

U.S. DEPARTMENT OF COMMERCE
Office of Inspector General



**PUBLIC
RELEASE**

***INTERNATIONAL
TRADE ADMINISTRATION***

*US&FCS Portugal Is Effectively
Providing Services, But Should
Strengthen Program Management*

Audit Report No. BTD-10594-9-0001 / March 1999

Office of Audits, Business and Trade Audits Division



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EXECUTIVE SUMMARY

Portugal is a member country of the European Union (EU), the United State's largest trading partner. As of 1997, direct exports to Portugal amounted to approximately \$1 billion per year. With the rapid growth of the Portuguese economy, standard measures of that nation's economic performance are now approaching the average of its EU partners. However, as only the 34th largest market for direct U.S. exports of goods and services, Portugal is not ranked highly by U.S. business as a new market to explore.

In general, EU economic assistance has helped to sustain Portugal's economic growth above the EU average. From 1997 to 2000, the Portuguese government will invest nearly \$20 billion in regional development projects, with one-third financed by EU structural funds. These funds are deployed not only to industry, but in virtually every sector of the economy, with a significant portion being applied to the improvement of Portugal's transportation infrastructure.

The Department of Commerce's operations in Portugal are carried out by the U.S. and Foreign Commercial Service (US&FCS), which manages two offices in Lisbon and Porto. Its FY 1997 total operating budget amounted to \$752,000. According to US&FCS's Overseas Resource Allocation Matrix, at the time of our audit US&FCS Portugal was 43rd out of 96 countries in terms of operations and administrative funding.¹

The Office of Inspector General conducted a performance audit of US&FCS operations in Portugal. We have divided our findings into two broad areas: program performance and general management, and internal control environment.

Program Performance and General Management

Because U.S. exporters consider the Portuguese market to be peripheral to other European markets due to its small size, US&FCS Portugal has focused its attention on servicing Portuguese importers and distributors interested in importing U.S. products. The senior commercial officer stated that the primary goal of US&FCS Portugal for FY 1997 and FY 1998 was to increase success stories² resulting from US&FCS assistance to Portuguese importers. The post also planned to coordinate regional promotion of Portugal through Showcase Europe, manage the

¹ The Overseas Resource Allocation Matrix is a US&FCS management tool to guide overseas resource allocation decision-making.

² Success stories are a performance measure of export actions in which the Department played a role. Success stories result from trade event activities, products, services, or counseling and describe the type of US&FCS assistance provided to the company.

Showcase Europe home page, and create a companion page for European agents and distributors.³

US&FCS Portugal's trade promotion program reflects US&FCS's regional priorities. However, while the Porto office is generating a large number of success stories, the quantity and sector coverage represented by these success stories, as well as the absence of a strong working relationship with the Porto branch of the American Chamber of Commerce, indicate that Porto activity may be too narrowly focused and inadequately integrated with the overall objectives of US&FCS Portugal. The Agent/Distributor Service (ADS)⁴ provided by US&FCS Portugal also requires significant improvement in management and timeliness.

Internal Control Environment

US&FCS Portugal plays an active role in the International Cooperative Administrative Support Services (ICASS) system (indeed, the senior commercial officer is the ICASS counsel chairperson) and maintains an adequate internal control environment. The internal control weaknesses, which we view as not material, include a lack of (1) asset management control over vehicles and inventory and (2) controls over cash collections. While the amount of cash collected is relatively small, the procedures and controls should be strengthened to safeguard against the potential misuse of receipts and ensure accurate reporting. Additionally, we were unable to determine whether the post met US&FCS requirements for trust fund activity, although the amount of activity was low.

Finally, Federal laws and regulations (Federal Manager's Financial Integrity Act, the Chief Financial Officers Act, and GAO regulations) require that US&FCS Washington account for its foreign service national severance cost liability. The FSN personnel benefits, including severance pay, are in accordance with prevailing practices in Portugal. The embassy personnel office provided us with a severance cost liability calculation of over \$517,000. We reviewed the severance pay plan; the amount of severance liability could be significantly less depending on the interpretation of this plan. US&FCS should obtain legal review of the plan and conduct a detailed analysis to determine the precise amount of the liability.

Our most important recommendations call for the Assistant Secretary and Director General of US&FCS to:

³ The Showcase Europe strategy coordinates US&FCS efforts to approach Europe on a regional basis and to move U.S. firms exporting to one or more European markets into additional markets.

⁴ The Agent/Distributor Service is a customized overseas search for qualified agents, distributors, and representatives for U.S. firms.

1. Reassess the general mission and activity of the Porto office in order to determine how it could more effectively support the objectives of US&FCS. To this end, determine (a) why an active relationship with the Porto branch of the Chamber of Commerce has not been established; and (b) whether US&FCS Porto is adequately focused and integrated into the overall objectives of US&FCS Portugal.
2. Ensure that US&FCS management works with the senior commercial officer to adopt a more formal system for monitoring ADS timeliness. Staff should also be held accountable for timeliness problems, as well as recognized and rewarded for meeting the established ADS deadline.
3. In concert with the Department of State's General Services Office, perform an inventory to ensure that all US&FCS assets are appropriately identified with bar code tags. For any items missing from the inventory records, obtain an explanation from the property custodian as to the location or disposition of the equipment or other asset.
4. Direct the US&FCS Offices of International Operations and Planning to obtain legal review of the severance pay agreement and conduct a detailed analysis to assess the amount of unfunded severance liability for the post.

In its response to our draft report, US&FCS generally agreed with our recommendations and described a number of measures it has taken to implement the recommendations. These include: (1) improving the relationship with the Porto branch of the American Chamber of Commerce and increasing the number of visits to Lisbon by the Porto FSN; (2) processing all ADS requests within timeframes established under US&FCS guidelines; and (3) maintaining an up-to-date inventory of office and residential property.

We have made minor changes in response to the comments and reiterated our recommendations without change in the final report. Summaries of US&FCS's response for each set of findings and recommendations begin on pages 7 and 14, and we have attached US&FCS's complete response to the report.

INTRODUCTION

Under the authority of the Inspector General Act of 1978, as amended, and the requirements of the Omnibus Trade and Competitiveness Act of 1988, the Office of Inspector General conducted a performance audit of Department of Commerce operations in Portugal. Our fieldwork was conducted during December 8-12, 1997.

