



UNITED STATES DEPARTMENT OF EDUCATION

OFFICE OF INSPECTOR GENERAL

THE INSPECTOR GENERAL

SEP 19 2001

ED-OIG/A19-B0005

Kriss Ethridge, Program Manager
Raytheon Systems Company
7700 Arlington Boulevard
Falls Church, VA 22042-2900

Dear Mr. Ethridge:

This **Final Audit Report** (Control Number ED-OIG/A19-B0005) presents the results of our audit of controls over Government property managed by Raytheon Systems Company (Raytheon). The objective of our audit was to determine whether Raytheon had adequate controls over Department of Education (Department) property under the Federal Family Education Loan (FFEL) Program contract.

BACKGROUND

The FFEL contract was originally awarded to E-Systems effective April 30, 1992. Raytheon subsequently acquired E-Systems. Under this contract, Raytheon provides automated and manual support for all Departmental loan processing and debt collection activities required to administer the FFEL program. The contract is currently in effect through September 30, 2001, with an option to extend through December 31, 2002.

AUDIT RESULTS

Overall, we found improvements were needed in Raytheon's controls over Government property. Our audit revealed that Raytheon did not adequately account for or report on Government property, did not appropriately identify Government property, and did not comply with inventory requirements. In our opinion, these weaknesses result in more than a relatively low risk that errors, irregularities, and other inefficiencies may occur, resulting in inefficient and/or ineffective performance. Our audit did not disclose any fraud.

Raytheon responded to our draft report, concurring with the results and supporting the recommendations provided. Raytheon also described specific corrective actions it intends to take and specific timeframes in which it expects the actions to be completed. In our draft report, we recommended that Raytheon account for the 17 items that could not be located. Raytheon responded that the items "...were not reconcilable" and that the

items "... were not salvageable when they were of no further use and were disposed of." Raytheon outlined changes planned to prevent future occurrences of disposing of Government property without proper recordkeeping. We have modified our recommendations from the draft report accordingly. The full text of Raytheon's response is included as Attachment A to this audit report.

Finding No. 1 Raytheon Did Not Adequately Account for and Report on Government Property

Raytheon reported 303 items of Government property in its possession as of December 31, 2000. We found that the Government property report listed items that Raytheon could not account for, and that reporting was incomplete. Specifically, we found:

- Raytheon could not account for 17 items of Government property;
- Government property records did not include 29 items located at Raytheon facilities;
- Records did not include unit costs for any of the items; and
- Raytheon did not provide the Department with an annual report of the total value of Government property in its possession.

Government property was located at the Raytheon facilities in Falls Church, VA, and Greenville, TX. Raytheon reported a total of 13 items for Falls Church. We were able to locate only one item. We also identified an additional eight items of Government property that were not included on the report for that facility.

Raytheon reported a total of 290 items for Greenville. We randomly tested 29 items and were able to account for 24 items. We also identified an additional 21 items of Government property that were not included on the report. At the time of our fieldwork, Raytheon staff were conducting an inventory. Upon our arrival at the Greenville facility, we were provided with an updated Government property report dated April 17, 2001. This report included 15 of the 21 items not included on the December 31, 2000, report. Raytheon staff added the remaining six items during our site visit.

Federal Acquisition Regulation (FAR) Part 45 prescribes policies and procedures for contractors' use and management of Government property. The following requirements relate to the issues noted:

- FAR §45.505(a): "The contractor's property control records shall constitute the Government's official property records unless an exception has been authorized. The contractor shall establish and maintain adequate control records for all Government property, including property provided to and in the possession or control of a subcontractor."

- FAR §45.505(c): "Official Government property records must identify all Government property and provide a complete, current, auditable record of all transactions."
- FAR §45.505-1(a): "...Property control records shall provide the following basic information for every item of Government property in the contractor's possession, regardless of value...(6) Disposition."
- FAR §45.505-2(a)(1): "The contractor's property control system shall contain the unit price for each item of Government property...."
- FAR §45.505-14(a): "The contractor's property control system shall provide annually the total acquisition cost of Government property for which the contractor is accountable under each contract with each agency, including Government property at subcontractor plants and alternate locations."

