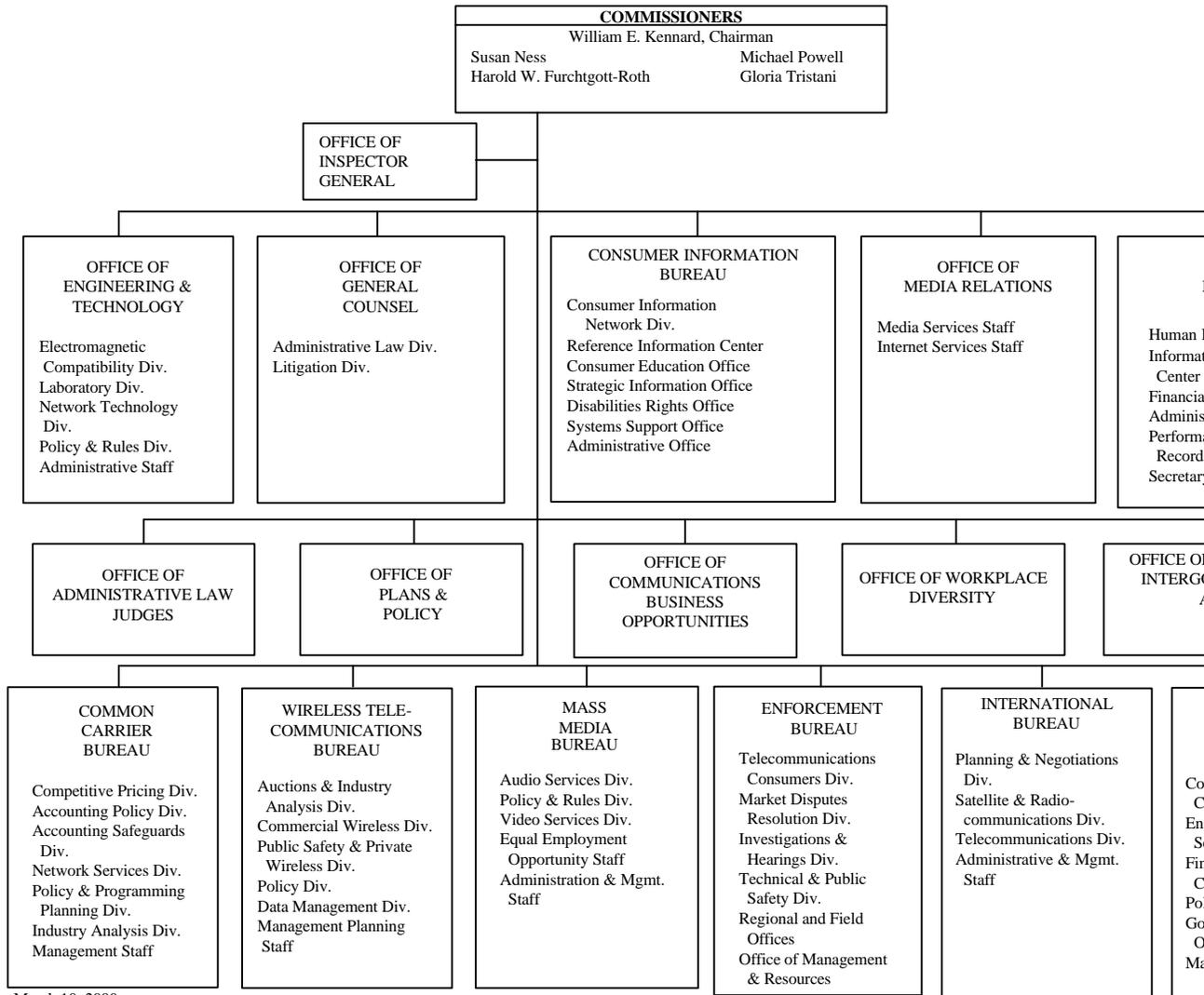
### INTERNATIONAL BUREAU

Planning & Negotiations  
Div.  
Satellite & Radio-  
communications Div.  
Telecommunications Div.  
Administrative & Mgmt.  
Staff  
Administrative Office

### CABLE SERVICES BUREAU

Consumer Protection &  
Competition Div.  
Engineering & Technical  
Services Div.  
Financial Analysis &  
Compliance Div.  
Policy & Rules Div.  
Government & Public  
Outreach Staff  
Management Staff

## Federal Communications Commission



March 10, 2000

## **Limitations of the Financial Statements**

The financial statements have been prepared to report the financial position and results of operations of the FCC. While the statements have been prepared from the books and records of the FCC in accordance with the formats prescribed by the Office of Management and Budget, the statements are in addition to the financial reports used to monitor and control budgetary resources which are prepared from the same books and records.

The statements should be read with the realization that they are for a component of the U.S. Government, a sovereign entity. One implication of this is that liabilities cannot be liquidated without legislation that provides resources to do so.

## Facilitating the Communications Revolution – The FCC’s Implementation of the Government Performance and Results Act

*“Over the next five years, the FCC must wisely manage the transition from an industry regulator to a market facilitator....[D]uring this crucial period of transition, the overall strategic objective of the FCC must be to continue to promote competition, open markets, and technological innovation, while also continuing to protect and empower consumers as they navigate the world of communications.”*

*st Century”*

**I. Overview:** With rapid changes in the technology sectors, the FCC’s strategic planning process has been an evolving one. In the coming years, we expect U.S. communications markets to be characterized predominately by vigorous competition that will reduce the need for direct regulation. We anticipate that the advent of Internet-based and other new technology-driven communications services will impact various sectors of the communications industry. The FCC’s primary goals of promoting competition in communications, protecting consumers, and supporting access for every American to existing and advanced communications services will continue.

To ensure the FCC is making strides in fulfilling the Agency’s mission, performance goals were developed in accordance with the Government Performance and Results Act (GPRA). Performance measures included in this overview were drawn from the FCC’s Strategic Plan *st Century”* (August 1999).<sup>1</sup> In cases where the strategic plan does not include numeric goals, we used measures from the Agency’s FY 2000 budget request to Congress. The limited number of performance measures selected for this Annual Financial Report was based on links to the most significant program and financial measures.

**II. Goals and Objectives:** As a result of the changing communications environment, a number of the FCC’s current functions and regulatory structures have been streamlined or eliminated. Increased automation and efficiency will enable the FCC to further streamline its licensing activities, accelerate the decision-making process, and allow the public faster and easier access to information. The FCC will be a “one-stop, digital shop” where form filing and document-location are easy and instantaneous.

The FCC will focus on sustaining competitive communications markets and protecting the public interest where markets fail to do so. Our core activities include: 1) licensing of current and, where appropriate, emerging technologies; 2) consumer protection, consumer information, and universal service; 3) enforcement; 4) the promotion of competitive markets domestically and internationally; and 5) spectrum management.<sup>2</sup>

The FCC’s strategic goals and objectives, listed in the chart below, are aligned with our core functions. Note that those objectives in italics are detailed further in part IV of this Section.

<sup>1</sup> “A New FCC for the 21<sup>st</sup> Century” is on FCC’s website: [http://www.fcc.gov/21st\\_century/draft\\_strategic\\_plan.pdf](http://www.fcc.gov/21st_century/draft_strategic_plan.pdf). The “Year 1” column in Appendix A of the strategic plan represents the FY 2000 goals.

<sup>2</sup> FCC’s “FY 2001 Budget Estimates to Congress”, page 1.

### Goals and Objectives Articulated in the Strategic Plan<sup>3</sup>

**A. Create A Model Agency For The Digital Age.**

- 4 *Lead the way in the Information Age.* (3)
- 4 Reorganize to create an agency infrastructure conducive to convergence.
- 4 *Create a faster, flatter, more functional agency.* (4)
- 4 Preserve and increase the wealth of knowledge and expertise of FCC staff.

**B. Promote Competition In All Communications Markets.**

- 4 Eliminate barriers to entry in domestic markets.
- 4 *Deregulate as competition develops.* (2)
- 4 Enforce the rules so that businesses compete fairly.
- 4 Promote competition in international communications markets.

**C. Promote Opportunities For All Americans To Benefit From The Communications Revolution.**

- 4 *Ensure access for all Americans to existing and future communications services.* (1)
- 4 Promote opportunities to expand direct participation in existing and future communications businesses.
- 4 Foster a consumer friendly marketplace.

**D. Manage The Electromagnetic Spectrum (The Nation's Airwaves) In The Public Interest.**

- 4 Create more efficient spectrum markets.
- 4 *Increase the amount of spectrum available for use, particularly for new services.* (5)

**III. Performance Measures Highlighted in Financial Statement:** The performance measures for the FY 2000 Annual Financial Report highlighted below have been selected because they are:

- a. aligned with the Agency's mission and goals;
- b. limited to the FCC's most significant programs; and
- c. consistent with the Agency's implementation of the Government Performance and Results Act (GPRA) as reflected in budget documents and other related materials.

**IV. Measurement of Five Performance Objectives for FCC's Performance Goals:** This section discusses five performance objectives that enable the Agency to meet the performance goals, and the FCC's success in achieving its FY 2000 targets. The five performance objectives were selected from the FCC's strategic and performance plans. Each section below includes a table that identifies the FCC's FY 2000 accomplishments. Where FY 1999 data is available, it also is highlighted.<sup>4</sup>

<sup>3</sup> March 2000 "Report Card on Implementation": [http://www.fcc.gov/21st\\_century/report\\_card\\_march2000.pdf](http://www.fcc.gov/21st_century/report_card_march2000.pdf).

<sup>4</sup> For a discussion of FCC's progress in achieving FY 1999 goals, see the March 2000 "Report Card on Implementation".

**Performance Objective #1: Promote Opportunities For All Americans To Benefit From The Communications Revolution**

This performance goal encourages the development of competitive and innovative communications systems, by promoting opportunities for all Americans to access existing and future communications services, and by fostering a more consumer friendly environment. As the FCC strives to promote competition, we will continue to monitor the marketplace to ensure that the benefits of advanced telecommunications services and the new information economy is available to everyone, able-bodied or disabled, in every school, classroom, library, and rural community throughout the United States.

<b>Performance Objective</b>	<b>Performance Measure</b>	<b>FY 2000 Target</b>
Continue oversight of the universal service discount mechanism for schools, libraries and rural health care providers to ensure their efficient and effective operations. Fully implement the Schools and Libraries Program	Public school instructional classrooms and libraries receiving telecommunications services, Internet access, or internal connections at reasonable rates	75% <sup>5</sup>

The Schools and Libraries support mechanism – often called the “E-rate” – provides support for eligible schools and libraries to help offset the cost of telecommunications services. The range of discounts available corresponds to the income level of students in their community as well as the location of the school or library (e.g., urban or rural). Income for a school or district is measured by the percentage of students eligible for the National School Lunch Program. For fiscal year 2000, the Universal Service Fund (USF), for the Schools and Libraries Program, collected gross receipts of approximately \$2.0 billion, with outlays of approximately \$1.6 billion. In FY 1999, the USF collected gross receipts of approximately \$1.5 billion, with outlays of approximately \$1 billion.<sup>6</sup>

In FY 1999, funding for the Schools and Libraries Program to support the Education-rate (E-Rate), which provides discounts to schools and libraries for telecom services, internet access, and internal connections, increased the percentage of public school instructional classrooms connected to the Internet to 63%. By 1999, 83% of public and private schools (as distinct from instructional classrooms) were connected to the Internet.<sup>7</sup> FY 2000 classroom actual connection rates will be available after the National Center for Education Statistics (NCES) publishes their year 2000 report.<sup>8</sup>

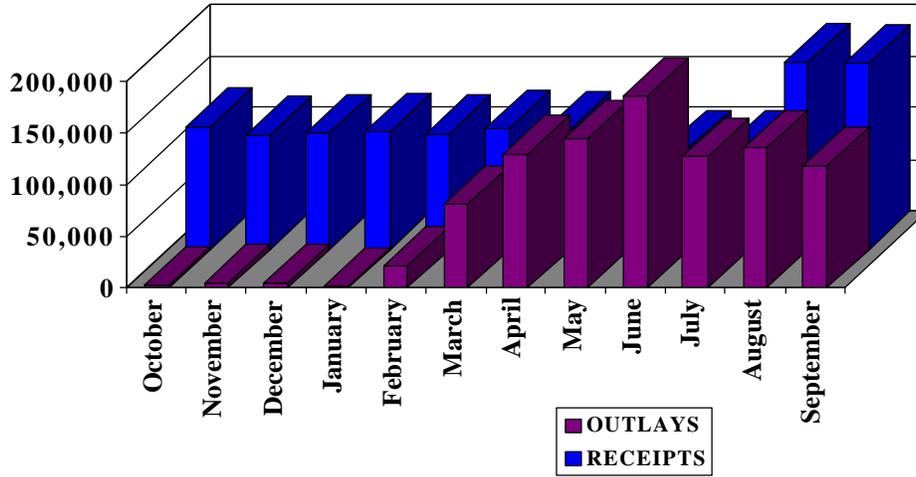
<sup>5</sup> FCC’s Strategic Plan includes this measure as 85% for all public schools. However, since this goal was achieved for schools, the USF raised the bar, by revising the performance measures to 75% of instructional classrooms as opposed to schools.

<sup>6</sup> Gross receipts and outlays are based on monthly SF-224 reports, using the FCC’s fiscal year October 1 to September 30.

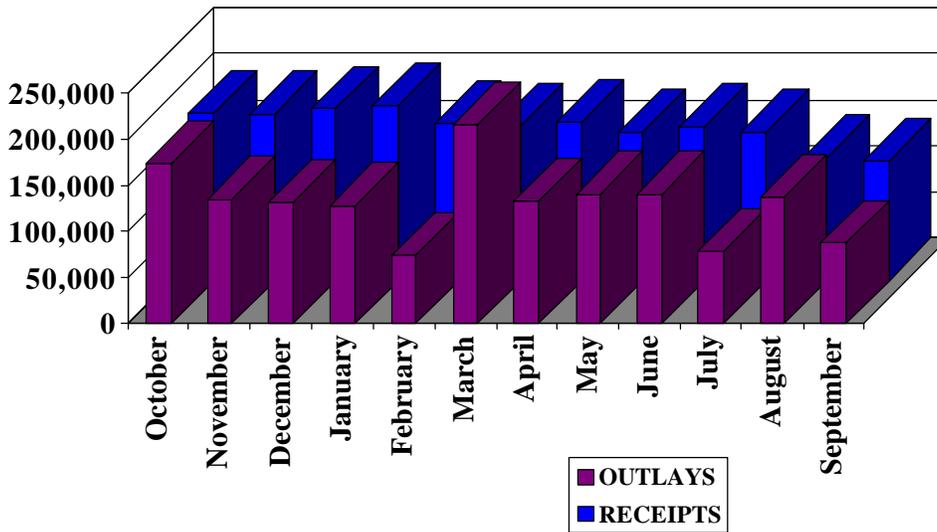
<sup>7</sup> National Center for Education Statistics, “Internet Access in U.S. Public Schools and Classrooms: 1994-99” (February 2000).

<sup>8</sup> The Schools and Libraries Funding Year starts July 1 and ends June 30 of the following year.

USF - Schools and Libraries Fund  
 FY 1999  
 (in thousands)



USF - Schools and Libraries Fund  
 FY 2000  
 (in thousands)



**Performance Objective #2: Promotion of Competitive Markets Domestically and Internationally**

This performance goal points to the FCC’s efforts to eliminate outdated rules, which plays an important role in accelerating the transition to fully competitive markets. Consumers ultimately pay the cost of unnecessary regulation. Thus, one of the FCC’s primary objectives must be to deregulate as competition develops, and to substitute market-based approaches for direct regulation.<sup>9</sup> As part of this initiative, FCC is working to reduce the burden on the participants in the FCC’s programs.

<b>Performance Objective</b>	<b>Performance Measure</b>	<b>FY 2000 Target</b>	<b>FY 2000 Actual</b>	<b>Percent Achieved</b>
Reduce the burden of filing, reporting, record keeping and accounting requirements across all communications industries	Reduction in the number of forms / information collections required by FCC	10%	- 31 Forms	7%

According to performance data collected from the various Bureaus and Offices, the total number of FCC forms at the start of FY 2000 was 197. During FY 2000, 31 forms were combined or eliminated. During the year additional forms were created to accommodate new collection needs, leaving the total number of forms at the end of FY 2000 at 183 (a 7% reduction from FY 1999).

The Information Collection Budget (ICB) compiled annually, tracks the number of FCC forms as well as burden hours and costs to the public. The FCC’s FY 2000 ICB (December 1999) estimated a burden reduction on the public of 17% over FY 1999, including nearly 2 million burden hours attributed to refinements in access reform rules; 244,000 burden hours as a result of changes in accounting and cost allocation rules and ARMIS reporting system; and about 2.5 million burden hours due to the elimination of unnecessary collections. In some cases, combining, rather than eliminating collections achieved reductions. The Wireless Telecommunications Bureau (WTB) combined 40 forms into 4, creating schedules and clarifying required collections.

The FY 2001 ICB (November 2000) estimates a burden reduction on the public of 10.9% over FY 2000. Significant estimated savings include: 500,000 burden hours, attributed to our reduced Part 61 requirements; 400,000 burden hours, as a result of section 11 reviews of our accounting rules and related reporting requirements for incumbent local exchange carriers; a 1,738,597 burden hour reduction for Customer Proprietary Network Information (CPNI) requirements due to elimination of unnecessary showings; and a 953,389 burden hour reduction due to elimination of a Notice of Proposed Rulemaking (NPRM) for the Commission’s broadcast and cable equal employment opportunity rules and policies and termination of the EEOO streamlining proceeding. The WTB also developed the interactive, web-based Universal Licensing System (ULS), an “intelligent” licensing system with built-in security, which encourages electronic filing of collections.

<sup>9</sup> “A New FCC for the 21<sup>st</sup> Century” p.14, FCC’s website: [http://www.fcc.gov/21st\\_century/draft\\_strategic\\_plan.pdf](http://www.fcc.gov/21st_century/draft_strategic_plan.pdf).

**Performance Objective # 3: Create A Model Agency For The Digital Age**

This performance goal promotes efficient and innovative licensing and authorization of services by automating functions and fully implementing automated licensing and electronic filing systems across the agency. As the FCC promulgates policies conducive to advances in information technology, we must also lead the way in electronic government. Across the agency, we must invest in new technology that will improve our processes and allow us to be as responsive to the public as possible. We must continue to automate our processes and to make information available to the public electronically on an interactive basis.

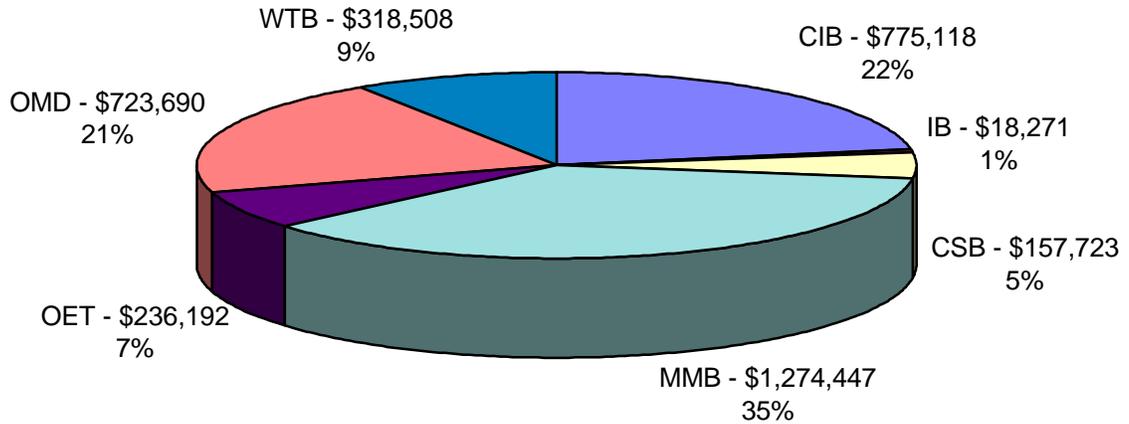
<b>Performance Objective</b>	<b>Performance Measure</b>	<b>FY 2000 Target</b>	<b>FY 2000 Percent Achieved</b>
Create a paperless FCC by automating functions and fully implementing automated licensing and electronic filing systems across the agency to promote "one-stop shopping."	Increase the percentage of electronic licensing and filing (measure percentage of FCC licensing/ filings within systems offering electronic interface).	60%	59.9%

This goal may never achieve 100% since it is not feasible to automate all application processes or to require that all forms be filed electronically without jeopardizing accessibility (e.g., those without access to the technology, Braille readers). This measure examines the number of electronic filings where electronic filing systems exist. By the end of FY 2000, a total of 108 services were available, of which 78 services (72%) had electronic filing capacity. The Agency came within one-tenth of one percent in meeting the 60% goal set for FY 2000. Note that the Mass Media Bureau did not offer electronic filing until the third quarter of FY 2000.

<b>Bureau</b>	<b>Number of Electronic Applications/Filings</b>	<b>Total Number of Applications/Filings</b>	<b>Percent Achieved</b>
Common Carrier Bureau	743	3,030	24.5%
International Bureau	987	4599	21.4%
Mass Media Bureau	9,948	36,373	27.3%
Office of Engineering and Technology	3,500	4,078	85.8%
Wireless Telecommunications Bureau	317,764	506,922	62.6%
<b>AGENCY TOTAL</b>	<b>332,942</b>	<b>555,002</b>	<b>59.9%</b>

The FY 2000 Budget included \$16.1 million allocated toward the Commission's information technology (IT) program. More than \$12 million funded current IT operations, systems maintenance and limited life-cycle replacement. The remaining amount, approximately \$3.5 million was obligated toward initiatives that promoted: electronic filing, streamlined application processes, enhanced customer access to information, database consolidation or integration, facilitation of the creation of a paperless environment, and security of mission-related systems. The pie chart below details the IT actual obligations by Bureau or Office.

## ELECTRONIC FILING / SYSTEM DEVELOPMENT



### **Performance Objective #4: Create A Model Agency For The Digital Age**

This performance goal promotes efficient and innovative licensing and authorization of services by creating a faster, flatter, more functional Agency with substantially reduced backlogs in licensing applications, petitions for reconsideration, and other proceedings. The FCC must be structured to react quickly to market developments, to work more efficiently in a competitive environment, and to focus on bottom line results for consumers. Ultimately, the Agency must be structured to render decisions quickly, predictably, and without imposing needless costs on industry or consumers through unnecessary delays.

<b>Performance Objective</b>	<b>Performance Measure</b>	<b>FY 2000 Target</b>	<b>FY 2000 Percent Achieved</b>
Substantially reduce our backlog in licensing applications and petitions for reconsideration and other proceedings. (A backlog is defined as 1.5 times the actual speed of disposal.)	Overall reduction in backlogs goals	75% CSB*	+6.9%
		75% WTB*	-2.2%
		50% IB*	-4.3%
		50% OET*	-1.9%
		50% CCB*	No backlog

\* In some cases FCC may not meet timelines due to external requirements, including involvement of outside agencies.

This measure specifically looks at backlogs in processing applications within the Cable Services Bureau (CSB), Wireless Telecommunications Bureau (WTB), Common Carrier Bureau (CCB), International Bureau (IB), and the Office of Engineering and Technology

(OET). This measure excludes from the analysis: the Enforcement Bureau, where enforcement activities are now consolidated for handling formal complaints; the Consumer Information Bureau which now handles informal complaints; or the Mass Media Bureau which is currently implementing an auto-processing system for broadcast applications. In FY 2000, the agency made significant strides in reducing backlogs in the Enforcement and Consumer Information Bureaus.

Because of changes in the agency structure, it is not possible to use FY 1999 data as a basis for comparison (e.g., the Enforcement Bureau and Consumer Information Bureau did not exist, and as such the backlogs in those areas were spread across other Agency bureaus and offices). In addition, the FCC has changed the way it calculates the percentage of backlogged applications. In the past, FCC did not take into consideration the workload for processing new applications, which impacts the Agency's ability to respond to overage cases. Since baseline data does not exist for FY 1999, this analysis compares the change from the end of the first quarter to the end of the fourth quarter.

Overall, these FCC bureaus/offices reduced backlogs from 7.88% in the first quarter to 4.76 % in the 4<sup>th</sup> quarter (-3.12%).

As seen by this specific measure, the FCC's Strategic Plan focuses on backlog reduction efforts in specific Bureaus and Offices. By reducing the number of forms required, and enabling the public to file these applications electronically, the FCC will be in a better position to respond to backlogged applications, thereby providing better customer service. For example, FTE resources were reallocated to the Enforcement Bureau and the Consumer Information Bureau, both of which experienced significant reductions in backlogs in FY 2000. In FY 2000, the FCC refocused its backlog reduction efforts toward the elimination of a significant number of informal complaints in the Consumer Information Bureau (CIB). When our efforts in CIB as well as efforts in the Enforcement Bureau and the Mass Media Bureau are included in the analysis, the Agency's backlog was reduced from 40% to 4%.

#### **Performance Objective #5: Manage The Electromagnetic Spectrum (The Nation's Airwaves) In The Public Interest**

This performance goal promotes efficient and effective management in the use of the Nation's airwaves in the public interest for all non-Federal government uses, accompanied by increased accessibility of available spectrum to the public. As markets become more competitive and new technologies are introduced, demand for spectrum will increase. The Commission must seek new methods to ensure that available spectrum is put to the highest value use. All else being equal, increasing the availability of spectrum will reduce the cost of using spectrum, and thereby increase the output and reduce the price of spectrum-based services. It will also create new opportunities for competitive technologies and services, including public safety services, for the American public.

<b>Performance Objective</b>	<b>Performance Measure</b>	<b>FY 2000 Target</b>	<b>FY 2000 Actual</b>
Create incentives for freeing up spectrum. Increase the amount of spectrum available for use, particularly for new services.	Allocate 4 GHz of spectrum for unlicensed services.	4 GHz	TBD

In FY 2000, the FCC increased the amount of spectrum available to the public for unlicensed services. Unlicensed services are those services made available through rulemaking (e.g., low power TV) to allow and encourage the introduction of new services, particularly in rural or underserved areas.

In FY 2000, eight (8) auctions were held, and the FCC recorded \$1.3 billion in net winning bids. This amount represents the net winning bids excluding possible defaults and the costs to the FCC of \$45.4 million. This amount is recognized as revenue in the year the license is granted, rather than when the auction is held or cash is received. The FY 2001 budget estimated that a total of \$2.076 billion in auction receipts would be generated from the anticipated auctions in FY 2000. One of the anticipated auctions (#35) originally scheduled for FY 2000 was postponed until FY 2001. The FCC delayed the auction to allow for preparation of responses to the protests filed during the public comment period, for which the FCC has since responded. The auction was rescheduled for December 2000.

## **Financial Management and Systems**

The Office of Managing Director has responsibility for implementing accounting and financial policies, systems, and reports; improving reliability of financial information; implementing debt collection; and implementing financial management legislation including the following:

- Prompt Payment Act of 1982
- Federal Managers' Financial Integrity Act (FMFIA) of 1982
- Cash Management Improvement Act
- Federal Credit Reform Act of 1990, as amended
- Government Performance Results Act of 1993
- Government Management Reform Act of 1994
- Federal Financial Management Improvement Act of 1996
- Debt Collection Improvement Act of 1996

In the FCC's efforts to achieve compliance with applicable legislation, it is necessary to have effective management and system controls in place. The FCC has established formal policies and procedures regarding the processing, maintaining and reporting of financial information. The FCC is currently in the process of updating its policies and procedures. Although the FCC has made significant improvement with regards to its management controls, additional improvement is needed as indicated by the results of the fiscal year 2000 financial statement audit.

With regards to system controls, the security administration and/or system maintenance support for the financial systems is performed by the Financial Systems Operations Group, within the Office of Managing Director. The following summarizes several significant financial systems.

- Federal Financial System
- Collections System
- Nortridge Loan System
- Revenue & Accounting Management Information System

The Federal Financial System (FFS) is a Commercial Off-the-Shelf (COTS) software package adapted to handle all of the collections accounting and loan management for the FCC, and is represents the general ledger accounting system. It is designed to interface with FCC's central accounting system, FFS, and licensing systems throughout the Commission as needed.

The Collections System is a custom-built database application adapted to store and display all of the collections accounting for the FCC. It is designed to interface with FCC licensing and other systems throughout the Commission as needed. FCC also uses a COTS software package, adapted for tracking civil monetary penalties with the status of Notices of Apparent Liability (NALs). It also records the collection of receipts, produces dunning letters for past due accounts, and issues reminders to forward account forfeitures to the Office of General Counsel (OGC) for referral to the Department of Justice (DOJ) for collection.

The Nortridge Loan System (NLS) is a COTS software package designed and developed for lenders of all types and sizes. NLS incorporates the latest in client-server and object oriented technology along with standard, familiar, Windows operation to provide an ideal solution for lending operations. The FCC currently uses NLS to record payments received by licensees under the Spectrum Auction Direct Loan program.

The Revenue Accounting and Management Information System (RAMIS) is a COTS software package modified to handle all of the collections accounting and loan management specific to the FCC. It is designed to interface with FCC's central accounting system, FFS, and licensing systems throughout the Commission as needed. Once all reporting modules are complete, all collection activity of the FCC, including civil monetary penalties and loans, will be recorded and tracked in RAMIS. Implementation of RAMIS is intended to assist the FCC in achieving better system integration, as well as system requirements established by the Joint Financial Management Improvement Program. As of the date of our FY 2000 audit FCC was still in the conversion phase of implementation and no audited financial activity was recorded in the RAMIS system.

Not included as part of its systems but still an important financial management tool for FCC management in FY 2000 are the Loan Model Spreadsheets used to calculate loan balances on FCC's credit reform loans. The spreadsheets were maintained by an outside contractor throughout the course of the year and served as the basis for numbers used in

the calculation of FCC's subsidy re-estimate. Ultimately, these spreadsheets will be replaced by an outside loan servicing system.

## **Highlights of Financial Statements**

### **Results of Financial Position and Operations**

A significant aspect of the FCC's operations pertains to its Spectrum Auction activities. The net loans receivable, which represents installments due from licenses under the Spectrum Auction program, is approximately \$9.6 billion of the total assets of approximately \$14.4 billion. There is a direct correlation among the loans receivable and the borrowings of approximately \$5.3 billion and Unexpended Appropriations of approximately \$6.1 billion. These balances were impacted by the results of the subsidy costs and reestimate process, as discussed below.