Performance audits are objective, systematic examinations of an organization, program, activity, or function in order to provide information to improve accountability and facilitate decision-making by parties with responsibility to oversee or initiate corrective action. By identifying systemic strengths and weaknesses, the OIG will help the Department's managers implement more efficient and effective operations to better serve their customers.

PURPOSE AND SCOPE

The OIG is committed to the pursuit of operational effectiveness throughout the Department, challenging management to achieve excellence with respect to programmatic, administrative, and financial operations. The purpose of this performance audit was to evaluate the effectiveness of the Department's operations in Portugal, which are carried out primarily through the U.S. and Foreign Commercial Service's offices in Lisbon and Porto.

In accordance with the General Accounting Office's (GAO) *Assessing Internal Controls in Performance Audits*, we reviewed US&FCS Portugal's internal control environment relating to administrative and financial management. We conducted tests to achieve our objective of determining the effectiveness of administrative and financial management controls.

We tested US&FCS Portugal's operations for compliance with the GAO *Policy and Procedures Manual for Guidance of Federal Agencies* and the Federal Managers' Financial Integrity Act of 1982. The report findings and recommendations draw upon significant tests of records; physical evidence; documentary evidence, including accounting records and memorandums; and analytical evidence based on data obtained. We also held interviews with US&FCS personnel, partner organizations, and clients. We did not rely on computer-generated data to support our findings. Our audit covered a review of programmatic, management, administrative, and financial issues.

We reviewed the policies, procedures, and practices being implemented by US&FCS Portugal to determine whether it is successfully and efficiently meeting its mission: to assist U.S. companies, particularly small and medium-sized enterprises, with export assistance. We also determined whether US&FCS Portugal's goals and objectives are being achieved, and whether these goals and objectives are in line with Department objectives. The audit evaluated the effectiveness and efficiency of operations, and assessed the operation's compliance with applicable laws, regulations, and procedures.

In conducting our audit, we placed primary emphasis on the following areas:

- program performance and general management
- internal control environment

The audit also considered ITA headquarters and domestic office activities that are coordinated with US&FCS Portugal. The audit was conducted in accordance with Generally Accepted Government Auditing Standards and was performed under the authority of the Inspector General Act of 1978, as amended, and Department of Commerce Organization Order 10-13, dated May 22, 1980, as amended.⁵

In the absence of an ambassador to Portugal, we discussed our observations with the chargé d'affaires, and held an exit conference with the US&FCS Portugal Senior Commercial Officer (SCO) and the Regional Director for Europe on December 12, 1997. During this conference, the SCO generally agreed with our observations.

BACKGROUND

PORTUGUESE MARKET

Portugal is a steadily expanding part of the European Union (EU) single market. With access to the EU market, a low-cost work force, and government incentives, Portugal is considered a good place to establish distribution and production facilities. While the small size of the Portuguese market discourages U.S. firms from placing emphasis on it, many U.S. firms already export to Portugal indirectly through the distribution channels of other EU countries. The tax benefits gained from importing from other EU countries tend to encourage these indirect U.S. exports to Portugal. Given the priorities of the Portuguese government and the technological and industrial edge of U.S. firms, the following areas have been identified by ITA as holding the most promise for U.S. exporters to Portugal: telecommunications; pollution control and waste management; energy conservation; medical and health management; computers, peripherals, and software; franchising; laboratory and scientific instruments; apparel; airport and ground support equipment; and defense articles and services.

US&FCS PORTUGAL

US&FCS Portugal has its primary office in Lisbon, as well as a satellite office in the industrial region of Porto. Together, both offices target local Portuguese importers in order to promote

⁵ The OIG discloses that two audit team members formerly worked for ITA; however, they had no material involvement with US&FCS Portugal operations.

trade relationships between Portuguese importers and U.S. exporters. This outreach primarily consists of counseling and recruiting local companies for regional trade events.

The Showcase Europe (SCE) regional initiative, begun in 1995, is managed by US&FCS posts in Europe and is an integral part of the agency's operations in Portugal. This strategy coordinates the efforts of US&FCS posts and domestic offices to present the European market on a regional basis and thus encourage U.S. firms to broaden their export horizons with respect to the European market. Showcase Europe emphasizes eight key sectors that represent major opportunities for U.S. exporters within Europe.⁶ Each SCE sector is managed by an individual commercial office in Europe, but the sectors are not specific to a single country. US&FCS Portugal is responsible for the development of the SCE internet homepage.

⁶ The Showcase Europe Strategy (SCE) focuses on eight key industry sectors: Aerospace, Automotive Parts, Energy and Power Generation, Environmental Technologies, Franchising, Medical/Pharmaceutical, Telecommunications/Communications and Information Technologies, and Travel and Tourism

FINDINGS AND RECOMMENDATIONS

US&FCS Portugal's management exhibited a number of strengths, such as successful relationships with government and business organizations and a proactive SCO who involves his staff in the development and implementation of office plans. However, despite strong leadership of US&FCS Portugal activities, some program operations and internal controls over US&FCS assets need strengthening.

We have categorized our audit findings and recommendations into two areas:

- program performance and general management
- internal control environment

I. PROGRAM PERFORMANCE AND GENERAL MANAGEMENT

Because U.S. exporters consider the Portuguese market to be peripheral to other European markets due to its small size, US&FCS Portugal has focused its attention on servicing Portuguese importers and distributors interested in importing U.S. products. The SCO stated that the primary goal of US&FCS Portugal for FY 1997 and FY 1998 was to increase success stories⁷ resulting from US&FCS assistance to Portuguese importers. The post would also coordinate regional promotion of Portugal through Showcase Europe, manage the SCE home page, and create a companion page for European agents and distributors. While generating a high number of success stories, it is unclear whether the Porto satellite office is sufficiently integrated into the activity of the primary office in Lisbon. The post should also improve its management of the Agent/Distributor Service (ADS).

A. US&FCS Portugal Maintains Positive Relationships with Organizations and Assists Businesses

The relationships established by the post with other U.S. government agencies and business organizations are positive and productive, but improvements are needed in the Porto region. Officials at the State Department, the Department of Defense, and the U.S. Information Service were complimentary in describing their interaction with post officials. The current Director of the American Chamber of Commerce (AmCham)⁸ in Lisbon now views the relationship between AmCham and US&FCS Portugal to be excellent, a positive change in recent years. The SCO has

⁷ Success stories are a performance measure of export actions in which the Department played a role. Success stories result from trade event activities, products, services, or counseling and describe the type of assistance provided to the company by the US&FCS.

