



Office of Inspector General

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

AUD-FM-17-42

Office of Audits

May 2017

# Audit of Department of State FY 2016 Compliance With Improper Payments Requirements

## FINANCIAL MANAGEMENT DIVISION

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# OIG HIGHLIGHTS

AUD-FM-17-42

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Financial Management Division

## Audit of Department of State FY 2016 Compliance With Improper Payments Requirements

### What Was Found

Kearney found that the Department was in compliance with improper payments requirements for FY 2016, as presented in Table 1.

**Table 1: Compliance with Improper Payment Criteria**

Improper Payment Criteria	Compliance
Conducted Risk Assessment	Yes
Published Agency Financial Report	Yes
Published Estimate	Not applicable*
Published Corrective Actions	Not applicable*
Published and Met Reduction Targets	Not applicable*
Published Error Rate Less than 10 percent	Not applicable*

\* These requirements apply only to agencies that have identified programs susceptible to significant improper payments.

**Source:** Kearney prepared using criteria from the Office of Management and Budget Circular A-123, Appendix C.

Kearney found that the Department performed the required risk assessments using criteria defined by OMB Circular A-123 for all programs meeting minimum thresholds. However, the CGFS process for performing risk assessments did not consider the results of some OIG audit reports. By improving its quality control procedures, the Department may improve its conclusions related to the susceptibility of some programs to improper payments.

In addition, the Department published its FY 2016 AFR on its website and the AFR included the required improper payment disclosures. Although the Department included all required disclosures, some optional information on improper payments identified outside of the payment recapture process was not provided. Because much of this information is available, it would be prudent and useful to the users of the AFR to include this information.

### What Was Audited

In FY 2016, improper Federal payments Government-wide totaled approximately \$144 billion. The Improper Payments Information Act (IPIA), as amended, requires Federal agencies to annually identify programs and activities at high risk of improper payments and estimate the amount of improper payments, among other requirements. In addition, inspectors general are required to annually determine whether agencies are in compliance with improper payments requirements.

Acting on behalf of the Office of Inspector General (OIG), Kearney & Company, P.C. (Kearney), an independent certified public accounting firm, conducted this audit to determine whether the Department of State (Department) was in compliance with IPIA, as amended.

### What OIG Recommends

OIG made five recommendations to the Bureau of the Comptroller and Global Financial Services (CGFS) to address areas identified in this report that can be improved, including refining quality control procedures in the risk assessment process and reporting optional information in the Agency Financial Report (AFR).

CGFS concurred with all the recommendations, which OIG considers resolved, pending further action. The CGFS response and OIG's reply follow each recommendation in the Audit Results section of this report. The CGFS response to a draft of this report is reprinted in its entirety in Appendix C.

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## Audit of Department of State FY 2016 Compliance With Improper Payments Requirements

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

Kearney & Company, P.C. (Kearney), has performed an audit of the Department of State FY 2016 compliance with improper payments requirements. This performance audit, performed under Contract No. SAQMMA14A0050, was designed to meet the objective identified in the report section titled "Objectives" and further defined in Appendix A, "Purpose, Scope, and Methodology," of the report.

Kearney conducted this performance audit from January 2017 through April 2017 in accordance with *Government Auditing Standards*, 2011 Revision, issued by the Comptroller General of the United States. The purpose of this report is to communicate the results of Kearney's performance audit and its related findings and recommendations.

Kearney appreciates the cooperation provided by personnel in Department of State offices during the audit.

A handwritten signature in blue ink that reads "Kearney &amp; Company". The signature is stylized and cursive.

Kearney & Company, P.C.  
Alexandria, Virginia  
May 8, 2017

# CONTENTS

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OBJECTIVE.....	1
BACKGROUND .....	1
Department of State Payments.....	2
AUDIT RESULTS.....	3
Finding A: Program Risk Assessments Were Performed, but Quality Control Procedures Could Be Improved .....	4
Finding B: Agency Financial Report Was Published and Included Required Disclosures, but Some Optional Information for One Disclosure Was Incomplete .....	7
RECOMMENDATIONS .....	11
APPENDIX A: PURPOSE, SCOPE, AND METHODOLOGY .....	12
Prior Reports.....	13
Work Related to Internal Controls .....	14
Use of Computer-Processed Data.....	14
APPENDIX B: PRIOR OIG RECOMMENDATIONS.....	15
APPENDIX C: THE BUREAU OF THE COMPTROLLER AND GLOBAL FINANCIAL SERVICES RESPONSE.....	17
ABBREVIATIONS .....	19

## OBJECTIVE

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The objective of this audit was to determine whether the Department of State (Department) was in compliance with the Improper Payments Information Act of 2002<sup>1</sup> (IPIA), as amended, for FY 2016. To accomplish this objective, Kearney & Company, P.C. (Kearney), acting on the Office of Inspector General's (OIG) behalf, evaluated whether the Department conducted a program-specific risk assessment for all programs covered by Office of Management and Budget (OMB) requirements and reviewed the Department's FY 2016 Agency Financial Report (AFR) to determine whether the Department complied with improper payments reporting requirements.