We found that Raytheon did not comply with the requirements detailed above because the property was not managed under Raytheon's established Government property system. This system, which was reviewed and accepted by the Department of Defense in August 1999, addresses the FAR requirements listed above. Further, Raytheon program staff managing the property were not familiar with the FAR requirements. Also, the fact that some property was not clearly identified as Government-owned may have contributed to difficulties in compiling the Government property reports (see Finding No. 2 for further discussion of this issue).

We also found that Raytheon staff did not maintain records documenting the disposal of Government property. At the Falls Church facility, Raytheon staff stated that the 12 items we could not locate had been disposed of several years earlier, but could not provide any records to support the disposition. At the Greenville facility, five items could not be located. Of these, Raytheon staff stated that three items were awaiting disposition in the warehouse, but the items were not listed on the warehouse inventory listing. Raytheon staff reported that the other two items had been sold at a General Services Administration auction, but records were not available to document the specific items sold.

As a result of the issues noted above, the Department lacks assurance that Raytheon is appropriately accounting for Government property in its possession. The Department also does not have accurate data on Government property in the possession of the contractor.

Finding No. 2 Raytheon Did Not Appropriately Identify Government Property

During our review, we found that Government property was not appropriately identified. At the Greenville facility we found:

- Twenty-six items had no bar code labels;
- Seven items had bar code labels, but not the red labels designated by Raytheon for Government property; and
- Some items included multiple bar codes, from Raytheon and from prior companies, that had not been removed when updated bar codes were applied.

FAR §45.506(a) states:

Upon receipt of Government property, the contractor shall promptly --

- (1) Identify the property in accordance with agency regulations;
- (2) Mark the property in accordance with this section; and
- (3) Record the property in its property control records.

FAR §45.506(b)(1) requires that, except for certain materials and situations where marking is impractical, "...all Government property shall be marked with an indication of Government-ownership."

Since the property for the FFEL contract was not managed under Raytheon's established Government property system, Raytheon did not promptly identify and mark Government property as such. Raytheon's system addressed the FAR requirements for identifying and recording Government property. Most of the 26 items we noted without bar codes were imaging workstations that Raytheon staff stated were received over a year ago. As part of the planned transition to a new asset management system, Raytheon staff stated they will remove all old bar codes where possible and apply new bar codes.

Property that is not marked as Government-owned may be inadvertently used for other purposes, or not included in inventories or reports of Government property. As discussed in Finding No. 1, numerous items of Government property were not initially reported. The risk for inappropriate use is increased since many similar types of both Raytheon and Government-owned property were being used in the same physical location.

Finding No. 3 Raytheon Did Not Comply with Government Property Inventory Requirements

Raytheon did not provide the Department with a report of the results of its periodic inventories. Its most recent inventory of Government property under the FFEL contract was conducted in October 1999.

FAR §45-508 states:

The contractor shall periodically physically inventory all Government property...in its possession or control and shall cause subcontractors to do likewise....

FAR §45.508-2 requires that:

The contractor shall, as a minimum, submit the following to the [Government] property administrator promptly after completing the physical inventory:

- (a) A listing that identifies all discrepancies disclosed by a physical inventory.
- (b) A signed statement that physical inventory of all or certain classes of Government property was completed on a given date and that the official property records were found to be in agreement except for discrepancies reported.

Raytheon's established practice includes annual inventories of Government property. Raytheon's *Material Control Handbook*, Section IV 4002, II.A.1, dated August 27, 1998, states that for agencies other than the Department of Defense, a schedule of physical inventories of items will be performed during October-December.

Raytheon acknowledged that while they updated and submitted the Government property report each quarter they did not provide a report highlighting the results of inventories taken. As a result, the Department has not been notified of changes in or losses of Government property. Without reports of inventories, the Department does not have assurance that Raytheon is appropriately accounting for Government property in its possession.

