INACTIVE OBLIGATIONS

Federal Aviation Administration

Report Number: FI-2005-044
January 31, 2005

Memorandum

U.S. Department of Transportation
Office of the Secretary of Transportation
Office of Inspector General

Subject: ACTION: Report on the Audit of Inactive Obligations, FAA
FI-2005-044

Date: January 31, 2005

From: Alexis M. Stefani
Principal Assistant Inspector General
for Auditing and Evaluation

Reply to Attn. of: JA-20

To: Federal Aviation Administrator

This report presents the results of our audit of inactive obligations at the Federal Aviation Administration (FAA). An "obligation" represents a liability that is created when an agency enters into a binding legal agreement, such as a contract.

The head of each agency is required to certify annually to the Department of the Treasury that obligated amounts are accurate and continue to represent valid liabilities. When obligations are no longer needed or exceed estimated needs, the agency should deobligate the unneeded amounts and reapply them to other projects. In most cases, once the money is appropriated, FAA has up to 8 years to spend it. Otherwise, unused funds are returned to the U.S. Treasury and are no longer available to support FAA's mission.

The Aviation Trust Fund supports FAA's Facilities and Equipment (F&E) and Research, Engineering and Development (RE&D) programs. These programs are critical for increasing the capacity, efficiency, safety, and security of the National Airspace System. In today's tight budget environment, it is important to ensure that all funds are used efficiently and that unneeded obligations are not allowed to sit idle, as this leaves less money available for other projects.

In fiscal year (FY) 1999, FY 2000, and FY 2002, we reported a total of $241 million in unneeded obligations in FAA's accounting records.[1] In response to those reports, FAA acknowledged the need to strengthen its funds management

[1] OIG Report Number FE-1999-131, "Inactive Obligations, DOT," September 27, 1999; OIG Report Number FI-2000-125, "Inactive Obligations on Contracts, DOT," September 25, 2000; and OIG Report Number FI-2002-082, "Audit of Financial Statements for Fiscal Years 2001 and 2000, FAA," February 27, 2002. Reports can be found on our website: www.oig.dot.gov.

efforts and took corrective actions. Those actions included implementing an Agency-wide policy requiring quarterly reviews of all obligations greater than $5 million, inactive obligations greater than $1.5 million with no expenditures for 18 months, and inactive obligations from $500,000 to $1.5 million with no expenditures for 30 months.

This report assesses the effectiveness of FAA's efforts to reduce the number of unneeded obligations in response to our prior recommendations. Our audit objective was to determine whether FAA's inactive obligations represent valid financial liabilities or can be used on other projects. We performed the audit in accordance with Government Auditing Standards prescribed by the Comptroller General of the United States.

Responsibility for managing programs and associated contracts at FAA is shared by two organizations. The Office of the Chief Operating Officer of the Air Traffic Organization is responsible for managing programs and associated contracts awarded by FAA Headquarters and the William J. Hughes Technical Center. The Office of the Assistant Administrator for Region and Center Operations has responsibility for managing programs and associated contracts in FAA's nine regions and the Mike Monroney Aeronautical Center. This audit reviewed inactive obligations for programs and contracts administered by Headquarters and the two operational centers. We also reviewed inactive obligations for contracts at the FAA Eastern Region.

FAA accounting records showed about $2.1 billion of contract-related obligations associated with FAA's F&E and RE&D programs on December 31, 2002. We identified 3,705 obligations, totaling $117 million, with no activity within 18 months. Consistent with our prior audits, we defined inactive obligations as those with no expenditures within an 18-month period. We selected a judgmental sample of 878 inactive obligations, valued at $81 million, to review. Our audit scope and methodology are described in Exhibit A.

RESULTS IN BRIEF

FAA needs to do more to ensure unneeded funds are identified and freed up for use on active projects. Considering budgetary constraints and significant air traffic modernization needs, it is critical that FAA implements an effective process to review inactive obligations. The idle amounts of unneeded obligations can be deobligated and used to cover expenditures on existing active contracts or to finance new contracts.

Yet of the $81 million in inactive obligations reviewed, we identified $35 million that was unneeded or about 43 percent of the total amount reviewed. Having $35 million in unneeded obligations should be a matter of concern to FAA management. Also, during our review, FAA officials claimed much of the remaining $46 million (57 percent) of the inactive obligations as still needed, but these claims were not supported with adequate documentation. Accordingly, FAA's Chief Financial Officer should require that a team of financial managers, program officials, and contracting officers scrub the $46 million of inactive obligations to determine whether additional funds should be deobligated.

At the time of our November 17, 2004 draft report, FAA agreed that about $21 million of the $35 million that we had identified was not needed, and FAA had deobligated the funds. In its December 15, 2004 response to our draft report, FAA agreed to deobligate the remaining $14 million since it could not document that these obligations represented valid liabilities as required in Treasury guidance.[2] FAA had been still researching the need for the $14 million at the time of our draft report.