## BACKGROUND

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According to the Department of the Treasury, improper Federal payments Government-wide totaled approximately \$144 billion in FY 2016.<sup>2</sup> Improper payments are payments that should not have been made or that were made in an incorrect amount. Improper payments include overpayments and underpayments, duplicate payments, payments made to an ineligible recipient, payments for an ineligible good or service, payments for goods or services not received (except for such payments authorized by law), payments that do not account for credit for applicable discounts, and payments for which an agency cannot determine whether the payments were proper because of a lack of or insufficient supporting documentation.

The Federal Government has implemented safeguards to reduce improper payments. In 2002, Congress enacted IPIA, which required Federal agencies to annually identify programs and activities<sup>3</sup> at high risk of improper payments, estimate the amount of improper payments in those programs, perform recovery auditing if program payments exceeded \$500 million, and report to Congress on steps taken to reduce improper payments.

In July 2010, the Improper Payments Elimination and Recovery Act<sup>4</sup> (IPERA), which amended IPIA, was signed into law. IPERA strengthened IPIA by increasing requirements for identifying and reporting on improper payments. IPERA clarified the programs to be reviewed and expanded improper payments recapture activities. IPERA also required inspectors general to annually determine whether agencies were in compliance with improper payments requirements and established additional requirements for agencies that were deemed noncompliant.

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<sup>1</sup> Pub. L. No. 107-300.

<sup>2</sup> Department of the Treasury, "Improper Payment Rates Across the Federal Government," <<https://paymentaccuracy.gov/improper-payment-rates-across-the-federal-government/>>, accessed on March 25, 2017.

<sup>3</sup> The terms "program and activity" are referred to in this report as "program."

<sup>4</sup> Pub. L. No. 111-204.

In January 2013, the Improper Payments Elimination and Recovery Improvement Act of 2012<sup>5</sup> (IPERIA) was enacted. IPERIA further amended IPIA by redefining “payment” to include payments that were made to employees and requiring that OMB identify high-priority Federal programs for greater levels of oversight and review,<sup>6</sup> provide guidance to agencies for improving estimates of improper payments, and establish a working system for prepayment and pre-award review. In October 2014, OMB issued guidance for agencies implementing IPIA, IPERA, and IPERIA requirements as Appendix C, “Requirements for Effective Estimation and Remediation of Improper Payments,” of OMB Circular A-123, “Management’s Responsibility for Enterprise Risk Management and Internal Control.”<sup>7</sup> The guidance, among other things, defines the programs and payments that agencies must assess for the risk of improper payments and provides requirements for determining whether the risk of improper payments is significant for developing an estimate of improper payments, for performing recapture audit activities, and for reporting improper payments activities.

## Department of State Payments

The Department is the primary agency through which the U.S. Government conducts its diplomacy. The Department operates more than 270 embassies, consulates, and other posts worldwide. The Department provides policy guidance, program management, administrative support, and in-depth expertise in areas such as law enforcement, economics, the environment, intelligence, arms control, human rights, counternarcotics, counterterrorism, public diplomacy, humanitarian assistance, security, nonproliferation, and consular services.

Because of the nature and the extent of its programs, the Department makes significant payments to third-party vendors, contractors, grantees, and employees. During FY 2016, the Department made payments of approximately \$36.7 billion, of which \$28.4 billion was subject to IPIA<sup>8</sup> requirements.<sup>9</sup> The payments subject to IPIA requirements included payments to vendors and contractors; payments to employees; and Federal Financial Assistance payments, including grants, assessed contributions,<sup>10</sup> and voluntary contributions.<sup>11</sup> The amount and volume of payments made by the Department, the Department’s emphasis on expediting certain payments

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<sup>5</sup> Pub. L. No. 112-248.

<sup>6</sup> The Department does not have any high-priority programs, as identified by OMB.

<sup>7</sup> OMB Circular A-123 was updated in July 2016; however, Appendix C of Circular A-123 (dated October 2014) remains in effect.

<sup>8</sup> Unless otherwise indicated, the term “IPIA” implies “IPIA as amended by IPERA and IPERIA” in this report.

<sup>9</sup> OMB Circular A-123, Appendix C, states that agencies are not obligated to review intra-governmental transactions for improper payments unless directed to do so by OMB. Of the \$36.7 billion in Department payments, approximately \$8.3 billion was intra-Governmental and intra-Departmental transactions.

<sup>10</sup> Assessed contributions represent assistance provided to foreign countries, international societies, commissions, or proceedings or to projects that are lump sum, quota of expenses, or fixed by treaty.

<sup>11</sup> Voluntary contributions represent discretionary financial assistance provided to foreign countries, international societies, commissions, proceedings, or projects.

(for example, payments for necessary foreign financial assistance), and the decentralized nature of the Department's operations increase the Department's risk for improper payments.

The Bureau of the Comptroller and Global Financial Services (CGFS) has oversight responsibilities for the Department's financial management program. Financial management program responsibilities include establishing financial policy and procedure, analyzing and reporting financial information, managing financial information systems, and establishing management controls. Management controls, also known as "internal controls," are the processes designed and implemented by an organization to help it accomplish its goals or objectives. Important internal control activities include those aimed at ensuring that only proper payments are made. Within CGFS, the Office of Management Controls (CGFS/MC) is responsible for overseeing the Department's management control program and other financial management functions, such as administering compliance with IPIA.