⁸ American Chambers of Commerce abroad are associations of business executives that represent U.S. businesses in host countries before governments, the business community, and the general public.

assisted the AmCham with a number of its activities, including the development of an action plan outlining proposed activities and objectives. However, the director of the Porto committee of AmCham stated that there is no substantive interaction with the US&FCS Porto office.

US&FCS Portugal also shares communication and logistics responsibilities with respect to specific trade events with the local franchising institute. Franchising is one of the eight key sectors selected for focus by posts in Showcase Europe, and the Lisbon office provides critical support to US&FCS Spain, the sector coordinator. Consequently, US&FCS Portugal's relationship with the institute is timely and could be productive.

US&FCS Portugal also supports the Showcase Europe strategy in several ways. It manages the SCE internet web site that provides comprehensive resources on, and advertising for, SCE events and related information. As the coordinating office, Portugal works with the other SCE managers and US&FCS domestic offices to develop new information and update existing information on trade-related issues and events.

B. Management of Products and Services Can Be Improved

We reviewed the market research and Agent/Distributor Services provided by US&FCS Portugal, as well as the quality and quantity of reported success stories. While the quality of the market research is good, and the volume and value of success stories in FY 1996 and FY 1997 are commendable, the numerical distribution of success stories between Lisbon and Porto is uneven. Also, delivery of the ADS is often untimely.

US&FCS Porto Market Focus, While Successful, Needs to be Reassessed

US&FCS maintains a two-person office in Porto, a large commercial city, to cover the northern half of Portugal, which has been characterized as the industrial half. As the U.S. business presence is relatively small, US&FCS Porto primarily focuses its research and services on the Portuguese distributors and importers in the area. The Porto office has developed an extensive database of prospective importers, updated with personal contact and follow-up. The office also provides ADS, prepares market research, and maintains a small library of reference materials.

In terms of the volume and value of success stories, the Porto office is extremely productive and thus appears to be adequately providing information and support to Portuguese importers. In FY 1996 and FY 1997, the principal foreign service national (FSN) in Porto reported twice as many success stories as reported by Lisbon, as well as a significant percentage of the total value (89 percent in FY 1996 and 30 percent in FY 1997).

US&FCS has identified "Best Prospect" sectors (country-specific sectors with exceptional potential for U.S. exporters within three years) and eight key SCE sectors for focus by posts. In FY 1996 and FY 1997, 64 and 50 percent of the Portugal post's reported success stories,

respectively, were in those categories. When we examined them further, the success stories reported for US&FCS Lisbon reflected a significant focus on achieving results in Best Prospect and Showcase Europe. The same analysis showed that Porto, in contrast, did not generate results that were focused on Best Prospect or SCE sectors; in FY 1997, only 25 percent of the success stories from the Porto office were in the SCE sectors (primarily the automotive and medical sectors). In addition, in FY 1996, the SCE sector-related success stories reported by the Porto office accounted for just 37 percent of the total Porto success stories. Again, these success stories were primarily in the automotive and medical sectors.

When considering the comments by the director of the Porto Committee of the AmCham that there is not substantive interaction with US&FCS Porto, together with the lack of success in reaching US&FCS target sectors, we conclude that while US&FCS Porto is successfully providing information to Portuguese importers/distributors and generating success stories, the activity and objectives of the office may be too narrow and inadequately integrated into the post's overall objectives.

US&FCS Portugal ADS Reports Not Timely

Based on a review of US&FCS Portugal records, we found that delivery of ADS research reports regularly exceeds the 30-day deadline specified in the US&FCS manual. ADS is a fee-based service in which a prospective U.S. exporter requests information on the most promising agent/distributor prospects. ADS research typically reports up to six qualified, reputable, and interested prospects.

In FY 1996 and FY 1997 combined, the Post received 11 ADS requests. The average number of days between the time post acknowledged receipt of an ADS request and the time a completed ADS report was sent to the domestic office was 86 days and 63 days, respectively. One ADS report took 284 days to complete and forward to the domestic office. In general, while a log was maintained, there was no active monitoring of ADS progress. The SCO appeared to be unaware of how untimely ADS reports were, although correspondence from him to his staff clearly shows his commitment to providing a quality product to U.S. companies.

As noted above, US&FCS has adapted itself to Portugal's secondary-market status by focusing on the information needs of Portuguese distributors/importers interested in U.S. products; i.e., the reverse of a traditional ADS, which focuses on the needs of U.S. exporters. While this strategy appears to be generating results, the service should still be an integral part of services provided to U.S. companies and should be provided in a timely manner.

C. Personnel Management Needs Attention

Staff morale at US&FCS Portugal can be characterized as fair. The staff appear to enjoy their work, receive adequate management direction, and interact positively with the SCO. The SCO

has developed a work plan for the office that presents program objectives, targets client needs, and addresses each employee's role. Interviews with the FSN staff, however, indicated a lack of career advancement potential, which has lowered staff morale. Because most of the staff at US&FCS Portugal have been employed there for more than 20 years, nearly every employee has reached the maximum grade and step level. In addition, US&FCS Portugal's low ranking on the US&FCS Overseas Resource Allocation Matrix reduces its ability to employ higher graded positions. The absence of career growth or promotion potential for any employee (until a senior FSN retires) will continue to have a negative impact on motivation.

RECOMMENDATIONS

We recommend that the Assistant Secretary and Director General:

1. Reassess the general mission and activity of the Porto office in order to determine how it could more effectively support the objectives of US&FCS. To this end, determine (a) why an active relationship with the Porto branch of the Chamber of Commerce has not been established; and (b) whether US&FCS Porto is adequately focused and integrated into the overall objectives of US&FCS Portugal.
2. Ensure that US&FCS management works with the senior commercial officer to adopt a more formal system for monitoring ADS timeliness. Staff should also be held accountable for timeliness problems, as well as recognized and rewarded for meeting the established ADS deadline.
3. Explore available performance incentives and recognition techniques to counteract low morale among US&FCS Portugal staff.