The amounts being freed up as a result of our review were for contracts and interagency agreements that were completed or canceled as long as 20 years ago. Most of these contracts[3] were never closed, and unused obligations were idle for years. FAA is in the process of reusing these funds or returning them to Treasury. The following are examples of the $35 million that FAA agreed to deoligate.

- About $1.7 million was obligated for an interagency agreement with the National Oceanic and Atmospheric Administration in September 2000, but no expenditures were made against this obligation. In response to our review, FAA deobligated these funds.

- An obligation made in November 1991 had its last expenditure in August 1992. FAA officials at the Technical Center were of the opinion that the project was being managed by Headquarters. Ultimately, FAA officials agreed that the remaining obligated balance of about $1.2 million was not needed and deobligated the funds to use on other projects.[4] The funds were idle for over 10 years.

- An obligation totaling $858,952 was made in August 1998 associated with a contract with Delta Airlines. No expenditures have been made for this

[2] Annual Treasury Financial Management Bulletins, including Bulletin No. 2004-005, Yearend Closing, provide that agencies that have not reviewed their unliquidated obligations during the year must do so before yearend closing. This ensures agencies properly record transactions meeting the criteria of valid obligations set forth in Title 31 United States Code (U.S.C.), Section 1501. Agencies are required to retain work papers and records on verifications to support future audits. Additionally, 31 U.S.C. 1501 states that obligations shall be recorded only when supported by documentary evidence. According to 31 U.S.C. 1108, the head of an agency shall submit an annual certification, supported by records, showing compliance with Section 1501.

[3] We reviewed FAA contracts, purchase orders, and interagency and rental agreements. In this report, the term "contracts" will refer to all of these types of legal agreements.

[4] Because this obligation was associated with an appropriation that does not expire, the funds can be reused on another project.

obligation. FAA officials were unable to locate the contract file, and information was unavailable because the contract was no longer assigned to a contracting officer at the time of our draft report.

The unneeded obligations identified in this review were allowed to sit idle for years for various reasons.

- Quarterly reviews of inactive obligations were either not performed or inadequately completed. Financial managers, program officials, and contracting officers were not adequately coordinating the review process to determine whether inactive obligations were still needed.

- Financial managers, program officials, and contracting officers were not held accountable for reviewing inactive obligations. For example, performance standards for these officials did not include requirements to review inactive obligations.

- FAA's policy does not require a review of inactive obligations with balances of less than $500,000. We included inactive obligations of less than $500,000 in our review to determine whether the policy needs to be adjusted, because about 68 percent of FAA's inactive obligations on F&E and RE&D accounts (about $79 million of $117 million) fell into that category. In fact, of the $35 million in unneeded obligations that FAA agreed to deobligate, about $24 million was for projects with inactive obligations of less than $500,000.

In addition to deobligating the entire $35 million of idle obligations identified, we are recommending that FAA revise its policy for reviewing inactive obligations to ensure that the review is coordinated among financial managers, program officials, and contracting officers. Best practices should be developed to perform these reviews and should include procedures to: (1) maintain a database that identifies the program official and contracting officer responsible for each inactive obligation; (2) require that financial managers periodically furnish lists of inactive obligations to program officials and contracting officers; (3) require that program officials research the need for each inactive obligation; (4) require that contracting officers close contracts and deobligate unneeded funds when notified that performance is completed; (5) require that contracting officers contact responsible program officials when contractual performance periods are completed to determine whether inactive obligations are still needed; and (6) require that financial managers scrub inactive obligations when program officials indicate that the obligations are still needed without providing support. We are also recommending that performance standards for financial managers, program officials, and contracting officers be modified to require that reviews of inactive obligations be completed in accordance with FAA's policy and that FAA revise its policy to periodically review inactive obligations of less than $500,000.

In its December 15, 2004 response to our draft report, FAA agreed with or provided an acceptable alternative action for our five recommendations (see Appendix). FAA indicated specific actions it plans to take for each recommendation. However, FAA's response is vague when addressing our recommendation to modify its policy to annually review the large volume of idle obligations of less than $500,000 and lacks a target completion date. In its response to our Audit Report on FAA's Financial Statements for FY 2001 and FY 2000,[5] FAA agreed to a similar recommendation to revise its procedures to lower its threshold for annually reviewing inactive obligations to $100,000 from $500,000. However, the recommendation was not implemented. Additionally, FAA has not provided target completion dates for recommendations requiring that FAA identify best practices for reviewing inactive obligations and modify performance standards for financial managers, program officials, and contracting officers to ensure adequate reviews are performed.

Therefore, we are requesting that within 30 days FAA provide more details on how it intends to modify its policy to review inactive obligations of less than $500,000 and timeframes to implement that recommendation and the recommendations to identify best practices for completing reviews and modify performance standards to ensure adequate reviews.