## AUDIT RESULTS

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Kearney found that the Department complied with improper payments requirements.<sup>12</sup> The Department performed risk assessments using required criteria defined by OMB Circular A-123 for all programs meeting its minimum threshold for evaluation. Although the Department conducted the required risk assessments, Kearney found that quality control procedures related to the Department's risk assessment process could be improved. In addition, the Department published its AFR<sup>13</sup> for FY 2016 and posted the AFR on the Department's website. The AFR included the disclosures required by OMB. Although the Department included all required disclosures, some optional information on improper payments identified and recovered outside the payment recapture efforts was not provided. Because much of this information is available, it would be prudent and useful to the users of the AFR to include this information.

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<sup>12</sup> OMB Circular A-123, Appendix C, identifies six requirements that agencies must meet to be compliant with improper payment requirements: (1) conduct a program specific risk assessment for each program; (2) publish an AFR for the most recent fiscal year and post the report and accompanying materials required by OMB to the agency website; (3) publish improper payment estimates for all programs identified as susceptible to improper payments, if required; (4) publish programmatic corrective actions plans in the AFR, if required; (5) publish and meet annual reduction targets for each program at risk for improper payments, if required; and (6) report a gross improper payment rate of less than 10 percent for each program for which an improper payment estimate was obtained and published in the AFR. Requirements 3 through 6 apply to agencies that have identified programs susceptible to significant improper payments in the year after a significant risk program has been identified. The Department has not identified any programs susceptible to significant improper payments. Therefore, only Requirements 1 and 2 apply to the Department.

<sup>13</sup> Federal agencies may publish their financial statements in either an AFR or a Performance Accountability Report. The Department has elected to use the AFR format.



## **Finding A: Program Risk Assessments Were Performed, but Quality Control Procedures Could Be Improved**

IPIA requires agencies to periodically review all programs and identify those that may be susceptible to significant improper payments. OMB Circular A-123, Appendix C, requires that agencies perform risk assessments for programs deemed at low risk of having significant improper payments at least once every 3 years.

The Department performed the required program risk assessments in FY 2016. Specifically, CGFS/MC performed risk assessments using required criteria (that is, risk factors) defined by OMB Circular A-123 for all programs meeting its minimum threshold for evaluation. However, CGFS/MC did not consider the results of some OIG audit reports in performing risk assessments. By improving its quality control procedures, the Department may improve its conclusions related to the susceptibility of some programs to improper payments.

### ***Improper Payments Risk Assessments Were Performed***

OMB Circular A-123, Appendix C, requires that agencies perform a risk assessment of all programs for susceptibility to significant improper payments. The Circular defines “significant improper payments” as gross annual improper payments in the program exceeding (1) both 1.5 percent of program outlays and \$10 million of all program payments made during the fiscal year or (2) \$100 million. Agencies must institute a systematic method of performing the risk assessments. An agency can perform a quantitative evaluation based on a statistical sample, or it can perform a qualitative evaluation by considering risk factors likely to contribute to significant improper payments.

During FY 2016, CGFS/MC performed and documented a qualitative risk assessment of all 35 programs that the Department has identified as being subject to IPIA requirements.<sup>14</sup> Because, for most programs, FY 2016 was the first year of the 3-year risk assessment cycle required by OMB Circular A-123,<sup>15</sup> CGFS/MC opted to perform risk assessments for all applicable programs, including those that had been assessed within the last 2 years. To perform risk assessments of the 35 programs with net expenditures of \$100 million or more, CGFS/MC developed a scorecard for each program that includes an evaluation of the 9 risk factors specified by OMB.

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<sup>14</sup> CGFS/MC excluded programs from the risk assessment that had less than \$100 million in net program expenditures within the fiscal year because CGFS/MC believes that the likelihood of improper payments of more than \$10 million (10 percent or more) is remote, and therefore do not warrant further assessment.

<sup>15</sup> OMB Circular A-123, Appendix C, states “[f]or programs that are deemed to be low risk of significant improper payments, agencies must perform risk assessments at least once every three years thereafter (programs that have been determined to be susceptible to significant improper payments and that are already reporting an estimate—or in the process of establishing an estimate—do not have to perform additional risk assessments). However, if a low risk program experiences a significant change in legislation and/or a significant increase in its funding level, agencies are required to re-assess the program’s risk susceptibility during the next annual cycle, even if it is less than [3] years from the last risk assessment.”



The scorecard included a total of 11 criteria,<sup>16</sup> such as whether or not the program was new, the volume of payments made, and significant deficiencies identified in audit reports (for example, OIG and Government Accountability Office reports).

CGFS/MC obtained information for its scorecard evaluation by reviewing the Department's FY 2017 Congressional Budget Justification, information on internal and external websites, information contained in internal and external reports, and discussions with officials from the responsible bureaus and offices. On the basis of information obtained, CGFS/MC assigned a numerical rating of 1, 3, or 5 to each program for each scorecard criterion, with a rating of 1 representing low risk, 3 representing moderate risk, and 5 representing high risk. CGFS/MC then averaged the ratings for each program to determine the program's overall risk level. The overall ratings showed that 33 of the 35 programs were at low risk for incurring significant improper payments and that 2 programs were at moderate risk.