US&FCS's Response to Draft Report and OIG Analysis

In its reply to our draft report, US&FCS agreed to, or has taken action consistent with, our recommendations. While we are encouraged by US&FCS's commitment to ensuring that the Porto office is involved in the SCE and Best Prospect sectors, we recommend that the Porto office's relationship with the local AmCham be reassessed. A summary of US&FCS's position on each recommendation is presented with OIG comments on the US&FCS response.

Recommendation #1:

Reassess the general mission and activity of the Porto office in order to determine how it could more effectively support the objectives of US&FCS. To this end, determine (a) why an active relationship with the Porto branch of the Chamber of Commerce has not been established; and (b) whether US&FCS Porto is adequately focused and integrated into the overall objectives of US&FCS Portugal.

US&FCS Response: The SCO was not present at the OIG's meeting with the Director of the Porto Committee of the AmCham and requests a debriefing to discuss the outcome of the meeting before addressing the reported inadequate relationship with the Porto AmCham and to clarify the nature of actions to be taken by the post. US&FCS pointed out that the offices meet regularly; most of the reference publications used at the Porto AmCham were donated by US&FCS; the offices are located in the same building; and US&FCS Porto assists the part-time AmCham employee in answering members' questions. If improvement in the relationship is necessary, it lies with the SCO and not necessarily with the US&FCS Porto office.

Subsequent to the audit, the SCO has met several times with the Porto AmCham to explore further areas of cooperation and now believes that the relationship is excellent. The SCO points out that more than 80 percent of the AmCham members are Portuguese manufacturers who want to export to the United States. The post's interest in these members is necessarily very limited, sometimes leading to unfulfilled expectations. Also, many Porto businesses still feel slighted by the 1991 closure of the US Consulate in Porto.

With respect to the focus of the Porto office and the extent of integration into the overall objectives of US&FCS Portugal, the sole Porto Commercial Assistant is responsible countrywide for one of the SCE sectors and the two Portugal Best Prospect sectors. The Porto FSN handles all inquiries from businesses in the north that are not part of another FSN's portfolio. The wide focus leads to success stories from a range of industry sectors. As a result of comments by the IG team during its debrief, the SCO has increased the number of visits by the Porto FSN to Lisbon from once a year to once a quarter. The SCO also encourages Lisbon-based FSNs to travel to Porto when sector market research warrants such a visit.

OIG Comments: Our conclusion with respect to the relationship with the Porto AmCham was based on our interview with the Porto AmCham Director; however, as the report states on page 2, we discussed these and other findings with the SCO and US&FCS Regional Director for Europe on December 12, 1997, at the end of our visit. While the offices might have regularly met prior to our audit, the Porto Director's comments concerned a lack of substantive joint projects to promote US products and services. To the extent that the SCO has met with the Director subsequent to our visit and initiated such projects (which were not detailed in the response), the SCO is meeting the intent of the recommendation. Similarly, the SCO's actions to increase the number of visits by the Porto FSN to Lisbon, as well as Porto's involvement in the SCE and Best Prospect sectors, are responsive to the recommendation. We would be pleased to discuss this further with the SCO if so desired.

However, the fact that so many of the AmCham members are apparently not interested in distributing US products and services, as cited in the response, might indicate that the benefits of Porto's relationship with the AmCham should be reassessed. We did not recommend that US&FCS *strengthen* the relationship, merely that it determine why it is not more *active*. More

needs to be done to ensure that Porto focuses on promoting US exports to the region in the face of such reluctance. We are therefore reiterating our recommendation without change.

Recommendation #2:

Ensure that US&FCS management works with the senior commercial officer to adopt a more formal system for monitoring ADS timeliness. Staff should also be held accountable for timeliness problems, as well as recognized and rewarded for meeting the established ADS deadline.

US&FCS Response: Following the IG audit, a FSN was formally assigned to monitor ADS timeliness and alert the SCO to potential delays. Since the audit, all ADS requests have been received and processed within ADS guidelines.

OIG Comments: We concur with US&FCS's response to our recommendation. No further action is needed.

Recommendation #3:

Explore available performance incentives and recognition techniques to counteract low morale among US&FCS Portugal staff.

US&FCS Response: Staff is concerned with lack of advancement potential and income tax liability. The latter is an issue over which the USG has no control. The SCO has improved office environment and work conditions. He has awarded cash awards to FSNs for superior performance. The SCO notes that more flexibility in the grade structure and recognizing spot performance with money would be of great assistance in motivating FSNs worldwide.

OIG Comments: We concur with US&FCS's response to our recommendation. We recognize the limitations on each SCO in this area.

II. INTERNAL CONTROL ENVIRONMENT

US&FCS should improve internal control systems to better meet the requirements of the Federal Managers' Financial Integrity Act of 1982 (FMFIA) (31 U.S.C. §3512(b)). The internal control weaknesses, which we view as not material, include a lack of (1) asset management control over vehicles and inventory and (2) controls over cash collections. Management has segregated key duties and responsibilities among State Department and USFCS personnel in authorizing, processing, recording, and reviewing transactions among key individuals, except during cash collections. Documentation of trust fund costs should be improved, even though there was little activity. There appears to be a significant unfunded severance liability for US&FCS Portugal, although a more detailed analysis of the severance pay agreement may yield a smaller amount. US&FCS Portugal is actively engaged in the International Cooperative Administrative Support Service system (ICASS) to ensure that the expenses charged are accurate and the services meet quality standards.

A. Asset Management Needs to Be Strengthened

According to 4 FAM 031.7, *Control of Property*, agencies are to maintain inventory controls and accountability systems for property. US&FCS Portugal has not properly implemented asset management procedures in two areas, vehicle use and inventory controls, to ensure that assets are safeguarded against waste, loss, unauthorized use, and misappropriation.

Vehicle use

The US&FCS *Operations Manual* requires that posts with vehicles keep use records that track official and personal use. US&FCS staff must reimburse the government for all personal use of the vehicle. The vehicle lease inventory for the Portugal post showed two vehicles, a 1993 Opel Omega and a 1985 Opel Record. But use records have not been maintained for either vehicle, and the keys for the Opel Record were missing. As a result, the system and controls are inadequate, with the potential for a high risk of misuse. If the Opel Record is no longer needed, the vehicle should be turned over to State Department's general services officer for disposal.