RECOMMENDATIONS

We recommend that the Chief Operating Officer for Student Financial Assistance require Raytheon to:

- 1.1 Ensure staff responsible for managing Government property are familiar with the requirements in the FAR;
- 1.2 Ensure records of Government property are accurate and complete;
- 1.3 Ensure adequate records are maintained to document the disposition of Government property;
- 1.4 Provide an annual report of the total value of Government property in its possession;

2. Appropriately identify and mark Government property; and
3. Ensure that results of Government property inventories are reported to the Department.

AUDIT OBJECTIVE, SCOPE, AND METHODOLOGY

The objective of our audit was to determine whether Raytheon had adequate controls over the management of Government property.

To achieve our objective, we conducted interviews with Department and Raytheon staff involved in managing Government property, reviewed FAR requirements and Raytheon policies and procedures, physically validated equipment selected in our samples, and traced equipment information to Raytheon source documents.

Our audit was based on Raytheon's report of Government property under the FFEL contract as of December 31, 2000. The report included a total of 303 items of Government property. At the Falls Church facility, we attempted to validate all 13 items listed. At the Greenville facility, we selected a random sample of 29 items from the 290 total items to physically validate.

In order to test the Government property report for completeness, we judgmentally selected an additional sample of 53 items physically located at the Greenville facility to determine if these items appeared on the report.

We tested the accuracy, authenticity, and completeness of the December 31, 2000, Government property report by comparing the physical equipment to computer data, and comparing computer data to the physical equipment. Based on these tests and assessments, we concluded that the December report was sufficiently reliable to be used in meeting the audit's objective. Discrepancies noted have been detailed in the Audit Results section of this report.

Fieldwork was performed at applicable Department of Education offices during the period October 2000 through May 2001. We also performed fieldwork at the Raytheon facility in Falls Church, VA, on March 14, 2001, and at the facility in Greenville, TX, on April 17-19, 2001. Our audit was performed in accordance with Government Auditing Standards appropriate to the scope of the review described above.

STATEMENT ON MANAGEMENT CONTROLS

We made a study and evaluation of Raytheon's current management control structure over Government property in effect during the period of our review. Our study and evaluation was conducted in accordance with Government Auditing Standards.

For the purpose of this report, we assessed and classified the significant management control structure into the following categories:

- Recordkeeping
- Reporting
- Identification of Government property
- Physical inventories

Raytheon management is responsible for establishing and maintaining a management control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of control procedures. The objectives of the system are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition and that the transactions are executed in accordance with management's authorization and recorded properly so as to permit effective and efficient operations.

Because of inherent limitations in any management control structure, errors or irregularities may occur and not be detected. Also, projection of any evaluation of the system to future periods is subject to the risk that procedures may become inadequate because of changes in conditions, or that the degree of compliance with the procedures may deteriorate.

Our assessment disclosed weaknesses and inadequacies in Raytheon's current management control structure over Government property which, in our opinion, result in more than a relatively low risk that errors, irregularities and other inefficiencies may occur resulting in inefficient and/or ineffective performance. These findings and their effects are discussed in the Audit Results section of this report.

ADMINISTRATIVE MATTERS

This report incorporates the comments you provided in response to the draft audit report. If you have any additional comments or information that you believe may have a bearing on the resolution of this audit, you should send them directly to the following Department

of Education official, who will consider them before taking final Departmental action on the audit:

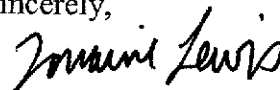
Greg Woods, Chief Operating Officer
Student Financial Assistance
U.S. Department of Education
Regional Office Building, Room 4004
7th and D Streets, SW
Washington, DC 20202

Office of Management and Budget Circular A-50 directs Federal agencies to expedite the resolution of audits by initiating timely action on the findings and recommendations contained therein. Therefore, receipt of your comments within 30 days would be greatly appreciated.