CGFS/MC performed an additional assessment of the two programs that were at moderate risk. This additional risk assessment considered factors such as the location in which the programs' costs were incurred and whether significant deficiencies in the programs' internal control had been previously identified. The results of these additional assessments indicated that both programs' overall risk remained moderate and that further evaluations were therefore not necessary. CGFS/MC concluded that none of the Department's programs was susceptible to significant improper payments as defined by OMB Circular A-123, Appendix C.

### *Quality Control Procedures Could Be Improved*

CGFS/MC considered and documented its assessed risk for each of the nine risk factors required by OMB Circular A-123. Kearney found that the implementation of the risk assessment process could be improved. Specifically, Kearney found that CGFS/MC did not consider two OIG audit reports with improper payment implications that were published in FY 2016 when conducting its risk assessments.

One factor that OMB Circular A-123, Appendix C, requires be considered during the risk assessment is "significant deficiencies in the audit reports of the agency including, but not limited to, the agency Inspector General or the Government Accountability Office audit report findings." Although CGFS/MC includes this requirement in its risk assessment and did consider some OIG reports that related to the programs that CGFS/MC identified, CGFS/MC did not consider two pertinent FY 2016 OIG reports during the risk assessment process.

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<sup>16</sup> CGFS has elected to split one risk factor required to be considered by OMB Circular A-123, Appendix C, —"[r]esults from prior improper payment work"—into two criteria on its score card. Specifically, CGFS/MC considers the amount of identified improper payments from prior work and the number of identified improper payments from prior work as separate criteria. Further, CGFS/MC considers one risk factor that is not required by the circular—significant increases in funding. Therefore, CGFS/MC has 11 total criteria for consideration in its risk assessments, rather than the 9 specified by OMB.

For example, one OIG report<sup>17</sup> identified issues that should have been considered during a risk assessment for improper payments, including \$1.5 million in questioned costs. Although CGFS/MC identified this report in compiling its list of all OIG audit reports, it was not identified as having questioned costs relevant for IPIA risk assessments, even though the Middle East Partnership Initiative program is part of the Economic Support Fund program, for which CGFS/MC performs a risk assessment. According to CGFS/MC officials, the questioned costs and recommendations in the audit report were erroneously not identified as having an IPIA impact, and as a result the report was not taken into account when completing the risk assessments. Kearney also found that CGFS/MC did not consider the results of another audit<sup>18</sup> during the risk assessment process for the same error. This report identified \$2.8 million in questioned costs (and projected an additional \$2.6 million in questioned costs), which should have been considered during the risk assessment of the Political-Military, Nonproliferation, Antiterrorism, Demining program.

CGFS/MC has written policies and procedures requiring officials to compile all audit reports during its risk assessment process. However, Kearney found that a single CGFS/MC official reviews the audit findings and recommendations from the reports and determines whether there is an improper payments impact. After the improper payments impact determination, each report is then attributed to an IPIA program, when applicable, and risk assessment scores are assigned. A CGFS/MC supervisor reviews the list of audit reports to ensure that all relevant reports are considered, but does not review the determinations regarding whether audit findings and recommendations have an improper payments impact.

Although CGFS/MC conducted the required risk assessments for all its programs, without improved quality control procedures, audits noting questioned costs may not be considered during risk assessments. After Kearney noted the two missing OIG audit reports from the risk assessments, CGFS/MC officials re-calculated the risk scores for the identified programs. According to CGFS/MC officials, when they recalculated the overall risk scores for the Economic Support Fund and the Political-Military, Nonproliferation, Antiterrorism, Demining programs assuming a "high" risk for the "significant deficiencies identified in audit reports" risk factor, the overall risk scores remained "low." However, this may not have been the case if the composition of scores for other risk factors were different, and strengthened quality control procedures may lead the Department to more accurate conclusions regarding the susceptibility of its programs to improper payments in future risk assessments.

**Recommendation 1:** OIG recommends that the Bureau of the Comptroller and Global Financial Services develop and implement additional quality control procedures requiring that a supervisor review determinations regarding the improper payments impact of audit

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<sup>17</sup> OIG, *Audit of the Bureau of Near Eastern Affairs Financial Management of Grants and Cooperative Agreements Supporting the Middle East Partnership Initiative*, (AUD-MERO-16-42, July 2016).

<sup>18</sup> OIG, *Audit of the Bureau of Political-Military Affairs Federal Assistance Awards*, (AUD-SI-16-49, September 2016).

findings and recommendations for the applicable fiscal year during the risk assessment process.

**Management Response:** CGFS stated it “concur[red] with the finding to improve our quality control measures with respect to audit findings and recommendations that note questioned costs.”

**OIG Reply:** OIG considers this recommendation resolved, pending further action. This recommendation can be closed when OIG receives documentation demonstrating that CGFS has developed and implemented additional quality control procedures requiring that a supervisor review determinations regarding the improper payments impact of audit findings and recommendations for the applicable fiscal year during the risk assessment process.