FINDING AND RECOMMENDATIONS

We issued audit reports in FY 1999, FY 2000, and FY 2002 that identified a total of $241 million of unneeded obligations at FAA. The results of our prior reviews are summarized in Exhibit B. In response to those reports, FAA acknowledged the need to strengthen its funds management efforts and took action to address the problems. Despite FAA's efforts, a significant number of unneeded obligations still exist, indicating that more aggressive corrective action is needed. We reviewed $81 million of inactive obligations and identified $35 million, or 43 percent of the amount reviewed, that no longer represented valid financial liabilities. The results of our review are summarized in Table 1. A detailed summary of our review of inactive obligations stratified by dollar range is in Exhibit C.

[5] OIG Report Number FI-2002-082, "Financial Statements for Fiscal Years 2001 and 2000," February 27, 2002.

Table 1. Unneeded Inactive Obligations as of December 31, 2002

Inactive Obligation Balances	**Samples Reviewed**		**Unneeded Obligations**	
	Number	**Amount ($000)**	**Number**	**Amount ($000)**
$500,000 and Greater	32	$38,658	13	$11,132
Less Than $500,000	846	$41,931	640	$23,712
Total	**878**	**$80,589**	**653**	**$34,844**

Although our review of inactive obligations concentrated on FAA Headquarters, the William J. Hughes Technical Center, the Mike Monroney Aeronautical Center, and the FAA Eastern Region, poor management of inactive obligations is a problem throughout FAA's regions. For example, we recently completed a review of the administration and oversight of contracts issued by three FAA regions. Although the purpose of the review was not to specifically assess inactive obligations, we identified about $233,000 of obligations associated with inactive contracts that could have been put to better use on other programs.

In this audit, we found that over $11 million of inactive obligations with balances of $500,000 or more and $24 million of inactive obligations with balances of less than $500,000 were unneeded. FAA policy does not require reviews of inactive obligations of less than $500,000, yet about 68 percent (about $79 million of $117 million) of all inactive obligations for F&E and RE&D accounts, as of December 31, 2002, were of less than $500,000.

FAA agreed that about $21 million of the $35 million we identified was not needed and has deobligated the funds. FAA had been researching the need for the remaining $14 million of inactive obligations for over a year. In its December 15, 2004 response to our draft report, FAA agreed with our recommendation to deobligate the remaining $14 million of inactive obligations since it could not document that these obligations represented valid liabilities as required in Treasury guidance. A detailed summary of amounts that FAA deobligated and those it was researching is presented in Table 2. A detailed summary of amounts deobligated and being researched by dollar ranges of inactive obligations reviewed is in Exhibit D.

Table 2. Summary of Unneeded Inactive Obligations, and Amounts FAA Agreed To Deobligate*

Remaining Obligation Balances	Amounts FAA Agreed to Deobligate at the Time of Our Draft Report		Amounts FAA Agreed to Deobligate in Its Response to Our Draft Report		Total Amount of Unneeded Inactive Obligations ($000)
	Number	Amount ($000)	Number	Amount ($000)	
Obligations of $500,000 and Greater	6	$5,841	7	$5,291	$11,132
Obligations of Less Than $500,000	538	$14,841	102	$8,871	$23,712
Total	**544**	**$20,682**	**109**	**$14,162**	**$34,844**

*As of December 31, 2002

Unneeded Amounts Are Being Deobligated

The $35 million that FAA agreed to deobligate was for contracts that were completed or canceled as long as 20 years ago. The obligations remained idle for years because the contracts were never closed. FAA officials were able to find contract documentation or coordinate with vendors to conclude that the inactive balances were no longer needed.

The following are examples of the $21 million of unneeded obligations that FAA deobligated by the time of our November 17, 2004 draft report.

- A project from the early 1990s had an obligation of $1.5 million. At the time of our audit, about $300,000 had been spent. When we asked about the need for the remaining $1.2 million, FAA deobligated it.

- An obligation of $1.7 million was created in September 2000 with the National Oceanic and Atmospheric Administration for Automated Surface Observing Systems services, equipment, and maintenance at airports and other surface weather observing sites nationwide. No expenditures had been made against this obligation, and FAA deobligated the funds.

FAA had been researching the need for the remaining $14 million of obligations that we reported as being unneeded since we began the audit. Accordingly, we recommended that FAA deobligate these amounts in our draft report. In its response to our recommendation FAA agreed to deobligate the $14 million.

At the time of our draft report, FAA was unable to locate the files for 10 contracts with inactive obligations totaling about $486,000. Additionally, 133 inactive obligations totaling about $12.5 million were associated with contracts that were no longer assigned to contracting officers. Program officials responsible for managing these obligations were not identified in most instances. Contracting officers or program officials changed positions or retired without being replaced, or contracts were completed but not closed. As a result, contracts were no longer being actively managed, and FAA was unable to obtain sufficient information to determine whether the inactive obligations were still valid.[6] The following are examples of obligations that FAA was researching at the time of our draft report but have agreed to deobligate in its response.