The FCC is required to annually adjust its allowance for losses on their credit portfolios based on the most current performance information. In accordance with OMB guidance, the FCC calculated its subsidy reestimate based on the most recent economic conditions and technical assumptions available. The FCC's subsidy reestimate shows a \$4.3 billion reduction in the Spectrum Auction Loan Portfolio subsidy cost, primarily due to the projected improved performance of the defaulted C Block and F Block loan portfolios. The average subsidy rate (the subsidy cost expressed as a percent of the original loan amount) falls from 52.08% from the prior year to 18.08% for the current year. In other words, the FCC expects to lose 18 cents for every dollar lent out through the Spectrum Auctions installment loan program.

The most significant changes in the reestimate of the subsidy costs are attributable to the C and F Block installment licenses. There were no significant changes to the assumptions used for projection purposes of estimated cash flows for the other Spectrum Auction licenses. Based on the FY 2000 subsidy reestimate, the FY 1997 C and F Block installment licenses account for 97% of the Spectrum Auction subsidy cost (94% and 3%, respectively).

The C Block FY 1997 Cohort Subsidy Reestimate for FY 2001 resulted in a subsidy rate change from 54.34% in FY 2000 to 17.96% in FY 2001 and a subsidy cost change from \$4,882.5 million in FY 2000 to \$1,613.7 million in FY 2001. The major driver was due to the new recovery assumptions of approximately \$7.9 billion from Auction 35 and a 100% recovery rate on other defaulted loans. The reestimate also reflects 12 months of additional payment data and a change in projected vs. actual defaults from FY 2001 – FY 2006.

The F Block FY 1997 risk category subsidy reestimate for FY 2001 resulted in a subsidy rate change from 27.62% in FY 2000 to 6.08% in FY 2001 and a subsidy cost change from \$137.4 million to \$30.2 million. Consistent with C Block, the major driver for the change was due to an increase in the recovery projection from 50% to 100%.

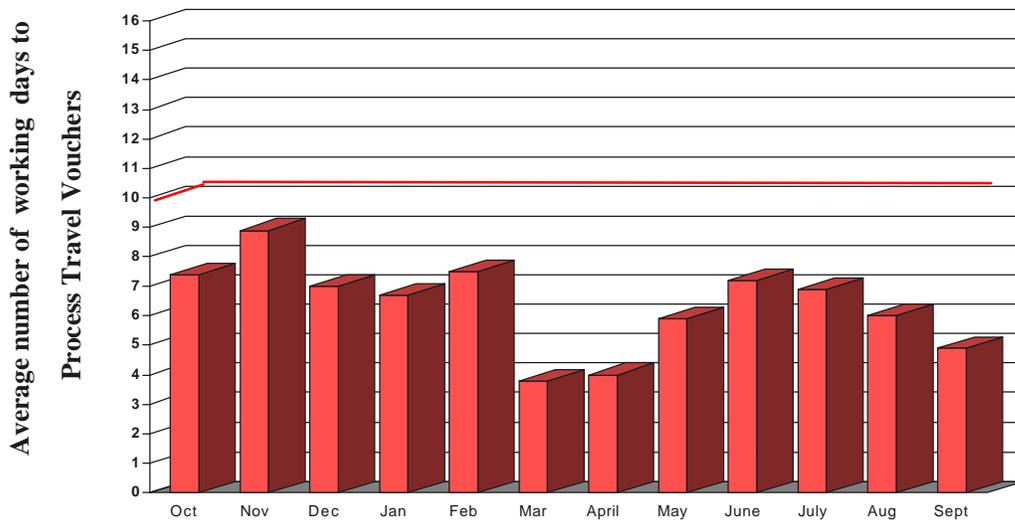
Another significant aspect of the financial statements is the Universal Service. The Fund has grown over the past year, collections have kept pace with the new support requirements of carriers and the Fund has met all obligations during the year. Management expects the Fund to continue to meet all obligations presented.

The USF had a total distribution of \$4.029 billion in fiscal year 2000. Net collections (\$4.539 billion) exceeded the total distributed by \$510 million. Those collections when added to previous collections and receivables constitute the total net assets of the Fund, \$2.449 billion. Those assets are sufficient to meet the total liabilities of the Fund.

The level of collections and disbursements may vary based on the enhanced support for low-income customers living on reservations. The demand for the Low Income support mechanism is estimated to increase greater than the historical growth in FY 2001. The FCC estimated that demand would increase by \$8.75 million dollars for October 1 through December 31, 2000 as a result of its Tribal Lands order and the enhanced support provided to low income customers living on reservations.

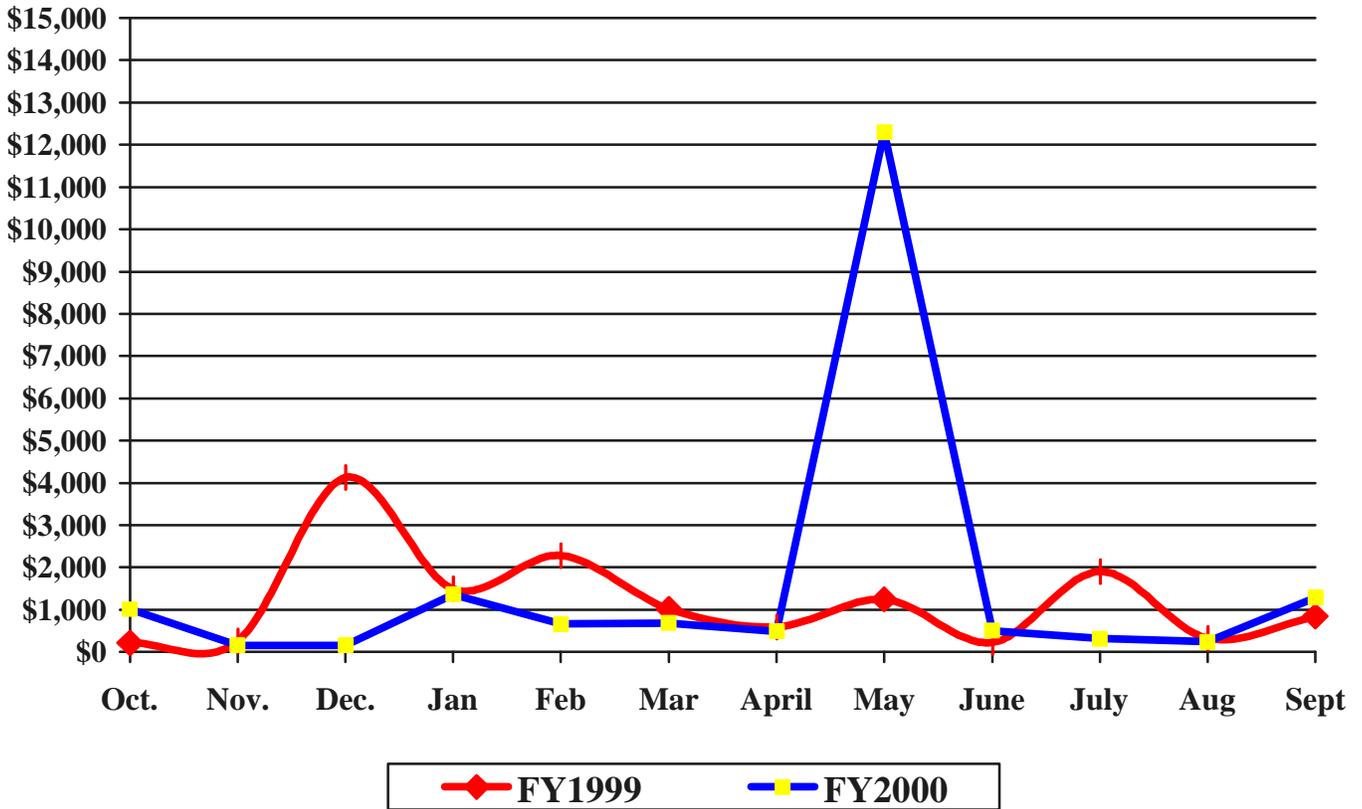
The remainder of this section highlights FCC activities related to travel voucher processing, prompt payment interest information, electronic credit card payments, electronic fund transfers, collections, and budget authority and FTE information.

# Travel Voucher Processing FY 2000



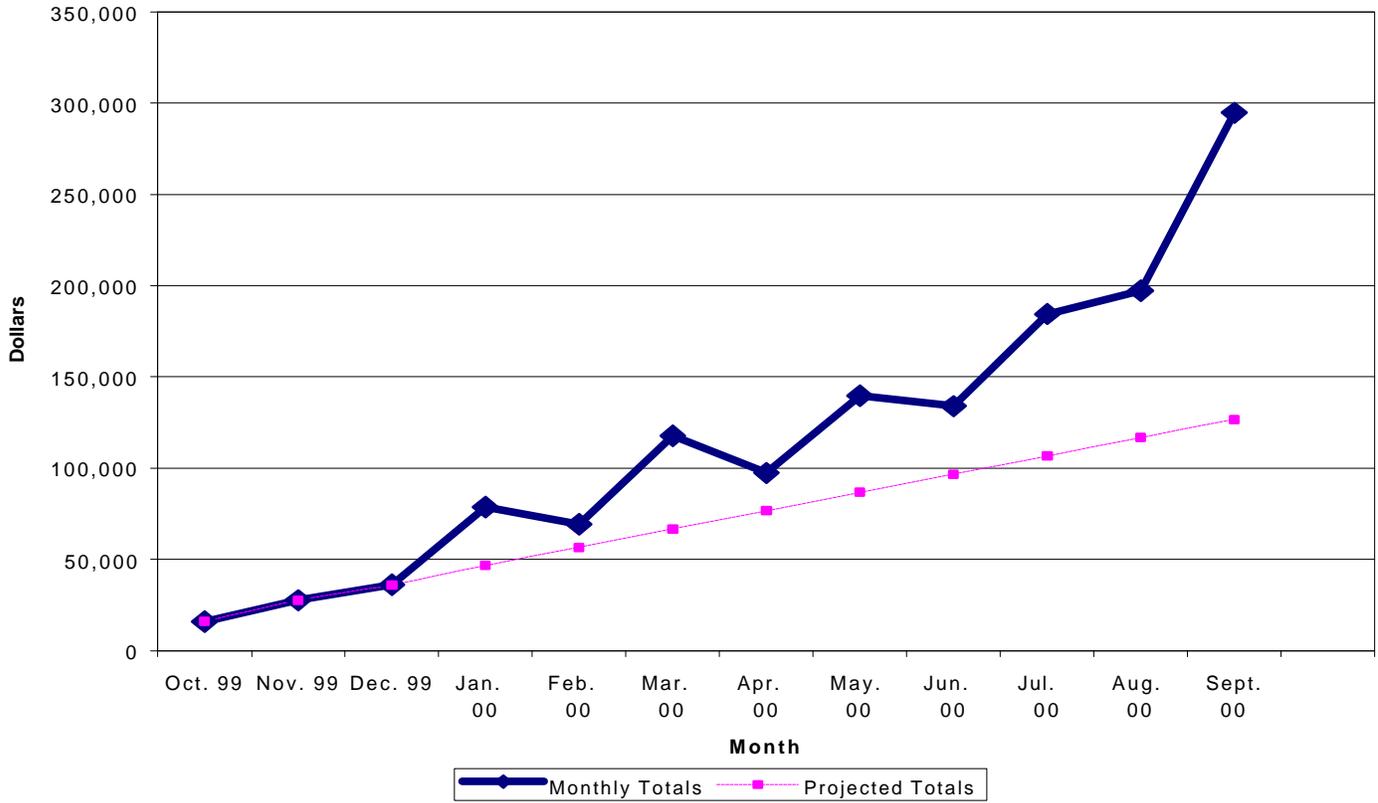
The FCC's travel voucher processing goal of ten working days begins with the receipt of a correct voucher with all proper backup documentation. Federal Travel Regulations allows 30 days. During FY2000, 1,746 travel vouchers were processed with an average processing time of 6.5 working days.

## PROMPT PAYMENT INTEREST FY 2000



Total prompt payment interest during FY 2000 is \$20,123.24. Included in this total is \$12,050.52 paid on travel from the central billing account in May for the period covering June 1999 through April 2000, due to a contract dispute between the General Services Administration (GSA) and the card processor. The FCC processed 6,421 invoices totaling \$59,420,521.00 during FY 2000 of which 1,453 invoices totaling \$5,285,128.00 were subject to prompt payment interest.

Rosie Monthly Totals & Projected Totals



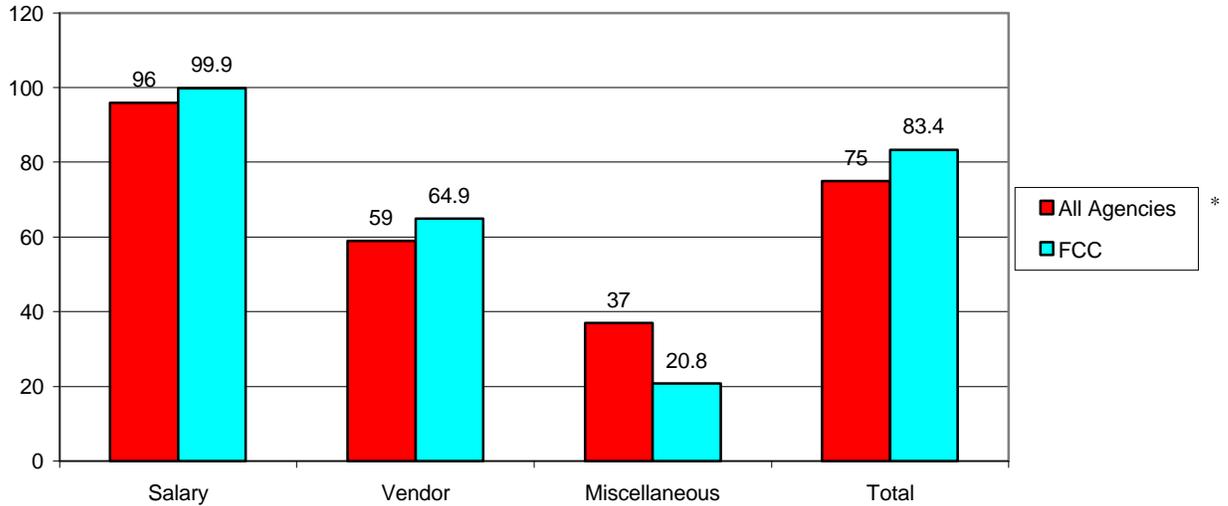
**ROSIE - Remittance Over Secure Internet (E-Commerce)**

ROSIE is a payment system that allows license applicants to pay their application fees electronically via credit card. The system has been built to Department of Treasury security specifications, employing the latest encryption technology and architecture to safeguard data. ROSIE is accessed via links from licensing systems that offer the electronic credit card payment option.

ROSIE was implemented in August 1999, processing 108 payments for \$6,648. Since then, ROSIE usage has steadily increased until by the end of FY 2000, it was processing 1,500 payments for \$200,000 in an average month. In fiscal year 2000, 12,732 payments for a total of \$1,392,550 were processed. Along the way, enhancements have been made to strengthen security and make ROSIE more customer-friendly.

FCC regards this first venture into electronic commerce as a great success and is endeavoring to expand the on-line payment option to include all payments made to the agency.

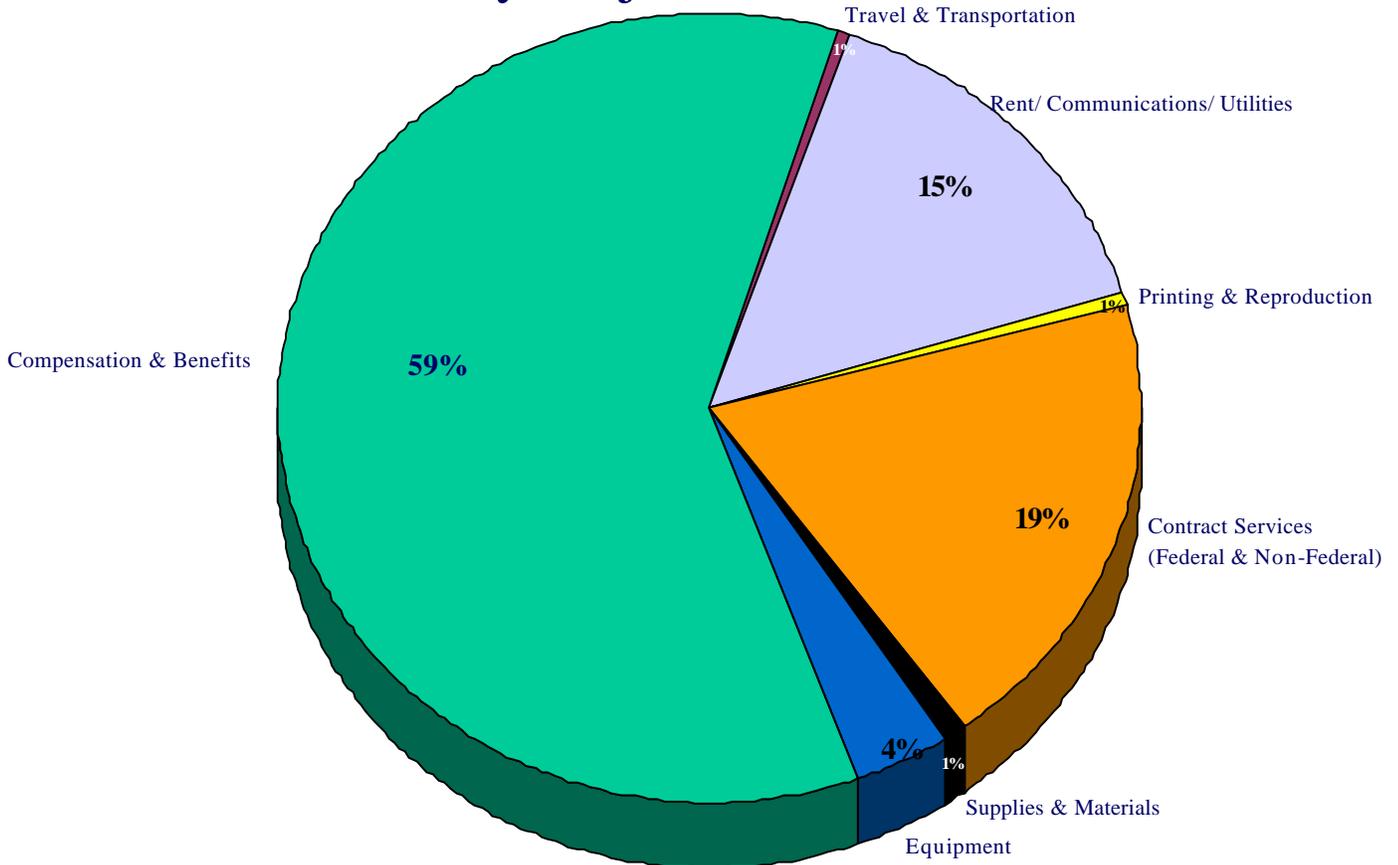
### % of Payments via EFT FY 2000



FCC has worked to increase its level of payments via EFT/direct deposit. Through various outreach programs, such as including letters to vendors with contract and purchase order mailings, offering e-mail notifications of EFT payments, and telephoning vendors, we have increased our percentage of vendor payments via EFT from 60% in FY 1999 to 78% during September of FY 2000. We also have an initiative in progress to increase the percentage of fee refunds via EFT. Currently, all refunds are paid by check and comprise approximately 94% of FCC's miscellaneous payments. We are endeavoring to convert these check payments to EFT by capturing bank information from the applicant's remittance. We hope to implement this capability during FY 2001.

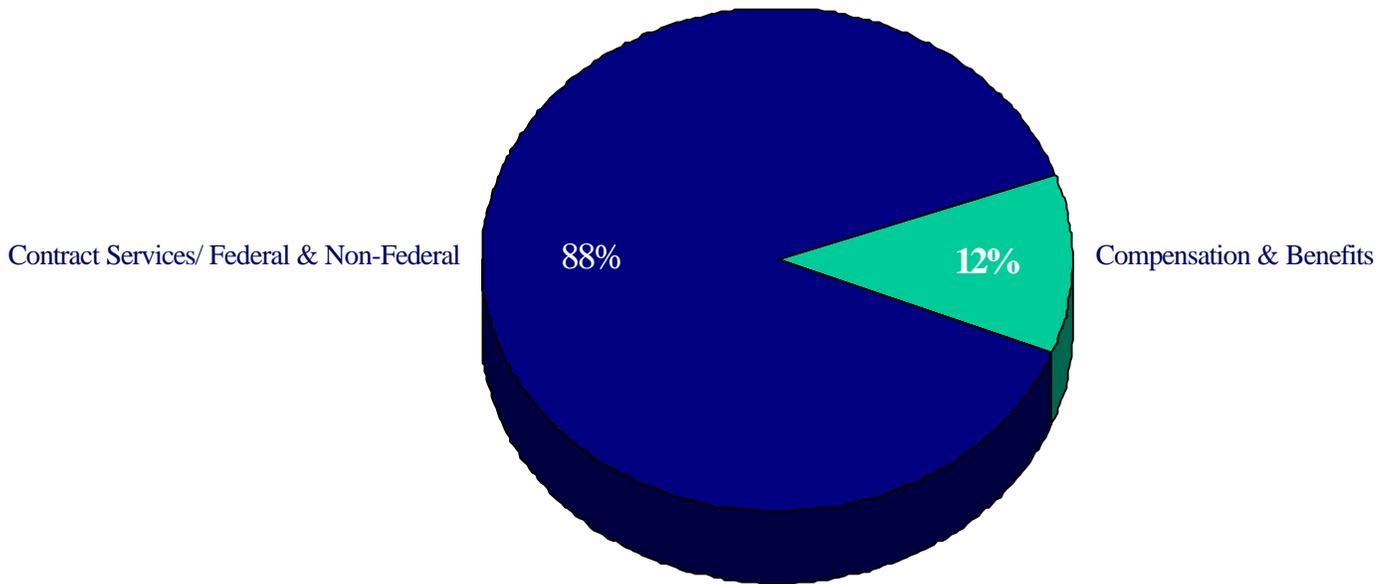
\* Data for "all agencies" was obtained from the Department of the Treasury Financial Management Services website for FY 2000 Government-wide Treasury-disbursed cumulative payment volume.

## FY 2000 Budget Authority Distribution by Object Class



This chart illustrates the distribution of obligations by budget category in FY 2000 (excluding the Universal Service Funds and the Auctions Loan Program administrative funds). These obligations are funded from multiple funding sources including annual appropriations, offsetting collections (regulatory fees, interagency and travel reimbursements), Auctions Loan Program reimbursements, and Y2K appropriated funds.

## FY 2000 Budget Authority Distribution by Object Class Credit Program Account (0300)



This chart illustrates the distribution of administrative cost by budgetary category required to provide for Auctions Loan Program activities in FY 2000.

**Federal Communications Commission**  
**Consolidated Balance Sheet**  
**As of September 30, 2000**  
(dollars in thousands)

**ASSETS**

**Entity Assets:**

Intragovernmental

Fund Balance with Treasury (Note 2)	\$ 1,903,494
Accounts Receivable (Note 5)	39
Total Intragovernmental	<u>1,903,533</u>

Cash and Other Monetary Assets (Note 3)	64
Accounts Receivable, net (Note 5)	20,704
Loans Receivable, net (Note 6)	9,592,520
Forfeited Property (Note 7)	61
Property, Plant, and Equipment, net (Note 8)	39,399
Total Entity Assets	<u>11,556,281</u>

**Non-Entity Assets:**

Intragovernmental

Fund Balance with Treasury (Note 2)	\$ 304,171
Investments (Note 4)	1,297,611
Total Intragovernmental	<u>1,601,782</u>

Cash and Other Monetary Assets (Note 3)	49,259
Investments (Note 4)	743,924
Accounts Receivable, net (Note 5)	482,218
Interest Receivable	897
Total Non-Entity Assets	<u>2,878,080</u>

Total Assets	<u>\$ 14,434,361</u>
--------------	----------------------

**LIABILITIES**

**Liabilities Covered by Budgetary Resources:**

Intragovernmental

Liability for Borrowings from Treasury (Note 9)	\$ 5,307,271
Other Accrued Liabilities (Note 12)	345,717
Total Intragovernmental	<u>5,652,988</u>

Accounts Payable (Note 10)	409,629
Other Debt (Note 11)	125,274
Other Accrued Liabilities (Note 12)	55,908
Total Liabilities Covered by Budgetary Resources	<u>6,243,799</u>

**Liabilities Not Covered by Budgetary Resources:**

Intragovernmental

Other Unfunded Liability (Note 12)	443
------------------------------------	-----

Payable to Providers (Note 13)	2,052,849
Accrued Unfunded Leave	12,548
Other Unfunded Liability (Note 12)	69,982
Total Liabilities not Covered by Budgetary Resources	<u>2,135,822</u>

Total Liabilities	<u>\$ 8,379,621</u>
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**NET POSITION**

Unexpended Appropriations (Note 15)	\$ 6,122,690
Cumulative Results of Operations	(67,950)
Total Net Position	<u>6,054,740</u>

Total Liabilities and Net Position	<u>\$ 14,434,361</u>
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The accompanying notes are an integral part of these statements

**Federal Communications Commission**  
**Consolidating Balance Sheet**  
**As of September 30, 2000**  
(dollars in thousands)

	FCC	USF	TOTAL
<b>ASSETS</b>			
<b>Entity Assets:</b>			
<u>Intragovernmental</u>			
Fund Balance with Treasury (Note 2)	\$ 1,903,494	\$ -	\$ 1,903,494
Accounts Receivable (Note 5)	39	-	39
Total Intragovernmental	1,903,533	-	1,903,533
Cash and Other Monetary Assets (Note 3)	64	-	64
Accounts Receivable, net (Note 5)	20,704	-	20,704
Loans Receivable, net (Note 6)	9,592,520	-	9,592,520
Forfeited Property (Note 7)	61	-	61
Property, Plant, and Equipment, net (Note 8)	39,399	-	39,399
Total Entity Assets	11,556,281	-	11,556,281
<b>Non-Entity Assets:</b>			
<u>Intragovernmental</u>			
Fund Balance with Treasury (Note 2)	\$ 304,171	\$ -	\$ 304,171
Investments (Note 4)	-	1,297,611	1,297,611
Total Intragovernmental	304,171	1,297,611	1,601,782
Cash and Other Monetary Assets (Note 3)	48,108	1,151	49,259
Investments (Note 4)	-	743,924	743,924
Accounts Receivable, net (Note 5)	76,868	405,350	482,218
Interest Receivable	858	39	897
Total Non-Entity Assets	430,005	2,448,075	2,878,080
Total Assets	\$ 11,986,286	\$ 2,448,075	\$ 14,434,361
<b>LIABILITIES</b>			
<b>Liabilities Covered by Budgetary Resources:</b>			
<u>Intragovernmental</u>			
Liability for Borrowings from Treasury (Note 9)	\$ 5,307,271	\$ -	\$ 5,307,271
Other Accrued Liabilities (Note 12)	345,717	-	345,717
Total Intragovernmental	5,652,988	-	5,652,988
Accounts Payable (Note 10)	14,403	395,226	409,629
Other Debt	125,274	-	125,274
Other Accrued Liabilities (Note 12)	55,908	-	55,908
Total Liabilities Covered by Budgetary Resources	5,848,573	395,226	6,243,799
<b>Liabilities not Covered by Budgetary Resources:</b>			
<u>Intragovernmental</u>			
Other Unfunded Liability (Note 12)	443	-	443
Payable to Providers (Note 13)	-	2,052,849	2,052,849
Accrued Unfunded Leave	12,548	-	12,548
Other Unfunded Liability (Note 12)	69,982	-	69,982
Total Liabilities not Covered by Budgetary Resources	82,973	2,052,849	2,135,822
Total Liabilities	5,931,546	2,448,075	8,379,621
<b>NET POSITION</b>			
Unexpended Appropriations (Note 15)	\$ 6,122,690	\$ -	\$ 6,122,690
Cumulative Results of Operations	(67,950)	-	(67,950)
Total Net Position	6,054,740	-	6,054,740
Total Liabilities and Net Position	\$ 11,986,286	\$ 2,448,075	\$ 14,434,361

**Federal Communications Commission**  
**Consolidated Statement of Net Cost**  
**For the Year Ended September 30, 2000**  
(dollars in thousands)

**PROGRAM COSTS:**  
**Authorization of Service**

Program Costs		
Intragovernmental	\$ 292,770	
With the Public	(664,112)	
Less: Earned Revenues	<u>(534,779)</u>	
Net Program Costs		<u>(906,121)</u>

**Policy and Rule Making**

Program Costs		
Intragovernmental	572,598	
With the Public	(1,298,869)	
Less: Earned Revenues	<u>(1,045,917)</u>	
Net Program Costs		<u>(1,772,188)</u>

**Enforcement**

Program Costs		
Intragovernmental	444,371	
With the Public	(1,008,003)	
Less: Earned Revenues	<u>(811,702)</u>	
Net Program Costs		<u>(1,375,334)</u>

**Public Information Service**

Program Costs		
Intragovernmental	91,348	
With the Public	(207,221)	
Less: Earned Revenues	<u>(166,867)</u>	
Net Program Costs		<u>(282,740)</u>

**Universal Service**

Program Costs		
Intragovernmental	-	
With the Public	39,608	
Less: Earned Revenues	<u>(39,608)</u>	
Net Program Costs		<u>-</u>

**Total Net Program Costs** \$ (4,336,383)

**UNASSIGNED COSTS:**

Imputed Costs	9,755	
Depreciation	11,256	
Bad Debt Expense	<u>51</u>	
<b>Total Unassigned Costs</b>		<u>21,062</u>

**Net Cost of Operations** \$ (4,315,321)

The accompanying notes are an integral part of these statements

**Federal Communications Commission**  
**Consolidating Statement of Net Cost**  
**For the Year Ended September 30, 2000**  
(dollars in thousands)