Inventory controls

During a review of the post's inventory management system, we identified a significant lack of control over US&FCS furniture and equipment assets. Embassy administrative staff maintain control over the inventory in the Non-Expendable Property Application (NEPA) System, which is an ICASS service charged to each agency. The State Department has an inventory process whereby all purchases are received by the administrative section, bar-coded, and processed into the NEPA system. In addition to the NEPA system, each US&FCS post works with the Washington-based US&FCS Office of Information Systems (OIS) to maintain a computer equipment inventory.

We reviewed the NEPA and computer inventory reports and found inadequate recording of the inventory. Over \$5,000 in assets were unaccounted for in the official inventory. In Porto alone, multiple items were identified that were not listed on the official inventory: a cellular telephone, a computer, printers, a copying machine, an answering machine, and a fax machine. When State's general services officer was questioned, she could not explain how Porto could receive equipment without it being logged into the State Department system.

B. Financial Management Controls Need Improvement

Three offices of the State Department (the Budget and Financial Office (B&F), General Services Office (GSO), and Personnel Office) maintain a number of internal accounting and administrative controls. We reviewed the State Department controls applicable to US&FCS Portugal. The B&F and GSO have controls over the procurement and payment cycle to ensure that appropriate reviews and authorization signatures are on purchase orders and other documents. However, we noted weaknesses in the US&FCS financial controls that should be addressed.

Controls over Cash Collections Should be Strengthened

We reviewed post and B&F cash receipts procedures and controls. While the amount of cash collected at post is relatively small, amounting to just \$3,873 in FY 1997, the procedures and controls should be strengthened to safeguard against the potential misuse of receipts and ensure accurate reporting. We found that the post does not (1) maintain a contemporaneous log as the cash is received; (2) use sequentially numbered receipts; (3) fix accountability for each segment of the event cycle (*e.g.*, receipt of cash and preparation of receipts) with one person; (4) periodically reconcile post deposit records with accounting records maintained by the B&F Office or Office of Trade Event Management collection reports; and (5) maintain continuous control over cash receipts. Due to the small amount of collections, we assessed the risk for potential misuse or misreporting of cash receipts as moderate.

Supervision over Porto Petty Cash Should Be Strengthened

The FSN in Porto maintains a petty cash fund of \$1,000 in local currency. The SCO in Lisbon has direct control over the petty cash and visits Porto twice a month, at which time cash counts are conducted. However, when interviewing the embassy administrative officer, we learned that the State Department does not supervise or review the US&FCS petty cash fund. The State Department has authority over administrative matters at post and has the resources and training in financial functions. Normal procedures for posts with a petty cash fund call for the State Department to authorize allotments and provide supervisory oversight and guidance to the US&FCS employee and supervisor.

We also found that the librarian/secretary and cleaning contractor (both part-time, purchase order contractors) in Porto are paid from the petty cash fund. In a 1994 internal US&FCS management

report, the post was instructed to refrain from paying such expenses from the fund and to convert the employees to personal service contracts (PSCs). At the time of our audit, post officials had not implemented the instruction; instead, the purchase orders were cut on a monthly basis. US&FCS Portugal has processed over 84 purchase orders for one employee since 1990.

C. Post Needs to Document Trust Fund Balances

US&FCS trade events are intended to be self-supporting and collections for these events are accumulated in a trust fund. In order to assess whether the post is recovering the full costs of trade events and activity, the post must maintain income and expense accounting records. While the collections at post in FY 1997 were relatively small, almost \$3,900, we were unable to determine the expenditures and whether the post met US&FCS requirements for trust fund activity. For the Informatica trade fair, the headquarter's Office of Trade Event Management reported expenses of \$21,935. For the same event, the State Department B&F Regional Administrative Management Center reported expenses of \$19,106.⁹

FY 1997 Trust Fund Gains and Losses

Event	Collections	Expenditures	Gain (Loss)
Informatica Trade Fair	\$20,541	\$21,935	(\$1,394)
Gold Key	\$2,245	no records	unknown
Business Facilitation	\$1,628	no records	unknown

We reviewed the trade event and trust fund financial records to verify that revenues were sufficient to cover the related expenses. As shown in the table above, the post Gold Key and business facilitation programs had revenues but no costs recorded. When advised of this, the SCO indicated that the costs are so low and similar to operating and administrative related costs, that the latter account will typically fund the expenses.

US&FCS regulations also require that the post maintain records to demonstrate that more than 50 percent of the guests entertained at US&FCS events represent local organizations. The records attached to documents maintained by the State Department B&F Office do not always demonstrate that the guests meet this criteria.

⁹ Informatica Trade Fair collections were made through the Washington, DC-based Office of Trade Event Management and were not considered US&FCS Portugal post collections for the purpose of our analysis. Instead, collections for this event were considered as total collections for US&FCS Portugal events.

D. US&FCS Portugal Has an Unfunded Personnel Liability

Federal laws and regulations (FMFIA, the Chief Financial Officers Act, and GAO regulations) require that US&FCS Washington account for its FSN severance cost liability. The FSN personnel benefits, including severance pay, are in accordance with prevailing practices in Portugal. The embassy personnel office provided us with a severance cost liability calculation of over \$517,000. The personnel staff told us that the calculations were based on retroactive service prior to June 1992, the date of the severance pay plan, through December 1997. We were also advised that if US&FCS employees were terminated, they would receive severance payments even if they were eligible for an immediate retirement annuity.

We reviewed the severance pay plan. The plan does not expressly state that the creditable service includes the period of employment prior to June 1992. The plan also does not address whether employees receive severance benefits if eligible for an immediate retirement annuity. Under the federal civilian retirement systems, federal workers do not receive severance pay if they can retire on an immediate annuity. Since the FSNs have a lengthy employment history (the average length of service is 22 years), with much of the service prior to June 1992, the amount of severance liability could be significantly less than the amount calculated. The interpretation of the severance plan could materially affect the amount of the unfunded severance pay liability. US&FCS should obtain a legal review to interpret the laws and regulations as they apply to the plan and conduct a detailed analysis to determine the precise amount of the liability.