- In September 1998, FAA obligated $1.5 million under an agreement with the National Oceanic and Atmospheric Administration for personnel, equipment, and digital charting for FAA's Digital Bright Radar Indicator Tower Equipment (BRITE). No expenditures have been made since September 2000, and an unexpended balance of about $1.1 million remains.

- In November 1999, FAA obligated $900,000 under a contract with Unitech for engineering and technical support services related to telecommunications. Since December 1999, no expenditures have been made, and an unexpended balance of about $800,000 remains. At the time of our audit, there was no contracting officer assigned to manage the contract.

- In April 1993, FAA obligated $1.3 million for an agreement with the National Aeronautics and Space Administration's Ames Research Center. Since December 1999, no expenditures have been made. An unused balance of about $650,000 remains. The interagency agreement is not being actively managed.

Inactive Obligations With Balances of Less Than $500,000

As of December 31, 2002, FAA had 3,673[7] obligations totaling about $79 million that were of less than $500,000 with no payment activity for at least 18 months.

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[6] Based on findings and recommendations in prior audits, FAA has taken action to improve its contracting practices. For example, FAA has closed out about $4.7 billion in completed cost-reimbursable contracts, performed a bottom-up review of its contract management practices, and implemented a centralized filing system. Therefore, we are not making additional recommendations for contract management practices at this time.

[7] The initial universe of inactive obligations for contracts was 3,705. Of these, 3,673 were for obligations of less than $500,000. From the universe of 3,705, we judgmentally selected 878 inactive obligations for this audit. Of these, 846 were for obligations of less than $500,000.

These obligations represented about 68 percent of FAA's total inactive obligations of about $117 million. We reviewed 846 of the inactive obligations of less than $500,000, totaling about $42 million, to determine how many were unneeded. We found that 640 obligations totaling about $24 million, or about 57 percent of the amount reviewed, were unneeded. FAA deobligated about $15 million at the time of our draft report and has agreed to deobligate the remaining $9 million in its response to our draft report (see Table 2).

Based on our review, FAA agreed to deobligate the following examples of inactive obligations of less than $500,000.

- In FY 1985, FAA created three obligations totaling about $819,000 for training and software programming. None of the individual obligations exceeded $500,000. No money was ever expended against these obligations. FAA has agreed to deobligate these funds.

- In FY 2000, FAA created an obligation for about $368,000 under a real estate lease agreement for a major air traffic control facility. FAA misidentified accounting information and had to obligate new funds to cover the expenditure, leaving the original obligation untouched. There was no contracting officer assigned to manage the contract. FAA has deobligated these funds.

- In June 1996, FAA obligated $1,000,000 for a contract with the Jet Propulsion Lab at the California Institute of Technology. The last expenditure under this obligation occurred in 1998. FAA had no contracting officer assigned to manage the contract, which had been completed for over 4 years with a remaining inactive balance of almost $19,000 at the time of our review. FAA agreed the funds were not needed and deobligated them.

- FAA obligated about $163,000 for a contract in September 1999. The last expenditure was made in May 2001, and the remaining obligation is about $102,000. The contract was no longer assigned to a contracting officer, and the FAA program officials did not notify the original contracting officer that the contract had been completed.

Reasons Unneeded Inactive Obligations Were Not Identified

We identified three primary reasons why unneeded inactive obligations were not identified. First, the quarterly reviews of inactive obligations were either not performed or were inadequately completed. Financial managers, program officials, and contracting officers were not appropriately coordinating to determine whether inactive obligations were still needed. Second, performance management techniques were not used to hold financial managers, program officials, and contracting officers accountable for reviewing inactive obligations. Third, FAA's policy does not require a review of inactive obligations with balances of less than $500,000.

Required Reviews Were Not Performed or Were Inadequately Completed

FAA's policy on reviewing inactive obligations places the burden for conducting the reviews on financial managers. However, financial managers need input from contracting officers and program officials to determine whether obligations are still needed.

Financial managers must review obligation and payment records to identify inactive obligations and provide program officials and contracting officers with lists of inactive obligations. Program officials, responsible for requesting goods and services, must determine whether the goods and services have been delivered and whether significant additional amounts will be billed. This information must be passed to contracting officers, who are responsible for closing the contracts and deobligating unneeded funds.

We found a breakdown in coordination of reviews between financial managers, program officials, and contracting officers. The reviews were not being adequately performed by any of the groups. Financial managers did not ensure that all program officials and contracting officers received lists of inactive obligations for contracts. Also, financial managers did not sufficiently follow up to obtain responses on the status and need for inactive obligations. Contracting officers and program officials were not consistently obtaining enough information to demonstrate whether the obligation was still valid. Over $5 million of the $11 million of unneeded obligations for inactive projects of $500,000 or more was for projects that were still being researched after more than a year.