	FCC	USF	TOTAL
<b>PROGRAM COSTS:</b>			
<b>Authorization of Service</b>			
Program Costs			
Intragovernmental	\$ 292,770	\$ -	\$ 292,770
With the Public	(664,112)	-	(664,112)
Less: Earned Revenues	(534,779)	-	(534,779)
Net Program Costs	(906,121)	-	(906,121)
<b>Policy and Rule Making</b>			
Program Costs			
Intragovernmental	572,598	-	572,598
With the Public	(1,298,869)	-	(1,298,869)
Less: Earned Revenues	(1,045,917)	-	(1,045,917)
Net Program Costs	(1,772,188)	-	(1,772,188)
<b>Enforcement</b>			
Program Costs			
Intragovernmental	444,371	-	444,371
With the Public	(1,008,003)	-	(1,008,003)
Less: Earned Revenues	(811,702)	-	(811,702)
Net Program Costs	(1,375,334)	-	(1,375,334)
<b>Public Information Service</b>			
Program Costs			
Intragovernmental	91,348	-	91,348
With the Public	(207,221)	-	(207,221)
Less: Earned Revenues	(166,867)	-	(166,867)
Net Program Costs	(282,740)	-	(282,740)
<b>Universal Service</b>			
Program Costs			
Intragovernmental	-	-	-
With the Public	-	39,608	39,608
Less: Earned Revenues	-	(39,608)	(39,608)
Net Program Costs	-	-	-
<b>Total Net Program Costs</b>	<b>\$ (4,336,383)</b>	<b>\$ -</b>	<b>\$ (4,336,383)</b>
<b>UNASSIGNED COSTS:</b>			
Imputed Costs	9,755	-	9,755
Depreciation	11,256	-	11,256
Bad Debt Expense	51	-	51
<b>Total Unassigned Costs</b>	<b>21,062</b>	<b>-</b>	<b>21,062</b>
<b>Net Cost of Operations</b>	<b>\$ (4,315,321)</b>	<b>\$ -</b>	<b>\$ (4,315,321)</b>

**FEDERAL COMMUNICATIONS COMMISSION**  
**Consolidated Statement of Changes in Net Position**  
**For the Year Ended September 30, 2000**  
(dollars in thousands)

<b>Net Cost of Operations</b>		\$	(4,315,321)
<b>Financing Sources:</b>			
Appropriations Used	44,625		
Imputed Financing	9,755		
Transfers In	94		
Transfers Out	(28,141)		
Downward Re-estimate (Note 6)	(4,282,602)		
Loss (Note 11)	(125,424)		
Total Financing Sources			(4,381,693)
<b>Net Results of Operations</b>			(66,372)
Prior Period Adjustments (Note 17)			(1,760,291)
Cancelled Appropriations			(777)
Change in Cumulative Results of Operations			(1,827,440)
Increase in Unexpended Appropriations (Note 15)			6,093,786
<b>Change in Net Position</b>			4,266,346
Net Position - Beginning of Period			1,788,394
<b>Net Position - End of Period</b>		<b>\$</b>	<b>6,054,740</b>

The accompanying notes are an integral part of these statements

**FEDERAL COMMUNICATIONS COMMISSION**  
**Consolidating Statement of Changes in Net Position**  
**For the Year Ended September 30, 2000**  
(dollars in thousands)

	<u>FCC</u>	<u>USF</u>	<u>TOTAL</u>
<b>Net Cost of Operations</b>	\$ (4,315,321)	\$ -	\$ (4,315,321)
<b>Financing Sources:</b>			
Appropriations Used	44,625	-	44,625
Imputed Financing	9,755	-	9,755
Transfers In	94	-	94
Transfers Out	(28,141)	-	(28,141)
Downward Re-estimate (Note 6)	(4,282,602)	-	(4,282,602)
Loss (Note 11)	(125,424)	-	(125,424)
Total Financing Sources	<u>(4,381,693)</u>	<u>-</u>	<u>(4,381,693)</u>
<b>Net Results of Operations</b>	(66,372)	-	(66,372)
Prior Period Adjustments (Note 17)	(1,760,291)	-	(1,760,291)
Cancelled Appropriations	<u>(777)</u>	<u>-</u>	<u>(777)</u>
Change in Cumulative Results of Operations	(1,827,440)	-	(1,827,440)
Increase in Unexpended Appropriations	<u>6,093,786</u>	<u>-</u>	<u>6,093,786</u>
<b>Change in Net Position</b>	4,266,346	-	4,266,346
Net Position - Beginning of Period	<u>1,788,394</u>	<u>-</u>	<u>1,788,394</u>
<b>Net Position - End of Period</b>	<u>\$ 6,054,740</u>	<u>\$ -</u>	<u>\$ 6,054,740</u>

**Federal Communications Commission**  
**Consolidated Statement of Budgetary Resources**  
**For the Year Ended September 30, 2000**  
(dollars in thousands)

**Budgetary Resources:**

Budget Authority	\$ 2,125,225
Unobligated Balances - Beginning of Period	70,817
Spending Authority from Offsetting Collections	2,912,267
Adjustments	<u>(583,620)</u>
Total Budgetary Resources	<u><u>\$ 4,524,689</u></u>

**Status of Budgetary Resources:**

Obligations Incurred	\$ 2,665,943
Unobligated Balances - Available	1,822,928
Unobligated Balances - Not Available	<u>35,818</u>
Total Status of Budgetary Resources	<u><u>\$ 4,524,689</u></u>

**Outlays:**

Obligations Incurred	\$ 2,665,943
Less: Spending Authority from Offsetting Collections and Adjustments	(2,940,885)
Obligated Balance, net - Beginning of Period	56,665
Obligated Balance Transferred - net	-
Less: Obligated Balance, net - End of Period	<u>(45,148)</u>
Total Outlays	<u><u>\$ (263,425)</u></u>

The accompanying notes are an integral part of these statements

**Federal Communications Commission**  
**Consolidating Statement of Budgetary Resources**  
**As of September 30, 2000**  
(dollars in thousands)

	FCC	USF	TOTAL
<b>Budgetary Resources:</b>			
Budget Authority	\$ 2,125,225	\$ -	\$ 2,125,225
Unobligated Balances - Beginning of Period	70,817	-	70,817
Spending Authority from Offsetting Collections	2,912,267	-	2,912,267
Adjustments	(583,620)	-	(583,620)
	<u>\$ 4,524,689</u>	<u>\$ -</u>	<u>\$ 4,524,689</u>
Total Budgetary Resources			
<b>Status of Budgetary Resources:</b>			
Obligations Incurred	\$ 2,665,943	\$ -	\$ 2,665,943
Unobligated Balances - Available	1,822,928	-	1,822,928
Unobligated Balances - Not Available	35,818	-	35,818
	<u>\$ 4,524,689</u>	<u>\$ -</u>	<u>\$ 4,524,689</u>
Total Status of Budgetary Resources			
<b>Outlays:</b>			
Obligations Incurred	\$ 2,665,943	\$ -	\$ 2,665,943
Less: Spending Authority from Offsetting Collections and Adjustments	(2,940,885)	-	(2,940,885)
Obligated Balance, net - Beginning of Period	56,665	-	56,665
Obligated Balance Transferred - net	-	-	-
Less: Obligated Balance, net - End of Period	(45,148)	-	(45,148)
	<u>\$ (263,425)</u>	<u>\$ -</u>	<u>\$ (263,425)</u>
Total Outlays			

The Accompanying Notes are an integral part of these statements

**Federal Communications Commission**  
**Consolidated Statement of Financing**  
**For the Year Ended September 30, 2000**  
(dollars in thousands)

**Obligations and Nonbudgetary Resources**

Obligations Incurred	\$ 2,665,943
Less: Spending Authority for Offsetting Collections and Adjustments	(2,912,267)
Downward Adjustment for Prior Year Unpaid Obligations	(28,607)
Change in Receivables	1,794,483
Financing Imputed for Cost Subsidies	9,755
Transfers-out	(1,500)
Exchange Revenue Not in Entity's Budget	(281,515)
Total Obligations as Adjusted, and Nonbudgetary Resources	<u>\$ 1,246,292</u>

**Resources That Do Not Fund Net Cost Of Operations**

Change in Amount of Goods, Services, and Benefits Ordered But Not Yet Received or Provided	5,331
Change in Unfilled Customer Orders	(1)
Costs Capitalized on the Balance Sheet General Property, Plant and Equipment	(619)
Loans	(1,137)
Financing Sources That Fund Costs of Prior Period	(1,821,450)
Other	651,038
Total Resources That Do Not Fund Net Cost of Operations	<u>(1,166,838)</u>

**Costs That Do Not Require Resources**

Depreciation and Amortization Expense	11,284
Bad Debts	52
Changes in Other Accrued Liabilities	1,255
Loss on Future Revenues	(125,273)
Subsidy Re-estimate	(4,282,602)
Total Costs That Do Not Require Resources	<u>(4,395,284)</u>

**Financing Sources Yet to be Provided** 509

**Net Cost of Operations** \$ (4,315,321)

The accompanying notes are an integral part of these statements

**Federal Communications Commission**  
**Consolidating Statement of Financing**  
**September 30, 2000**  
(dollars in thousands)

	FCC	USF	TOTAL
<b>Obligations and Nonbudgetary Resources</b>			
Obligations Incurred	\$ 2,665,943	\$ -	\$ 2,665,943
Less: Spending Authority for Offsetting			
Collections and Adjustments	(2,912,267)	-	(2,912,267)
Downward Adj PY Unpaid Obligations	(28,607)	-	(28,607)
Change in Receivables	1,794,483	-	1,794,483
Financing Imputed for Cost Subsidies	9,755	-	9,755
Transfers-in/(out)	(1,500)	-	(1,500)
Exchange Revenue Not in Entity's Budget	(281,515)	-	(281,515)
Total Obligations as Adjusted, and Nonbudgetary Resources	\$ 1,246,292	\$ -	\$ 1,246,292
 <b>Resources That Do Not Fund Net Cost Of Operations</b>			
Change in Amount of Goods, Services, and Benefits			
Ordered But Not Yet Received or Provided	5,331	-	5,331
Change in Unfilled Customer Orders	(1)	-	(1)
Costs Capitalized on the Balance Sheet			
General Property, Plant and Equipment	(619)	-	(619)
Loans	(1,137)	-	(1,137)
Financing Sources that Fund Costs of Prior Period	(1,821,450)	-	(1,821,450)
Other	651,038	-	651,038
Total Resources That Do Not Fund Net Cost of Operations	(1,166,838)	-	(1,166,838)
 <b>Costs That Do Not Require Resources</b>			
Depreciation and Amortization Expense	11,284	-	11,284
Bad Debts	52	-	52
Changes in Other Accrued Liabilities	1,255	-	1,255
Loss on Future Revenues	(125,273)	-	(125,273)
Subsidy Re-estimate	(4,282,602)	-	(4,282,602)
Total Costs That Do Not Require Resources	(4,395,284)	-	(4,395,284)
 <b>Financing Sources Yet to be Provided</b>	 509	 -	 509
 <b>Net Cost of Operations</b>	 \$ (4,315,321)	 \$ -	 \$ (4,315,321)

The Accompanying Notes are an integral part of these statements

**Federal Communications Commission**  
**Consolidated Statement of Custodial Activity**  
**For the Year Ended September 30, 2000**  
(dollars in thousands)

<b>Beginning Custodial Balances</b>	
Spectrum Auctions	\$ 218,714
Upfront Deposits	23,781
Payable to Providers	1,545,412
Total Beginning Custodial Balance	1,787,907
 <b>FY2000 Revenue Activity:</b>	
Sources of Cash Collections:	
Spectrum Auctions	750,590
Upfront Deposits	439,122
Contributions & Investment Interest	4,539,259
Total Cash Collections	5,728,971
 <b>Accrual Adjustments</b>	 64,437
 <b>Total Custodial Funds</b>	 7,581,315
 <b>Disposition of Collections:</b>	
Transferred to Others:	
Recipient Spectrum Deposit	(24,476)
Recipient Treasury General Fund	(536,485)
Recipient Telecommunication Development Fund	(2,531)
Recipient USF Providers	(4,029,528)
Total Transfers	(4,593,020)
 <b>Amounts Yet to be Transferred</b>	 2,988,295
 <b>Refunds and Other Payments</b>	 (520,966)
 <b>Retained by the Reporting Entity</b>	 (2,467,329)
 <b>Net Custodial Revenue Activity</b>	 \$ -

The accompanying notes are an integral part of these statements

**Federal Communications Commission**  
**Consolidating Statement of Custodial Activity**  
**As of September 30, 2000**  
(dollars in thousands)

	FCC	USF	TOTAL
<b>Beginning Custodial Balances</b>			
Spectrum Auctions	\$ 218,714	\$ -	\$ 218,714
Upfront Deposits	23,781	-	23,781
Payable to Providers	-	1,545,412	1,545,412
Total Beginning Custodial Balance	<u>242,495</u>	<u>1,545,412</u>	<u>1,787,907</u>
<b>FY2000 Revenue Activity:</b>			
Sources of Cash Collections:			
Spectrum Auctions	750,590	-	750,590
Upfront Deposits	439,122	-	439,122
Contributions & Investment Interest	-	4,539,259	4,539,259
Total Cash Collections	<u>1,189,712</u>	<u>4,539,259</u>	<u>5,728,971</u>
<b>Accrual Adjustments</b>	64,437	-	64,437
<b>Total Custodial Funds</b>	1,496,644	6,084,671	7,581,315
<b>Disposition of Collections:</b>			
Transferred to Others (by Recipient):			
Recipient Spectrum Deposit	(24,476)	-	(24,476.00)
Recipient Treasury General Fund	(536,485)	-	(536,485.00)
Recipient Telecommunication Development Fund	(2,531)	-	(2,531)
Recipient USF Providers	-	(4,029,528)	(4,029,528)
Total Transfers	<u>(563,492)</u>	<u>(4,029,528)</u>	<u>(4,593,020)</u>
<b>Amounts Yet to be Transferred</b>	933,152	2,055,143	2,988,295
<b>Refunds and Other Payments</b>	(520,579)	(387)	(520,966)
<b>Retained by the Reporting Entity</b>	<u>(412,573)</u>	<u>(2,054,756)</u>	<u>(2,467,329)</u>
<b>Net Custodial Revenue Activity</b>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

The Accompanying Notes are an integral part of these statements

**FEDERAL COMMUNICATIONS COMMISSION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**September 30, 2000**

(dollars in thousands unless otherwise stated)

**Note 1 - Summary of Significant Accounting Policies:**

**Reporting Entity**

The Federal Communications Commission (“FCC” or “Commission”) is an independent United States government agency, directly responsible for reporting to Congress. The FCC was established by the Communications Act of 1934, as amended, and is charged with regulating interstate and international communications by radio, television, wire, satellite and cable. The FCC's jurisdiction covers the 50 states, the District of Columbia, and the U.S. possessions.

The FCC is directed by five Commissioners appointed by the President of the United States and confirmed by the Senate for five-year terms, except when filling an unexpired term. The President designates one of the Commissioners to serve as Chairperson. Only three Commissioners may be members of the same political party. None of them can have a financial interest in any Commission-related business.

The FCC's operations are divided among the following bureaus and offices: International, Cable Services, Engineering and Technology, Mass Media, Common Carrier, Wireless Telecommunications, Consumer Information, and Enforcement. In addition, a significant program of the FCC, as designated in the U.S. Budget is the Universal Service Fund (USF). USF consists of five elements, four of which are the universal service support mechanisms and the fifth being the Telecommunications Relay Service (TRS) Fund. The universal service support mechanisms were established pursuant to Section 254 of the Communications Act of 1934, as amended. The Universal Service Administrative Company (USAC) was appointed by the FCC to administer the four universal service support mechanisms: high cost areas, low income consumers, schools and libraries, and rural health care providers. It also submits projections of demand and administrative expenses for each of these mechanisms and quarterly universal service contribution data to the FCC. The National Exchange Carrier Association (NECA) administers the TRS Fund.

**Basis of Accounting**

The consolidated financial statements have been prepared from the accounting records of FCC in conformity with generally accepted accounting principles (GAAP), and standards specified by the Office of Management and Budget (OMB) in OMB Bulletin No. 97-01, *Form and Content of Federal Agency's Financial Statements*, as amended. GAAP for Federal entities are the standards prescribed by the Federal Accounting Standards Advisory Board (FASAB), which was designated the official accounting standards-setting body for the Federal government by the American Institute of Certified Public Accountants. The consolidated financial statements are different from the financial reports, also prepared by FCC pursuant to OMB directives, that are used to monitor and control FCC's use of budgetary resources.

**FEDERAL COMMUNICATIONS COMMISSION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**September 30, 2000**

(dollars in thousands unless otherwise stated)

**Note 1 - Summary of Significant Accounting Policies (continued):**

**Basis of Presentation**

The accompanying consolidated financial statements have been prepared to report the financial position and results of operations of the FCC for the fiscal year ended September 30, 2000. The consolidated financial statements have been prepared from the books and records of the FCC in accordance with OMB Bulletin No. 97-01, as amended, and generally accepted accounting principles of the United States.

The preparation of financial statements, in accordance with accounting principles generally accepted in the United States, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from those estimates.

The FCC is not a designated Agency in the Chief Financial Officer's Act of 1990 (CFO Act), as amended, and therefore, has not been subject to the financial statement preparation requirements of the CFO Act in the past. Financial statements were prepared for the first time in fiscal year 1999 to assist the Department of the Treasury's Financial Management Service (FMS), in meeting its government-wide financial statement preparation effort. For fiscal year 1999 reporting purposes, only the consolidating balance sheet was presented and audited. For fiscal year 2000, all required statements listed in OMB Bulletin No. 97-01, as amended, were prepared and subjected to audit. The financial statements include all funds and programs for which the FCC is responsible. All significant intra-entity balances and transactions have been eliminated in consolidation. A distinction has been made in the financial statements between asset and liability balances arising from transactions with other Federal government agencies and all other asset and liability balances. These balances are specifically identified under the heading Intragovernmental.

**Assets**

Assets are tangible or intangible items owned by FCC that would have probable economic benefits that can be obtained or controlled by FCC. The consolidated balance sheet presents assets in one of two categories: entity or non-entity. Entity assets are those assets which the reporting entity holds and has the authority to use in its operations. Non-entity assets are assets the entity holds but does not have the authority to use in its operations.

**Funds with the U.S. Treasury**

The FCC maintains four types of accounts with the U.S. Treasury: appropriated, revolving, deposit, and suspense. The appropriated and revolving accounts may be used by the FCC to finance expenditures depending on budgetary availability. The deposit accounts are used to hold funds received through spectrum auctions, international telecommunications settlements, or

**FEDERAL COMMUNICATIONS COMMISSION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
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**Note 1 - Summary of Significant Accounting Policies (continued):**

**Funds with the U.S. Treasury (continued)**

regulatory fee monies until they can be distributed to the proper account. The suspense account is used to clear unidentified collections and reimbursements. There are no USF balances maintained by the U.S. Treasury.

**Cash and Other Monetary Assets**

Entity – Entity cash represents USF cash on deposit at several commercial banks. It is cash that can be used for any authorized program purpose. The commercial accounts are in the form of money market mutual funds. USAC, the administrator of the USF, considers all highly liquid securities, purchased with an original maturity of three months or less, to be cash equivalents. Interest proceeds are reinvested and remain available for USF use.

Non-Entity – Non-Entity cash consists of cash deposits held at Mellon bank. FCC has custodial responsibility for these funds. These funds represent third party advances made pursuant to the FCC Spectrum Auction activities. Upon conclusion of individual auctions, funds on deposit are offset against amounts due from successful bidders or returned to unsuccessful bidders. The funds are held in an interest bearing account, for subsequent transfer to the Telecommunications Development Account (TDA), during and for a 45 day period after the close of a given auction.

The Telecommunications Act of 1996 established the Telecommunication Development Fund (TDF), the purpose of which is to: (1) promote access to capital for small businesses in order to enhance competition in the telecommunications industry; (2) stimulate new technology development, and promote employment and training; and (3) support universal service and promote delivery of telecommunications to underserved rural and urban areas. Pursuant to 47 U.S.C. Section 309(j)(8), the FCC is authorized to transfer interest accrued on deposits from the TDA to the TDF.

Cash on deposit typically exceeds federally insured limits. The Federal Reserve requires the bank to collateralize all funds on deposit from FCC at 110 percent.

**Accounts Receivable**

Accounts receivable are recorded net of any related allowance for doubtful accounts. The allowance is determined based on analysis of individual accounts. For specific entity accounts receivables in FY 2000, the allowance was established using predetermined percentages against the respective year the receivable was established, ranging from 0 percent to 100 percent.

**FEDERAL COMMUNICATIONS COMMISSION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
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(dollars in thousands unless otherwise stated)

**Note 1 - Summary of Significant Accounting Policies (continued):**

**Loans**

Reporting requirements for direct loan obligations made after fiscal year 1991, are governed by the Federal Credit Reform Act (FCRA) of 1990, as amended. The FCRA requires that the present value of the subsidy costs (present value of the estimated cash outflows over the life of the loans minus the present value of the estimated cash inflows, discounted at the interest rate of marketable Treasury securities with a similar maturity term) associated with direct loans be recognized as a cost in the year that the loan is obligated. Direct Loans are reported net of an allowance for subsidy at present value.

**Investments**

Investments are reported net of any unamortized premium or discount. The USF's investments include intragovernmental securities and repurchase agreements. All commercial investments are considered to be short term with maturity dates that do not exceed one year.

**Property, Plant and Equipment**

The basis for recording purchased general Property, Plant and Equipment (PP&E) is full cost, including all costs incurred to bring the PP&E to and from a location suitable for its intended use. The cost of PP&E acquired through donation is the estimated fair value when acquired. The cost of PP&E transferred from other Federal entities is the net book value of the transferring entity.

All PP&E with an initial acquisition cost of \$25,000 or more and an estimated useful life of two years or greater are capitalized. Bulk purchases of similar items, which individually are not worth \$25,000, but collectively are greater than \$250,000 are also capitalized using the same equipment categories and lives as capital acquisitions. PP&E are depreciated on a straight-line basis over the estimated useful life of the item. The useful lives used are: twenty years for buildings, seventeen years for patents, seven years for equipment, five years for computers and peripherals, and three years for software. Land and land rights, including permanent improvements, are not depreciated. Also, software in process is not depreciated. Normal maintenance and repair costs are expensed as incurred.

The FCC's authority relative to seized and forfeited property is located in 47 U.S.C., Section 510. Seized property consists of real property seized in illegal telecommunication operations. The property is considered prohibited and held pending an outcome of court proceedings. Seized assets that are monetary instruments shall be recognized as an asset when seized and a corresponding liability shall be reported equal to the seized asset value. FCC has no seized assets that are monetary instruments. Forfeited property consists of seized property legally turned over to the FCC and disposed of through the General Services Administration's (GSA)

**FEDERAL COMMUNICATIONS COMMISSION  
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**September 30, 2000**

(dollars in thousands unless otherwise stated)

**Note 1 - Summary of Significant Accounting Policies (continued):**

**Property, Plant and Equipment (continued)**

surplus process or destroyed. The values assigned to the seized and forfeited property are determined by FCC engineers and are based on current market values for comparable property.

**Accounts Payable and Accrued Liabilities**

Accounts payable and accrued liabilities represent a probable future outflow or other sacrifice of resources as a result of past transactions or events. FCC liabilities cannot be liquidated without legislation that provides resources to do so. Since the FCC is a component of the U.S. Government, a sovereign entity, payments of all liabilities other than contracts can be abrogated by the sovereign entity.

Liabilities Covered by Budgetary Resources – Represent liabilities funded by available budgetary resources including: (1) new budget authority, (2) spending authority from offsetting collections, (3) recoveries of unexpired budget authority, (4) unobligated balances of budgetary resources at the beginning of the year, and (5) permanent indefinite appropriations or borrowing authority, as of the Consolidated Balance Sheet date. All liabilities covered by budgetary resources are classified as current and are expected to be paid within one year following the reporting date.

Liabilities Not Covered by Budgetary Resources – Exist when funding has not yet been made available through Congressional appropriations or current earnings. FCC recognizes such liabilities for employee annual leave earned but not taken, and amounts billed by the Department of Labor for Federal Employee's Compensation Act (disability) payments.

**Liability for Borrowings to Treasury**

This account represents amounts due to the Bureau of Public Debt, U.S. Treasury, to support the Spectrum Auction Loans Program. Borrowings are determined based on the FCC's subsidy estimate and reestimate in accordance with the FCRA of 1990, as amended, and guidance issued by OMB.

**Payable to Providers**

This account contains amounts awaiting approval for payment to USF providers (Schools and Libraries, Rural Healthcare, High Cost and Low Income) and TRS providers that were not disbursed as of September 30, 2000.

**FEDERAL COMMUNICATIONS COMMISSION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**September 30, 2000**

(dollars in thousands unless otherwise stated)

**Note 1 - Summary of Significant Accounting Policies (continued):**

**Retirement Plans and Other Benefits**

Federal Employee benefits consist of the actuarial portions of future benefits earned by Federal employees, but not yet due and payable. These costs include pensions, other retirement benefits, and other post-employment benefits. These benefits are normally administered by OPM and not by FCC. Since FCC does not administer the benefit plans, FCC does not recognize any liability on the Consolidated Balance Sheet for pensions, other retirement benefits, and other post-employment benefits. FCC does, however, recognize the imputed costs and imputed financing related to these benefits in the Statement of Net Cost and the Statement of Changes in Net Position, respectively.

Pensions provide benefits upon retirement and may also provide benefits for death, disability, or other termination of employment before retirement. Pension plans may also include benefits to survivors and dependents, and they may contain early retirement or other special features. Most FCC employees participate in the Civil Service Retirement System (CSRS) or the Federal Employee Retirement System (FERS). Under CSRS, FCC makes matching contributions equal to seven percent of basic pay. For FERS employees, FCC contributes the employer's matching share for Social Security and contributes an amount equal to one percent of employee pay to a savings plan and matches up to an additional four percent of pay. Most employees hired after December 31, 1983, are covered by FERS. The Office of Personnel Management reports on CSRS and FERS assets, accumulated plan benefits, unfunded liabilities, if any, applicable to Federal employees.

The actuarial liability for future workers' compensation benefits includes the expected liability for death, disability, medical and miscellaneous costs for approval compensation cases. The liability is determined using a method that utilizes historical benefit payment patterns related to a specific incurred period to predict the ultimate payment related to that period. No actuarial liability is determined by the Department of Labor (DOL) for the FCC, due to the immateriality to the Federal government as a whole.

**Leave**

Annual leave is accrued as earned, and the accrual is reduced as leave is taken. Each year, the balance in the accrued annual leave account is adjusted to reflect leave balances and current pay rates. Annual leave is reflected as a liability that is not covered by current budgetary resources. Sick leave and other types of non-vested leave are expensed as taken.

**FEDERAL COMMUNICATIONS COMMISSION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**September 30, 2000**

(dollars in thousands unless otherwise stated)

**Note 1 - Summary of Significant Accounting Policies (continued):**

**Revenues and Other Financing Sources**

Regulatory Fee Collections - The Omnibus Budget Reconciliation Act of 1993 directed the FCC to assess and collect regulatory fees to recover the costs incurred in carrying out certain provisions of the Agency's mission. Regulatory fees are intended to offset costs associated with the FCC enforcement, policy and rulemaking, international, and user information activities. Since 1993, Congress has annually reviewed the regulatory fee collection requirements of the Commission and established the total fee levels to be collected. Fees collected up to the level established by Congress are applied against the FCC's annual appropriation via a negative warrant processed at the close of each fiscal year. Only once, in fiscal year 1998, have fee attainments been less than the established level. In fiscal year 2000, regulatory fee collections exceeded the established level of \$185,754 by \$1,500.

Application Fees - Congress authorized the FCC (Section 8 47 U.S.C.) to impose and collect application processing fees and directed the FCC to prescribe charges for certain types of application processing or authorization services it provides to communications entities over which the FCC has jurisdiction. Application fees are deposited in the U.S. Treasury and are not available for the FCC to use.

Annual Appropriations - The FCC receives an annual salaries and expense appropriation from Congress. These funds are used to fund operations during the course of the fiscal year and are repaid to the U.S. Treasury once regulatory fees have been collected. The annual appropriation for fiscal year 2000 was \$209,909; however, FCC repaid \$185,754 to the U.S. Treasury in the form of a negative warrant. Therefore, the resulting net appropriation retained was \$24,155.

Subsidy Estimates and Reestimates - The FCC receives permanent-indefinite authority in accordance with the FCRA of 1990, as amended, to fund its subsidy estimates and reestimates, unless otherwise prescribed by OMB. This authority funds repayment to the U.S. Treasury for the portion of Spectrum Auction loans that will not be recovered from the borrower.

Offsetting Collections - One of FCC's primary functions is the management of the Auction Spectrum Program on behalf of the U.S. Government. Proceeds from the auctions are initially remitted to the FCC and later transferred to the U.S. Treasury, net of anticipated auction related costs. Under 47 U.S.C. Section 309, a portion of the Spectrum auction proceeds may be retained by the FCC to offset the cost of performing the auction function. Collections used to offset the cost of performing the auctions totaled \$45,407 for FY 2000.

Reimbursable Work Agreements - The FCC recognizes reimbursable work agreement revenue when earned, i.e. goods have been delivered or services rendered. As of September 30, 2000, FCC has agreements with other agencies totaling approximately \$1,000.

**FEDERAL COMMUNICATIONS COMMISSION**  
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**Note 1 - Summary of Significant Accounting Policies (continued):**

**Revenues and Other Financing Sources (continued)**

Exchange and Non-exchange Revenue - Exchange revenue is the amount of money earned for goods and services provided to other agencies and the public. For example, Spectrum Auction sales and reimbursable agreements are considered exchange revenue to the Federal government. Non-exchange revenue is recorded for transactions where revenue is earned at no substantial cost to the provider. For example, collections from fines and forfeitures are considered non-exchange revenue.

Based on interpretation of SFFAS No. 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*, the collections and disposition of monies of the Universal Service Fund have been reported as non-exchange revenue on the Statement of Custodial Activity. In addition, the portion of USF's expenses related to managing and overseeing the Universal Service Fund are reported as operating expenses on the FCC's Consolidated Statement of Net Cost. See Note 18 for additional details.

**Transactions with Related Parties**

In the course of its operations, FCC has relationships and financial transactions with numerous Federal agencies. The more prominent of those relationships are with the U.S. Department of Treasury and the Office of Management and Budget. FCC also has relationships with agencies such as the General Services Administration, the Department of Labor, the Office of Personnel and Management, and the Department of Agriculture, National Finance Center, among others.

In addition to its relationships and financial transactions with Federal agencies, the FCC has a direct relationship with several organizations that were established to assist the FCC in carrying out its mission. Such organizations include: the Universal Service Administrative Company, which administers the four universal service support mechanisms: high cost areas, low income consumers, schools and libraries, and rural health care providers. The National Exchange Carriers Association (NECA) administers the TRS Fund and the North American Numbering Plan Billing and Collection Agent. The purpose of the TRS Fund is to compensate TRS providers for the reasonable costs of providing interstate telephone transmission services that enable persons with hearing or speech disabilities to use wireline or wireless telecommunications services. The North American Numbering Plan Administrator (NANPA) administers the numbering resources to support the industry's efforts to accommodate current and future numbering needs. The Local Numbering Portability Administration (LNPA) works with carriers to update data tables for required number portability.