E. US&FCS Portugal Is Actively Engaged in ICASS

US&FCS Portugal is actively engaged in ICASS to ensure that expenditures are accounted for properly in accordance with FMFIA. The SCO is the current chairman of the ICASS council, but due to the relatively small size of the agencies operating in the embassy, there is no ICASS working group. There is an ongoing review of the services provided and costs that the commercial service is assessed. Currently, ICASS costs represent 29 percent of US&FCS Portugal's total operating costs. The SCO has paid particular attention to identify the types of personnel that State includes in its allocation of the administrative costs, and to verify that such staff are actually providing a service to the post.

RECOMMENDATIONS

We recommend that the Assistant Secretary and Director General of US&FCS:

1. Require US&FCS to maintain vehicle use records that identify the user and account for all kilometers driven, and to ensure reimbursement to the government for any personal use.
2. Require US&FCS to turn over the 1985 Opel Record to the State Department's General Services Office for disposition if the vehicle is no longer needed.

3. In concert with the State Department's General Services Office, perform an inventory to ensure that all US&FCS assets are appropriately identified with bar code tags. For any items not included in the inventory records, obtain an explanation from the property custodian as to the location of the equipment or other asset.
4. Direct US&FCS to improve internal controls over cash collections by:
 - maintaining a contemporaneous log of cash received,
 - using sequentially numbered receipts,
 - fixing accountability for each segment of the cash collection and deposit cycle with one person,
 - reconciling the official post receipt records with State B&F cash collection reports, and
 - maintaining control of the cash until deposited with the B&F cashier and an official deposit record is received.
5. Request that the State Department B&F Office within the U.S. embassy in Portugal provides the necessary guidance and supervision over the management of the petty cash allotment.
6. Ensure that US&FCS refrains from making contractor payments from the petty cash allotment as instructed in the 1994 US&FCS management report on Portugal.
7. Require that representation expense vouchers submitted to B&F have adequate documentation of the 50-percent local organization rule.
8. Require US&FCS to maintain adequate accounting records for trust fund account expenditures.
9. Direct US&FCS to obtain legal interpretation of the laws and regulations as necessary and review the severance pay agreement to assess the amount of unfunded severance liability for the post.

US&FCS's Response to Draft Report and OIG Analysis

In its reply to our draft report, US&FCS agreed to, or has taken action consistent with, all of our recommendations.

Recommendation #1:

Require US&FCS to maintain vehicle use records that identify the user and account for all kilometers driven, and to ensure reimbursement to the government for any personal use.

US&FCS Response: A vehicle use log was initiated immediately prior to the IG audit. The section's secretary maintains use records in the vehicle file. Similar logs are also now maintained for fax and long distance phone usage.

OIG Comments: When we inquired into the use of the log during our audit (early December 1997), we found that a log for one vehicle had just been initiated, but it included only one entry for use, and the user was not identified. No log existed for the use of the other vehicle.

We concur with US&FCS's response to our recommendation. No further action is needed.

Recommendation #2:

Require US&FCS to turn over the 1985 Opel Record to the State Department's General Services Office for disposition if the vehicle is no longer needed.

US&FCS Response: The vehicle was disposed of by GSO on March 31, 1998. At the time of the audit, US&FCS informed the auditors that the keys were with GSO since we had already turned the vehicle over to them for disposal.

OIG Comments: The OIG auditor interviewed the SCO and his secretary on these issues in early December 1997, and the auditor attempted to inspect the vehicle. The secretary told the auditor, in the presence of the SCO, that she did not have the keys and did not know who did have the keys. As a result, the auditor was unable to enter the vehicle to read the odometer or check for vehicle records possibly stored in the vehicle.

We concur with US&FCS's response to our recommendation. No further action is needed.

Recommendation #3:

In concert with the State Department's General Services Office, perform an inventory to ensure that all US&FCS assets are appropriately identified with bar code tags. For any items not included in the inventory records, obtain an explanation from the property custodian as to the location of the equipment or other asset.

US&FCS Response: Embassy's GSO now maintains an up-to-date, bar-coded inventory of office and residential property. The last complete physical inventory was in September 1998. GSO now records all new purchases upon receipt.

OIG Comments: We concur with US&FCS's response to our recommendation. No further action is needed.

Recommendation #4:

Direct US&FCS to improve internal controls over cash collections by:

- I maintaining a contemporaneous log of cash received,*
- I using sequentially numbered receipts,*
- I fixing accountability for each segment of the cash collection and deposit cycle with one person,*
- I reconciling the official post receipt records with State B&F cash collection reports, and*
- I maintaining control of the cash until deposited with the B&F cashier and an official deposit record is received.*

US&FCS Response: US&FCS agrees with each recommendation in this area. The post currently uses OF-58 receipts issued by the Embassy cashier, but will confer with other European posts to determine the method they use in issuing receipts. The Lisbon office secretary is the sole individual handling collections, deposits, and receipts. The post has requested approval to purchase a small safe to store checks when the Embassy cashier is closed. OIO/Europe management will authorize the post to proceed accordingly.

OIG Comments: We concur with US&FCS's response to our recommendation, with one exception. To minimize the risk, however already low, of loss of collection revenue, the post should not assign the entire cash collection/deposit/receipt process to one person. To best implement a sound system of internal controls, we recommended fixing responsibility for *each* segment of the process with one person.

Recommendation #5:

Request that the State Department B&F Office within the U.S. embassy in Portugal provides the necessary guidance and supervision over the management of the petty cash allotment.

US&FCS Response: The SCO and the post's Financial Management Officer will set up a periodic schedule of reviews and visits to provide oversight.

OIG Comments: We concur with US&FCS's response to our recommendation.

Recommendation #6:

Ensure that US&FCS refrains from making contractor payments from the petty cash allotment as instructed in the 1994 US&FCS management report on Portugal.

US&FCS Response: Upon the post's request, OIO management authorized the conversion of the librarian/secretary to PSC status. However, OIO management does not agree that the

cleaning person should be so converted. The post will explore other options, such as hiring a firm for periodic cleaning for the Porto office.

OIG Comments: We concur with US&FCS's response to our recommendation.

Recommendation #7:

Require that representation expense vouchers submitted to B&F have adequate documentation of the 50-percent local organization rule.

US&FCS Response: US&FCS agrees with the recommendation, but requests clarification of the 50-percent rule as it applies to a gathering of three. OIO management has asked the Office of General Counsel for advice. Such scenarios frequently occur, such as lunches involving only the Ambassador, the SCO, and a single business representative.