### **Finding B: Agency Financial Report Was Published and Included Required Disclosures, but Some Optional Information for One Disclosure Was Incomplete**

The Department published on its website its FY 2016 AFR, which included the required improper payments disclosures. For example, CGFS disclosed its improper payments risk assessment process; all programs that were assessed for risk in the year; and recapture audit activities, results, and future targets. Although the Department included all required disclosures, optional information on improper payments identified and recovered outside its payment recapture audit activities was not provided. Because much of this information is available, it would be prudent and useful to the users of the AFR to include this information.

#### ***Required Improper Payments Disclosures Were Made***

IPIA states that for an agency to be in compliance with the act, the agency must publish an AFR for the most recent fiscal year and post that report, with the information on improper payments required by OMB, on the agency’s website. OMB Circular A-123, Appendix C, requires an agency to disclose specific information relating to improper payments in its annual AFR in the format provided in OMB Circular A-136, Revised, “Financial Reporting Requirements.”

The Department published its FY 2016 AFR on its website. The AFR included the required improper payments disclosures. For example, the AFR included summary information on improper payments, a description of the Department’s improper payments risk assessment process, a listing of all programs assessed for risk in FY 2016, and a description of the Department’s payment recapture audit program, including the results of recapture activities as well as recapture targets for future years.

### *Some Optional Information for One Disclosure Was Not Included*

Although the Department included all required disclosures in its FY 2016 AFR, optional information on improper payments identified outside of the payment recapture process was not provided. OMB Circular A-136 states that agencies should “report on [improper payments] identified and recovered through sources other than payment recapture audits.”<sup>19</sup>

To fulfill this requirement, CGFS reported the amounts identified and recovered by the CGFS Office of Claims during post-payment reviews of vendor and employee payments, the amounts identified and recovered by CGFS’s Office of Global Compensation during post-payment reviews of American and Foreign Service National employee transactions, and amounts identified and recovered as a result of the CGFS Retirement Accounts Division’s annuity payment reviews.

The circular further states that “agencies could report on [improper payments] identified through...agency post-payment reviews or audits; Office of Inspector General reviews; [and] Single Audit reports.”<sup>20</sup> However, Kearney found that CGFS did not include improper payments identified in OIG reports; Defense Contract Audit Agency reports; or improper payment reviews performed by other Department offices and bureaus during contract and grant oversight activities, such as contract and grant closeout procedures, management post-payment reviews, and grant compliance reviews. Although including this information in the AFR is not required, the Department would be providing useful information on improper payments if it included this information in the AFR. Further, CGFS/MC has much of the information related to the identification of improper payments by other offices available for the purposes of reporting.

For example, CGFS/MC officials were aware of the amount of Department improper payments identified in OIG and Defense Contract Audit Agency reports. However, CGFS/MC officials elected not to include the information in the AFR because they did not have information related to the collection of those funds. According to CGFS/MC officials, OMB officials instructed them not to include improper payments identified outside of payment recapture activities without the corresponding collection information for such improper payments in the AFR. However, CGFS was unable to provide documentation of such instruction from OMB officials, and existing OMB guidance<sup>21</sup> does not preclude reporting improper payments without the corresponding collection information. Further, CGFS did not take action to determine the collection status of the resolution of the questioned costs identified by OIG or the Defense Contract Audit Agency.

In addition, during FY 2016, CGFS/MC collected information from Department bureaus and offices to determine the type of data available regarding improper payments that were identified by the bureaus and offices during contract and grant oversight activities. However,

<sup>19</sup> OMB Circular No. A-136, II.5.8. “IPIA (as amended by IPERA and IPERIA) Reporting Details,” Section X, Subsection d.

<sup>20</sup> Ibid.

<sup>21</sup> Ibid.

CGFS/MC did not obtain or report any improper payment information related to those activities in the FY 2016 AFR.

By not including complete information in its AFR, the Department did not provide users of the report with all relevant information about its efforts to prevent and then identify and recover improper payments.

**Recommendation 2:** OIG recommends that the Bureau of the Comptroller and Global Financial Services develop and implement a method to obtain information regarding the collection status of improper payments identified in OIG reports for the applicable fiscal year.

**Management Response:** CGFS stated it was “appreciative of receiving suggestions for improvement for some optional information that do not affect the Department’s compliance with IPIA, as amended. We concur in principle with the recommendations. We will evaluate these recommendations and implement them to the extent they are material and consistent with efforts to identify and lower regulatory burdens.”

**OIG Reply:** On the basis of management’s response, OIG considers this recommendation resolved, pending further action. This recommendation can be closed when OIG receives documentation demonstrating that CGFS has developed and implemented a method to obtain information regarding the collection status of improper payments identified in OIG reports for the applicable fiscal year.

**Recommendation 3:** OIG recommends that the Bureau of the Comptroller and Global Financial Services develop and implement a method to obtain information regarding the collection status of improper payments identified in Defense Contract Audit Agency reports for the applicable fiscal year.