**FEDERAL COMMUNICATIONS COMMISSION  
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**Note 1 - Summary of Significant Accounting Policies (continued):**

**Net Position**

Net position account balances consist of the following components:

Unexpended Appropriations – Represents amounts of spending authority that are unobligated and available to the FCC, or obligated but not expended. Unexpended appropriations can also result from downward reestimates of mandatory loan programs.

Cumulative Results of Operations – Represents the FCC’s net results of operations since inception, including (1) the cost of property and equipment acquired that has been financed by appropriations, less accumulated depreciation, and (2) the amount of appropriated funding that will be needed in future periods to liquidate liabilities incurred through the current fiscal year. Funding for these items is generally received in the year that amounts become due and payable.

**Note 2 - Fund Balances with Treasury:**

	<u>Entity</u>	<u>Non-Entity</u>	<u>Total</u>
General Funds	\$1,893,358	\$ -	\$1,893,358
Revolving Funds	10,136	-	10,136
Deposit Funds	<u>-</u>	<u>304,171</u>	<u>304,171</u>
Total Fund Balance	<u>\$1,903,494</u>	<u>\$ 304,171</u>	<u>\$2,207,665</u>

General Funds - These funds consist of salaries and expense appropriation accounts used to fund agency operations and capital expenditures, no year accounts used to carryover spectrum auction and regulatory fee funds not obligated in the year received, and the credit reform program account.

Revolving Funds – The financing account is considered to be a revolving fund by the U.S. Treasury. This is the only revolving fund maintained by FCC. This fund records cash flows associated with the FCC’s Auction Spectrum Loan program.

Deposit Funds - These funds are maintained to account for receipts awaiting proper classification or receipts being held in escrow until proper distribution can be made. The three deposit accounts used by FCC hold spectrum auction receipts, international telecommunications settlements, and regulatory fee monies. Deposit funds are not available for use by the FCC unless they are properly identified or reclassified as FCC funds, otherwise, these funds will be returned to the depositor or transferred to the U.S. Treasury.

**FEDERAL COMMUNICATIONS COMMISSION  
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(dollars in thousands unless otherwise stated)

**Note 3 – Cash and Other Monetary Assets:**

	<u>Entity Assets</u>	<u>Non-Entity Assets</u>	<u>Total</u>
Imprest Fund	\$ 64	\$ -	\$ 64
Money Market Funds		1,151	1,151
Cash on deposit with commercial banks	<u>-</u>	<u>48,108</u>	<u>48,108</u>
Total Cash	<u>\$ 64</u>	<u>\$ 49,259</u>	<u>\$ 49,323</u>

Non-entity cash on deposit with commercial banks represents amounts deposited by bidders as upfront money for auctions and related interest. None of the money held on deposit is available to the FCC for use in its operations. Upon completion of the Spectrum auction process, deposits from unsuccessful bidders will be returned, while successful bidder deposits will be transferred to an FCC deposit symbol at the U.S. Treasury. Interest earned is transferred to the Telecommunication Development Fund (TDF).

Money Market Funds represent payments received from USF contributors that have not yet been distributed to the program recipients. All money held in commercial accounts by USF is deposited in a money market type fund earning interest between 6.1 and 6.5 percent.

**Note 4 – Investments:**

	<u>Cost</u>	<u>Amortization Method</u>	<u>Unamortized (Premium) Discount</u>	<u>Investments, Net</u>
Intragovernmental				
Marketable Securities	\$ 1,297,611	SL	\$ -	\$ 1,297,611
Other Securities:				
Repurchase Agreements	716,360	N/A	-	716,360
TRS (Other)	18,588	N/A	-	18,588
Interest Receivable	<u>8,976</u>		N/A	<u>-</u> <u>8,976</u>
Total Other Securities	743,924			743,924
Total Investments	<u>\$ 2,041,535</u>		<u>\$ -</u>	<u>\$ 2,041,535</u>

**FEDERAL COMMUNICATIONS COMMISSION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**September 30, 2000**

(dollars in thousands unless otherwise stated)

**Note 4 – Investments (continued):**

Investment balances represent funds that have been invested by USF in Federal and Commercial securities and repurchase agreements. Marketable Federal securities are securities that can be bought and sold on the open market. Repurchased agreements are collateralized by 110 percent by government securities. All commercial investments are considered to be short term with maturity dates greater than three months but not to exceed one year.

All losses associated with USF investments are considered temporary, therefore, net investments is the same as market value.

**Note 5 - Accounts Receivable, Net:**

The following summarizes accounts receivable as of September 30, 2000:

	<u>Entity</u>	<u>Non-Entity</u>	<u>Total</u>
Intragovernmental:			
Gross Accounts Receivable	\$ 67	\$ -	\$ 67
Allowance for Doubtful Accounts	( 28)	( -)	( 28)
Net Accounts Receivable	<u>\$ 39</u>	<u>\$ -</u>	<u>\$ 39</u>
With the Public:			
Gross Accounts Receivable	\$ 20,852	\$ 528,936	\$ 549,788
Allowance for Doubtful Accounts	<u>(148)</u>	<u>(46,718)</u>	<u>(46,866)</u>
Net Accounts Receivable	<u>\$ 20,704</u>	<u>\$ 482,218</u>	<u>\$ 502,922</u>

Included in the entity receivable balance is \$20.7 million specific to 47 U.S.C., Section 9 regulatory fees and the related late penalties due but not paid as of September 30, 2000. Gross non-entity receivables with the public are largely composed of the \$429.7 million due from USF contributors. The allowance of \$29.5 million is related to the USF contributors' receivable balance and was determined at the individual account level based upon a detail analysis of aged receivables. TRS receivables of \$5.1 million are also included in the non-entity receivable balances.

The FCC non-entity receivables include an amount of \$63.6 million for the Broadband Personal Communications Services licenses. The Pioneer licensees were permitted to pay for their licenses in installment payments over a five-year period. A subsequent agreement was reached by OMB, the Congressional Budget Office (CBO), the U.S. Department of Treasury, and the FCC that installment financed purchases of Spectrum Licenses should fall under FCRA requirements. In fiscal year 1999, this agreement was applied retroactively to earlier installment

**FEDERAL COMMUNICATIONS COMMISSION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**September 30, 2000**

(dollars in thousands unless otherwise stated)

**Note 5 - Accounts Receivable, Net (continued):**

financed licenses with the exception of Pioneer. A decision was made by FCC and OMB not to bring the Pioneer installments under FCRA of 1990, as amended because the installment payments for Pioneer will be completed in fiscal year 2001. In addition to the Pioneer receivables, the FCC has \$23 million in receivables related to fines and forfeitures.

**Note 6 - Direct Loans, Non-Federal Borrowers:**

Under Section 309(j)(3) of the Communications Act of 1934, as amended, Congress directed the FCC to implement a competitive bidding (auctions) system for licensing the spectrum, in order to expand economic opportunity, promote competition, and facilitate the development and delivery of new and improved telecommunications services to the public. Section 309(j)(4) gave the Commission certain instructions for implementing the regulations for this system, including a directive to ensure that small businesses, rural telephone companies, and women and minority-owned businesses were provided with an opportunity to participate in the provision of spectrum-based services. By statute, the FCC can use various means to facilitate expanded participation, including alternative payment schedules, tax certificates, bidding preferences, and other procedures.

To address the mandate, the FCC provided installment financing in its Spectrum Auction events, including the C Block Broadband Personal Communications Services' (PCS), F Block PCS, Narrowband PCS, Interactive Video and Data Service (IVDS), Multipoint Distribution Service (MDS), and 900MHz Specialized Mobile Radio (SMR). Under the installment financing program, winning bidders were generally given five or ten-year periods to repay their net winning bid amount (less the down payment amount), with up to five-year interest-only initial payment periods. Interest rates varied by the type of borrower. Retention of licenses granted at auction was strictly conditioned on making full and timely payment of amounts as they become due.

FCC's first auction was conducted in 1994, and starting in 1995, installment payment mechanisms were used to finance portions of some of the winning bid amounts. In 1996, OMB, CBO, U.S. Department of Treasury and FCC concluded that going forward installment financed arrangements would be treated as direct loans and reported in accordance with FCRA. The FCC complied with this arrangement. After the FCC completed the fiscal year 1998 subsidy reestimate, it began a comprehensive review of its loan portfolio data. In fiscal year 1999, FCC agreed with OMB to reclassify earlier installment arrangements and bring all such arrangements under FCRA with the exception of Pioneer as discussed in Note 5. As of fiscal year 2000, the FCC's installment loan portfolio is tracked under nine cohorts. The loans receivable balance and value of the assets related to the direct loans are not the same as the proceeds FCC would expect to receive from selling their loans.

**FEDERAL COMMUNICATIONS COMMISSION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

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(dollars in thousands unless otherwise stated)

**Note 6 - Direct Loans, Non-Federal Borrowers (continued):**

In accordance with Statement Federal Financial Accounting Standards (SFFAS) No. 2, *Accounting for Direct Loans and Loan Guarantees*, Federal agencies are required to reestimate the subsidy cost allowance annually as of the date of the financial statements. Any increase or decrease in the subsidy cost allowance resulting from the reestimates is recognized as a change in the subsidy expense.

For FY 2000, the FCC is reporting a decrease in the subsidy cost allowance of approximately \$4.3 billion. This decrease is a result of a downward reestimate. This downward reestimate was primarily caused by recent market activity that resulted in greater than previously estimated recoveries from reaucted spectrum licenses. According to the FY 2000 reestimate, the FCC expects to recover an amount greater than the gross receivable balance. Therefore, the FY 2000 subsidy cost allowance becomes a receivable rather than a loss. This receivable is added to the gross receivable balance, and therefore causes an increase to the net loan receivable balance.

As required under the Federal Credit Reform Act of 1990, as amended, the FCC coordinated with the Office of Management and Budget (OMB) in developing estimation guidelines, regulations, and the criteria to be used in calculating the subsidy cost allowance. This joint effort is undertaken to facilitate the development and improvement of cost and recovery rate estimates. This note should be read with the understanding that the FCC is a component of the Federal government. Therefore, the subsidy cost allowance has been prepared under specific guidance provided by the OMB in efforts to ensure that the objectives of the Federal government, taken as a whole, are being achieved and does not represent the FCC's current policy position on the auction of Spectrum held previously by other parties.

For budget purposes, OMB continues to request the FCC revise the assumptions used, based on events subsequent to September 30, 2000, to produce the cash flow estimates. The effects of the revisions have not yet been determined but will likely have a material impact to the subsidy costs. In accordance with OMB Circular A-34, once the impact of such revisions is determined, the results will be taken into consideration in making the reestimate for the following year.

Loans Receivable - Loans Receivable for post 1995 Spectrum License Auctions (with the exception of Pioneer Licenses) are recorded at the principal outstanding, net of allowances for subsidy. Allowance for subsidy costs represent the difference between the present values of estimated net cash inflows and outflows of the Spectrum License Auction Loans. The allowance for subsidy cost is amortized using the effective interest method based on the U.S. Treasury's interest rate at the time loans were disbursed. These funds are used to offset the annual interest expense to the U.S. Treasury on outstanding FCC borrowings. The allowance for subsidy also provides for write-offs on defaults and other costs that may affect cashflows.

Accrued Interest - FCC accrues interest on loans as it is earned. Current FCC policy automatically grants Spectrum Auction loans two three-month grace periods for which borrowers are charged late fees. In accordance with the FCC rules, at the end of the six-month period, loans

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**Note 6 - Direct Loans, Non-Federal Borrowers (continued):**

are considered to be in default and the license is automatically cancel. For financial reporting purposes, it is the FCC's policy to discontinue accruing interest on loans that are beyond the six-month grace period, since these loans are considered non-performing. Therefore, it is the FCC's policy to accrue and record interest only on the performing loans for financial reporting purposes.

**Direct Loans Obligated After FY 1991**

<u>Loan Program</u>	<u>Gross Loans Receivable</u>	<u>Interest Receivable</u>	<u>Other Receivables</u>	<u>Allowance for Subsidy</u>	<u>Net Loans Receivable</u>
FY 2000	\$8,177,261	\$ 429,889	\$ 2,952	\$982,418	\$9,592,520

As approved by OMB, the amounts above do not include the balances related to the Broadband PCS Pioneer Installment Financed Licenses for reasons previously mentioned.

**Subsidy Expense for Post-FY 1991 Direct Loans**

1. Current Year's Direct Loans:

<u>Loan Program</u>	<u>Interest Differential</u>	<u>Defaults</u>	<u>Fees</u>	<u>Other</u>	<u>Total</u>
Spectrum Auctions	\$ (58)	\$ 151	\$ -	\$ -	\$ 93

2. Direct Loan Modification and Reestimates:

<u>Loan Program</u>	<u>Modification</u>	<u>Reestimates</u>
Spectrum Auctions		
FY 2000	\$ -	\$3,381,499

3. Total Direct Loan Subsidy Expenses:

Total Current Year Direct Loans	\$ 93
Modifications	
Reestimates	<u>3,381,499</u>
Total	<u>\$3,381,592</u>

4. Administrative Expense:

Spectrum Auctions Total	<u>\$ 4,836</u>
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**Note 6 - Direct Loans, Non-Federal Borrowers (continued):**

As previously described, all Federal agencies are required to annually adjust their allowance for losses on their credit portfolios based on the most current performance information. In accordance with OMB guidance, the FCC calculated its subsidy reestimate based on the most recent economic conditions and technical assumptions available. The FCC's subsidy reestimate shows a \$4.3 billion reduction in the Spectrum License Auction Loan Portfolio subsidy cost, primarily due to the projected improved performance of the defaulted C Block and F Block loan portfolios. The average subsidy rate (the subsidy cost expressed as a percent of the original loan amount) falls from 52.08 percent from the prior year to 18.08 percent for the current year. In other words, the FCC expects to lose 18 cents for every dollar lent out through the Spectrum License Auctions installment loan program.

The most significant changes in the reestimate of the subsidy costs are attributable to the C and F Block installment licenses. There were no significant changes to the assumptions used for projection purposes of estimated cash flows for the other Spectrum License Auctions licenses. Based on the FY 2000 subsidy reestimate, the FY 1997 C and F Block installment licenses account for 97 percent of the Spectrum Auction subsidy cost (94 percent and 3 percent, respectively).

The FCC added \$10.6 million to its allowance for certain loans and reduced the allowance by \$4.3 billion for other loans. The "Interest on Reestimate" represents the interest earned/lost from origination until December 2000, the time of the reestimate, which increased the downward reestimate by \$901 million.

The C Block FY 1997 Cohort Subsidy Reestimate for FY 2001 resulted in a subsidy rate change from 54.34 percent in FY 2000 to 17.96 percent in FY 2001 and a subsidy cost change from \$4.9 billion in FY 2000 to \$1.6 billion in FY 2001. The major driver was due to the new recovery assumptions of approximately \$7.9 billion from Auction 35 and a 100 percent recovery rate on other defaulted loans. The reestimate also reflects 12 months of additional payment data and a change in projected vs. actual defaults from FY 2001 – FY 2006.

The F Block FY 1997 risk category subsidy reestimate for FY 2001 resulted in a subsidy rate change from 27.62 percent in FY 2000 to 6.08 percent in FY 2001 and a subsidy cost change from \$137.4 million to \$30.2 million. Consistent with C Block, the major driver for the change was due to an increase in the recovery projection from 50 percent to 100 percent.

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**Note 7 – Seized and Forfeited Property:**

**Seized Property**

FCC seizes property from illegally operated radio and other communication operations. The property is held pending the outcome of court proceedings. The property is comprised of prohibited property, radio frequency, audio equipment and other. The values assigned to the property are determined by FCC engineers based on current market values for comparable property. Seized Property as of September 30, 2000:

	<u>Beginning</u> <u>Balance</u>	<u>Number</u> <u>Seized</u>	<u>Number</u> <u>Forfeited</u>	<u>Ending</u> <u>Balance</u>	<u>Amount</u>
Prohibited (a)	36	10	5	41	\$ -
Radio Frequency	66	46	22	90	7
Audio	2,363	135	162	2,336	44
Other		<u>163</u>	<u>74</u>	<u>149</u>	<u>88</u>
	<u>4</u>				
Totals	<u>2,628</u>	<u>265</u>	<u>338</u>	<u>2,555</u>	<u>\$ 55</u>

**Forfeited Property**

Forfeited property consists of seized property legally turned over to the FCC. FCC does not resell the items. Forfeited items are either disposed of through the GSA surplus process or destroyed. The property is comprised of prohibited property, radio frequency, audio equipment and other. The values assigned to forfeited property are determined by FCC engineers, which are based on current market values for comparable property. Forfeited Property as of September 30, 2000:

	<u>Beginning</u> <u>Balance</u>	<u>Number</u> <u>Forfeited</u>	<u>Number</u> <u>Disposal</u>	<u>Ending</u> <u>Balance</u>	<u>Amount</u>
Prohibited (a)	17	5	1	21	\$ -
Radio Frequency	86	22	12	96	4
Audio	397	162	70	489	49
Other		<u>121</u>	<u>149</u>	<u>98</u>	<u>172</u>
	<u>8</u>				
Totals	<u>621</u>	<u>338</u>	<u>181</u>	<u>778</u>	<u>\$ 61</u>

(a) Prohibited items are those with no legal market in the United States. At the FCC, prohibited items are typically radio transmitters, the marketing of which would be in violation of the Communications Act.

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**Note 8 - Property, Plant and Equipment, net:**

The following summarizes general property, plant and equipment (PP&E) as of September 30, 2000:

<u>Classes of PP&amp;E</u>	<u>Acquisition Cost</u>	<u>Accumulated Depreciation</u>	<u>Net Book Value</u>	<u>Service Life in Years</u>
Land	\$ 1,292	\$ -	\$ 1,292	N/A
Buildings	4,091	3,848	243	20
Furniture	19,158	5,018	14,140	7
Non-Computer Equip.	6,647	5,084	1,563	7
Computer Equip.	13,450	7,722	5,728	5
Bulk Purchases	4,409	1,907	2,502	5 - 7
Vehicle Systems	2,924	1,150	1,774	7
Broadcast Station Equipment	4,497	4,359	138	7
Patent	800	137	663	17
ADP Software	14,024	6,577	7,447	3
ADP Software, In Process	<u>3,909</u>	<u>-</u>	<u>3,909</u>	N/A
Totals	<u>\$ 75,201</u>	<u>\$ 35,802</u>	<u>\$ 39,399</u>	

**Note 9 - Borrowings from the U.S. Treasury:**

The FCC borrows from the U.S. Treasury for costs associated with its Spectrum Auction Loan Program. Borrowings are determined upon calculation of the subsidy estimates and reestimates in accordance with the FCRA of 1990, as amended. The borrowings pertain to all loan cohorts.

Beginning Balance	\$3,938,605
Net Borrowing	<u>1,368,666</u>
Ending Balance	<u>\$5,307,271</u>

The weighted average interest rate on borrowings from the U.S. Treasury for fiscal year 2000 was approximately 7.0 percent. The calculation was made in accordance with OMB Circular A-34, *Budget Execution*. Total interest paid on borrowings from the U.S. Treasury was \$368.5 million for fiscal year 2000.

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**Note 10 – Accounts Payable:**

The Accounts Payable – FCC balance reflects amounts owed for goods and services that have been received, but not liquidated as of September 30, 2000. Accounts Payable - USF mainly represents administrative costs incurred primarily by and due to USAC for USF and to NECA for TRS.

	<u>Intragovernmental</u>	<u>With the Public</u>	<u>Total</u>
Accounts Payable - FCC	\$ -	\$ 14,403	\$ 14,403
Accounts Payable – TRS	\$ -	9,532	9,532
Accounts Payable - USF	<u>-</u>	<u>385,694</u>	<u>385,694</u>
Totals	<u>\$ -</u>	<u>\$ 409,629</u>	<u>\$409,629</u>

**Note 11 – Other Debt:**

The majority of Other Debt is comprised of a liability of \$125.3 million as a result of litigation against the FCC. This liability is considered long-term and liquidation of the liability is dependent upon the outcome of upcoming auctions.

**Note 12 - Other Liabilities:**

	<u>Intragovernmental</u>	<u>With the Public</u>	<u>Total</u>
Covered By Budgetary Resources:			
Liability for Custodial Receivable	\$ 96,347	\$ 740	\$ 97,087
Liability for Custodial Receipts	229,999	-	229,999
Auction Deposits	17,002	46,799	63,801
Accrued Payroll	1,762	8,369	
10,131	Miscellaneous	<u>607</u>	<u>607</u>
-	<u>607</u>	-	
Total Covered Budgetary Resources	<u>\$ 345,717</u>	<u>\$ 55,908</u>	<u>\$ 401,625</u>
Not Covered By Budgetary Resources:			
FECA Liability	\$ 443	\$ -	\$ 443
Deferred Revenue	<u>-</u>	<u>69,982</u>	<u>69,982</u>
Total Not Covered By Budgetary Resources	<u>\$ 443</u>	<u>\$ 69,982</u>	<u>\$ 70,425</u>

The FCC liability for custodial receivables represents an offset to non-entity receivables that when collected, will be deposited into the U.S. Treasury General Fund.

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**Note 12 - Other Liabilities (continued):**

The liability for custodial receipts represents Spectrum Auction monies being held by FCC for transfer to the U.S. Treasury General Fund. A portion of these funds may be used to cover the cost of fiscal year 2000 auctions. It is anticipated that all custodial receipts currently held will be transferred to the U.S. Treasury or used as offsetting collection in fiscal year 2001.

**Note 13 - Payable to Providers:**

The USF collects funds from contributing telecommunications service providers in accordance with FCC regulations. Pursuant to FCC rules, the universal service support funds are made available to service providers to assist in making access to telecommunication services more affordable to remote or rural areas, low-income neighborhoods, rural health care providers, and public and private schools and public libraries. The Telecommunications Relay Services (TRS) fund compensates service providers for the reasonable costs of providing interstate telephone transmission services that enable persons with hearing or speech disabilities to use wireline or wireless telecommunications services. Accordingly, the payable to providers in the amount of approximately \$2.1 billion represents collected contributions as of September 30, 2000 that have yet to be distributed to eligible service providers.

**Note 14 - Leases:**

Operating Leases:

The FCC has operating leases for rental of office space and office equipment. The copier lease arrangements are renewable annually with five possible annual renewal periods.

Future lease obligations under operating leases are as follows:

<u>Fiscal Year</u>	<u>Bldg</u>	<u>Copier</u>	<u>Total</u>
2001	31,241	538	31,779
2002	38,192	564	38,756
2003	38,959	592	39,551
2004	39,738	622	40,360
2005	<u>40,532</u>	<u>653</u>	<u>41,185</u>
Total Future Lease Payments	<u>\$188,662</u>	<u>\$ 2,969</u>	<u>\$191,631</u>

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**Note 15 – Net Position:**

Net position is the difference between assets and liabilities. The section contains two line items: Unexpended Appropriations, including unobligated appropriations and undelivered orders, and Cumulative Results of Operations. Unobligated appropriations are either available for obligation or not available (permanently or temporarily) pursuant to a specific provision in law. Undelivered orders represent appropriations obligated (i.e. legally reserved) for the amount of goods or services ordered but not yet received.

Cumulative results of operations include the following:

- The net accumulated difference between expenses consuming budgetary resources and financing sources providing budgetary resources.
- Investment in capitalized assets, which increases as capital assets are acquired and decreases as capital assets are consumed (depreciated) or disposed of; and
- The excess of certain liabilities not covered by budgetary resources, net of certain assets not providing budgetary resources, whose liquidation will require funding from future congressional appropriations or other budgetary resources.

Unexpended Appropriations consists of the following:

Unobligated:

Available	\$ 6,103,668
Unavailable	6,992
Undelivered Orders	17,336
Non-Budgetary Accruals	\$ <u>(5,306)</u>

Total	\$ <u>6,122,690</u>
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In accordance with FCRA of 1990, as amended, the FCC will recognize the budgetary effects of the downward reestimate of approximately \$4.3 billion in the subsequent fiscal year. Therefore, the downward reestimate, based on interpretation of the accounting standards and as discussed in detail in Note 6, is not reported on the Statement of Budgetary Resources but is included in Unexpended Appropriation as a recovery of previously recognized subsidy expense for financial reporting purposes in FY 2000.

**Note 16 – Gross Costs and Related Exchange Revenue:**

Section 9(a) of the Communications Act of 1934, as amended, authorizes the Commission to assess and collect annual regulatory fees to recover the costs, as determined annually by Congress, that it incurs in carrying out enforcement, policy and rulemaking, international, and user information activities. OMB Circular No A-25 revised, *User Charges*, requires an agency to assess a user charge against each identifiable recipient for special benefits derived from Federal activities beyond those received by the general public. The Circular also requires that user fees

**Note 16 – Gross Costs and Related Exchange Revenue (continued):**

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be established to recover the full cost to the Federal government of providing the service when the Government is acting in its capacity as sovereign. Where a statute prohibits certain aspects of the user fee, the statute shall take precedence over the requirements of Circular A-25. Accordingly, Congress required the FCC to recover approximately \$185.8 million through its regulatory fees. These fees were established by Congressional authority, and consistent with OMB Circular A-25, the FCC did not determine the full costs associated with its regulatory activity in the establishment of regulatory fees.

With regards to the costs reported on the Statement of Net Cost, these costs are allocated to the five budgeted FCC programs on the basis of total and direct program costs. There are four common cost pools, which consist of Leave Costs, Other Costs, Bureau Overhead Costs and Executive Direction Costs and the costs are allocated in that order. All four cost pools are allocated on the basis of total costs and are ultimately distributed either to activity codes for Salaries and Expenses related costs or auctions related costs. Specifically, Leave Costs are allocated on a total cost basis and all other costs allocated based on direct program costs. At the completion of the common cost allocation process, all costs were summarized according to the four programs included in the annual budget submission to OMB and the Congress.

Costs for intragovernmental and with the public were separately identified by the FCC. The FCC then determined the percentage of intragovernmental costs and costs with the public as a ratio to total costs. These percentages were used in allocating program costs between intragovernmental and with the public at the program level on the statement of net costs.

The most significant costs of the FCC pertains to its credit reform activities, included interest expense on borrowings of approximately \$368 million, interest on the subsidy of approximately \$901 million, and the downward reestimate of the subsidy costs on the installment loan program of approximately \$3.4 billion described in "Total Direct Loan Subsidy Expenses" in Note 6 above. These costs have been allocated on the Statement of Net Cost consistent with the basis of Executive Direction Costs, among the programs, excluding the USF, reflected on the Statement of Net Cost. Other costs allocated among the programs include approximately \$145 million for salaries and related benefits, and approximately \$55 million related to contractual services.

Exchange revenue is allocated on a one to one basis with ending gross costs and is largely composed of \$2.3 billion in interest revenue related to the downward reestimate of recoveries on credit reform loans. In addition to interest revenue are earned revenues of \$185.8 million from annual regulatory fees, \$45 million reimbursed to cover Spectrum Auction costs, \$28 million in application fees ultimately passed on to the U.S. Treasury, and \$1 million in reimbursable revenue with other Federal, state, and local agencies.

Also, based on interpretation of SFFAS No. 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*, as issued by the Federal Accounting Standards Advisory Board (FASAB), the FCC recorded the portion of expenses related to managing and overseeing the USF as operating expenses.

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**Note 17 – Prior Period Adjustments:**

During fiscal year 2000, prior period adjustments were made to the accounting records. These adjustments were made as a result of the extensive efforts endured in preparing a comprehensive set of financial statements for the first time ever. The adjustments are summarized as follows:

Recognize property and related depreciation for items purchased in prior years but not identified until the current year	\$ 1,745
Reduce overstated depreciation on Furniture	(7,298)
Reclassify credit reform funds from Cumulative results to appropriated capital.	1,826,241
Reclassify auctions and regulatory funds from appropriated capital to cumulative results	11,160
Removal of liability for moving and furniture costs	(74,132)
Regulatory Fees	2,534
Other	<u>41</u>
Total	<u>\$1,760,291</u>

The majority of the items above occurred as a result of the manner in which closing entries were reflected in the accounting records. Specifically, the \$1.8 billion resulted from a downward reestimate that was incorrectly classified as cumulative results of operations in the accounting system in fiscal year 1999. In accordance with SFFAS # 2, *Accounting for Direct Loans and Loan Guarantees*, as amended, the \$1.8 billion was reclassified to unexpended appropriations. The removal of the liability for moving and furniture as part of the FCC's move into the current Headquarters location resulted in the retroactive recognition of "Other Financing Sources." As a means of recognizing these resources without reflecting them in the current year, the FCC has recognized a prior period adjustment.

A prior period adjustment of approximately \$64 million was also made to the loans receivable balance and the related allowance. The adjustment was not recorded on the Statement of Changes in Net Position since it only impacted the Consolidated Balance Sheet, and accordingly, the adjustment had no net effect on this fiscal year's Statements of Net Cost and Changes in Net Position.

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**Note 18 – Dedicated Collections:**

U.S. telecommunication companies are obligated to pay assessments for universal service support and for telecommunications relay service, which are established by the FCC. These assessments are accounted for in the U.S. Budget as the “Universal Service Fund.” As defined by the Statement of Federal Financial Accounting Standards (SFFAS) No. 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*, as issued by the Federal Accounting Standards Advisory Board (FASAB). Such monies are not considered exchange revenues because neither the FCC nor the USF sacrificed value or received value in return for the collection and disbursement of the contributed funds (e.g., provided goods or services for a price).

Based on interpretation of SFFAS No. 7, the FCC considers the assessments collected under the Universal Service Fund as dedicated funds. The following summarizes the significant assets, liabilities, and related costs incurred with managing the Universal Service Fund. See Other Accompanying Information for complete disclosure of all activity related to the Universal Service Fund.

Assets

Investments (see note 4)	\$2,041,535
Accounts Receivable	405,350

Liabilities

Payable to Providers	\$2,446,379
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Costs

Program Costs	\$39,608
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The program costs are expenses related to managing and overseeing the USF. The USF is charged administrative expenses from the Universal Service Administrative Company and the National Exchange Carriers Association for expenses such as salaries and benefits of the employees dedicated to managing the universal service support mechanisms and the telecommunications relay services mechanism, rent and utilities for office space used, providing accounting and other financial reporting related services, and other miscellaneous activities.