The program official[8] responsible for managing the obligation plays a key role in efforts to identify unneeded obligations. The program official must notify the contracting officer as soon as goods and services are accepted so that the contracting officer can take steps to close the contract and deobligate the remaining funds. If the funds are deobligated promptly, they can be used to finance new projects or used to pay for expenditures or cost overruns on other projects. However, program officials responsible for managing contractual obligations were not coordinating with contracting officers, and, as a result, funds were not being used effectively.

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[8] A business manager assigned to each program is generally responsible for managing obligations. The business manager maintains records to ensure that sufficient funds are available to cover expenditures under existing and new contracts and identifies obligations that are no longer needed. The business manager should notify contracting officers when work is completed or canceled so that unused obligations can be deobligated.

Contracting officers have a responsibility to manage contracts until goods and services are accepted and the contract is closed. Any remaining obligations can then be deobligated for use on other projects. Many contracts were old and were no longer being managed. Although the contracts had been completed or canceled, they were never closed. For example, we found that 133 obligations associated with about $12.5 million of contracts had been inactive and were no longer assigned to contracting officers. FAA needed considerable time to locate the files and even then, in many cases, it did not have sufficient information to determine whether the remaining obligation was still needed. FAA could not find 10 contract files associated with about $486,000 of the obligations being researched.

FAA must modify its policy and develop best practices for reviewing inactive obligations. The best practices should include procedures to: (1) maintain a database that identifies the program official and contracting officer responsible for each inactive obligation; (2) require that financial managers periodically furnish lists of inactive obligations to program officials and contracting officers; (3) require that program officials research the need for each inactive obligation, document the results, and notify financial managers and contracting officers of unneeded obligations; (4) require that contracting officers close contracts and deobligate unneeded funds when notified that performance is completed; (5) require that contracting officers contact responsible program officials when contractual performance periods are completed to determine whether inactive obligations are still needed; and (6) require that financial managers scrub inactive obligations when program officials indicate that the obligations are still needed without providing support.

Performance Management Techniques Are Not Used

FAA financial managers, program officials, and contracting officers need to be held accountable for ensuring that unneeded obligations are identified in a timely manner and deobligated and used elsewhere. Collectively they know when contractual performance is completed and whether excess obligations exist that should be deobligated. FAA can improve its financial management practices by making the determination of valid obligation amounts a required management practice. Financial managers, program officials, and contracting officers who are responsible for requesting goods and services and managing obligation balances need to be held accountable by including provisions in their performance standards for managing funds and deobligating unneeded obligations.

Reviews of Inactive Obligations of Less Than $500,000 Not Required

FAA policy does not require any review of inactive obligations that are valued at less than $500,000. Overall, we found that a significant number of unneeded inactive obligations with balances of less than $500,000 existed at the accounting offices visited simply because they are not periodically reviewed. Treasury guidance requires that agencies review and certify the validity of all obligations, so obligations of less than $500,000 should be reviewed to ensure they are valid.

Most of FAA's inactive obligations were of less than $500,000 (3,673 of 3,705). About 68 percent of the total value of all inactive obligations ($79 million of $117 million) was for inactive obligations of less than $500,000. We reviewed a judgmental sample of 878 inactive obligations, of which 846 were for inactive obligations of less than $500,000. Of about $42 million associated with obligations of less than $500,000 reviewed, we identified about $24 million (57 percent) in unneeded obligations that should be put to use on other projects.

We previously recommended that FAA amend its policy to begin reviewing inactive obligations under $500,000. In our Audit Report on FAA's Financial Statements for FYs 2001 and 2000, we reviewed inactive obligations of $100,000 or more and identified about $45 million of inactive obligations that were no longer needed. About $23 million of the unneeded amount was for inactive obligations with balances of $100,000 or more but less than $500,000. As a result of the significant identified unneeded obligations with balances less than $500,000, we recommended that FAA amend its policy to lower its threshold for reviewing inactive obligations to $100,000 from $500,000. Although FAA concurred with the recommendation, FAA did not amend its policy to implement the recommendation.

RECOMMENDATIONS

FAA had already deobligated $21 million of inactive obligations by the time we issued our draft report. Additionally, FAA has agreed to our recommendation to deobligate the remaining $14 million that we identified as being unneeded. We recommend that the FAA Administrator direct the Chief Operating Officer of the Air Traffic Organization, Assistant Administrator for Region and Center Operations, and the Chief Financial Officer to develop and implement management controls to:

1. Ensure that quarterly reviews and documented annual reviews of inactive obligations are performed as required by FAA's policy.

2. Identify best practices for reviewing inactive obligations and require that financial managers, program officials, and contracting officers use these practices in their reviews.

3. Modify performance standards for financial managers, program officials, and contracting officers to require that adequate reviews of inactive obligations be performed in accordance with FAA policy.