**Management Response:** CGFS stated it was “appreciative of receiving suggestions for improvement for some optional information that do not affect the Department’s compliance with IPIA, as amended. We concur in principle with the recommendations. We will evaluate these recommendations and implement them to the extent they are material and consistent with efforts to identify and lower regulatory burdens.”

**OIG Reply:** On the basis of management’s response, OIG considers this recommendation resolved, pending further action. This recommendation can be closed when OIG receives documentation demonstrating that CGFS has developed and implemented a method to obtain information regarding the collection status of improper payments identified in Defense Contract Audit Agency reports for the applicable fiscal year.

**Recommendation 4:** OIG recommends that the Bureau of the Comptroller and Global Financial Services develop and implement a method to obtain information on improper payments identified and recovered by other Department of State bureaus and offices through contract and grant oversight activities, such as contract and grant closeout procedures, during the applicable fiscal year.

**Management Response:** CGFS stated it was "appreciative of receiving suggestions for improvement for some optional information that do not affect the Department's compliance with IPIA, as amended. We concur in principle with the recommendations. We will evaluate these recommendations and implement them to the extent they are material and consistent with efforts to identify and lower regulatory burdens."

**OIG Reply:** On the basis of management's response, OIG considers this recommendation resolved, pending further action. This recommendation can be closed when OIG receives documentation demonstrating that CGFS has developed and implemented a method to obtain information on improper payments identified and recovered by other Department bureaus and offices through contract and grant oversight activities, such as contract and grant closeout procedures, during the applicable fiscal year.

**Recommendation 5:** OIG recommends that the Bureau of the Comptroller and Global Financial Services develop and implement a process to report all improper payments identified by sources outside payment recapture audits for the applicable period in the annual Agency Financial Report. The process should require the Bureau of the Comptroller and Global Financial Services to present this information even if corresponding collection information is not readily available, unless written instructions advising otherwise is obtained from the Office of Management and Budget.

**Management Response:** CGFS stated it was "appreciative of receiving suggestions for improvement for some optional information that do not affect the Department's compliance with IPIA, as amended. We concur in principle with the recommendations. We will evaluate these recommendations and implement them to the extent they are material and consistent with efforts to identify and lower regulatory burdens."

**OIG Reply:** On the basis of management's response, OIG considers this recommendation resolved, pending further action. This recommendation can be closed when OIG receives documentation demonstrating that CGFS has developed and implemented a process to report all improper payments identified by sources outside payment recapture audits for the applicable period in the annual Agency Financial Report.

## RECOMMENDATIONS

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**Recommendation 1:** OIG recommends that the Bureau of the Comptroller and Global Financial Services develop and implement additional quality control procedures requiring that a supervisor review determinations regarding the improper payments impact of audit findings and recommendations for the applicable fiscal year during the risk assessment process.

**Recommendation 2:** OIG recommends that the Bureau of the Comptroller and Global Financial Services develop and implement a method to obtain information regarding the collection status of improper payments identified in OIG reports for the applicable fiscal year.

**Recommendation 3:** OIG recommends that the Bureau of the Comptroller and Global Financial Services develop and implement a method to obtain information regarding the collection status of improper payments identified in Defense Contract Audit Agency reports for the applicable fiscal year.

**Recommendation 4:** OIG recommends that the Bureau of the Comptroller and Global Financial Services develop and implement a method to obtain information on improper payments identified and recovered by other Department of State bureaus and offices through contract and grant oversight activities, such as contract and grant closeout procedures, during the applicable fiscal year.

**Recommendation 5:** OIG recommends that the Bureau of the Comptroller and Global Financial Services develop and implement a process to report all improper payments identified by sources outside payment recapture audits for the applicable period in the annual Agency Financial Report. The process should require the Bureau of the Comptroller and Global Financial Services to present this information even if corresponding collection information is not readily available, unless written instructions advising otherwise is obtained from the Office of Management and Budget.



## APPENDIX A: PURPOSE, SCOPE, AND METHODOLOGY

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The Improper Payments Elimination and Recovery Act of 2010<sup>1</sup> (IPERA), which amended the Improper Payments Information Act of 2002<sup>2</sup> (IPIA), requires the Office of Inspector General (OIG) to conduct an annual audit of the Department of State's (Department) compliance with improper payments requirements. In accordance with the IPERA requirement, an independent certified public accounting firm, Kearney & Company, P.C. (Kearney), acting on OIG's behalf, performed this audit to determine whether the Department was in compliance with IPIA, as amended.<sup>3</sup>

Kearney conducted fieldwork for this performance audit from January through March 2017 in the Washington, DC, metropolitan area. The audit was conducted in accordance with generally accepted government auditing standards. Those standards require that Kearney plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for the findings and conclusions based on the audit objective. Kearney believes that the evidence obtained provides a reasonable basis for the findings and conclusions based on the audit objective.

Kearney focused the scope of the audit on the following objectives: (1) to evaluate whether the Department conducted a program-specific risk assessment for all programs covered by Office of Management and Budget (OMB) requirements, (2) to determine whether the Department's FY 2016 Agency Financial Report (AFR) complied with improper payments reporting requirements, and (3) to reach a conclusion as to whether the Department was compliant with IPIA according to OMB guidance.