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**Note 19 – Contingencies:**

A contingency is an existing condition, situation, or set of circumstances involving uncertainty as to possible gain or loss to FCC. The uncertainty will ultimately be resolved when one or more future events occur or fail to occur. With the exception of pending, threatened, or potential litigation, a contingent liability is recognized when a past transaction or event has occurred, a future outflow or other sacrifice of resources is more likely than not, and the related future outflow or sacrifice is measurable. For pending, threatened, or potential litigation, a liability is recognized when a past transaction or event has occurred, a future outflow or other sacrifice of resources is likely, and the related future outflow or sacrifice of resources is measurable.

The FCC is in the process of determining whether a liability needs to be recorded in its financial records for FY 2000 as a result of the FCC's move to the current Headquarter facilities. FCC is seeking determination from OMB if a liability exists and whether the FCC or another agency will be responsible for liquidating the potential liability. As of September 30, 2000, the FCC is awaiting decision from OMB and the FCC is unable to reasonably estimate an amount and predict the outcome of OMB's decision.

FCC is a party in various administrative proceedings, legal actions and claims brought by or against the agency. In addition, several bankruptcy proceedings are ongoing related to the loan portfolio. See Note 6 for more information related to the loans. In the opinion of FCC management, the ultimate resolution of proceedings, actions and claims, outside of the loans, will not materially affect the financial position or results of operations of FCC. Additionally, there are certain matters under consideration at the Department of Justice, which may result in future proceedings or actions. As of September 30, 2000, the Department of Justice and FCC management are not in a position to assess the outcome of these matters.

Subsequent to the end of the fiscal year, FCC management became aware that additional matters may be raised which would have the potential to be material. Review is at an extremely preliminary stage and therefore FCC management is not in a position to assess these matters for any purpose.

**Note 20 - Statement of Budgetary Resources:**

Total budgetary authority for the FCC as of September 30, 2000 is \$4,524,689.

All unobligated budgetary authority is in compliance with applicable appropriation laws with regards to time limitations, restrictions and purpose. The unobligated balance of budgetary authority available for apportionment is \$1,847,387, which is mostly made up of the fiscal year 1999 downward reestimate of \$1,821,450. The fiscal year 2000 downward reestimate of \$4,282,602 is currently reflected in unexpended appropriations and will have a budgetary impact in fiscal year 2001. The unobligated balance of budgetary authority unavailable of \$11,359 represents expired amounts related to the annual appropriations received for Salaries and Expenses. This balance is only available for any upward adjustment to existing obligations.

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**Note 20 - Statement of Budgetary Resources (continued):**

FCC receives borrowing authority consistent with the Federal Credit Reform Act of 1990, as amended. The borrowing is authorized through an indefinite permanent authority at interest rates set each year by the U.S. Treasury. In addition, the FCC has permanent indefinite authority for subsidizing the Spectrum Auction direct loan program.

With the exception of a monetary credit that resulted as a judgment against the FCC, all borrowings are from the Bureau of Public Debt. In accordance with applicable standards, all funds are borrowed at the beginning of the period. Therefore, the FCC does not carry over any unused borrowing authority. Repayments of borrowings are made in accordance with the terms of the Federal Credit Reform Act of 1990, as amended. Financing sources for repayment are collections from borrowers or subsidy.

There were no adjustments made to the beginning balance of budgetary resources. In addition, there was no contributed capital received during the fiscal year 2000.

**Note 21 – Statement of Financing:**

Financing Sources yet to be Provided of \$509 represents the increase in the Accrued Unfunded Leave balance (\$12,548) over the prior year. The other Liabilities Not Covered by Budgetary Resources shown on the balance sheet, Other Unfunded Liability – Intragovernmental (\$443), Payable to Provider (\$2,052,849), and Other Unfunded Liability - With the Public (\$69,982) represent custodial liabilities that have no impact on the statement of financing.

**Note 22 – Cost and Revenue by Budget Function:**

The FCC's costs and revenue, by budget function, are consistent with that shown on the Statement of Net Cost.

**FEDERAL COMMUNICATIONS COMMISSION**

**REQUIRED  
SUPPLEMENTAL  
INFORMATION**

**FEDERAL COMMUNICATIONS COMMISSION  
REQUIRED SUPPLEMENTAL INFORMATION  
September 30, 2000  
(Dollars in thousands)**

**Intra-Governmental Assets**

<u>Trading Partner</u>	<u>Fund</u>	<u>Accounts</u>	<u>Investments</u>
<b>Entity</b>	<u>Balance</u>	<u>Receivable</u>	
Department of Treasury	\$1,903,494	\$ -	\$ -
Other	<u>-</u>	<u>39</u>	<u>-</u>
Sub-Total	<u>\$1,903,494</u>	<u>\$ 39</u>	<u>\$ -</u>
<b>Non-Entity</b>			
Department of Treasury	<u>\$ 304,171</u>	<u>\$ -</u>	<u>\$1,297,611</u>
Total	<u>\$2,207,665</u>	<u>\$ 39</u>	<u>\$1,297,611</u>

**Intra-Governmental Liabilities**

<u>Trading Partner</u>	<u>Borrowings</u>	<u>Other</u>
<b>Funded</b>	<u>From</u>	<u>Liabilities</u>
	<u>Treasury</u>	<u>Liabilities</u>
Department of Treasury	\$5,307,271	\$ 326,346
Other	<u>-</u>	<u>19,371</u>
Sub-Total	<u>\$5,307,271</u>	<u>\$ 345,717</u>
<b>Unfunded</b>		
FECA	<u>\$ -</u>	<u>\$ 443</u>
Total	<u>\$5,307,271</u>	<u>\$ 346,160</u>

**Intra-governmental Non-Exchange Revenue**

The FCC does not have any intra-governmental non-exchange revenue. All of the FCC's non-Exchange revenues are from the public, which includes collections attributable to civil monetary penalties and the Universal Service Fund.

**FEDERAL COMMUNICATIONS COMMISSION  
REQUIRED SUPPLEMENTAL INFORMATION  
September 30, 2000  
(Dollars in thousands)**

**DEFERRED MAINTENANCE**

To determine the estimated cost of deferred maintenance, FCC contracted with professional building inspectors to inspect its real property holdings containing include buildings and structures. The inspection reports were, in most cases, comprehensive reviews of the buildings and ground conditions and included all items that required attention, whether critical to the functionality of the building or more of a cosmetic nature. Although FCC does not consider the amounts material, it has identified approximately \$1.7 million related to deferred maintenance.

FCC intends to review the deferred maintenance items on a quarterly basis to determine which items should be funded and whether funds are available to support the work. Using the inspection reports and cost estimates as a baseline, FCC also intends to create a spreadsheet showing a year-by-year schedule of maintenance and replacement items to assist in budget planning.

**FEDERAL COMMUNICATIONS COMMISSION**

**OTHER  
ACCOMPANYING  
INFORMATION**



## Independent Auditor's Report

To the Inspector General of the  
Federal Communications Commission

We have audited the accompanying consolidated balance sheet of the Federal Communications Commission (FCC) as of September 30, 2000, and the related consolidated statements of net cost, changes in net position, budgetary resources, financing, and custodial activity for the year then ended (collectively the Principal Statements). These Principal Statements are the responsibility of FCC's management. Our responsibility is to express an opinion on these Principal Statements based on our audit.

We conducted our audit in accordance with the U. S. generally accepted auditing standards; the standards applicable to the financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin 01-02, *Audit Requirements for Federal Financial Statements*. These standards require that we plan and perform the audit to obtain reasonable assurance about whether the Principal Statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the Principal Statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall Principal Statements' presentation. We believe our audit provides a reasonable basis for our opinion.

In our opinion, the Principal Statements and related notes present fairly, in all material respects, in conformity with U. S. generally accepted accounting principles, FCC's assets, liabilities, and net position; net cost; changes in net position; budgetary resources; reconciliation of net cost to budgetary obligations; and custodial activity as of September 30, 2000 and for the year then ended.

In accordance with *Government Auditing Standards*, we have also issued our reports dated February 9, 2001 on our consideration of FCC's internal control over financial reporting, and on our tests of FCC's compliance with certain provisions of laws and regulations. These reports are an integral part of our audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Our audit was made for the purpose of forming an opinion on the basic Principal Statements taken as a whole. The Management Discussion and Analysis and Required Supplemental Information are not a required part of the Principal Statements but are supplementary

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information required by OMB Bulletin No. 97-01, *Form and Content of Agency Financial Statements*. The other Accompanying Information is presented for the purposes of additional analysis and is not a required part of the Principal Statements. Such information contains a wide range of data, some of which are not directly related to the Principal Statements. We have applied certain limited procedures, which consisted principally of comparing this information for consistency with the Principal Statements and discussing the methods of measurement and presentation with FCC management. However, we did not audit the information and express no opinion on it.

*Clifton Gunderson LLP*

Calverton, Maryland  
February 9, 2001



## Independent Auditor's Report on Internal Control

To the Inspector General of the  
Federal Communications Commission

We have audited the Principal Statements (hereinafter referred to as "financial statements") of the Federal Communications Commission (FCC) as of and for the year ended September 30, 2000, and have issued our report thereon dated February 9, 2001. We conducted our audit in accordance with U. S. generally accepted auditing standards; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 01-02, *Audit Requirements for Federal Financial Statements*.

In planning and performing our audit, we considered FCC's internal control over financial reporting by obtaining an understanding of FCC's internal controls, determined whether internal controls had been placed in operation, assessed control risk, and performed tests of controls in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements. We limited our internal control testing to those controls necessary to achieve the objectives described in OMB Bulletin No. 01-02. We did not test all internal controls relevant to operating objectives as broadly defined by the Federal Managers' Financial Integrity Act (31 U.S.C. 3512), such as those controls relevant to ensuring efficient operations. The objective of our audit was not to provide assurance on internal control. Consequently, we do not provide an opinion on internal control.

Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be reportable conditions. Under standards issued by the American Institute of Certified Public Accountants, reportable conditions are matters coming to our attention relating to significant deficiencies in the design or operation of the internal control that, in our judgment, could adversely affect the agency's ability to record, process, summarize, and report financial data consistent with the assertions by management in the financial statements. Material weaknesses are reportable conditions in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Because of inherent limitations in internal controls, misstatements, losses, or noncompliance may nevertheless occur and not be detected. However, we noted certain matters discussed in the following paragraphs involving the internal control and its operation that we consider to be reportable conditions and material weaknesses.

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In addition, with respect to internal controls related to performance measures reported in FCC's Management Discussion and Analysis (MD&A), we obtained an understanding of the design of significant internal controls relating to the existence and completeness assertions, as required by OMB Bulletin No. 01-02. Our procedures were not designed to provide assurance on internal controls over reported performance measures, and, accordingly, we do not provide an opinion on such controls. However, we noted certain significant deficiencies in internal control over reported performance measures discussed in the following paragraphs that, in our judgment, could adversely affect the agency's ability to collect, process, record, and summarize performance information and report performance measures in accordance with management criteria.

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## **MATERIAL WEAKNESSES**

### **I. Financial Reporting (Repeat Condition)**

The Chief Financial Officers (CFO) Act of 1990 assigned responsibility for developing and operating financial management systems to each Federal agency. OMB Bulletin No. 97-01, *Form and Content of Agency Financial Statements*, as amended (OMB Bulletin No. 97-01, as amended) defines the form and content of financial statements to be prepared by each agency. To accomplish the objective of complying with the CFO Act, the agency is required to develop a system to prepare a complete set of financial statements on a timely basis in accordance with generally accepted accounting principles. The statements are to result from an accounting system that is an integral part of a total financial management system containing sufficient structure, effective internal control, and reliable data. Financial reporting also consists of policies and procedures related to the processing and summarizing of accounting entries, and the preparation of financial statements.

FCC achieved an exceptional goal in preparing its first complete set of financial statements for fiscal year 2000; just one year after its first ever balance sheet and notes were prepared and audited. FCC staff, increasing cooperation and coordination among offices and bureaus, and services from external consultants, among others, were instrumental in achieving this goal. However, we believe that FCC's financial reporting process continues to need refinement. This refinement should allow FCC to prepare reliable financial statements in a more timely and efficient manner at the end of the fiscal year and interim periods throughout the year.

FCC's financial reporting weaknesses are detailed as follows:

#### **A. Develop an Integrated Financial Management System**

OMB Circular No. A-127, *Financial Management Systems* requires that each agency establish and maintain a single integrated financial management system. Without a single integrated financial management system to ensure timely and accurate financial data, poor policy decisions may occur, due to inaccurate or untimely information. Managers are less

likely to be able to report accurately to the President, Congress, and the public on Government operations on a timely manner. And, scarce resources are more likely to be directed toward the collection of information rather than to delivery of the intended programs.

Having a single, integrated financial management system does not necessarily mean having only one software application within each agency covering all financial management system needs. Also, it does not mean that all information is physically located in the same database. Rather, a single, integrated financial management system is a unified set of financial systems linked together electronically in an efficient and effective manner to provide agency-wide financial system support. Integration means that the user is able to have one view into systems such that, at whatever level the individual is using the system, he or she can obtain needed information efficiently and effectively through electronic means. Interfaces are acceptable as long as the supporting detail is maintained and accessible to managers. Interface linkages must be electronic unless the number of transactions is so small that it is not cost beneficial to automate the interface. Easy reconciliations between systems, where interface linkages are appropriate, must be maintained to ensure data accuracy.

FCC utilizes the Federal Financial System (FFS) as its general ledger and core financial management system. FFS is not capable of generating most data analysis user reports on a real time basis. Users have to request reports which are generated by a software application whose operations are only known to some staff of Financial Operations (FO). Other financial management systems used at FCC include the property management system, loan database spreadsheets, license databases, collection system, cost system, commercial accounting software for fines and forfeitures, and various spreadsheet applications. None of these financial management systems are integrated.

#### **Management Comments:**

Management concurs. The effort to develop an integrated financial system has been ongoing since FY 1999. Current efforts involve implementation of the Revenue Accounting and Management Information System (RAMIS) as well as upgrading the cost accounting system and reconfiguring FFS. RAMIS has been partially implemented for FY 2001 and is integrated with the core financial accounting system. FCC hired a contractor to help develop the functional requirements applicable for the replacement of the current cost accounting system and has targeted FY 2002 for implementation of a new cost accounting system. FCC also contracted with the developer of FFS to explore the capabilities of this system.

FCC noted FFS is incapable of generating real time reports but can respond in real time to specific inquiries. Currently, the data warehouse utility is updated nightly to include previous day's transaction information. Using data warehouse capabilities, report information is frequently tailored to meet the needs of various users.

## **B. Establish and Maintain an Adequate Audit Trail Used in Preparing the Financial Statements**

FCC employs spreadsheet applications to create, document, report, and support its financial statements. These spreadsheets are linked to several different files. The files were not provided to the auditors at the same time as the spreadsheets and receipt was after several requests. Numerous numbers in the spreadsheets are keyed numbers and could not be traced back to the trial balance. When audit trails were available, most of them were a series of numbers in a comment box without an explanation or clear explanation of the various Standard General Ledger (SGL) accounts comprising the total. In addition, adjusting entries were prepared as post closing entries resulting in some discrepancies in the Statement of Net Cost, Statement of Changes in Net Position, and the trial balance. Also, some adjusting entries were not reflected in all affected financial statements until they were brought to FCC's attention by the audit process.

Although the use of spreadsheet applications appears to be common practice in the preparation of financial statements throughout the Federal government, adequate audit trails are necessary for review verification and ultimately audit. Lack of adequate audit trails increases the risk of errors. FCC's process of preparing financial statements is manually intensive, time consuming, and lacks controls over the completeness of final data used to prepare the financial statements. The lack of control over the completeness of final data and inadequate audit trails was evidenced upon technical review of the financial statements. Additionally, entity personnel encountered the same difficulties when researching compiled numbers in response to audit inquiries.

Maintaining an adequate audit trail enhances the quality of the agency report, reduces the risk of errors through an organized systematic process, and allows a person to independently review the report data accumulation process. Additionally, adequate audit trails facilitate the financial statement compilation process and helps ensure completeness of data upon review by management.

### **Management Comments:**

Management concurs. Fiscal year 2000 was the first year FCC prepared all required financial statements to audit. As part of our effort to identify early audit issues, interim statements were prepared; however, parts of the preparation process were not fully established at fiscal year-end. FCC is formalizing policies and procedures specifically related to financial reporting with planned implementation by the close of FY 2001. In addition, FCC reviewed the spreadsheets used to prepare FY 2000 financial statements and made revisions that include using the updated OMB Bulletin No. 97-01, as amended crosswalks to prepare the Statement of Financing and the Statement of Custodial Activity.

### **C. Correct and Update Federal Financial System Setup and Posting Model Definitions (Modified Repeat Condition)**

Last year's material weakness in the reporting process noted incorrect accounting entries associated with the transaction codes set up in FFS. FCC had not updated its FFS system setup and posting model definitions for many years. As SGL numbers, definitions, and standard accounting entries were updated and revised by the Department of the Treasury, Financial Management Service (FMS) over the years, and as FCC accounting activities became more complex, the FCC general ledger system set-up remained unchanged.

In response to the weakness noted, FCC management reviewed and updated, as a start, the auction and credit reform related transaction codes and accounting entries during the current fiscal year. In preparing the annual financial statements, however, FCC identified additional FFS year-end closing process errors. FCC hired a contractor to provide guidance in implementing recommended changes to the FCC's current configuration of the FFS tables and posting models. This system's deficiencies impair the quality and the reliability of the financial management information. A summary of the contractor's posting analysis findings are as follows:

- Incorrect debit/credit postings, inconsistencies between certain tables, and inaccurate closing accounts;
- Current value of funds rate in a table has not been updated;
- Report reference tables are out-of-date and will require significant changes in order for the FCC to facilitate Federal Agencies' Centralized Trial Balance System (FACTS) I and II reporting and to generate SF-133, Report on Budget Execution, and FMS 2108, Year-End Closing Statement. FCC, however, has not used the external reporting capabilities of FFS;
- Out-dated SGL accounts, account titles, and cross-references, plus inaccurate natural balances;
- Several of the reports reference tables are no longer required; and
- The report reference tables are out-of-date related to referencing the SF-133 and FMS-2108 in several areas, including formatting, balance indicators, and account references.

The contractor made detailed recommendations to enhance compliance with the SGL and facilitate use of external reporting capabilities of FFS.

#### **Management Comments:**

Management concurs. Prior to the FY 2000 closing, FCC was aware the FFS posting model contained incorrect definitions and had taken steps to contract with the FFS developer to identify and correct deficiencies. The contractor has since completed its evaluation and reviewed recommendations have been corrected in FFS. In conjunction with the FFS review, FCC also worked with the contractor to update the reporting tables needed to prepare the

SF-133 and FMS 2108 from FFS. FCC continues to explore modifications to FFS to improve its financial reports.

#### **D. Improve Analysis of Budgetary Accounts**

In preparing the Statement of Budgetary Resources and Statement of Financing, FCC encountered a great deal of difficulty due to erroneous balances accumulating in the accounting system over time that remained unadjusted. Although FCC explained that most of the variances we identified are due to beginning balances and the FFS closing process system deficiencies as explained above, the process of correction and procedural changes at year-end resulted in time consuming analysis and delays in preparing these statements.

##### **Management Comments:**

Management concurs. FCC addressed some of the budgetary issues by modifying current transaction codes and will continue to address improper budgetary balances as identified. The preparation of quarterly financial statements, FACTS II quarterly reporting, update of the SF-133 and 2108 reporting module, and monthly reconciliations in FY 2001 will help to eliminate issues created by prior period transactions.

#### **E. Record Activities Timely and Prepare and Analyze Financial Activity (Modified Repeat Condition)**

Although FCC prepared its interim financial statements (except for the Statement of Financing) at June 30, 2000, the interim statements did not reflect current accounting activities for certain areas and there was no evidence of adequate management review. Interim financial statements are supposed to reflect the current financial condition and operations to allow management to analyze data and make decisions based on reported information. We noted that activities were not being recorded timely. For example,

- All interim regulatory fee sampled items (4 of 4) examined were not recorded in FFS for more than three months between the date of an authorized transaction and the entry into FFS;
- All interim fines and forfeitures receivable sampled items (4 of 4) reviewed were not recorded in FFS quarterly and the amount recorded was the total net balance of the activities; and
- Loan collection transaction activity was not recorded in FFS during the year but only applied to principal, interest, and other accounts at year-end.

Not recording or delays in recording transactions make data on the interim financial statements unreliable and unusable for management decision purposes. *Standards for Internal Control in the Federal Government*, issued by the General Accounting Office (GAO) in November 1999, page 15 states that “Transactions should be promptly recorded to maintain their relevance and value to management in controlling operations and making decisions.”

Account analyses and reconciliations for accounts such as Loans Receivable; Interest Receivable; Accounts Payable; Accounts Receivable; and Property, Plant, and Equipment were not periodically performed during the entire fiscal year, and for most accounts, analyses were performed only once at fiscal year-end in preparation for financial statement reporting. As a result, significant journal vouchers prepared as part of a general account “clean-up” for the year-end were identified and posted. Regular financial statement preparation and analysis on a monthly or quarterly basis may eliminate the need for many of these adjustments during the year-end closing process and reduce the risk that material errors or irregularities in general ledger accounts remain undetected until after the end of the fiscal year.

**Management Comments:**

Management concurs. Beginning with second quarter FY 2001 balances, all principal statements and related footnotes are prepared on a quarterly basis. In addition, the Financial Operations Center has added six additional positions to improve the timeliness and completeness of the financial statement reconciliation effort and recommended reviews. FCC analyzed current reconciliations to identify monthly reconciliations not in place and established procedures for performing those reconciliations.

FCC is improving the recordation of its loan receivable and interest receivable transactions via RAMIS. This system will receive a download from the bank and create FFS transactions within 24 hours of receipt of payment by the bank. This will enhance FCC’s ability to routinely reconcile balances and ensure current, accurate management information on the status of its portfolio. Until the system is fully implemented, FCC continues to rely on the loan model prepared by its contractor recognizing the associated delays inherent in the process.

FCC agrees additional steps are needed to improve the completeness of interim statements. FY 2001 will show considerable progress towards this goal.

**F. Formalize Financial Reporting Processes and Responsibilities in the Preparation of Financial Statements (Modified Repeat Condition)**

Preparation of the annual financial statements is the responsibility of the agency’s management. In carrying out this responsibility, each agency CFO should prepare a policy memorandum that guides fiscal management personnel in the preparation of the annual financial statements. FCC does not have a formalized financial reporting process nor does it have written documentation that provides an integrated view of the procedures, personnel, and systems employed in preparation of the financial statements. Moreover, FCC did not have a process for identification of transactions requiring elimination at the consolidated level. Although FCC management told us that formalized financial reporting policy and guidelines have been drafted, a copy has not been provided for review as part of the audit process. The existence of written procedures will provide structure to the preparation and review process.

The FMS, Financial Standards and Reporting Division issued the *Accounting Policies and Procedures Guide for Federal Intragovernmental Transactions*. Although the guide is for intragovernmental transactions, it provides guidance related to elimination within an entity in preparing consolidated financial statements. This guide provides government-wide policies and procedures to account for and reconcile transactions occurring within and between each entity. In page 18 of this guide, it states “Each agency should develop and implement procedures to provide for the preparation of financial reports in accordance with the policies and procedures in this guide. Amounts reported in the basic financial statements, supplemental information, and in the footnotes should be supported by schedules summarizing and documenting the combination of SGL accounts comprising each total on the financial statements. Elimination entries should be supported with schedules summarizing the SGL accounts that are combined to total the amounts eliminated.” It also states in page 17 that “Consolidated financial statements present an agency’s financial information as a single entity. Elimination entries remove redundant activity and account balances within the consolidated statements. Each agency should have procedures for capturing this activity and balances within the agency to facilitate elimination process. Elimination entries should be performed at the consolidated level. Agencies should implement policies and procedures providing guidance within the agency for the identification of transactions requiring elimination at the consolidated level to facilitate financial statement preparation.”

**Management Comments:**

Management concurs. FCC established a separate Financial Statements and Policy Group within its Financial Operations Center to address both financial statement preparation and financial policies and procedures. The group was established in FY 2000. The group’s first priority is the completion of the policies and procedures manual begun in FY 2000. Currently, six of the eight chapters are in final draft status. Upon completion, the manual will be available to all employees via the FCC Intranet and an agency initiated training program.

**G. Inadequate Discussion in Management’s Discussion and Analysis**

FCC’s MD&A did not adequately discuss the requirements of the Federal Accounting Standards Advisory Board’s (FASAB), Statement of Federal Financial Accounting Standards (SFFAS) No. 15, *Management’s Discussion and Analysis* pertaining to the future effects on the entity of existing, currently known demands, risks, uncertainties, events, conditions, and trends.

MD&A should describe important existing, currently-known demands, conditions, risks, uncertainties, events, conditions and trends (current factors) – both favorable and unfavorable – that affect the amounts reported in the financial statements and supplementary information. The discussion of these current factors should go beyond a mere description of existing conditions to include a discussion of the possible future effect of those factors.

**Management Comments:**

Management concurs. The FY 2000 financial statement compilation efforts focused on the principal statements and related footnotes. In addressing the MD&A section, management chose to focus its efforts on the establishment of performance measures where performance reporting was established or could be modified to meet reporting requirements. In FY 2001, FCC plans to incorporate a section to address future effects and consider other areas where improvements can be made.

**H. Combination of Reportable Conditions May Materially Impact Financial Statements (Repeat Condition)**

Reportable conditions noted in this report are internal control weakness relating to reconciliation procedures which could collectively have a material impact on FCC's ability to produce reliable financial statements in an efficient and timely manner and to comply with the intent of the CFO Act.

**Management Comments:**

While acknowledging conditions exist, management does not feel they impact the financial statements as evidenced by the audit opinion.

**Recommendations:**

We believe that FCC's continued efforts to meet its commitment to excellence in financial reporting have resulted in many positive changes in this year's financial reporting process. We still believe, however, that strong oversight from key financial and operational offices such as the CFO, Information Technology Center (ITC), and Administrative Office (AO), is needed to ensure that financial statements are prepared accurately and timely. We recommend the following:

1. Conduct an overall assessment of the financial management systems in use and the degree of integration needed. Prepare a plan outlining what the steps are (i.e., processes, data stewardship, management information, systems architecture, internal control), the timelines for completion, and the estimated cost to implement and maintain an integrated system.

**Management Comments:**

Management concurs. FCC reviewed several of its financial management systems and are at various stages of implementation. RAMIS will integrate with FFS for loans, fines and forfeitures, and eventually all receivables of the FCC. In addition, during FY 2001 FCC will review potential cost accounting systems which also will integrate with FFS.

2. Train FFS users to use the application software currently employed to ensure users can generate common widely-used reports (except for special reports) that are needed for account analysis without having to request the report be generated by another user (i.e., obtain the information needed efficiently and effectively through electronic means).

**Management Comments:**

Management concurs. FCC requested additional licenses to FFS data warehouse in order to provide broader access to report and query tools. Additional training classes for users will be conducted in FY 2001.

3. Establish and maintain an adequate audit trail used in preparing the financial statements. Modify as deemed appropriate and apply commonly used SGL crosswalks in preparing the principal financial statements.

**Management Comments:**

Management concurs. The crosswalks for FY 2001 were updated to incorporate the FY 2001 OMB crosswalks. In addition, financial reporting policies and procedures will be completed and implemented prior to FY 2001 close.

4. Identify and document in the accounting policies and procedures the transactions requiring elimination at the consolidated level and provide pro-forma eliminating entries.

**Management Comments:**

Management concurs. A section will be incorporated into the financial reporting policies and procedures that addresses elimination entries.

5. For intragovernmental transactions, accumulate the detail and summary information for each activity by trading partner by employing the following:
  - a) Incorporate the trading partner code as part of the account coding classification.
  - b) Incorporate the trading partner code in the customer/vendor identification code in accounts receivable/accounts payable systems.
  - c) Incorporate the trading partner code into data captured when transactions are entered into accounting systems.

**Management Comment:**

Management concurs and noted elements of this information is captured within FFS.

6. Update and correct FFS to comply with the transaction posting models consistent with SGL guidance and policies when recording and classifying transactions. Ensure that changes made to FFS are tested and accepted before they go into live production.

**Management Comments:**

Management concurs. FCC hired the developer of FFS to perform a review of the posting model and provide recommendations. Recommendations were received and many have been enacted in the system. All changes are tested and accepted prior to implementation.

7. Review all frequently used transaction types and transaction codes to ensure that the accounting entries (budgetary and proprietary) are correct.

**Management Comments:**

Management concurs and stated this type of review is now a part of the ongoing reconciliation process.

8. Record transactions on a timely basis. Proper cut-off should be implemented when preparing interim financial statements.

**Management Comments:**

Management concurs. As the quarterly financial preparation becomes more familiar, management believes cut-off procedures also will become better defined. As RAMIS and the new cost system are implemented, recordation times will improve.

9. Update and circulate to appropriate employees the Financial Coding Handbook. Ensure that appropriate employees receive adequate training.

**Management Comments:**

Management concurs and noted FCC currently distributes to all appropriate staff an updated version of the coding handbook at the beginning of each fiscal year. Additional training classes are being held in FY 2001.

10. Ensure compliance with the standards required in preparing MD&A as outlined in SFFAS 15. Specifically, discussions related to the future effects on the entity of existing, currently known demands, risks, uncertainties, events, conditions and trends should be included or expanded.

### **Management Comments:**

Management concurs. FCC will review the MD&A standards again as part of the FY 2001 financial preparation procedures.

11. Finalize written policies and procedures on the financial reporting processes. The written policies should provide sufficient guidance for the year-end closing of the general ledger as well as interim and annual financial statements' preparation and analysis. The procedures should at least address the following issues:
  - a) Prepare and review a complete set of financial statements in accordance with generally accepted accounting principles at least quarterly.
  - b) Establish milestones by setting dates for critical phases such as general ledger closing, preparation of statements, notes, and accountability report, quality control review, etc.
  - c) Collect common closing and adjusting entries in a formal listing, which is used when the general ledger is closed and financial statements are prepared.
  - d) Identify the individuals who will be involved in the financial reporting process and establishing clearly defined roles and responsibilities for the staff involved in the preparation of interim and year-end financial statements.
  - e) Prepare and retain all journal entries in sufficient detail with supporting documentation, and post all journal vouchers in the general ledger.
  - f) Retain all documentation supporting the request, purpose and approval of all object class designations. Also, a listing of all current object codes including a statement of the purpose of each code should be maintained and provided to all personnel with the responsibility to initiate, prepare, and approve accounting transactions to ensure that object codes are used appropriately.
  - g) Require supervisory review for all entries posted to the general ledger and consolidating financial statements. A supervisor should review revisions to previously approved entries and revised financial statements. All entries and review should be evidenced in writing.
  - h) Prepare and analyze formal monthly reconciliations of subsidiary and summary account balances. FCC should also consider a "formal closing" of all accounts at an interim date(s), which will reduce the level of accounting activity and analysis required at year-end. This "formal closing" entails ensuring that all transactions are recorded in the proper period through the month-end. With complete and timely transaction recording, analysis of all major accounts can be performed effectively.