4. Revise FAA's policy to ensure that inactive obligations of less than $500,000 are reviewed annually.

5. Deobligate the $14 million of inactive obligations covered in this review that are still being researched.

MANAGEMENT COMMENTS AND OIG RESPONSE

We provided FAA with a draft of this report on November 17, 2004, and FAA provided a written response on December 15, 2004. FAA's Assistant Administrator for Financial Services and Chief Financial Officer agreed with four of five recommendations and partially concurred with one recommendation (see Appendix). For the recommendation that received a partial concurrence, FAA's proposed alternative planned actions meet the intent of our recommendation.

Specific comments by the Assistant Administrator and FAA's planned actions on our recommendations are provided below.

Recommendation 1: FAA concurred. FAA stated that it will develop a coordinated process to be used by financial managers, contracting officers, and program managers to oversee inactive obligations. FAA is currently testing a pilot process in two regions, which includes the establishment of a new report to facilitate the identification and research of obligations. This pilot will be the foundation of the corporate approach that will be implemented in FAA during FY 2005. Included in this approach is a comprehensive update to the policy, quarterly and annual reviews, and use of performance measures to monitor overall performance.

OIG Response: FAA's planned actions meet the intent of our recommendation, and the proposed FY 2005 timetable is acceptable.

Recommendation 2: FAA concurred. FAA stated it plans to establish performance measures to monitor the number and dollar amount of inactive obligations reviewed and deobligated. This information will be reported to the Administrator and at FAA Management Board meetings on a periodic basis. Additionally, FAA plans to have the Office of Financial Services research other best practices to determine what controls can be implemented to significantly reduce inactive obligations.

OIG Response: FAA's planned actions meet the intent of our recommendation. We request that FAA provide us with a timeframe with milestones for completing these actions.

Recommendation 3: FAA partially concurred. FAA stated that implementing a single performance standard for every FAA employee involved with an obligation would not guarantee a reduction in inactive obligations and was therefore not the best approach. FAA agreed to use performance standards when warranted, considering factors such as the employee's prior response to inactive obligations and the volume and the dollar amount of the obligations. FAA stated it will be more proactive in managing the issue of inactive obligations rather than implementing a wholesale performance standard.

OIG Response: FAA's proposed alternative procedures meet the intent of our recommendation. However, we request that FAA provide us with a timeframe for completing the proposed actions.

Recommendation 4: FAA concurred. FAA stated that it will reassess the current policy to determine how best to handle the large volume of low-dollar inactive obligations.

OIG Response: Although FAA agrees with the recommendation, its response does not indicate whether it intends to revise its policy to ensure that inactive obligations of less than $500,000 are reviewed annually. It indicates that it will assess how to review these obligations. Therefore, we are requesting that FAA provide more details on how it plans to modify its policy to review the low-dollar inactive obligations. We are also requesting that FAA provide us with a timeframe for implementing the planned action.

Recommendation 5: FAA concurred. FAA stated it will deobligate the entire $14 million no later than April 30, 2005.

OIG Response: FAA's planned action is in agreement with our recommendation.

ACTION REQUIRED

Actions taken and planned by FAA are reasonable, and FAA's alternative course of action for Recommendation 3 is acceptable. In accordance with Department of Transportation Order 8000.1C, we request additional comments and a completion target date for Recommendation 4 and completion target dates for Recommendations 2 and 3 within 30 days.

We appreciate the cooperation and assistance of FAA's representatives. If you have any questions concerning this report, please call me at (202) 366-1992 or Theodore Alves, Assistant Inspector General for Financial and Information Technology Audits, at (202) 366-1496.

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cc: FAA Deputy Administrator
Air Traffic Chief Operating Officer
FAA Chief of Staff
Anthony Williams, ABU-100

EXHIBIT A. SCOPE AND METHODOLOGY

FAA reported a balance of contract-related F&E and RE&D obligations in its accounting books and records of about $2.1 billion on December 31, 2002. Using computer inquiries into the Departmental Accounting and Financial Information System (DAFIS), we identified a universe of 3,705 contract-related inactive obligations totaling $117 million. We defined an inactive obligation as an obligation having no activity for 18 months as of December 31, 2002.

We verified the reliability of obligation balances and expenditures in DAFIS for FY 2001 and prior years in our annual audits of FAA's financial statements. An independent accounting firm, KPMG, verified the reliability of obligation balances and expenditures in DAFIS in annual audits of FAA's financial statements for FY 2002 and FY 2003. We determined that the DAFIS transactions and obligation balances were reliable based on the annual audit results. We also traced obligation balances to contracts and expenditures to invoices and public vouchers on a judgmental basis throughout our audit and found no exception with the DAFIS balances and expenditure data.

The objective of the audit was to determine whether FAA's inactive obligations represented valid financial liabilities. To determine the validity of FAA's inactive obligations as recorded in DAFIS, we judgmentally selected 878 obligations totaling $81 million from the 3,705 contract-related inactive obligations. We stratified the judgmentally selected sample by dollar range. We selected high-dollar inactive obligations of over $500,000 and inactive obligations between $100,000 and $499,999. We also reviewed contract-related obligations under $100,000. The reasons for this stratification follow.