Statements that managerial practices need improvements, as well as other conclusions and recommendations in this report, represent the opinions of the Office of Inspector General. Determinations of corrective action to be taken will be made by the appropriate Department of Education officials.

In accordance with the Freedom of Information Act (5 U.S.C. §552), reports issued by the Office of Inspector General are available, if requested, to members of the press and general public to the extent information contained therein is not subject to the exemptions in the Act.

Sincerely,



Lorraine Lewis

Attachment

29 August 2001

Ms. Michele Weaver-Dugan
Director, Operations Internal Audit Team
U.S. Department of Education
Office Of Inspector General
400 Maryland Avenue, S.W.
Washington, DC 20202-1600

REFERENCE: ED-OIG/A19-B0005, dated 3 August 2001

Dear Ms. Weaver-Dugan:

Raytheon Company is pleased to provide you with comments to the referenced draft audit report, which presented the results of an audit of controls over Government property managed by Raytheon Company under the Federal Family Education Loan (FFEL) Program contract. Our comments are structured to follow the 'Recommendations' section of the referenced report.

1.1 Ensure staff responsible for managing Government property are familiar with the requirements in the FAR:

Comment: Raytheon Company has distributed applicable Federal Acquisition Regulations (FAR) data to our FFEL Program Configuration Management staff. Our personnel involved in the acquisition, disposition, and management of Government property, have been briefed on the requirements of FAR. The FFEL Configuration Manager will be responsible for ensuring that personnel working with the inventory of Government property associated with the FFEL Program understand and comply with these FAR requirements.

1.2 Ensure records of Government property are accurate and complete.

Comment: The FFEL Configuration Management Plan documents the processes used on the program to manage Government property. To ensure that Government property records are processed correctly, this plan will be updated with three new sections:

- 5.3.1 Hardware configuration item record entry and maintenance.
- 5.3.2 Hardware configuration item disposal.
- 5.3.3 Hardware Inventory reporting.

FFEL COTR. The FFEL Configuration Manager has submitted GPCC 010268 for approval to initiate these changes to the FFEL Configuration Management Plan.

1.3 Account for the 17 items identified in this report.

Comment: The 17 unaccounted items referenced in this report are not reconcilable. They were items that were not salvageable when they were of no further use and were disposed of. The changes to the Configuration Management Plan shown in item 1.2 above will document the hardware configuration item disposal process and prevent future occurrences of disposing of government property without proper record-keeping.

1.4 Ensure adequate records are maintained to document the disposition of Government property.

Comment: In accordance with the FFEL Program contract, Raytheon will continue to use the IBM Information Management system to maintain the FFEL Hardware Component Inventory. Record keeping will include equipment entries, location histories, and estimated pricing. Disposals will be recorded via memo with copies to the Department and to Raytheon's FFEL Configuration Management files. As stated in item 1.2 above, the Configuration Management Plan will be modified to reflect updated processes. We believe that current process weaknesses will be eliminated through this change.

1.5 Provide an annual report of the total value of Government property in its possession.

Comment: The FFEL Configuration Manager will provide the annual report of the total value of Government property in its possession at the beginning of each fiscal year. The report for fiscal year 2001 will be submitted to the Department no later than December 31, 2001.

2.1 Appropriately identify and mark Government property.

Comment: Government property held by Raytheon and associated with the FFEL Program has been labeled with red "Government owned" barcode tags. Updates will be reflected in our annual inventory.

3.1 Ensure that results of Government property inventories are reported to the Department.

Comment: The FFEL Configuration Manager will provide an annual inventory and a list of discrepancies, if any, between the data logged in the IBM Information Management system and the results of the present inventory. This reporting action will be including in the changes to the FFEL Configuration Management Plan described in item 1.2 above.

Raytheon believes that our responses to the Department of Education's audit findings will eliminate the weaknesses identified. Should you have any additional comments or questions, please contact me at (703) 289-1304.

Sincerely,

A handwritten signature in black ink, appearing to read 'P.K. Ethridge', written in a cursive style.

P.K. Ethridge
Program Manager

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