- i) Utilize established tools (i.e., checklists, implementation guides, etc.) available for assistance in financial statement compilation and review.
- j) Prepare and retain a comprehensive set of files, working papers and other documentation in support of all information included in the financial statements. This documentation should be more self-explanatory than what has been retained in the past. The documentation should be at a supporting detail level where an accountant/auditor can utilize provided documentation for substantiation of reported data without extensive explanation or re-creation by the original preparer.

### **Management Comments:**

Management concurs noting policies and procedures for financial operations, which are being coordinated by a certified public accounting firm, will be implemented in FY 2001.

## **II. Cost Accounting System (Repeat Condition)**

FCC's cost accounting system has not been a fundamental part of the financial management system. Although cost reports are generated and distributed to various FCC bureaus and offices, the reliability of these reports is questionable due to the lack of review of the cost allocation methodology and formulas, and the lack of review of proper application of the cost accounting activity codes. The cost accounting system is so inadequate that FCC does not use its reports in preparing its financial statements or analyzing program costs. In addition, we do not believe that the employees from bureaus and offices outside of FO, who are responsible for financial-related activities fully understand the importance of properly coding the obligations/expenditures.

In order to prepare the Statement of Net Cost by program costs in fiscal year 2000, FCC downloaded program costs from its FFS into a spreadsheet application. Using the spreadsheets, the indirect costs were allocated to each of FCC's five programs proportionately to total direct costs. Although we believe that specific earned revenue should be matched against specific program costs in accordance with the program description in its budget submission to Congress, FCC also allocated earned revenue on the same basis used to allocate costs.

Additionally, FCC identified five responsibility segments for cost allocation purposes but it did not determine related outputs for its responsibility segments as part of its cost methodology. SFFAS No. 4, *Managerial Cost Accounting Standards*, states that management of each reporting entity should define and establish responsibility segments and managerial cost accounting should be performed to measure and report the costs of each segment's outputs. Reporting entities should report the full costs of outputs in general purpose financial reports. Specifically, for each segment, managerial cost accounting should:

- Define and accumulate outputs, and if feasible, quantify each type of output in units
- Accumulate costs and quantitative units of resources consumed in producing the outputs, and

- Assign costs to outputs, and calculate the cost per unit of each type of output.

SFFAS No. 4 states that cost accounting information must rely on consistent and uniform terminology for concepts, practices and techniques to be useful. Reliable information on the costs of the federal programs and activities is crucial for effective management of government operations. In managing Federal government programs, cost information is essential in (1) budgeting and cost control, (2) performance measurement, (3) determining reimbursement and setting fees and prices, (4) program evaluations, and (5) making economic choice decisions.

Although implementation of a cost accounting “system” is not necessarily a prerequisite for compliance with SFFAS No. 4, the agency’s cost system or cost finding techniques should meet the required minimum level of cost accounting necessary to accomplish the many objectives associated with planning, decision-making, and reporting. This minimum level, in accordance with SFFAS 4 includes:

- Collecting cost information by responsibility segments,
- Measuring the full cost of outputs,
- Developing appropriate costing methodology,
- Providing information for performance measurement,
- Instituting a reporting frequency that is timely and on a regular basis,
- Integrating both managerial cost accounting and general financial accounting utilizing the SGL,
- Providing the appropriate precision of information (i.e., reliable and useful),
- Accommodating management’s special cost information needs that may arise due to unusual or special situations or circumstances, and
- Documenting all managerial cost accounting activity, processes, and procedures (should outline applicable activities, provide instructions for procedures and practices followed, list the cost accounts and subsidiary accounts related to the SGL, and contain examples of forms and other documents used).

### **Management Comments:**

Management concurs. The current cost accounting system was designed before FCC faced meeting the requirements of SFFAS No. 4 and was designed to meet budgetary requirements and accounting requirements of the original regulatory fee and auctions program, not cost accounting requirements of the CFO Act. Realizing the need for a more comprehensive and integrated cost accounting system, FCC hired an outside contractor to develop the functional requirements for a new cost accounting system. Until a new system is implemented, FCC will rely on spreadsheet allocations to perform its cost allocation. Where possible, FCC will adjust its current methodology and review operations to identify associated outputs.

### **Recommendations:**

12. Review the propriety of the costing methodology and the matching of earned revenue against costs (costing methodologies).

13. Determine outputs for all responsibility segments as required.
14. Document the costing methodologies and process in a formal policy and procedures manual or handbook. Management should determine which cost objects to define, the costing methodology to use, the type of costs to include for each reporting or decision making purpose (i.e., full cost), and other items of a similar nature.

**Management Comments:**

Management concurs with Recommendations 12, 13 and 14. As part of its development of the Financial Reporting Policies and Procedures, FCC will review the current net cost methodology. The review will address responsibility segment outputs as well as earned revenue matching.

15. Evaluate the adequacy of the cost accounting system or other cost-finding techniques (cost systems) in accumulating and allocating costs, matching revenue, accounting, and generating financial information. The cost systems should meet the minimum requirements outlined in the Joint Financial Management Improvement Program (JFMIP) *System Requirements for Managerial Cost Accounting*.

**Management Comments:**

Management concurs. In the short-term, FCC is reviewing its net cost methodology to identify improvements. As a long-term solution, FCC hired an outside contractor to assist with the development of functional requirements for a new cost accounting system.

16. Ensure that appropriate employees of bureaus and offices fully understand the importance of properly classifying costs and are trained on the proper application of the activity codes.

**Management Comments:**

Management concurs. The Financial System Operations Group annually updates and distributes to all appropriate staff a coding handbook identifying the proper codes for the fiscal year.

### **III. Universal Service Fund and Telecommunication Relay Service Fund Financial Reporting (Modified Repeat Condition)**

The Universal Service Fund (USF), including the Telecommunication Relay Service Fund (TRS) is an additional reporting component FCC included in its consolidated financial statements. FCC management concluded in August 1999 that the USF was a reporting entity to be consolidated with FCC. This conclusion was based on criterion from the Statement of Federal Financial

Accounting Concepts (SFFAC) No. 2, *Entity and Display* that USF appears in FCC's Federal budget section titled, *Federal Programs by Agency and Account*. FCC also included the TRS Fund in its fiscal year 2000 financial statements. The USF is administered by Universal Service Administrative Company (USAC), a not for profit corporation, which through a contract with the National Exchange Carrier Association (NECA), maintains the USF accounting records and sends reports to the Department of the Treasury. The TRS Fund is managed by the NECA, which reports the program's financial information directly to FCC.

FCC is in an on-going process of reviewing USF (and TRS) activities. At this time, FCC cannot assure that USF or TRS Fund activities were in compliance with all laws and regulations, as the issue of which laws and regulations were applicable to the USF and TRS Fund was still unresolved at the end of the audit. FCC management should provide direction regarding the laws and regulations with which USF and TRS Fund should comply as well as guidance regarding the form and content of information needed for financial statement reporting purposes (see our Report on Compliance with Laws and Regulations, CFO Act.)

In addition, FCC did not provide adequate direction to USAC or NECA for the financial reporting of USF and TRS Fund activities. The FCC financial statements were prepared by consolidating information provided by USAC and NECA into the FCC statements. FCC included this financial data into its financial statements with limited or no review of the reasonableness, accuracy, and propriety of these amounts. FCC had no employee assigned to review the processes and procedures used to gather and report the financial information submitted to FCC. The USAC officials responsible for providing this USF information were unsure, however, as to what information was required and whether their systems could provide that information. For example, USAC originally provided information for the Statement of Budgetary Resources and the Statement of Financing without assurance that the input was required, and since the USAC accounting system did not include budgetary information, the financial information provided was less reliable. In addition, the figures reported for Accounts Payable, Payable to Providers, and Property, Plant and Equipment had to be reclassified because of differences between FCC and USAC. These reclassifications took place after a series of draft financial statements had been submitted for audit contributing to delays in completing the audit.

FCC management is responsible for obtaining reasonable assurance on the completeness and the reliability of the USF and TRS Fund financial reporting and its compliance with laws and regulations before information is consolidated into the FCC statements. This assurance was not obtained.

### **Management Comments:**

FCC and USAC expended considerable time and effort in assessing the applicability of Federal laws and regulations to the USF during FY 2000. The Office of General Counsel (OGC) provided analysis and USAC took required steps to comply with the applicable federal laws and regulations.

USAC management remains confident that USAC systems can provide whatever information is required. USAC's reported information was appropriately classified for the USF as a stand-alone entity. As part of the consolidation with FCC, reclassifications were expected and made. FCC and USAC will institute a formal financial reporting compilation process to ensure this process does not cause delay in subsequent years. USAC provided assurance to FCC on the completeness and reliability of the financial information provided as well as assurance USF is in compliance with applicable laws and regulations.

**Recommendations:**

FCC management is aware of the issue of oversight of USF and TRS Fund financial reporting. The following actions should be implemented early in fiscal year 2001 in order to avoid repeating the problems:

17. Document clearly the legal, financial, and operational boundaries of FCC, USF, TRS, USAC, and NECA. With the assistance of OGC, USAC, and NECA, FCC management needs to formally define in writing each financial management role and responsibility to avoid confusion and misunderstanding.

**Management Comments:**

Management concurs noting the relationship between FCC, USF, and USAC is already defined in the extensive regulations and Commission orders governing the operations of USAC and the USF. USAC or NECA will continue to seek guidance and clarification as necessary from the Commission.

18. Obtain from the OGC a list of laws and regulations applicable to the financial activities of USF and TRS Fund and communicate this information to officials of USAC and NECA. Ensure that USF and TRS Fund financial activities are in compliance with these laws and regulations by reviewing these activities periodically.

**Management Comments:**

FCC and USAC will continue to review compliance with applicable laws and regulations on at least an annual basis.

19. Assign one or more staff from FO to obtain an in-depth understanding of USF and TRS Fund operations, including financial operations, and who will work in coordination with Common Carrier Bureau (CCB) to comprehensively review financial and operational information provided by USAC and NECA.

**Management Comments:**

Management concurs. Throughout FY 2000, FCC and USAC established a stronger working relationship as it relates to compilation of the financial statements and

subsequent audit. To ensure the relationship fully develops, FCC assigned a member of the new Financial Statements and Policy Group to gain an in-depth understanding as recommended by the auditors. This staff member will work closely with USAC to provide guidance in the generation of quarterly and year-end financial statements and supporting documentation.

20. Review monthly financial reports provided by USAC and NECA. Request additional information from USAC and NECA as necessary to obtain reasonable assurance that the financial data is reliable.

**Management Comments:**

FCC started preparing quarterly statements during FY 2001 and has already contacted both USAC and NECA concerning the USF and TRS information needed for the statements.

21. Develop a formal financial reporting compilation process that adequately addresses issues arising from its consolidating reporting components.

**Management Comments:**

Management concurs stating FCC is documenting its financial reporting process as part of a policies and procedures manual that will be implemented during FY 2001.

#### **IV. Loans Receivable and Related Accounts (Modified Repeat Condition)**

FCC uses installment payment mechanisms to finance some of the spectrum sales to successful and qualifying bidders. These direct loans are accounted for in accordance with the Federal Credit Reform Act (FCRA) which requires that the cost of direct loans be estimated at present value for the budget. Loans servicing and collecting responsibilities were outsourced to FMS, until mid-1999 when FCC discontinued this arrangement and brought all aspects of the loan servicing in-house. Although FCC intended to transfer the loan servicing and collection responsibilities to a private contractor, it did not occur in fiscal year 2000.

In 1999, when the loan servicing was transferred in-house, FCC discontinued using the loan servicing system as its loan subsidiary system. However, the incumbent system continued to be used for other processes such as billings, collections, installment payment amounts and dates received. In 1999, FCC started using spreadsheet applications (loan models) developed by a public accounting firm (consultants) hired by FCC to verify that loan balances were valid, accurate, and auditable. These loan models were instituted as the loan subsidiary system. FCC planned to replace these loan models with RAMIS by September 30, 2000; however, this plan did not materialize according to the schedule. RAMIS is modified off-the-shelf software that will handle accounting for all collections and loan management within FCC and interfaces with other FCC financial systems. Consequently, FCC continued to use the loan models as its loan

subsidiary system with the assistance of the consultants in maintaining the loan models during fiscal year 2000.

**A. FCC Current Loan Subsidiary Ledger System Is Inadequate (Modified Repeat Condition)**

FCC's loan subsidiary ledger system is comprised of the loan models, which are elaborate and complex spreadsheets with configuration settings and information for original and adjusted loan principal, daily earned interest, suspension interest, payment data, and application of payments, among other items. These loan models (1) document the loan terms as determined by FCC's rules and official loan documents; (2) recalculate loan balances for financial statement reporting purposes; and, (3) serve as the cash flow model data for the loan subsidy model calculator.

Our review of the loan models showed that improvements were made to enhance the usefulness of the spreadsheets. Additional information such as tracking of changes to the database and raw collection data were added. However, deficiencies noted in prior year remained uncorrected. These are as follows:

- Configuration settings are still easily changed manually. Alteration of relevant configuration settings used in loan balance calculation could produce significantly different results. Once one user alters a setting, it would be difficult for another user to know what changes were made unless the user is notified.
- The loan models and the spreadsheet process lacked documented and approved policies and procedures for its use and review of key input and output data.
- The loan models' formulas are not protected to prevent inadvertent or unintentional modifications nor is there assurance that enter/modify access to the spreadsheet process is limited to authorized staff. We believe FCC should take ownership of these critical loan systems and its staff should be trained to be able to independently use the loan models and to review the reports generated by the model to reduce reliance on the accountants.
- Continued heavy reliance is still placed on the consultants who are responsible for the complete process (i.e., from data entry/download, to adjustments, to review, and to report generation).
- FCC still does not physically maintain an official and back-up soft copy of the loan models, with updated information at least monthly, until a new system is implemented.

During the fiscal year, a processing file was incorrectly uploaded into the spreadsheet application subsidiary system requiring subsequent review and additional resources to correct the effects of the upload. A condition as such should have been detected by FCC's oversight of its consultants and/or its internal control of loan processing activities.

Throughout the fiscal year, FCC has been reviewing the loans and related account balances. Loan review, as defined by FCC, is a process performed by the consultants to correct data in the loan models as a result of discovery, review, and additional information obtained. Some of these reviews accounted for:

- Unallowed suspension interest – interest was suspended for certain debtors that were ineligible for the suspension of interest. FCC has to recalculate the interest earned before the loans went in default and adjust the interest (suspension vs. regular interest, overstated vs. understated amounts) as appropriate.
- Incorrect billings in the amounts and due date which caused debtors to pay less and/or later than they were scheduled incurring non-delinquent late fees.
- Policy decisions finalized in fiscal year 2000 that affected the loan and related account balances.

As a result of these reviews, interest receivable of at least \$180 million was adjusted downward in fiscal year 2000.

Our audit disclosed that loan models have not been fully updated to reflect changes from the loan review made during the year, resulting in inconsistencies of loan data among the loan model, subledger, and the cash flow model used in the subsidy calculation. To illustrate, a loan on the loan model reflects a default date of 10/30/98, which is the default date as if the loan was eligible for suspension interest after non-payment of the first payment due date of 7/31/98. These dates were incorrect since the loan was later identified as ineligible for suspension of interest. The subledger and the cash flow model shows the correct default date of 8/28/97, after the non-payment of the first payment due date of 2/28/97. FCC explained these inconsistencies were due to inherent limitations with using the spreadsheet application as the loan subsidiary system.

Also, the limitations of the spreadsheet application loan models required FCC to create separate subsidiary ledgers to account for the interest receivable earned but not yet billed. Interest receivable earned includes interest receivable on defaulted loans after the last billing date but before the next billing date. The loan models were not developed to calculate the interest earned as of a cut-off date if it differed from the billing date.

Generally, the reviewing process was manually intensive requiring FCC to apply collections manually to correct situations (i.e., recalculating correct interest and creating/setting a temporary credit to adjust late fees charged mistakenly in the loan models). The risk of error in this temporary solution (loan models) is higher as a result of the aforementioned conditions.

### **Management Comments:**

Management concurs. As stated in FY 1999, FCC hired a public accounting firm to ensure installment loan balances were valid, accurate, and auditable. Technical security concerns did not allow FCC to implement RAMIS in FY 2000 as planned. To meet the obligation to provide sound, reportable, and auditable financial data, FCC extended a contractual engagement with the same firm to continue to provide information until such time as FCC was able to bring RAMIS on-line. Currently, FCC operates both systems and plans to migrate fully to RAMIS in time for FY 2001 close. FCC intends to transfer the loan portfolio

to an outside loan servicer who is required to provide timely financial data to FCC and ensure proper billing, collection, and reporting of loans.

The \$180 million interest adjustment was a combination of correcting interest reported as revenue in FY 1999 to FY 2000 and an accrual for FY 2000. Since FCC did not prepare a Statement of Net Cost for FY 1999, only a balance sheet adjustment was provided. The adjustment had a zero net effect to the FY 2000 financial statements.

## **B. Reconcile General Ledger to the Subsidiary Ledger Balances (Modified Repeat Condition)**

A major objective of internal control is to ensure the integrity of the underlying accounting data supporting the financial statements. An important control in this regard is the reconciliation of FCC accounting records. An adequate reconciliation provides the assurance that processed transactions are properly and timely recorded in the accounting records and financial statements, which then allows management the ability to analyze its financial condition and results of operations on a routine basis.

FCC does not reconcile its loans and related account balances in the general ledger to the subsidiary records. At year-end, entries are made to recognize the effects of the subsidiary records in the general ledger accounts. To record and track credit reform collections received throughout the year in fiscal year 2000, FCC established an SGL Account 2402, Unapplied Collections. Balances in SGL 2402 were then reallocated at year-end to principal, interest, late fees, etc. based on the application of payments made in the loan models. At September 30, 2000, FCC had approximately \$12 million still remaining in this account.

### **Management Comments:**

Management concurs. Loan collection activity is currently processed from a lockbox at a Federally insured bank and downloaded to FCC nightly. From this download, two identical files are produced. One file updates the cash balance in the Financing account and the duplicate file is fed into a subsidiary system that updates individual loan balances. Segregated reconciled balances are entered into FFS to decrease the unapplied collections and update other categories. Finalization of this process and reconciled balances were not completed for FY 2000 until year-end.

The \$12 million outstanding in unapplied collections represents identified amounts that could not be applied at year-end due to insufficient payor supplied information. This is less than 3% of \$650 million collected in FY 2000 and remains a consistent payment application issue for this dynamic portfolio. As the portfolio is transferred to RAMIS and the loan servicer, additional steps will be implemented to lessen the unapplied balance.

**C. Implement Direct Loan System to Account for All Events in a Loan Cycle (Repeat Condition)**

FCC's plan of implementing RAMIS did not materialize in fiscal year 2000 as explained above. During the fiscal year, FCC continued to rely on various systems and spreadsheet applications to account and report direct loan transactions. As a result, there is a higher risk of human error resulting in inconsistent and/or disparate data in various systems and programs. *Direct Loan System Requirements* issued by JFMIP states that a direct loan system must interact with the core financial system to perform fund control checks, initiate or record payments, record the results of other direct loan-related financial transactions, and acknowledge receipt of financial information exchange. It must be able to perform automatic system balancing to ensure that direct loan partners are able to agree on transaction number and dollar values passed, processed and rejected. This automated balancing includes cumulative subsidiary account balancing to the general ledger. It should be able to support managerial accounting. These internal management information requirements are those required to establish credit management and financial reporting systems that are in compliance with standards provided in OMB Circulars No. A-34, *Instructions on Budget Execution*; A-123, *Management Accountability and Control*; A-127, *Financial Management Systems*; and A-129, *Managing Federal Credit Programs*. See Auditor's Report on Compliance with Laws and Regulations.

**Management Comments:**

Management concurs. FCC recognized RAMIS would not be implemented by the close of FY 2000 and contracted with a major public accounting firm to provide loan accounting activities until RAMIS was implemented. During FY 2001 FCC's loan portfolio will transfer to a loan servicing financial institution; however, FCC will maintain both RAMIS and the public accounting firm through September 30, 2001 as backup.

**D. Loan Documentation Needs Improvement (Repeat Condition)**

In managing the Federal government's receivables, OMB Circular No. A-129, *Managing Federal Credit Programs* identified documentation as one of the loan servicing requirements. It states that approved loan files (or other systems of records) shall contain adequate and up-to-date information reflecting terms and conditions of the loan, payment history, including occurrences of delinquencies and defaults, and any subsequent loan actions which result in payment deferrals, refinancing, or rescheduling. Accurate and complete documentation is critical to providing proper servicing to the debtor and pursuing collection of delinquent debt.

Our review disclosed that FCC's loan file documentation is still inconsistent and incomplete. For instance, 29 of 45 (64%) loan files reviewed do not have a series of the FCC Form 175, "Application to Participate in an FCC Auction"; one (2%) loan file contains an installment payment plan note without signature; three (7%) loan files do not have Installment Payment

Plan notes; one (2%) file under an assignee name was not updated upon an exchange of the Security Agreement. Also, FCC discontinued updating payment history on that loan file.

The issue of loan file documentation needing improvement needs to be addressed as FCC changes its environment regarding loan business practices. The criticality of the issue increases as FCC progresses to outsourcing its loan servicing business practices and migrates to the new loan subsidiary system aforementioned.

**Management Comments:**

Management concurs. Over the past two years, FCC has been involved in ongoing efforts to fully document and update loan histories to ensure that loan balances are fully supported. Where information gaps are identified, FCC continues efforts to ensure completeness.

**Recommendations:**

Although FCC management has implemented controls since it took over the loan servicing operations, controls need to be fully implemented for effective and efficient loan management. Also, while expert consultants were hired to assist in the credit reform program, the accuracy, reliability, and reasonableness of source data is still FCC management's responsibility.

We recommend the following:

22. While RAMIS is not operational and FCC uses the loan models, it should:
  - a) Ensure that access to the loan models is limited to authorized staff.
  - b) Train FCC employees to have adequate knowledge in using and reviewing the loan models. If consultants are responsible for updating and analyzing the loan models, FCC employees should review, at least monthly, the configuration settings and formulas of the loan models to ensure they were not changed. In addition, FCC employees should review the outputs of the spreadsheets.
  - c) Develop written policies and procedures for the use and review of the loan models and related output.
  - d) Hardcode or lock cells with formulas in the loan models to prevent inadvertent or unintentional changes.

**Management Comments:**

Management concurs with Recommendations 22a, 22b, 22c, and 22d noting FCC initiated steps to ensure that agency personnel have copies of contractor's data models and reviews and comparisons are performed routinely.

- e) Physically obtain and keep an official copy of the loan models updated at least monthly since these are FCC's subsidiary records and are maintained by consultants outside of FCC financial management systems. A back-up copy should also be maintained.

**Management Comments:**

Management concurs noting FCC receives and maintains two backup copies of the models quarterly. As needed, FCC requests and receives monthly updates.

23. Ensure that the loan subsidiary system being developed and tested (RAMIS) is capable of interfacing with other financial management systems.

**Management Comments:**

Management concurs noting RAMIS testing is ongoing for all phases of implementation to ensure proper integration.

24. Ensure that RAMIS meets all the applicable requirements for a direct loan system in the Federal Financial Management System Requirements (FFMSR) issued by JFMIP. One of these requirements is to ensure that the direct loan system can support the following functions:

- Loan extension
- Account servicing
- Department of the Treasury cross-servicing
- Portfolio management
- Delinquent debt collection
- Other reporting requirements

**Management Comments:**

Management concurs and states RAMIS is in compliance with all FFMSR and JFMIP requirements. Management added the new loan servicer is also contractually bound to meet these requirements.

25. Record loan activities promptly to maintain their relevance and value to management in controlling operations and making decisions.

**Management Comments:**

Management concurs noting, as aforementioned, it expects complete SGL compliance at the transaction level within 24 hours of receipt of funds.

26. Reconcile general ledger balances to the subsidiary records on a monthly basis.

27. Ensure all loan files are kept up-to-date, have consistent information, and contain relevant loan and other documents necessary to conform to private sector standards.
28. Establish effective controls for transfer of loan data files to the new loan system, and ultimately, to a loan servicer, if employed.

**Management Comments:**

Management concurs with Recommendations 26, 27, and 28 stating controls are in place to ensure proper transfer and FCC will have an independent, public accounting firm verify the balance.

**V. Information Technology**

Our review and testing of controls related to Information Technology identified the following conditions (see our Report on Compliance with Laws and Regulations, Federal Financial Management Improvement Act):

**A. FCC Is Not In Compliance with OMB Circular No. A-130 Requirement for a Comprehensive Security Plan (Modified Repeat Condition)**

Some of the key components of an entity-wide security program are the performance of risk assessments and the development of a comprehensive security plan. Each organization needs a set of management procedures for identifying and assessing risks, and deciding what policies and controls are needed to achieve effective security controls.

OMB Circular No. A-130, *Management of Federal Information Resources*, Appendix III, "Security of Federal Automated Information Resources," as revised in February 1996, established a minimum set of controls for federal agencies, including risk assessments, assigning responsibility for security, security planning, periodic review of security controls, and management authorization of systems to process information.

Deficiencies in security controls that, in our view, significantly impact FCC's ability to protect its sensitive or critical resources include:

- FCC lacks a comprehensive and integrated security management structure. In such an environment, responsibilities could be unclear leading to the possibility of applying security controls inconsistently throughout the agency. As a result, certain vulnerabilities may be overlooked. In addition, monitoring the effectiveness of procedures for security controls throughout the agency will be ineffective.
- FCC has not performed risk assessments for its major application systems and its mission-critical general support system. FCC did perform vulnerability assessments for several of its major applications and general support systems in fiscal year 2000, but has

not completed risk assessments as prescribed by OMB Circular No. A-123, *Management Accountability and Control*.

- FCC does not have security plans for any of its major application systems and mission-critical general support systems. FCC plans to complete a template for its security plans by fiscal year 2001.
- There is no periodic review of security controls over FCC's systems. In addition, FCC has not performed any formal certification and accreditation of its systems. FCC plans to conduct initial security reviews over a two-year period ending in fiscal year 2002. FCC plans to make these reviews part of its internal control review process.

### **Management Comments:**

Management concurs. FCC developed a comprehensive and integrated security management structure. The basis for this structure was the creation and distribution of FCC Instruction 1479.1, *FCC Computer Security Program Directive*. The directive provides the framework for the Computer Security Program and assigns responsibilities for managing and using FCC computer resources and provides a framework to ensure an adequate level of protection to Commission computer-based systems.

FCC performed vulnerability assessments of several of the Commission's major applications during FYs 2000 and 2001 and contracted for the services required to complete necessary reviews. Also, FCC completed a risk assessment of its network in November 2000. In addition, the process for conducting such reviews was modified to ensure the inclusion of OMB Circular No. A-123, *Management Accountability and Control* issues. The process used by the assessment team includes the framework described in the National Information Assurance Certification and Accreditation Process (NIACAP).

FCC contracted services required to develop security plans for both its general support systems and major applications, as required by OMB Circular No. A-130, *Management of Federal Information Resources*, Appendix III. FCC's general support system security plan has been developed and is being reviewed by management. Several major application security plans are being developed and reviewed at this time and all remaining plans have been scheduled for development in FYs 2001 or 2002.

### **B. FCC Needs Improved Controls to Protect Its Information (Modified Repeat Condition)**

For a computerized-dependent organization like FCC, achieving an adequate level of information protection is highly dependent upon maintaining consistently effective access controls and system software controls. Access controls should limit and monitor access to computer resources (i.e., data files, application programs, and computer-related facilities and equipment) to the extent necessary to provide reasonable assurance that these resources are protected against waste, loss, unauthorized modification, disclosure, or misappropriation. Such controls include logical/technical controls, for example, security software programs designed to prevent or detect unauthorized access to sensitive data. Similarly, system software controls should limit and monitor access to powerful programs and sensitive files

that control computer processing and secure the application and data supported by the system.

Our limited internal controls testing identified information protection-related weaknesses in FCC's information systems environment. Impacted areas included FCC's distributed computer system as well as its mainframe computers. These vulnerabilities expose FCC and its computer systems to risks of external and internal intrusion, subject sensitive FCC information related to its major applications to potential unauthorized access, modification, and/or disclosure, and increase the risks of fraud, waste and abuse.

Rights and privileges granted to users of the Collections System are undefined. The system administrator is not aware of what access rights are granted to each level or class of access. The system has no password history file, and does not conform to Federal Information Processing Standards (FIPS) Publication 112 "Password Usage." Incompatible duties are not adequately segregated, with application programmers having access to production data sets and performing functions in the production environment. Audit logging has also not been activated and there is no monitoring of access activities.

FCC has not assessed the risk of not protecting sensitive and mission critical files. No written criteria have been established to guide security personnel in monitoring and restricting access to production data and program files. FCC does not have an entity-wide security program in place; it does not sufficiently address mainframe components of its computing environment.

**Management Comments:**

Management concurs. FCC continually works to improve the posture and effectiveness of the computer security program. In addition, the Computer Security Officer is working with application custodians and application level security representatives to ensure required and adequate levels of protection are provided and required tasks addressed. The most recent initiatives include implementing system risk assessments, certification and accreditation, security test and evaluations, and the preparation of system level security plans. While the referenced mainframe computer is not managed by FCC, management will work with the custodial Federal agency to mitigate noted issues.

**C. FCC Needs to Accelerate Efforts to Develop and Test its Contingency Plans (Repeat Condition)**

Losing the capability to process, and protect information maintained on FCC's computer systems can significantly impact FCC's ability to accomplish its mission to serve the public. The purpose of service continuity controls is to ensure that, when unexpected events occur, critical operations continue without interruption or are promptly resumed. To achieve this objective FCC should have (1) procedures in place to protect information resources and minimize the risk of unplanned interruptions and (2) a plan to recover critical operations should interruptions occur. These plans should consider activities performed at FCC's

general support facilities, as well as the activities performed by users of specific applications. To determine whether the disaster recovery plans will work as intended, FCC should establish and periodically test the capability to perform its functions in disaster simulation exercises.