Obligation Amount	**Stratification Rationale**
$500,000 and greater	To evaluate the effectiveness of carrying out current FAA policy in identifying unneeded funds
$100,000 to $499,999	To evaluate the continued need to implement our prior audit recommendation to lower the review threshold
Up to $100,000	To evaluate FAA's compliance with Treasury guidance to review inactive obligations of less than $100,000

We visited the three FAA accounting offices with the largest number of high-dollar and old contract-related obligations with no expenditures for 18 months as of December 31, 2002. The three locations were FAA Headquarters in Washington, DC; the William J. Hughes Technical Center in Atlantic City, NJ; and the Mike Monroney Aeronautical Center in Oklahoma City, OK. We also reviewed contract-related obligations in the FAA Eastern Region.

For the four locations visited, we requested that FAA financial managers provide documentation to support that inactive obligations were still needed. We interviewed contracting officers and program officials and reviewed obligating documents, including contract files. We used DAFIS to validate that unneeded funds had been deobligated and could be used on active projects or returned to Treasury. We evaluated FAA's policies and procedures for identifying unneeded inactive obligations and deobligating unneeded amounts.

We have issued two reports[1] with significant recommendations addressing a material weakness that existed in FAA's management of cost-reimbursable contracts, primarily those awarded by FAA Headquarters and the William J. Hughes Technical Center. FAA has taken significant actions to strengthen its contract management, including dedicating $3 million for audits of 185 contracts, completing a bottom-up review of its Headquarters' contract management function, and implementing a centralized system for filing contracts managed at FAA Headquarters. We also recently issued a report on FAA's management of contracts at its regions,[2] which recommended significant corrective actions. Accordingly, we are not making recommendations to improve contract management in this report.

We performed our audit from May 2003 through September 2004. The audit was conducted in accordance with Government Auditing Standards prescribed by the Comptroller General of the United States and included such tests as we considered necessary to provide reasonable assurance of detecting abuse or illegal acts.

[1] OIG Report Number FI-2002-092, "Oversight of Cost-Reimbursable Contracts, FAA", May 8, 2002, and OIG Report Number FI-2004-031, "Report on Consolidated Financial Statements for Fiscal Years 2003 and 2002, DOT," January 30, 2004.

[2] OIG Report Number AV-2004-094, "FAA's Administration and Oversight of Regionally Issued Contracts," September 28, 2004.

EXHIBIT B. PRIOR OIG REPORTS ADDRESSING INACTIVE OBLIGATIONS

OIG Report Number FE-1999-131, "Inactive Obligations, DOT," September 27, 1999

We identified significant amounts of unneeded inactive obligations in several DOT Operating Administrations, including FAA. For FAA, we reported $179 million of unneeded funds that should be deobligated and reapplied to active aviation projects. In response, FAA implemented an Agency-wide policy requiring quarterly reviews of all inactive obligations (1) greater than $5 million, (2) from $1.5 million to $5 million with no payment activity for 18 months, and (3) from $500,000 to $1.5 million with no payment activity for 30 months.

OIG Report Number FI-2000-125, "Inactive Obligations on Contracts, DOT," September 25, 2000

We identified $17 million of unneeded funds on FAA's capital investment contracts that should be deobligated and applied to active projects. In response, DOT agreed to provide Agency-wide guidance to contracting officers on reviewing completed contracts to identify and deobligate unneeded funds.

OIG Report Number FI-2002-082, "Financial Statements for Fiscal Years 2001 and 2000, FAA," February 27, 2002

During our audit of FAA's FY 2001 financial statements, we identified $45 million of unneeded inactive obligations. We advised FAA's financial managers that as a result of our findings, FAA should lower its review threshold from $500,000 to $100,000 for projects with no payment activity for 30 months. FAA agreed but did not implement the change.

EXHIBIT C. UNNEEDED INACTIVE OBLIGATIONS STRATIFIED BY SIZE OF OBLIGATION*

Obligation Balances	Samples Reviewed		Unneeded Obligations	
	Number	Amount ($000)	Number	Amount ($000)
Greater than $1,500,000	5	$15,985	1	$1,658
$500,000 to $1,500,000	27	$22,673	12	$9,474
Subtotal of $500,000 and Greater	**32**	**$38,658**	**13**	**$11,132**
$100,000 to $499,999	185	$35,902	109	$19,407
$1,000 to $99,999	348	$5,958	275	$4,235
Less than $1,000	313	$71	256	$70
Subtotal of Less Than $500,000	**846**	**$41,931**	**640**	**$23,712**
Total	**878**	**$80,589**	**653**	**$34,844**