OIG Comments: We appreciate US&FCS's concern that the rule may interfere with events that are appropriate and necessary to the post's mission. We advise US&FCS to seek a rapid response from OGC, and to request that OGC consider the flexibility needed in the case cited.

Recommendation #8:

Require US&FCS to maintain adequate accounting records for trust fund account expenditures.

US&FCS Response: US&FCS agrees with the recommendation and will implement a system to record trust fund deposits and receipts.

OIG Comments: We concur with US&FCS's response to our recommendation.

Recommendation #9:

Direct US&FCS to obtain legal interpretation of the laws and regulations as necessary and review the severance pay agreement to assess the amount of unfunded severance liability for the post.

US&FCS Response: US&FCS will request ITA's Office of Financial Management to investigate the status of the unfunded liability and confer with OGC in making a definitive determination as to the precise amount.

OIG Comments: We concur with US&FCS's response to our recommendation.



UNITED STATES DEPARTMENT OF COMMERCE
International Trade Administration

Washington, D.C. 20230

ASSISTANT SECRETARY AND DIRECTOR GENERAL OF THE
U.S. AND FOREIGN COMMERCIAL SERVICE

MAR 15 1999

MEMORANDUM FOR: George E. Ross
Assistant Inspector General for Auditing

FROM: Awilda R. Marquez *ARM*

SUBJECT: US&FCS Response to Draft Audit Report
US&FCS Portugal – Draft Audit Report: BTD-10594-9-XXXX

I am pleased to provide you with US&FCS' response to your draft audit report of US&FCS' operations in Portugal. You will note that in many instances our post either has already taken action on the recommendations, or has indicated how it plans to address them.

We look forward to the issuance of the final report. Please let us know if we can be of further assistance.



General Comments:

Preface page i (paragraph 3) states that there are 11 local hires. Staff at the time of the audit consisted of 9 local hires as detailed in Appendix I of the draft report. Currently there are 7 local staff (5 FSNs and two part-time contractors).

Page five (paragraph 2) states that Lisbon is the Showcase Europe sector coordinator for franchising. While Lisbon provides critical support in this sector, US&FCS Spain is the sector coordinator for franchising in Europe.

Program Performance and General Management

Recommendation 1. Reassess the general mission and activity of the Porto office, determine why an active relationship with the Porto Chamber of Commerce has not been established, and determine if the Porto office is adequately focused and integrated into overall US&FCS Portugal objectives.

The SCO was not present at the IG's meeting with the Director of the Porto Committee of the American Chamber of Commerce. The SCO would like to discuss the outcome of that meeting with the IG before the post embarks on a course to address the reported inadequate relationship with the Porto Committee of the Chamber. Members of the Porto Committee of the American Chamber of Commerce regularly participate in scheduled meetings with US&FCS, which include Dr. Santos Carneiro, the Director of the Porto Committee and Adolfo Coutinho from the US&FCS Porto office. There is an average of two to three meetings per year with the Porto Committee, with some of the meetings taking place at the US&FCS Porto office. Most of the reference publications used at the AmCham office in Porto were donated by US&FCS. The Porto Committee office is located in the same building as the US&FCS office, which was a contributing reason in the post's decision to locate in the building. On a regular basis US&FCS Porto assists the part-time Porto AmCham employee in answering questions from AmCham members. The SCO requests a debrief of the IG's meeting with the Porto Chamber to clarify the nature of actions to be taken by the post.

Page four of the draft report states that the "Director of the AmCham in Lisbon now views the relationship between the AmCham and US&FCS Portugal to be excellent..." If improvement in the relationship with the Porto Committee of the AmCham is necessary, it lies with the SCO and not necessarily with the Porto office. Nevertheless, toward this end, and subsequent to the IG audit, the SCO has met several times with the director of the Porto Committee to explore further areas of cooperation. The SCO now believes that on a working level, as well as on a management level, its relationship with the Porto Committee is excellent. The SCO points out that the IG should be aware that more than 80 percent of the AmCham members are Portuguese manufacturers who want to export to the United States. The post's interest and assistance to these companies is necessarily very limited and this sometimes leads to unfulfilled expectations. The SCO

also points out that many businesses in Porto still feel slighted by the closure of the U.S. Consulate there in 1991.

With respect to whether US&FCS Porto is adequately focused and integrated into the overall objectives of US&FCS Portugal, CS Porto's sole Commercial Assistant Adolfo Coutinho is responsible countrywide for one of the eight SCE sectors (environmental technologies), and for the two CS Portugal Best Prospect sectors, which are not SCE sectors (laboratory and scientific equipment and apparel). Aside from these countrywide responsibilities, the FSN in Porto handles all inquiries from businesses in the north that are not part of another FSN's portfolio. As Porto is home to many of Portugal's small importers and distributors, the FSN there must provide assistance to a wide variety of sectors. This wide focus clearly leads to success stories from a range of industry sectors. However, as a result of the comments by the IG team during its debrief, the SCO has increased the number of visits by the Porto FSN to Lisbon (formerly once a year, now once a quarter). The SCO also encourages Lisbon-based FSNs to travel to Porto when market research in their sector warrants such a visit.

Recommendation 2. Ensure that US&FCS management works with the Senior Commercial Officer to adopt a more formal system for monitoring ADS timeliness.

This problem has been addressed. Following the IG audit, FSN Celeste Conde was formally assigned the job of monitoring CS Portugal's ADS timeliness and alerting the SCO to any potential delays. Since the inspection, all ADS requests have been received and processed within ADS guidelines.

Recommendation 3. Explore performance incentives and recognition techniques to counteract low morale.

Page six of the report characterizes morale as fair, not poor, and states that staff members appear to enjoy their work. Not only is staff concerned with lack of advancement potential, but during the inspection there was a pervasive concern about income tax liability--a tax which, heretofore, FSNs in Portugal had not been paying and an issue over which the USG has no control. The SCO has improved office environment and work conditions. He has given FSNs cash awards when allowed (at the annual Embassy awards ceremony) to cite individuals for superior performance, e.g., high numbers of success stories generated). The SCO notes that more flexibility in the grade structure and recognizing spot performance with money would be of great assistance in motivating its FSN work force worldwide.