Our review of FCC service continuity controls identified deficiencies that could affect FCC's ability to respond to a disruption in business operations as a result of a disaster or other long-term emergency. The deficiencies were as follows:

- FCC has not formally identified and prioritized all critical data and operations on its major applications and the resources needed to recover them if there is a major interruption or disaster.
- FCC has not formally identified and prioritized all critical data and operations on its networks and the resources needed to recover them if there is a major interruption or disaster. In addition, we could not determine whether FCC had established emergency processing priorities that will help manage disaster situations more effectively for the network.
- FCC has not integrated the contingency plans of its data centers, networks and telecommunication facilities in a comprehensive disaster recovery plan.

FCC is in the process of developing a comprehensive contingency plan. FCC plans to complete this effort by the end of fiscal year 2001.

**Management Comments:**

Management concurs. FCC plans to fund the development a Commission-wide Contingency of Operations Plan (COOP) in a multi-phased approach. The first phase includes the conduct of a business impact analysis to formally identify and prioritize all critical data and operations on major applications and the resources needed to recover if there is a major interruption or disaster. Upon completion, critical aspects of the COOP will be developed and tested.

**Recommendations:**

29. Establish a comprehensive and integrated security management structure to ensure that FCC's security policy is consistently applied.

**Management Comments:**

Management concurs stating FCC recently updated its computer security policy to reflect current computer and information security concerns and countermeasures. All computer security related policies are provided to each level of system level management to ensure consistency.

30. Conduct risk assessments for the FCC general support systems and major applications.

**Management Comments:**

Management concurs. FCC completed a risk assessment of its general support systems and its network in Fall 2000.

31. Develop and implement security plans for FCC's major application systems and mission-critical general support systems.

**Management Comments:**

Management concurs. FCC contracted for the required services to develop and implement security plans for its major application systems and mission-critical general support systems. Plans are being developed, using the guidance offered by National Institute of Standards and Technology (NIST), Special Publication 800-18, *Guidance on the Development of Security Plans*, to ensure compliance with OMB Circular No. A-130, Appendix III. The expected completion time frame of the plans is by second quarter FY 2002.

32. Certify and accredit FCC's major applications and general support systems, based on the security plans developed and implemented.

**Management Comments:**

Management concurs. FCC contracted for the required services to certify and accredit FCC's major applications and general support systems. These reviews are being conducted to ensure compliance with OMB Circulars No. A-123, A-127 and A-130, Appendix III. NIACAP is being used as the required model to support this effort. The expected completion time frame of the reviews is by fourth quarter FY 2002.

33. Establish a system to periodically review security controls over FCC's computer systems in accordance with OMB Circular No. A-130, *Management of Federal Information Resources*, Appendix III.

**Management Comments:**

Management concurs noting major application and general support system certification and accreditation review processes currently underway will allow for periodic review of these systems, as required by OMB Circular No. A-130, Appendix III.

34. Strengthen controls over access to protect all mainframe and client server-based resources.
35. Address inadequacies and inconsistencies in the mainframe and network access request process.

**Management Comments:**

Management concurs with Recommendations 34 and 35. FCC's Computer Security Officer will work directly with the administrators of the mainframe system, including network access request processes, to ensure adequate controls are implemented and test these processes.

36. Require periodic review of user privileges to ensure that capabilities are in line with job responsibilities.

**Management Comments:**

Management concurs. FCC's Computer Security Officer will develop a process to ensure Commission-wide compliance to require periodic review of user privileges to ensure capabilities coincide with job functions. The expected completion time frame for this effort is by second quarter FY 2002.

37. Enhance audit trail facility utilization and review.

**Management Comments:**

Management concurs. FCC's Computer Security Officer will develop and distribute a Commission-wide policy to make mandatory the use and review of appropriate system audit trail facilities within FCC, both at the general support and major application levels. The expected completion time frame of the plan is by first quarter FY 2002.

38. Develop and implement a FCC-wide security plan as prescribed by OMB Circular No. A-130, *Management of Federal Information Resources*.

**Management Comments:**

Management concurs. FCC contracted required services to develop and implement FCC-wide security plans for major application systems and mission-critical general support systems. These plans are being developed to ensure compliance with OMB Circular No. A-130, Appendix III and are being prepared using the guidance offered by NIST Special Publication 800-18, *Guidance on the Development of Security Plans*.

39. Develop and test contingency plans for FCC's major applications, networks, and telecommunications facilities.

**Management Comments:**

Management concurs. FCC noted the aforementioned COOP will address the recommendation.

40. Obtain written documentation from FCC's data centers of developed and tested contingency plans and participate in the scheduled tests of the plans.

**Management Comments:**

Management concurs. FCC's Computer Security Officer will obtain written documentation from its data centers of developed and tested contingency plans and request that FCC be able to participate in the scheduled future tests of the plans. The expected time frame for the completion of these plans is by the second quarter FY 2002.

41. Immediately develop a comprehensive contingency plan that integrates the individual plans of its data centers, networks, and telecommunications facilities.

**Management Comments:**

Management concurs and stated the contingency plan development team will factor in the integration of the FCC plan with those plans for non-FCC individual support data centers, networks, and telecommunications facilities.

## **REPORTABLE CONDITIONS**

### **VI. Review and Finalize Written Internal Control Documentation for Financial and Administrative Operations (Modified Repeat Condition)**

In response to last year's internal control report, FCC started to document its accounting policies and procedures related to various financial and administrative operations such as auctions; accounts receivable; property, plant, and equipment; accounts payable; payroll; and budget. All of the documents mentioned, except for the property, plant, and equipment and payroll, have not been finalized and require management review before finalization.

FCC's *Property Management Policies and Procedures* (manual), although finalized, has certain disconnects in definitions, policies, and procedures of property described in the manual versus the property items shown in the financial statements. The categories of personal property listed in the manual are Equipment, Software, Bulk Purchases, and Sensitive Property, while the note to the financial statements showed the categories as Furniture, Non-Computer Equipment, Computer Equipment, Bulk Purchases, Vehicle Systems, Broadcast Stations, Equipment, ADP Software, and ADP Software-In-Process. In addition, while reported separately as property in the notes of the financial statements, furniture is not mentioned in the manual as part of any category of property, nor is its inventory and valuation method, useful life, and disposal method described. These disconnects could result in confusion, misunderstanding, and inconsistencies in implementation of the policies and procedures.

Documented internal control and financial policies and procedures are a major part of managing an agency. These comprise the plans, methods, and procedures used to meet missions, goals, and objectives and in, doing so, support performance-based management. Internal control serves as the first line of defense in safeguarding assets and preventing and detecting errors and fraud. Documentation of control policies and procedures reduces the risk of misunderstanding, confusion, and inconsistent actions taken.

**Management Comments:**

Management concurs noting FCC has been developing a comprehensive policy and procedures manual. Upon completion, the manual will be placed on the FCC Intranet to provide easy access for staff. Additionally, management will conduct training sessions to familiarize staff with the new policies and procedures.

**Recommendations:**

We recommend that FCC:

42. Perform a global assessment of the financial and administrative operations that will require a written internal control policies and procedures manual. Consolidate all financial policies and procedures in a manual that is updated through controlled memoranda during the year. Update the manual for the memoranda changes annually or as necessary.

**Management Comments:**

Management concurs stating a global assessment was performed to identify sections to include in the manual under development. The procedures will include change procedures that control how and when policies and procedures are updated.

43. Perform an in-depth review of the draft and final written internal control policies and procedures manual to ensure that information is accurate, current as to the Federal internal control environment, and consistent with related documentation.

**Management Comments:**

Management concurs. Policies and procedures are being developed and are subject to management review throughout the process.

44. Ensure that FCC employees responsible for internal controls are provided with a copy of the internal control policies and procedures manual and are knowledgeable of the contents.

**Management Comments:**

Management concurs. As mentioned above, once completed the policies and procedures will be available via Intranet access.

45. Upon finalization of internal control policies and procedures manuals, conduct sufficient training of Commission personnel.

**Management Comments:**

Management concurs. A training plan will be developed to disseminate the information contained in the new manual.

**VII. Improve Internal Controls over Certain Accounts Receivable (Modified Repeat Condition)**

**A. Regulatory Fees**

The Omnibus Budget Reconciliation Act of 1993 requires FCC to collect regulatory fees to offset certain costs incurred in regulating its industry. The legislation also gives FCC the authority to review the regulatory fees and adjust the fees to reflect changes in its appropriation from year to year. It also authorizes FCC to charge a late payment penalty and to dismiss applications or revoke licenses for non-payment of the fees, and waive, reduce, or defer payment of a fee for good cause.

FCC's fee collection database is not linked to its licensing databases, making it difficult for FCC to perform routine automated checks on whether all licensees have paid their regulatory fee. In response to this weakness identified in the prior year report<sup>1</sup> and the GAO report<sup>2</sup>, FCC implemented the Commission Registration System (CORES), a commercial off-the-shelf software that will assign a specific FCC Registration Number (FRN) to a licensee to track all transactions related to that licensee. The FRN will be populated in RAMIS, and eventually linked to all the licensee databases in each bureau or office within FCC. Unfortunately, RAMIS was not operational during fiscal year 2000. In addition, CORES was not implemented until July 2000. The success of CORES as a complete database is yet to be evaluated due to the newness of the process and especially when registration in CORES is encouraged, not required.

To close the loop on the potential revenue gap from non-paying licensees, FCC instituted a new process for fiscal year 2000 collection after the regulatory fee payment deadline elapsed. The process requires FO (1) to send a list of entities that paid fees, along with the amount and

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<sup>1</sup> OIG Report titled, *Report on the Federal Communications Commission Fiscal Year 1999 Financial Statements* (00-AUD-01-01) dated July 7, 2000.

<sup>2</sup> GAO report titled, *Telecommunications: FCC Does Not Know If All Required Fees Are Collected* (RCED-99-216) dated August 31, 1999.

other relevant data to the appropriate bureaus and (2) to request that each bureau sends its lists of licensee/entities subject to the fee. A billing statement is then sent to licensees that were identified through this process. This process was labor intensive since FCC's organizational structure is decentralized with each bureau (program operation) still maintaining its own licensee database. These databases do not interface with each other or with the financial management system. In addition, the bureaus' databases do not always have the current status of a licensee.

In our review of the regulatory fees that were collected where there was a difference between the FCC estimated fee and the fee calculated by the licensee, we noted that FCC processed the licensee's lower amount without question or request for back-up documentation. While FCC stated that any differences are reviewed for further action, we found no evidence of this review in the files. Also, FCC believes that since its data is estimated based on historical data, the licensees' data will be more accurate. We believe that FCC, in order to assure itself that it is collecting appropriate amounts and its collection process is fair to all licensees, should review the basis of licensees' calculations when they differ substantially from the original estimate. This process will also assist FCC in estimating future regulatory fees. When discussed with management, FCC stated that it would now require the licensee to submit worksheets supporting their payment calculations.

## **B. Application-Processing Fees**

As authorized under Section 8 of the Communications Act of 1934, as amended, FCC collects application processing fees from applicants applying for certain licenses. Applicants submit a completed FCC application form with a "Remittance Advice" to a specific bank lockbox. The bank stamps the documentation with a received date, assigns a fee control number, deposits the payment with the Department of the Treasury, enters data from application into the fee collection database, and forwards the application documentation, and copies of proof of payments to FO. FO, without opening the application documentation package, forwards the package to the bureaus for processing.

As noted in our report last year and in the GAO report noted above, adequate documentation from the bureaus did not exist to show that application fees were paid. In addition, the bureaus' lack of access (read-only), whenever needed, to the fee collection database made it more difficult for them to verify proper payment of fees. FCC, in its responses, indicated that this weakness will be corrected by the implementation of RAMIS and CORES in fiscal year 2000. Unfortunately, as aforementioned, RAMIS was not operational, CORES was operational as of July 2000 and registration in CORES is voluntary, not mandatory.

Although FO noted that it has had requests for access to the Collections System from the bureaus to verify that proper payments were received and recorded in the system, the implementation of this verification process was not in effect for most of the fiscal year. Moreover, we do not believe that all bureaus requiring application-processing fees implemented this verification process.

In both the regulatory fee and the application-processing fee, there is a higher risk that fees required by legislation are not recorded and collected. Therefore, the conditions for a potential revenue gap still exist.

Internal controls, as used in OMB Circular No. A-123, *Management Accountability and Control* covers all aspects of an agency's operations (programmatic, financial, and compliance). Without integrated database systems accessible to all, and with the bureaus maintaining the customer database while FO maintains the collections data, the need for the bureaus (program) and the FO (financial) to coordinate and communicate in establishing and maintaining internal controls is mandatory.

**Management Comments:**

Management concurs. FCC noted deficiencies in the fee collection programs in 1998 and initiated comprehensive steps to fundamentally re-engineer the automated systems. FCC initiated steps to resolve issues originally identified in the GAO report. One major initiative is the implementation of two new systems, RAMIS and CORES. CORES assigns a specific FRN to a licensee that will be used to track all transactions related to that licensee. The FRN will be populated in RAMIS, and eventually linked to all the licensee databases in each bureau or office within FCC. Once RAMIS is operational, each phase of collections, whether it is the application fees or the yearly regulatory fees, will be processed through RAMIS. This will be extremely beneficial for the yearly regulatory fees because it will allow management to generate a record of each collection to be used as a basis for bill generation in subsequent years.

**Recommendations:**

FCC has initiated several manual processes and controls and has started implementing information technology systems to improve management of its account receivable. We recommend the following:

46. Ensure that RAMIS and CORES, when fully operational, address and provide solutions to weaknesses noted in our findings.

**Management Comments:**

Management concurs. FCC believes the systems will resolve the weakness.

47. Continue with the alternative procedures used to ensure that all fees are collected while the new systems are not fully operational. Improve on the procedures by evaluating the results of this year's manual processes used in identifying unpaid regulatory fees and maintain a historical record of the percentage of collections. Use this statistical information to determine how close actual payments are to FCC's estimate and adjust future estimates, if necessary.

**Management Comments:**

Management concurs. FCC plans to continue manually calculating unpaid regulatory fees until an automated system is implemented.

48. Document and implement standard procedures for bureaus to review payment of fees prior to processing an application. Verify compliance with the internal controls documented in the procedure manual.

**Management Comments:**

Management concurs. FO is working with the bureaus and offices to update its policies and procedures to ensure verification of payment of fees prior to processing an application or granting a right.

49. Increase communication and coordination between FO and the bureaus. Ensure that authorized bureau staff have at least read-only access to financial information relevant to their operations. The bureaus and FO should be proactive to the process instead of reactive.

**Management Comments:**

Management concurs. FO has taken a proactive approach to working with bureaus and offices on outstanding regulatory fee items and application fee issues.

50. Consider using CORES as a mandatory customer registration mechanism to ensure completeness of the database and consistent implementation of the registration procedures.

**Management Comments:**

Management concurs. FCC is currently addressing the full utilization of the FRN and CORES.

**VIII. Improve Supporting Documentation and Controls on Property and Equipment**

An agency must establish physical control to secure and safeguard vulnerable assets. Such assets should be periodically counted and compared to control records. Internal control and all transactions and other significant events need to be clearly documented, and the documentation should be readily available for examination. In addition, control activities help ensure that all transactions are completely and accurately recorded.

Although we were ultimately able to apply audit procedures to audit property and equipment, our review of property and equipment disclosed several internal control deficiencies as follows:

## **A. Inadequate Supporting Documentation**

- Documentation supporting 11 of 18 (61%) property sample items described in the property management system did not agree to the description on the property management system. The specific part and serial number on the supporting documentation was different from what was in the property management system.
- Three of eighteen (17%) sample items did not have receiving reports or packing slips to provide evidence of receipt.
- One of eighteen (6%) sample items did not have an invoice.
- One of eighteen (6%) sample items did not have an appropriate payment authorization.
- Two of eighteen (11%) sample items did not have a proof of payment such as an FFS disbursement document that ties to the property.
- Four of eighteen (22%) sample items did not have a required review/approval signature on one or more documents supporting the sample item.

## **B. Incorrect Dollar Values in the Property Records**

Six of eighteen (33%) sample items had incorrect dollar values in the property management records, requiring changes to be made when brought to the attention of FCC management.

## **C. Some Capitalized Costs Not Distinguished from Non-Capitalized Costs**

In reviewing accounting entries related to acquisition of certain equipment, we noted that the use of wrong budget object codes (BOC) resulted in capitalized costs not distinguished from non-capitalized costs. Specifically, ADP equipment acquisition was charged to BOC 3120, ADP Equipment, a BOC that is not to be used at the transaction level. FCC's *Financial Coding Handbook* (Fiscal Year 2000 edition) states BOC 3120 is to be used for budget allocation and operational transactions are not to be posted to it. Transactions are to be posted in FFS to either capitalized ADP equipment (BOC 3121) or non-capitalized ADP equipment (BOC 3122.) As a result, capitalized costs could not be distinguished from non-capitalized costs without a detailed account analysis.

### **Management Comments:**

Management concurs. FCC developed new processes and communications channels to improve property management and financial practices. Nevertheless, it recognized there is room for further advancement. FCC believes the shortcomings identified during the FY 2000 inventory/audit were directly related to insufficient personnel with the required training and experience in government asset management. To resolve the situation we have created four new positions to be filled in FY 2001: Inventory Operations Program Manager, Financial Audit Coordinator, Inventory Management Specialist, and Data Entry Clerk.

#### **D. Property Reconciliations Not Performed for Most of Fiscal Year 2000**

Property reconciliations were not performed for most of fiscal year 2000. We requested to see monthly reconciliations but were provided only with the June, July and September 2000 reconciliations.

##### **Management Comments:**

Management concurs recognizing property reconciliations were not performed for the entire year. FCC began addressing this issue as soon as the FY 1999 audit was completed; however, at that point several months had lapsed in FY 2000. In FY 2001, all months have and will be reconciled.

Our review of software acquisitions for completed and in-process transactions disclosed the following:

#### **E. Documentation Was Not Readily Available for Examination**

Overall, it took two months for FCC to obtain supporting documentation needed to vouch payments under multiple purchase orders to their respective software systems. Additionally, this documentation was provided after FCC performed an extensive review and search of software acquisitions. Audit procedures revealed that supporting documentation kept in files was disorganized, incomplete and not conducive to substantiation review. Information needed to compare specific purchase orders and payments with the software asset was not provided until after multiple requests and discussion.

##### **Management Comments:**

Management concurs. Capitalization of software was one of the final capital asset categories to be addressed, partly due to its complexity. FCC now has a system in place for identifying system costs as they are incurred and will be able to provide stronger and more timely support for FY 2001 balances.

#### **F. Documentation Did Not Demonstrate that Software Maintenance is Accurately Identified and Expensed**

FCC reports software as in process until it is certified for operation and classified as capitalized software subject to depreciation. FCC has been developing several software systems and each software system development life cycle can span for several years and involve multiple purchase orders. When purchase orders are originally prepared, they identify an accounting “string” of codes to be charged including the fund, SGL account, organization, BOC, etc. Since numerous payments may be made under the same purchase order, the payments are usually charged to the originally established accounting string, which may not be correct.

In our audit, the back up files for one of the capitalized software sample items included approximately \$40 thousand in payments that FO instructed ITC not to include in the cost of the asset because they were for software maintenance. We did not receive supporting documentation to assure ourselves that these payments were properly recorded.

Correct BOC classification has been an issue for FCC because often staff who enter BOC information in FFS are not knowledgeable of the differences in accounting for expenditures, (i.e., capitalized vs. non-capitalized, depreciable or expensed). The tendency is to charge the amount to the BOC already listed on the purchase order or invoice. Thus, if a purchase order is originally coded to capitalized software, and a payment relates to maintenance, it will normally be charged to the BOC originally coded on the purchase order or invoice.

### **Management Comments:**

Management concurs. The referenced asset for \$40,623, when researched by FCC staff with specific payment vouchers, was charged against BOC 2520, Contract Services – Non Federal, which is not a capitalized code. The BOC for this entry should have been 2572, ADP Software Maintenance. Neither of these BOCs represent capital expenses, therefore, the amount was properly expensed.

ITC will advise staff to pay close attention to the correct BOC usage. As part of the data collection activities underway for FY 2001, ITC has instituted necessary steps to ensure BOCs used are consistent with the ADP services provided. The Planning and Support Group (PSG) is reviewing all ITC-related service requests for proper BOC entries.

### **Recommendations:**

51. Include in the AO's procedures requirements that:

- a) The receiving unit prepares a receiving report when a packing slip is not included in the shipment.
- b) The receiving unit records all relevant asset information such as asset number, serial numbers and purchase order on the supporting documentation (order, receipt, and payment) to facilitate tracking and reconciliation of an asset in the property management system, in FFS, and the supporting documentation.
- c) Request assistance from the ordering office before assigning an asset number if there is any question as to how to assign asset and serial numbers to items received.
- d) For complex orders with multiple parts and lines in the purchase order, such as purchases of computer equipment or software, require the ordering office to provide instructions on the purchase order or other document sent to the warehouse or receiving unit as to how costs and assets are to be recorded in the master property record.

**Management Comments:**

Management concurs. FCC recognized the *Property Management Policies and Procedures* have certain “disconnects” in the definitions, policies, and procedures of property currently described. During the past year, FCC discovered many changes/updates which need to be incorporated into policies and procedures. FCC will ensure all financial policies and procedures and administrative requirements are captured in a revised edition.

52. Determine which office, FO or AO, is responsible for maintaining the completeness of supporting documentation. Consider including a checklist of relevant documentation that should be in an asset file to ensure completeness of supporting documentation.
53. To improve the accuracy of cost data in the management property record and the FFS, we recommend that FO:
  - a) Reconcile on a monthly basis the management property record and the FFS for capitalized assets and at least annually for non-capitalized assets.
  - b) Review FFS entries to ensure use of proper accounting BOC.
  - c) Restrict the use of budgetary BOC in FFS and train employees on the proper accounting entries.

**Management Comments:**

Management concurs with Recommendations 52 and 53 noting FCC has already acted on the recommendations.

54. To provide assurance that software maintenance costs are classified appropriately, we recommend that FO, working closely with ITC to:
  - a) Review capitalized software and software maintenance costs on a periodic basis.
  - b) Establish a formal mechanism to ensure that personnel responsible for knowing which costs are maintenance and which costs are developmental provide correct BOC guidance to personnel entering the information in FFS.
  - c) Provide training to appropriate personnel on proper allocation of costs to BOCs.

**Management Comments:**

Management concurs. Data is now being gathered and reviewed on a quarterly basis. Management noted it has collected the software inventory for the first quarter of FY 2001 and requested second quarter information. Management provided guidance to

Customer Service Representatives (CSR), Bureau and Office Contracting Officer Technical Representatives, and system owners on how to code maintenance versus development cost entries. The capture of data quarterly on software maintenance and development was formalized in September 2000 and is operational. All CSRs and PSG staff have been trained on the proper usage and data entry of both the procurement system and FFS and have been given documentation on the appropriate BOC definitions.

55. Ensure that software and systems' owners certify the transfer of a software system from development to operations (in-service) in order for the proper classification and proper depreciation of the asset.

**Management Comments:**

Management concurs stating FCC requires self-certifications quarterly from all system owners for their systems that have moved from development to production.

**IX. Improve Controls Over Accounts Payable (Modified Repeat Condition)**

FCC did not analyze its accounts payable on a routine basis to determine accuracy, reasonableness, and proper classification. Also, the accounts payable general ledger balance was not being reconciled to subsidiary records. Upon analysis of the subsidiary records, we noted vendors' accounts beginning with a Z code with a total of approximately \$15 million debit balances shown as outstanding accounts payable at September 30, 2000. A "Z" code is a vendor code in FFS that starts with the prefix Z. FCC could not initially explain the nature of the debit balances and had to research the issue. Eventually, FCC determined the debit balances were substantially due to auction up-front payments refunded to losing bidders from prior years activity dating back to at least 1996. When refunds were made, FCC debited accounts payable even though an accounts payable was not originally established.

FFS allows vendor accounts to be paid even without a payable being established, thus creating debit account balances. Although a correcting entry to reverse (or establish) an accounts payable was made when this error was discovered, the correcting entry was not matched with the vendor codes with debit balances. In addition, we noted numerous outstanding balances in the subsidiary ledger schedule being identified by a journal voucher, not by a vendor. We have identified at least 38 journal vouchers prepared to correct balances; most of these vouchers were not matched against a specific vendor balances. Also, FCC does not require all critical accounts payable fields such as the vendor balance field in FFS to be completed.

Standards for internal controls state that transactions are to be properly classified. Account balances should be analyzed on a periodic basis to ensure their propriety, accuracy, and timely detection of errors.

**Management Comments:**

Management concurs. FCC is aware of the issues identified with respect to accounts payable and has been working in FY 2001 to address the problems. Management affected several changes to the accounts payable subsidiary listing and a monthly reconciliation was established. FCC made a pointed effort to work with its fund managers in reviewing and eliminating stale accounts payable and unliquidated obligation balances during FY 2000. Management intends to continue improving this area for FY 2001.

**Recommendations:**

56. Review vendor account balances within the accounts payable subsidiary ledger.

**Management Comments:**

Management concurs. FCC added the vendor name to the monthly subsidiary listing so that vendor balances can be more easily identified. FCC will continue to work with its fund managers to conduct quarterly reviews of both accounts payable and unliquidated obligation balances.

57. Perform periodic reconciliation of the general ledger and the subsidiary ledger balances. Analyze the balances in the accounts periodically (monthly).
58. Activate user access controls and data entry field requirements to ensure that only appropriate activity is recorded in the accounts payable subsidiary ledger.

**Management Comments:**

Management concurs with Recommendations 57 and 58 and established a monthly reconciliation format and began reconciling accounts payable balances in FY 2001.

59. Minimize the use of journal vouchers. If a journal voucher has to be prepared, ensure that the appropriate subsidiary ledger is adjusted for the effect of the journal voucher.

**Management Comments:**

Management concurs stating wherever possible it will attempt to use transaction codes in order to establish and liquidate accounts payable.

60. Consider using a sub-SGL account (i.e., SGL 2110.1) to account for auction related payables. This will allow management to perform an effective and efficient review of the accounts payable and the auction-related transactions.

### **Management Comments:**

Management concurs stating it will consider a sub-SGL account in its general ledger structure.

### **X. Performance Goals and Results (Repeat Condition)**

The Government Performance and Results Act of 1993 (GPRA) places management expectations and requirements on federal agencies by creating a framework for more effective planning, budgeting, program evaluation, and fiscal accountability for federal programs. The intent of the GPRA is to improve public confidence in Federal agency performance, by holding agencies accountable for achieving program results, and to improve congressional decision-making by clarifying and stating program performance goals, measures, and costs “up front.” The annual financial statements is one medium for reporting performance goals and results.

In fiscal year 1999, FCC did not report performance goals and results in its MD&A. FCC explained that it was due to a problem in incorporating the provisions of GPRA into its annual financial statements, not due to lack of processes for identifying, assembling, analyzing, and reporting performance data, which we reported. In fiscal year 2000, FCC did include performance goals and results in its MD&A. These goals and results, however, could not be linked to the input (costs) as reported in the Statement of Net Cost. In addition, this information did not become available for our review until December 2000. There was no global list of performance goals and results (annual performance plans) where we could verify whether appropriate management and performance information was obtained at each level of organization. We could not verify the process where global performance goals and results are evaluated to determine the most significant activities and indicators for financial reporting purposes.

Goals and performance measures must be used in day-to-day management and built into the performance appraisal system to develop an understanding of the relationships between strategic goals and individual work assignments. GPRA’s objective is to manage for results. It offers a framework to integrate key management processes in order to provide policy and decision-makers with better information on program results and costs. Without timely feedback on the goals, results, and costs of a program, responsible managers are not able to use the valuable information to take action. As a result, GPRA becomes a useless paperwork exercise.

The FCC strategic plan provided to us was in draft and management intends to finalize it after the end of the audit. The reported measures of program and financial performance were consistent with information on major goals and objectives from the draft strategic plan but again, could not be linked to the program and costs featured in the Statement of Net Cost. The costs in the Statement of Net Costs are quantitative data for use in assessing or measuring the outputs and outcomes of specific performance indicators. As noted in item II of this report, FCC does not have adequate cost accounting systems to measure and report the costs of each segment’s outputs.

We believe that increased coordination and communication is still needed among the Performance Evaluation and Results Management Office (PERM - GPRA lead responsibility office), budget office, program offices (bureaus), and the fiscal accountability office (CFO's office) to ensure integration and consistency of processes, shared financial and operational information, and to promote understanding of the performance measurement system throughout the organization.

**Management Comments:**

Management concurs agreeing the goals and results reported in the MD&A section of the financial statements need to be linked to the Statement of Net Cost.

**Recommendations:**

61. Enhance communication and information sharing to achieve better results. Ensure that staff throughout FCC is aware of and managers are involved in setting organizational goals and objectives, regularly assessing progress, and making needed changes to help ensure success.
62. Use goals and performance measures in day-to-day management and build them into performance appraisal system to develop an understanding of the relationships between strategic goals and individual work assignments.
63. Increase coordination and communication among the PERM, budget office, program offices, and the CFO office. The CFO office should provide costs input in achieving the outputs and/or outcomes of performance goals.
64. Link objectives and performance measures to the strategic plan and the annual financial statements.

**Management Comments:**

Management concurs with Recommendations 61, 62, 63, and 64. Management noted there was continued and close coordination between all offices, bureaus, Budget Office, and Office of CFO. Any integration issues were the result of inadequate cost data, not inadequate coordination. As aforementioned, the CFO has begun work on designing a new cost accounting system.

**XI. OMB Circulars No. A-127 and A-130 Reviews (Repeat Condition)**

FCC has recently identified its major financial applications and general support systems, and established a timetable for meeting the requirements of OMB Circulars No. A-127, *Financial Management Systems* and A-130, *Management of Federal Information Resources* reviews of these applications. FCC plans to begin conducting OMB Circulars No. A-127 and A-130

reviews in Fiscal Year 2002. Until these reviews are performed and completed, FCC cannot determine compliance with these Circulars to include in its annual Federal Managers' Financial Integrity Act (FMFIA) report and ensure substantial compliance with Federal Financial Management Improvement Act (FFMIA).

**Recommendations:**

- 65. Institute a program for conducting periodic reviews in accordance with OMB Circulars No. A-127 and A-130.

**Management's Comments:**

Management concurs noting it contracted the required services to certify and accredit FCC's major applications and general support systems. These reviews are being conducted to ensure compliance with OMB Circulars No. A-123, A-127, and A-130, Appendix III.

- 66. Include the results of OMB Circulars No. A-127 and A-130 reviews as part of Section 4 reporting in FCC's annual FFMIA report.