***As of December 31, 2002**

EXHIBIT D. UNNEEDED INACTIVE OBLIGATIONS: DEOBLIGATED AND BEING RESEARCHED*

Obligation Balances	Amounts FAA Agreed to Deobligate at the Time of Our Draft Report		Amounts FAA Agreed to Deobligate in Its Response to Our Draft Report		Total Amount ($000)
	Number	Amount ($000)	Number	Amount ($000)	
Greater than $1,500,000	1	$1,658	0	$0	$1,658
$500,000 to $1,500,000	5	$4,183	7	$5,291	$9,474
Subtotal of $500,000 and Greater	**6**	**$5,841**	**7**	**$5,291**	**$11,132**
$100,000 to $499,999	66	$11,349	43	$8,058	$19,407
$1,000 to $99,999	233	$3,430	42	$805	$4,235
Less than $1,000	239	$62	17	$8	$70
Subtotal of Less Than $500,000	**538**	**$14,841**	**102**	**$8,871**	**$23,712**
Total	**544**	**$20,682**	**109**	**$14,162**	**$34,844**

***As of December 31, 2002**

EXHIBIT E. MAJOR CONTRIBUTORS TO THIS REPORT

<u>**THE FOLLOWING INDIVIDUALS CONTRIBUTED TO THIS REPORT.**</u>

Name	Title
Terrence J. Letko	Program Director
Mary Smothers	Project Manager
Robert Anderson	Senior Auditor
Thomas Wiener	Senior Management Analyst
Brian Frist	Management Analyst
Jill Cottonaro	Management Analyst
Kathleen Huycke	Editor
Narja Hylton	Auditor
Allison Horkan	Auditor

APPENDIX. MANAGEMENT COMMENTS

U.S. Department of Transportation
Federal Aviation Administration

Memorandum

Subject: **INFORMATION:** Draft Report on the Audit of Inactive Obligations, FAA

Date: DEC 15 2004

From: Assistant Administrator for Financial Services and Chief Financial Officer

Reply to Attn. of:

To: Assistant Inspector General for Financial and Information Technology Audits

As requested in your memorandum dated November 17, attached are the Federal Aviation Administration's comments to each recommendation in the subject report.

If you have questions or need further information, please contact Anthony Williams, Budget Policy Division, ABU-100. Mr. Williams can be reached at 267-9000.

Ramesh K. Punwani

Attachment

Federal Aviation Administration's (FAA) Response to the Office of Inspector General's Draft Report on the Audit of Inactive Obligations

Recommendation 1: Ensure that quarterly reviews and documented annual reviews of inactive obligations are performed as required by FAA's policy.

Response 1: Concur. The Office of Financial Services and Chief Financial Officer, Chief Operating Officer of the Air Traffic Organization, and the Assistant Administrator for Region and Center Operations will jointly develop a process to be used by financial managers, contracting officers, and program managers to oversee inactive obligations. FAA is currently testing a pilot process in two regions in response to a recommendation in the audit on "Administration of Regionally Issued Contracts." This pilot includes the establishment of a new DELPHI/PRISM report to facilitate identification and research of the obligations. The pilot will serve as the foundation for the corporate approach that will be implemented in FAA during fiscal year 2005. The approach will include a comprehensive update to the policy, quarterly reviews, annual reviews, and the use of performance measures to monitor overall performance.

Recommendation 2: Identify best practices for reviewing inactive obligations and require that financial managers, program officials, and contracting officers use these practices in their reviews.

Response 2: Concur. FAA will establish preliminary performance measures to monitor the number and dollar amount of inactive obligations reviewed and/or deobligated. This information will be reported to the Administrator and shared at FAA Management Board meetings on a periodic basis. In addition, the Office of Financial Services will research other best practices to determine what controls can be put in place to significantly reduce inactive obligations, freeing money up for other purposes.

Recommendation 3: Modify performance standards for financial managers, program officials, and contracting officers to require that adequate reviews of inactive obligation be performed in accordance with FAA policy.

Response 3: Partially concur. The establishment of a single performance standard for every FAA employee that is involved with an obligation will not guarantee a reduction in inactive obligations. FAA Management will use such a standard when warranted, using factors such as the employee's prior response to inactive obligations, the volume of obligations, and the dollar amount of the obligations. Organizational performance measures and FAA Management Board attention have worked well in resolving other management issues. The FAA will be more proactive in managing this issue rather than implement a wholesale performance standard.

<u>Recommendation 4</u>: Revise FAA policy to ensure that inactive obligations of less than $500,000 are reviewed annually.

<u>Response 4</u>: Concur. The FAA will revisit the current policy and determine how best to handle the large volume of low dollar inactive obligations.

<u>Recommendation 5</u>: Deobligate the $14 million of inactive obligations covered in this review that are still being researched.

<u>Response 5</u>: Concur. Program offices will be notified to issue purchase requests in PRISM to deobligate funding on these inactive obligations. These actions will be completed no later than April 30, 2005.