Internal Control Environment

Recommendation 1. Require US&FCS to maintain vehicle use records.

A vehicle use log was initiated immediately prior to the IG audit. A log sheet is located in the vehicle with records maintained by the section's secretary in the vehicle file.

Although not mentioned in the report, similar logs are now maintained for fax and long distance telephone usage.

Recommendation 2. Require US&FCS to turn over the 1985 Opel to General Services for disposition if vehicle is no longer needed.

The vehicle was disposed of by GSO on March 31, 1998. Post's request to the Embassy's GSO to dispose of this vehicle predated the IG audit by several years. At the time of the audit, US&FCS informed the inspectors that the keys to the Opel were with the GSO since we had already turned the vehicle over to them for disposal.

Recommendation 3. Perform an inventory to ensure that all US&FCS assets are appropriately identified with bar code tags.

Embassy's GSO now maintains an up-to-date, bar coded, inventory of office and residential property. The complete inventory was last physically reviewed in September 1998. To improve inventory control, the GSO receiving officer now inventories and bar codes all new purchases upon receipt.

Recommendation 4. Improve internal controls over cash collections.

- **Maintain a log of cash received.**
Post agrees and will implement immediately.
- **Use numbered receipts.**
Post currently uses OF-58 receipts issued by the Embassy cashier, but will confer with other CS posts in Europe to determine the method they use in issuing sequentially numbered receipts to post's clients.
- **Fix accountability for collection and deposit with one person.**
CS Lisbon's secretary is the sole individual handling collections, deposits, and receipts. Section does not have a safe. Post requests approval to purchase small safe for deposit of checks received when the Embassy cashier is closed. OIO/Europe management will authorize post to proceed accordingly.
- **Reconcile official post receipt records with State B&F cash collection reports.**
Post agrees and will implement recommendation.
- **Maintain continuous control over cash receipts until deposited with B&F.**
Post agrees and the SCO will monitor log and receipt records.

Recommendation 5. Request that the State Department exercise control over petty cash allotment in Porto.

SCO discussed this with post's Financial Management Officer. She agreed with the recommendation and in conjunction with SCO will set up a periodic schedule of reviews and visits to provide oversight for Porto.

Recommendation 6. Refrain from making contractor payments from petty cash allotment.

A formal request was sent to US&FCS to request that the part-time Porto secretary/librarian position be converted to a PSC. OIO/Europe management now has authorized the conversion of that position to PSC status. The cleaning person works a few hours a week. Until the draft report, post was not aware that this position should even be considered appropriate for a PSC position. OIO/Europe management does not agree that this position should be a PSC. Post will explore other options such as hiring a firm to handle periodic cleaning and window washing for the small Porto office.

Recommendation 7. Provide B&F documentation with representational vouchers showing the 50% local organization rule.

Post agrees with the recommendation, but is asking for clarification of the 50% rule as it may apply to a gathering of three. OIO/Europe management has inquired of the OGC to see how these events are to be handled under this rule. Such scenarios frequently occur throughout the CS, such as lunches that may involve only the U.S. Ambassador, the SCO, and a single foreign business representative.

Recommendation 8. Require adequate accounting records for trust fund accounts.

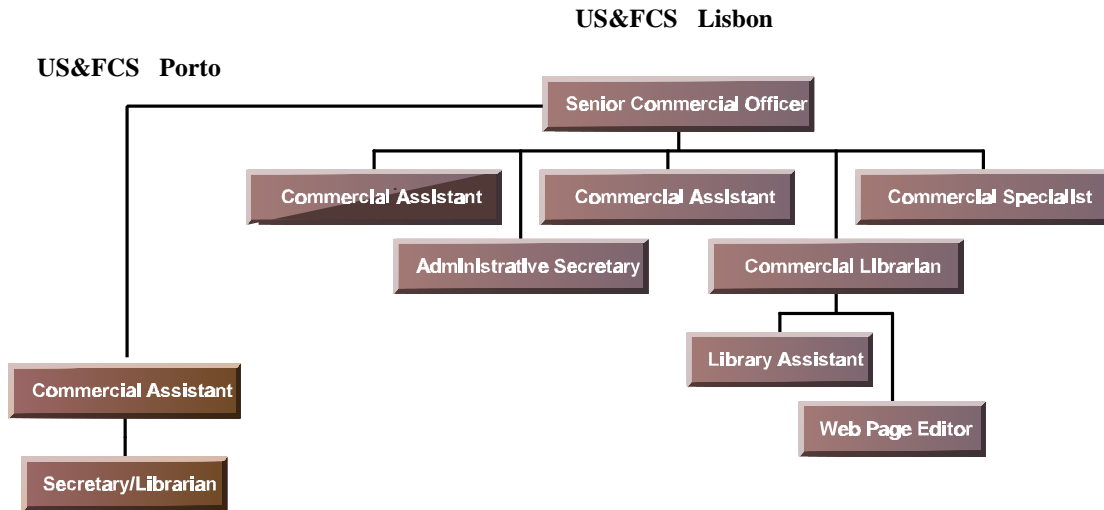
Post agrees and will implement a system within CS Portugal to log trust fund deposits and expenses. OIO/Europe management will provide post with an acceptable sample/template.

Recommendation 9. Obtain legal interpretation of the laws and regulations related to the severance pay agreement and assess the amount of unfunded severance liability for the post.

ITA's Office of Financial Management will be requested to investigate the status of Portugal's unfunded severance liability and confer with the OGC in making a definitive determination as to the precise amount of the liability.

APPENDIX II

US&FCS PORTUGAL ORGANIZATIONAL CHART



APPENDIX III

ACRONYMS

ADS	Agent/Distributor Service
AmCham	American Chamber of Commerce
B&F	Budget and Finance Office, Department of State
EU	European Union
FAM	Foreign Affairs Manual
FMFIA	Federal Managers' Financial Integrity Act of 1982
FSN	foreign service national
GAO	General Accounting Office
GSO	General Services Office, Department of State
ICASS	International Cooperative Administrative Support Service
ITA	International Trade Administration
NEPA	Non-Expendable Property Application System
OIG	Office of Inspector General
PSC	personal services contract
SCE	Showcase Europe
SCO	senior commercial officer
US&FCS	U.S. and Foreign Commercial Service
USG	United States Government