**Management's Comments:**

Management concurs adding ITC staff will coordinate with FO staff to ensure summaries of financial application level reviews performed to comply with OMB Circulars No. A-127 and A-130 are included in FMFIA reports.

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In addition to the reportable conditions described above, we noted certain matters involving internal control and its operation that we reported to the management of FCC in a separate letter dated February 9, 2001.

This report is intended solely for the information and use of the management of FCC, FCC Office of Inspector General, OMB, and Congress, and is not intended to be, and should not be, used by anyone other than these specified parties. We caution that misstatements, losses, and noncompliance may occur and not be detected by the testing performed and that such testing may not be sufficient for other purposes.

*Clifton Gundersen LLP*

Calverton, Maryland  
February 9, 2001



## Independent Auditor's Report on Compliance with Laws and Regulations

To the Inspector General of the  
Federal Communications Commission

We have audited the Principal Statements (hereinafter referred to as "financial statements") of the Federal Communications Commission (FCC) as of September 30, 2000 and have issued our report thereon dated February 9, 2001. We conducted our audit in accordance with U. S. generally accepted auditing standards; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 01-02, *Audit Requirements for Federal Financial Statements*.

The management of FCC is responsible for complying with laws and regulations applicable to FCC. As part of obtaining reasonable assurance about whether FCC's financial statements are free of material misstatements, we performed tests of its compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of financial statements amounts, and certain other laws and regulations specified in OMB Bulletin No. 01-02, including the requirements referred to in the Federal Financial Management Improvement Act of 1996 (FFMIA). We limited our tests of compliance to these provisions and we did not test compliance with all laws and regulations applicable to FCC.

The results of our tests of compliance with laws and regulations described in the preceding paragraph, exclusive of FFMIA, disclosed instances of noncompliance with the following laws and regulations that are required to be reported under *Government Auditing Standards* and OMB Bulletin No. 01-02, which are described below.

### Chief Financial Officers Act of 1990 (CFO Act)

The Government Management Reform Act of 1994 (GMRA) amended the requirements of the CFO Act by requiring, among other things, the annual preparation and audit of organization-wide financial statements of 24 executive departments and agencies. Although FCC is not listed in OMB Bulletin No. 01-02, as one of the agencies required to comply with these requirements, management has voluntarily elected compliance and as such is being evaluated accordingly.

The government has a responsibility to use timely, reliable, and comprehensive financial information when making decisions, which has an impact on citizens' lives and livelihood. To

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meet this responsibility, the CFO Act establishes a leadership structure, provides for long-range planning, requires audited financial statements, and strengthens accountability reporting.

Specifically, the CFO Act establishes the authority, functions and responsibilities of a CFO. These include, among others, that a CFO:

- Develop and maintain an integrated accounting and financial management system that complies with applicable accounting principles, standards, and requirements; internal control standards; and requirements of OMB, the Department of the Treasury, and others;
- Direct, manage, and provide policy guidance and oversight of all agency financial management personnel, activities, and operations;
- Implement agency asset management systems, including systems for cash management, credit management, debt collection, and property and inventory management and controls.

FCC does not meet the above criteria as explained in more detail in our Report on Internal Control, items I through V. The key items we identified include:

- FCC was not able to prepare reliable and timely financial management information efficiently for managing current operations.
- FCC's financial management systems do not comply with certain accounting standards and requirements, and internal control standards.
- FCC's financial information system is not fully integrated and relies on data from various subsystems and spreadsheet programs for the accounting, preparing, and reporting of financial statements.
- Policy guidance for financial management personnel, activities, and operations are not formalized in writing, not updated, or not practiced effectively.
- Direction, policy guidance and oversight of Universal Service Fund (USF) financial operations are inadequate.

In addition, FCCINST 1102.3, a FCC internal controls directive that assigns management responsibility and procedures for establishing, maintaining, evaluating, and reporting on internal controls expired in May 2000. There was no directive in effect after the expiration date.

### **Debt Collection Improvement Act of 1996 (DCIA)**

DCIA requires agencies to notify the Department of the Treasury of all debts that are delinquent for more than 180 days for offset and for referral to the Department of the Treasury for cross-servicing debt collection. In FCC's "Treasury's Report on Receivable Due From The Public"

(TROR) for administrative receivables submitted to the Department of the Treasury as of September 30, 2000, it reported \$20 million as the amount eligible for referral for offset, however, only \$109,000 of the \$20 million was referred to Department of the Treasury for cross-servicing. When this discrepancy was brought to FCC management's attention, FCC reviewed the debt eligible and actually referred to the Department of the Treasury and determined that \$18 million of the \$20 million should be referred for cross servicing.

Also, FCC is responsible for reporting receivable due from public for the USF and Telecommunication Relay Service Fund (TRS.) FCC has not been submitting the TROR for USF and TRS until September 30, 2000, the first time it has submitted the reports. We were not provided with the September 30, 2000 TROR report for USF and TRS and therefore were not able to review the reports for compliance.

### **Government Performance and Results Act of 1993 (GPRA)**

The GPRA requires federal agencies to submit to OMB a strategic plan and annual performance plans that set goals with measurable target levels of performance; and annual program performance reports that compare actual performance to annual goals. Although FCC officials informed us that they had completed their annual performance plan and their annual program performance report, they did not provide copies of these reports to us. FCC officials indicated to us that these reports were either not released outside the agency or were still under management review as of the end of our fieldwork.

Our review of these GPRA reports is required by OMB Bulletin No. 01-02. Without having access to these reports, we cannot assess FCC's compliance with certain provisions of GPRA.

### **Recommendation**

We recommend that FCC comply with the provisions of GPRA and provide copies of these documents for our review as part of future financial statement audit.

### **Federal Financial Management Improvement Act of 1996 (FFMIA)**

Under FFMIA, we are required to report whether the agency's financial management systems substantially comply with the Federal financial management systems requirements, applicable Federal accounting standards, and the United States Government Standard General Ledger (SGL) at the transaction level. To meet this requirement, we performed tests of compliance with FFMIA section 803(a) requirements.

The results of our tests disclosed instances, described below, where FCC's financial management systems did not substantially comply with certain requirements referenced in the preceding paragraph. The following instances of noncompliance have been identified and such matters are described in more detail in our Report on Internal Control.

## Federal Financial Management Systems

Agency financial management systems shall comply with the Integrated Financial Management Systems as discussed in further detail in OMB Circular No. A-127, *Financial Management Systems*, Section 7. As described in more detail in our Report on Internal Control, items I, II, IV, and V,

- Integrated Financial Management Systems - FCC's core financial system (Federal Financial System) and feeder systems (direct loans systems and spreadsheets, cost systems, property management system, license database, collection systems, certain accounts receivable systems, procurement systems and various spreadsheets) are not integrated or electronically interfaced. A user is not able to have one view into systems such that, at whatever level the individual is using the system, he or she can obtain the information needed efficiently and effectively through electronic means. The primary reason of the noncompliance is due to FCC management's lack of priority for financial management systems' enhancements until recently. In the last two years, FCC has developed a long-term plan for the full implementation of enhancements and/or integration of its financial management systems.
- Financial Reporting – FCC was not able to provide timely and reliable financial information for managing current government operations. The primary reason of the non-compliance is that financial activities are not recorded, prepared and analyzed timely.
- Security – During our review of the Information Technology controls, we identified several weaknesses, which are collectively considered a material weakness and are described in more detail in our Report on Internal Control, item V. The weaknesses include lack of compliance with OMB Circular No. A-130's, *Management of Federal Information Resources*, requirement for a comprehensive security plan, lack of necessary controls to protect information, and lack of a fully developed and tested contingency plan. The primary reason for the noncompliance is due to FCC management's lack of review of its compliance requirements for financial management systems. FCC has developed a corrective action plan to achieve compliance with OMB Circular No. A-130 requirements by fiscal year 2001.

## Accounting Standards

Due to the lack of an adequate cost accounting system, FCC was not able to produce managerial cost information consistent with standards in Statement of Federal Financial Accounting Standard No. 4, *Managerial Cost Accounting Standards*, as described in our Report on Internal Control, item II.

### Standard General Ledger at the Transaction Level

Implementing the Standard General Ledger (SGL) at the transaction level requires transactions be recorded in full compliance with the SGL Chart of Account's descriptions and posting models/attributes that demonstrate how the SGL is to be used for recording transactions of the Federal government accounting process. As described in detail in our Report on Internal

Control, item I, FFS was not in substantial compliance with the SGL at the transaction level. Some of FFS's deficiencies include: out-dated SGL accounts, account titles, and cross-references; inaccurate natural balances; incorrect debit/credit postings; inconsistencies between certain FFS tables and posting models; and inaccurate closing accounts. The primary cause of this non-compliance is FCC's lack of review of its FFS system setup and posting model definitions for many years.

**Management Comments:**

Management concurs. The aforementioned laws and regulations are addressed within the findings on the Independent Auditor's Report on Internal Control. As FCC corrects and resolves identified issues, the occurrences of non-compliance will reduce.

\*\*\*\*\*

Providing an opinion on compliance with certain provisions of laws and regulations was not an objective of our audit and, accordingly, we do not express such an opinion.

This report is intended solely for the information and use of the management of FCC, FCC OIG, OMB and Congress, and is not intended to be and should not be used by anyone other than these specified parties. We caution that non-compliance may occur and not be detected by the tests performed and that such testing may not be sufficient for other purposes.

*Clifton Gundersen LLP*

Calverton, Maryland  
February 9, 2001

**SECTION V**

**STATUS OF RECOMMENDATIONS FROM  
PRIOR YEAR FINANCIAL STATEMENT AUDIT**

**SECTION V STATUS OF RECOMMENDATIONS FROM PRIOR YEAR FINANCIAL STATEMENT AUDIT**

Starting with fiscal year 1999, FCC’s financial statements have been subjected to audit pursuant to the CFO Act of 1990, as amended. The matrix consists of unresolved OIG recommendations to correct internal control conditions identified by previous examinations and their status as of the completion of the fiscal year 2000 audit. A determination as to status of the recommendations was based on the audit fieldwork at FCC and discussion with FCC officials.

Condition	Recommendations	Action Complete	Action in Progress	Action in planning or planning complete	No specific action planned
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<p><b>I. Material Weakness: Financial Reporting</b></p> <p>FCC was unable to complete principal statements other than a Consolidating Balance Sheet, Notes To The Consolidating Balance Sheet and some Required Supplementary Information.</p>	<p>We recommend the following:</p> <p>a) Develop and implement written policies and procedures on the financial reporting process. The written policies and procedures should provide sufficient guidance for the year-end closing of the general ledger as well as interim and annual financial statement preparation and analysis. The procedures should also address the following issues:</p>		X		
<p>FCC does not have a formalized financial reporting process to provide for the preparation of Financial Statements to meet the requirements of the CFO Act, hence, there is no written documentation of this process.</p>	<p>1) Preparing and reviewing a complete set of financial statements to be presented in accordance with generally accepted accounting principles;</p>		X		
	<p>2) Establishing milestones by setting dates for critical phases such as general ledger closing, preparation of statements, notes, and accountability report, quality control reviews, etc.;</p>	X			

**SECTION V STATUS OF RECOMMENDATIONS FROM PRIOR YEAR FINANCIAL STATEMENT AUDIT**

Condition	Recommendations	Action Complete	Action in Progress	Action in planning or planning complete	No specific action planned
	3) Collecting common closing and adjusting entries in a formal listing, which is used when the general ledger is closed and financial statements are prepared;	X			
	4) Identifying the individuals who will be involved in the financial reporting process and establishing clearly defined roles and responsibilities for the staff involved in the preparation of interim and year-end financial statements;	X			
	5) Preparing and retaining all journal entries in sufficient detail with supporting documentation, and posting all entries in the general ledger;	X			
Combination of reportable conditions may materially impact financial statements.	6) Retaining all documentation supporting the request, purpose and approval of all object class designations. Also, a listing of all current object codes including a statement of the purpose of each code should be maintained and provided to all personnel with the responsibility to initiate, prepare, and approve accounting transactions to ensure that object codes are used appropriately;	X			
Supervisory review for all stages of financial reporting needs strengthening.	7) Require supervisory review (written) for all entries posted to general ledger and consolidating financial statements. A supervisor should review revisions to previously approved entries.	X			

**SECTION V STATUS OF RECOMMENDATIONS FROM PRIOR YEAR FINANCIAL STATEMENT AUDIT**

Condition	Recommendations	Action Complete	Action in Progress	Action in planning or planning complete	No specific action planned
FCC does not prepare and analyze interim financial activity in certain areas to provide for preparation of the annual financial statements to meet requirements of the CFO Act.	8) Preparing and analyzing formal monthly reconciliations of subsidiary and summary account balances and preparing financial statements on a quarterly basis. FCC should also consider a “formal closing” of all accounts at an interim date, which will reduce the level of accounting activity and analysis at year-end. This “formal closing” entails ensuring that all transactions are recorded in the proper period through the month end. With complete and timely transaction recording, analysis of all major accounts can be performed effectively.		X		
	9) Preparing and retaining a comprehensive set of files, working papers and other documentation in support of all information included in the financial statements.		X		
Inadequate staff with the substantive knowledge necessary to address the financial accounting issues common to the current financial environment.	b) Reemphasize duties and responsibilities within the Financial Operations area to address CFO Act accounting and reporting requirements. Reevaluate internal resource distribution to accomplish this objective. Provide training to staff especially in regard to financial reporting policies and procedures related to meeting the requirements of the CFO Act.			X	

**SECTION V**

**STATUS OF RECOMMENDATIONS FROM  
PRIOR YEAR FINANCIAL STATEMENT AUDIT**

Condition	Recommendations	Action Complete	Action in Progress	Action in planning or planning complete	No specific action planned
FCC has not reviewed its cost allocation methodology and formulas.	c) Review the propriety of the cost allocation methodology and currency of allocation data. Document the cost allocation process methodology. The documentation will be useful in FCC’s review of the Statement of Net Cost allocation of appropriate costs and revenues to relevant programs in the future.			X	
<b>II. Material Weakness: Universal Service Fund Reporting</b>	a) We recommend that management obtain an explicit understanding of what the FCC reporting entity encompasses by clearly defining the legal, financial and operational boundaries of the FCC, USF, and USAC. With the assistance of FCC’s Office of General Counsel, FCC, and USAC (on behalf of USF), FCC management needs to formally define in writing each financial management role and responsibilities to avoid confusion and misunderstanding.			X	
	b) Ensure that USF financial activities are in compliance with laws and regulations by defining in writing, as part of the written document to be developed in (a) above, and reviewing these activities periodically.			X	

**SECTION V STATUS OF RECOMMENDATIONS FROM PRIOR YEAR FINANCIAL STATEMENT AUDIT**

Condition	Recommendations	Action Complete	Action in Progress	Action in planning or planning complete	No specific action planned
	c) Assign one or more staff from the Financial Operations area that will acquire or have an in-depth understanding of USF operations and who will work in coordination with Common Carrier Bureau (CCB) to comprehensively review financial information provided by USAC.			X	
	d) Review monthly financial reports provided by USAC. Request additional information from USAC as necessary to obtain reasonable assurance that the financial data is reliable.		X		
	e) Segregate USAC financial information from USF for financial statement reporting purposes. USAC is not a FCC reporting entity.	X			
<p><b>III. Material Weakness: Loans Receivable and Allowance for Subsidy</b></p> <p>FCC does not have an effective direct loan system to account for all events in a loan cycle.</p>	<p>We recommend the following:</p> <p>a) Ensure that the integrated credit reform accounting system currently being developed is capable of interfacing with other financial management systems.</p>		X		
	<p>b) Ensure that the direct loan system can support the following functions:</p> <ul style="list-style-type: none"> <li>• loan extension,</li> <li>• account servicing,</li> </ul>		X		

**SECTION V**

**STATUS OF RECOMMENDATIONS FROM  
PRIOR YEAR FINANCIAL STATEMENT AUDIT**

Condition	Recommendations	Action Complete	Action in Progress	Action in planning or planning complete	No specific action planned
	<ul style="list-style-type: none"> <li>• Treasury cross-servicing,</li> <li>• portfolio management,</li> <li>• delinquent debt collection, and</li> <li>• other reporting requirements.</li> </ul>				
Current FCC subsidiary ledger system is inadequate and FCC did not review the results of contractor subsidiary spreadsheets.	c) Ensure that access to subsidiary spreadsheets is limited to authorized staff. These employees should be trained to have adequate knowledge for use and review of the spreadsheets. If an independent public accounting firm is responsible for updating the spreadsheets, FCC employees should review, at least monthly, the configuration settings and formulas of the spreadsheets to ensure they were not changed. In addition, FCC employees should review the outputs of the spreadsheets. Written policies and procedures should be developed for the use and review of the spreadsheets and related output.		X		
	d) Hardcode or lock cells with formulas in the spreadsheets to prevent inadvertent or unintentional changes.		X		
	e) Perform monthly reconciliation of the loans general ledger and subsidiary ledger balances.		X		

**SECTION V STATUS OF RECOMMENDATIONS FROM PRIOR YEAR FINANCIAL STATEMENT AUDIT**

Condition	Recommendations	Action Complete	Action in Progress	Action in planning or planning complete	No specific action planned
	<p>f) Physically obtain and keep an official copy of the spreadsheets updated at least monthly since the spreadsheets are the FCC's subsidiary ledger system and are being maintained by independent public accounting firm outside of FCC financial management systems. A back-up copy should also be maintained.</p>		X		
<p>FCC encountered difficulties in providing sufficient documentation and rationale to support a change in key cash flow assumptions that resulted in a material downward subsidy reestimate.</p>	<p>g) Ensure that support for subsidy estimates and reestimates are adequately documented, reviewed, and approved on a timely basis. Ensure that applicable documentation listed below is available to support subsidy estimates and reestimates:</p> <ul style="list-style-type: none"> <li>• Cash reports on historical performance;</li> <li>• Historical data and trends, citing sources of information and relevant time frame;</li> <li>• Sensitivity analysis or other analysis that identifies the most critical factors;</li> <li>• Reports from the accounting or management systems showing trends;</li> <li>• Actuarial studies;</li> <li>• Experience of other agencies with similar programs; and</li> <li>• Economic and/or industry data and subsequent analyses, including industry</li> </ul>		X		

**SECTION V STATUS OF RECOMMENDATIONS FROM PRIOR YEAR FINANCIAL STATEMENT AUDIT**

Condition	Recommendations	Action Complete	Action in Progress	Action in planning or planning complete	No specific action planned
	studies, journal articles, trade papers, and third party studies.				
	h) Compare actual cash flows with projected cash flows and actual costs of direct loans with their estimated costs. The efforts to make accurate projections should begin with establishing and using reliable records of historical credit performance data, and should take into consideration current and forecasted economic conditions.		X		
FCC loan files were found to be incomplete and documents in files were inconsistent.	i) Ensure that all loan files are kept up-to-date, have consistent information, and contain relevant loan documents.		X		
	j) Reconcile with all trading partners, i.e., Department of the Treasury Financial Management Service and Bureau of Public Debt, on a timely and periodic basis. Obtain and maintain evidence from trading partners to support all transactions.		X		
	k) Establish effective controls for transfer of loan data files to the new loan system, and ultimately to the loan servicer, if employed.		X		
<b>IV. Material Weakness: Information Technology</b>	We recommend the following: a) Establish a comprehensive and integrated security management structure to			X	

**SECTION V STATUS OF RECOMMENDATIONS FROM PRIOR YEAR FINANCIAL STATEMENT AUDIT**

Condition	Recommendations	Action Complete	Action in Progress	Action in planning or planning complete	No specific action planned
FCC is not in compliance with OMB Circular A-130 Requirement for a comprehensive security plan.	ensure that FCC's security policy is consistently applied.				
	b) Conduct risk assessments for the FCC networks and its major applications.			X	
	c) Develop and implement a FCC-wide security plan as prescribed by OMB Circular A-130.		X		
	d) Develop and implement security plans for FCC's major application systems and mission-critical general support systems.		X		
	e) Certify and accredit FCC's major applications and mission-critical general support systems, based on the security plans developed and implemented.		X		
	f) Establish a system to periodically review security controls over FCC's computer systems in accordance with OMB Circular A-130 Appendix III.		X		
FCC needs improved controls to protect its information.	g) Strengthen controls over access to protect all mainframe and client server based resources.		X		
	h) Address inadequacies and inconsistencies in the mainframe and network access request process.		X		
	i) Require periodic review of			X	

**SECTION V STATUS OF RECOMMENDATIONS FROM PRIOR YEAR FINANCIAL STATEMENT AUDIT**

Condition	Recommendations	Action Complete	Action in Progress	Action in planning or planning complete	No specific action planned
	user privileges to ensure that capabilities are in line with job responsibilities.				
	j) Enhance audit trail facility utilization and review.			X	
FCC needs to accelerate efforts to develop and test its contingency plans.	k) Develop and test contingency plans for its major applications, network and telecommunications facilities.			X	
	l) Obtain written documentation from its data centers of developed and tested contingency plan, and participate in the scheduled tests of the plans.			X	
	m) FCC management should immediately develop a comprehensive contingency plan that integrates the individual plans of its data centers, networks and telecommunications facilities.			X	
<b>V. Material Weakness: Controls Over Property, Plant, and Equipment</b>	We recommend the following:				
	a) Reconcile the general ledger control to subsidiary records at least monthly for now and at least quarterly once both offices are comfortable with the process and the data.		X		
	b) Improve coordination and communication between Financial Operations and Administrative Operations.			X	
	c) Review certain expense accounts (repairs and maintenance, EDP, and other related accounts)			X	

**SECTION V**

**STATUS OF RECOMMENDATIONS FROM  
PRIOR YEAR FINANCIAL STATEMENT AUDIT**

Condition	Recommendations	Action Complete	Action in Progress	Action in planning or planning complete	No specific action planned
	periodically to ensure that FCC meets FASAB standards for capitalization.				
	d) Ensure that information entered into the current management system is proper and supported by adequate documentation. Acquisition dates and life of assets should be reviewed to ensure that depreciation is properly calculated.		X		
	e) Maintain all copies of supporting documentation in an organized manner and in a centralized location, including documentation from field offices. Supporting documentation should be easily retrievable for management and others' review.		X		
	f) Assign a property custodian to each office or bureau, including field offices. Require the property custodian to certify that he/she has read and understood the duties and responsibilities of the position as documented in the property management policies and procedures. Provide training to property custodians and ensure that the Contracts and Purchasing Center maintain a current list of property custodians at all times. This will reduce the risk that		X		

**SECTION V**

**STATUS OF RECOMMENDATIONS FROM  
PRIOR YEAR FINANCIAL STATEMENT AUDIT**

Condition	Recommendations	Action Complete	Action in Progress	Action in planning or planning complete	No specific action planned
	property may not be recorded and tracked in the property management system.				
	g) Perform a complete annual physical inventory until FCC is assured that its property management system has accurate and up-to-date information. Perform the annual physical inventory on a cycle or selective basis only after this assurance is obtained.	X			
	h) Ensure that the draft Property Management Policies and Procedures manual is complete, facilitates compliance with generally accepted accounting principles, and is issued promptly to provide guidance to FCC staff. Control all updates or changes to the manual by a sequential tracking numbering system and update the entire manual on an annual basis, if necessary.	X			
	i) Implement policies and procedures to provide for review and evaluation of deferred maintenance to permit proper presentation for financial reporting purposes.	X			
<b>VI. Material Weakness: Unfunded Liability</b>	We recommend that FCC obtain sufficient evidence to support the amount recorded as a liability or reverse this liability.	X			

**SECTION V**

**STATUS OF RECOMMENDATIONS FROM  
PRIOR YEAR FINANCIAL STATEMENT AUDIT**

Condition	Recommendations	Action Complete	Action in Progress	Action in planning or planning complete	No specific action planned
	In addition, FCC management should review the validity and accuracy of supporting documentation prior to agreeing to and recording any such liability.				
<b>VII. Reportable Condition: Lack of Written Internal Control Documentation for Financial Operations</b>	We recommend that FCC:  a) Formalize its financial and internal control policies and procedures in writing. Design internal controls to provide reasonable assurance regarding prevention of, or prompt detection of unauthorized acquisition, use, or disposition of an agency's assets. Internal control is a series of actions and activities that occur throughout the operations and on an ongoing basis.		X		
	b) Physically maintain the written control policies and procedures in a central location within the Office of the CFO. All changes or updates to the written policies and procedures should be controlled.		X		
	c) Ensure that FCC employees responsible for internal controls are provided with a copy of the internal control policies and procedures manual and are knowledgeable of its contents		X		
<b>VIII. Reportable</b>	We recommend the following:  a) Ensure that the new systems		X		

**SECTION V STATUS OF RECOMMENDATIONS FROM PRIOR YEAR FINANCIAL STATEMENT AUDIT**

Condition	Recommendations	Action Complete	Action in Progress	Action in planning or planning complete	No specific action planned
<b>Condition: Accounts Receivable (Regulatory Fees and Application Processing Fees)</b>	[Revenue Accounting and Management Information System (RAMIS) and Commission Registration System (CORES)] address and provide solutions to weaknesses noted in our findings.				
	b) Implement alternative procedures to ensure that all regulatory fees are collected, late fees are assessed, and receivables are accrued while the new systems are not operational. Obtain cooperation and assistance from the bureaus in determining the licensees in their databases and compare licensee payment information to the licensee on the databases.	X			
	c) Increase communication and coordination between Financial Operations and the bureaus. Ensure that authorized bureau staff have at least read only access to financial information relevant to their operations.	X			
	d) Document and implement procedures for bureaus to review payment of fees prior to processing an application.		X		
	e) Implement procedures to ensure that collections processed by third party bank are processed and analyzed by FCC timely.	X			

**SECTION V STATUS OF RECOMMENDATIONS FROM PRIOR YEAR FINANCIAL STATEMENT AUDIT**

Condition	Recommendations	Action Complete	Action in Progress	Action in planning or planning complete	No specific action planned
	To facilitate FCC review and analysis, consider modifying the bank’s report to include other relevant information such as date collection is received and date collection is deposited with the Department of the Treasury.				
	f) Ensure that appropriate and valid data are used in calculating late fee assessments.		X		
<b>IX. Reportable Condition: Accounts Payable, Undelivered Orders, and Net Position</b>	We recommend that FCC: a) Reconcile accounts payable and UDO general ledger control with their subsidiary records monthly.		X		
	b) Ensure that electronic purchase order is complete, including completing the “responsible person” prior to its processing.				X
	c) Ensure payment sheets are completed and updated timely and perform periodic review and reconciliation of purchase orders and contracts.	X			
	d) Enforce the obligation certification process and work with Fund Managers to ensure year-end review of contracts and purchases occurs. FCC may consider requiring Fund Managers to provide justification for keep old undelivered orders open.	X			

**SECTION V**

**STATUS OF RECOMMENDATIONS FROM  
PRIOR YEAR FINANCIAL STATEMENT AUDIT**

Condition	Recommendations	Action Complete	Action in Progress	Action in planning or planning complete	No specific action planned
	e) Ensure that supervisors review supporting documentation for completeness, accuracy, and appropriateness before transactions are entered into FFS.	X			
<b>X. Reportable Condition: Treasury Fund Suspense Account Activity</b>	We recommend that the suspense balance is researched and appropriate correcting entries are made.		X		
<b>XI. Reportable Condition: Performance Measurement</b>	We recommend to:  a) Define the process and implement a mechanism for identifying, assembling, and analyzing, and reporting performance data. The documented process should include, at a minimum, the staff responsible for preparation and review, formulas, due dates, sources of data, review and analysis methodology, and supervisory verification and report retention.		X		
	b) Reevaluate performance goals and indicators reported in the strategic plan and ensure that the performance goals are outcome oriented.	X			
	c) Establish a formal commission-wide system for tracking the indicators such as integrated system databases.	X			

**SECTION V STATUS OF RECOMMENDATIONS FROM PRIOR YEAR FINANCIAL STATEMENT AUDIT**

Condition	Recommendations	Action Complete	Action in Progress	Action in planning or planning complete	No specific action planned
	d) Enhance the communication and coordination among key offices (PERM, CFO, Budget) responsible for the successful implementation of the GRPA.		X		
<b>XII. Reportable Condition: OMB Circulars No. A-127 and A-130 Reviews</b>	We recommend to: a) Institute a program for conducting periodic reviews in accordance with OMB Circulars A-127 and A-130.		X		
	b) Include the results of OMB Circulars A-127 and A-130 reviews as part of Section 4 reporting in FCC's annual FMFIA report.		X		
<b>XIII. Reportable Condition: FMFIA</b>	We recommend that FCC review its procedures in developing its FMFIA report to ensure all material weaknesses for all entities for all entities and operations are reported.		X		

## **SECTION VI**

### **ACRONYMS**

AO	Administrative Offices
BOC	Budget Object Code
CCB	Common Carrier Bureau
CFO Act	Chief Financial Officers Act of 1990
CG-LLP	Clifton Gunderson LLP
COOP	Contingency of Operations Plan
CORES	Commission Registration System
CSR	Customer Service Representative
DCIA	Debt Collection Improvement Act of 1996
FACTS	Federal Agencies' Centralized Trial-Balance System
FASAB	Federal Accounting Standards Advisory Board
FCC	Federal Communications Commission
FCRA	Federal Credit Reform Act of 1990
FFMIA	Federal Financial Management Improvement Act of 1996
FFMSR	Federal Financial Management System Requirements
FFS	Federal Financial System
FIPS	Federal Information Processing Standards
FMFIA	Federal Managers' Financial Integrity Act of 1982
FMS	Financial Management Service
FO	Financial Operations
FRN	FCC Registration Number
GAO	Government Accounting Office
GMRA	Government Management Reform Act of 1994
GPRA	Government Performance and Results Act of 1993
ITC	Information Technology Center
JFMIP	Joint Financial Management Improvement Program
MD&A	Management's Discussion and Analysis
NECA	National Exchange Carrier Association
NIACAP	National Information Assurance Certification and Accreditation Process
NIST	National Institute of Standards and Technology

**SECTION VI            ACRONYMS**

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OGC	Office of General Counsel
OIG	Office of Inspector General
OMB	Office of Management and Budget
OMB Bulletin No. 97-01, as amended	OMB Bulletin No. 97-01, "Form and Content of Agency Financial Statements"
PERM	Performance Evaluation and Results Management Office
PSG	Planning and Support Group
RAMIS	Revenue Accounting and Management Information System
SFFAC	Statement of Federal Financial Accounting Concepts
SFFAS	Statement of Federal Financial Accounting Standards
SGL	Standard General Ledger
TROR	Treasury's Report on Receivables
TRS	Telecommunication Relay Service Fund
USAC	Universal Service Administrative Company
USF	Universal Service Fund