To obtain background information, Kearney researched and reviewed Federal laws and regulations, as well as prior OIG and Government Accountability Office audit reports. Kearney also reviewed the United States Code and OMB Circulars.

Kearney designed the audit to obtain insight into the Department's current processes, procedures, and organizational structure regarding compliance with IPIA requirements. To expedite the audit process, Kearney leveraged the results of its FY 2016 financial statement audit and audits of the Department's FYs 2011–15 compliance with IPIA to confirm its understanding of the nature and profile of Department operations, IPIA standards, regulatory requirements, and supporting information systems and controls.

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<sup>1</sup> Pub. L. No. 111-204.

<sup>2</sup> Pub. L. No. 107-300.

<sup>3</sup> Unless otherwise indicated, the term "IPIA" implies "IPIA, as amended by IPERA and the Improper Payments Elimination and Recovery Improvement Act of 2012 (Pub. L. No. 112-248)" in this report.

Kearney conducted process walkthroughs and interviews with Department officials to obtain a sufficient understanding of the steps taken by the Department to assess the risk of improper payments, the Department's process of identifying significant improper payments, and the process of reporting improper payments information. Consistent with the fieldwork standards for performance audits, Kearney established performance criteria and identified sources of audit evidence to complete the testing phase.

During the testing phase, Kearney obtained and reviewed documentation supporting the Department's FY 2016 risk assessments and AFR disclosures. The testing phase provided Kearney with evidence to determine the findings of the report issued for the performance audit. The criteria determined in the planning phase served as the basis for assessing the Department's compliance with IPIA requirements. The testing phase included procedures to assess the Department's IPIA reporting process and the AFR disclosures. Specifically, Kearney performed procedures to ensure the completeness of the Department's listing of programs and activities subject to IPIA requirements. Kearney also evaluated the Department's risk assessment process for compliance with IPIA requirements, as well as reasonableness and objectivity. Finally, Kearney evaluated the Department's 2016 AFR disclosure against OMB Circular A-136<sup>4</sup> requirements to determine whether all required disclosures were made.

During the reporting phase, Kearney formally communicated to the Department the conclusions reached and the findings and recommendations for the actions it should take to comply with IPIA requirements.

## Prior Reports

In May 2016, OIG reported<sup>5</sup> that the Department was in compliance with IPIA requirements. Specifically, the Bureau of the Comptroller and Global Financial Services (CGFS) conducted a risk assessment for required programs. However, the method used for identifying programs with a significant change in funding may not have identified all programs with increased risks of significant improper payments. In addition, the Department published its AFR for FY 2015 with the disclosures required by OMB and posted the AFR on its website. However, one disclosure relating to improper payments identified and recovered outside the recapture audit process was incomplete. In the report, OIG restated its May 2015<sup>6</sup> recommendations that CGFS expand its process to identify programs with significant funding changes and develop and implement a method to obtain information on improper payments identified and recovered by other Department offices and bureaus.<sup>7</sup>

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<sup>4</sup> OMB Circular A-136, "Financial Reporting Requirements."

<sup>5</sup> OIG, *Audit of Department of State FY 2015 Compliance With Improper Payments Requirements* (AUD-FM-16-38, May 2016).

<sup>6</sup> OIG, *Audit of Department of State FY 2014 Compliance With Improper Payment Requirements* (AUD-FM-15-26, May 2015).

<sup>7</sup> See Appendix B: Prior Recommendations for additional details.

## Work Related to Internal Controls

Kearney performed steps to assess the adequacy of internal controls related to the areas audited. Specifically, Kearney assessed the controls contained in the Department's policies and procedures performing risk assessments and reporting improper payments information. However, Kearney did not perform testing of these controls because it was beyond the scope of this audit.

## Use of Computer-Processed Data

Kearney obtained computer-processed data from CGFS to aid in determining whether the Department complied with IPIA. More specifically, these data provided evidence that the Department had taken steps to comply with IPIA. Kearney did not perform tests to validate the spreadsheet amounts because such testing was not necessary to accomplish the audit objective. However, Kearney assessed the data provided as reasonable on the basis of its understanding of the financial information gained during the audit of the Department's FY 2016 financial statements. Kearney's assessment was also based on a comparison of the programs and activities that the Department had used as its baseline for performing risk assessments with a universe of FY 2015 expenditure transactions that Kearney obtained from the Global Financial Management System, the Department's core financial system.<sup>8</sup>

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<sup>8</sup> The Global Financial Management System supports the Department's mission by effectively accounting for business activities and recording the associated financial information, including obligations and costs, performance, financial assets, and other data.

## APPENDIX B: PRIOR OIG RECOMMENDATIONS

Table B.1 presents the status of the Office of Inspector General (OIG) recommendations from audits of the Department of State's compliance with improper payment requirements for FYs 2013–15, that is, the three previous fiscal years.

**Table B.1: Prior OIG Recommendations - FYs 2013–15**

Report Number	Fiscal Year	Number	Recommendation	Status
AUD-FM-14-23	2013	1	OIG recommends that the Bureau of the Comptroller and Global Financial Services: <ul style="list-style-type: none"> <li>• Expand its recapture audit procedures to include pension annuity and Payment Management System grant payments or formally document the justification for excluding these payment types.</li> <li>• Communicate the recapture audit exclusions to the Office of Management and Budget and OIG, along with the justification or cost-benefit analysis.</li> </ul>	Closed
		2	OIG recommends that the Bureau of Comptroller and Global Financial Services improve its controls for improper payments reporting to ensure that all payment types excluded from recapture audits are disclosed and all improper payments identified and recovered are reported in the Agency Financial Report.	Closed
AUD-FM-15-26	2014	1	OIG recommends that the Bureau of the Comptroller and Global Financial Services expand its process to identify programs with significant funding changes to consider additional factors that may increase the risk of significant improper payments, including, at a minimum, the percentage increase of the change.	Closed
		2	OIG recommends that the Bureau of the Comptroller and Global Financial Services develop and implement a method to obtain information on improper payments identified and recovered by other Department of State offices and bureaus to ensure that the Agency Financial Report includes all amounts required by the Office of Management and Budget.	Closed

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Report Number	Fiscal Year	Number	Recommendation	Status
		3	OIG recommends that the Bureau of the Comptroller and Global Financial Services fully implement recapture audit procedures for all payment types, including annuity payments, grant payments made through the Payment Management System, employee salary and benefit payments, and other excluded payments.	Closed
AUD-FM-16-38	2015		<i>OIG restated Recommendations 1 and 2 from AUD-FM-15-26 and did not issue any new recommendations in this report.</i>	Not Applicable

**Source:** Kearney prepared using OIG compliance information.

## APPENDIX C: THE BUREAU OF THE COMPTROLLER AND GLOBAL FINANCIAL SERVICES RESPONSE

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**United States Department of State**  
**Comptroller**  
**Washington, DC 20520**  
**MAY 05 2017**

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### **MEMORANDUM**

TO: OIG – Steve A. Linick

FROM: CGFS – Christopher H. Flaggs 

SUBJECT: Report on Audit of Department of State FY 2016 Compliance with  
Improper Payments Requirements (AUD/FM-17-XX, April 2017)

Thank you for the opportunity to comment on the Office of Inspector General's (OIG) Draft Report titled Audit of Department of State FY 2016 Compliance with the Improper Payments Requirements Report.

The Department has made significant efforts to comply with all requirements and guidance for the Improper Payments Information Act of 2002 (IPIA), Improper Payments Elimination and Recovery Act in 2010 (IPERA), and Improper Payments Elimination and Recovery Improvement Act in 2012 (IPERIA). We strive to do so in a manner that also leverages the good stewardship of government funds and ensures our initiatives are cost-effective. We are pleased that our program is “compliant” with IPIA, as amended, but we recognize that improvements can be made and will continue doing so. The Department takes the OIG recommendations very seriously, as demonstrated by the accomplishments relative to recommendations made in prior years’ audit reports.

Regarding Recommendation 1, we concur with the finding to improve our quality control measures with respect to audit findings and recommendations that note questioned costs. Although the recommendation language did not include a specific reference to audit reports noting questioned costs, the background narrative supporting the recommendation and discussions with the external auditors that you contracted, Kearney & Co, specify the recommendation was relevant for those reviews.

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-2-

Regarding recommendations No. 2, No. 3, No. 4, and No. 5, we are appreciative of receiving suggestions for improvement for some optional information that do not affect the Department's compliance with IPIA, as amended. We concur in principle with the recommendations. We will evaluate these recommendations and implement them to the extent they are material and consistent with efforts to identify and lower regulatory burdens.

As acknowledged in the Draft Report, the Department employs numerous preventative and identification methods to support the broad array of improper payments requirements. We have dedicated considerable resources to prevent improper payments from occurring, and are gratified in our track record of success. With the implementation of our Global Financial Management System in 2007, we fully integrated acquisitions into the financial system at the line level, significantly enhancing the integrity of our payments. In addition, we have strengthened our payment internal controls through our efforts under OMB's Do Not Pay initiative. Prior IPIA regulatory guidance was geared toward high-risk programs and activities that were deemed susceptible to significant improper payments. And, as part of our risk assessment process, we have identified no high-risk programs. Since we have no identified high risk programs, we have prioritized our recapture audit resources on conducting detailed reviews of programs that have been evaluated as medium risk through our risk assessment process.

We recognize that the IPIA, as amended, and related guidance has raised the bar on transparently accounting for and preventing improper payments for all Agencies, including the Department. We are committed to meeting these compliance requirements in a reasoned manner. We look forward to working with both the OIG and the Independent Auditor on further enhancements to our existing programs in the coming year.

If you have any questions concerning this status summary, please contact Carole Clay, Director of Management Controls (CGFS/MC), at (202) 663-2084.

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## ABBREVIATIONS

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AFR	Agency Financial Report
CGFS	Bureau of the Comptroller and Global Financial Services
CGFS/MC	Bureau of the Comptroller and Global Financial Services, Office of Management Controls
IPERA	Improper Payments Elimination and Recovery Act
IPERIA	Improper Payments Elimination and Recovery Improvement Act
IPIA	Improper Payments Improvement Act
OMB	Office of Management and Budget

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