UNITED STATES GOVERNMENT LIBRARY OF CONGRESS

Memorandum

Office of the Inspector General

TO: Jo Ann Jenkins
Chief Operating Officer

April 15, 2008

FROM: Karl W. Schornagel
Inspector General

SUBJECT: Summary of the Status of the Library's Fixed Asset Control System

Integrated Support Services (ISS) is responsible for maintaining the Library's fixed asset control system, reconciling this system to the Library's general ledger, and conducting annual fixed asset inventories. During the Library's FY 2007 financial audit, ISS advised the Office of the Chief Financial Officer (OCFO) that it could not locate a significant number of the Library's fixed assets.

We reviewed the variances and related reconciliations. We concluded that the Library's fixed asset control system was neither designed nor operating properly. There were control weaknesses throughout the fixed asset lifecycle, including the processes to:

- capitalize new assets,
- periodically reconcile subsidiary systems to the general ledger,
- maintain records to accurately account for physical inventory variances,
- dispose of retired assets, and
- oversee property records.

We analyzed the internal control system related to fixed assets. Our findings are summarized in the attached report, which:

- documents the elements and objectives of a sound fixed asset control system
- highlights the Library's control breakdowns, and
- briefly presents the Library's plan to resolve this situation.

Given this breakdown in controls, the Library's external auditors have reported a material weakness in their opinion on the Library's FY 2007 financial statements. Furthermore, the Library had to make significant adjustments to its financial statements. Since these control issues continued well into FY 2008, it is likely that the material weakness will also appear in the auditors' FY 2008 report. Finally, this breakdown has resulted in significant delays and substantial added audit costs in issuing the auditors' opinion on both the Library and Madison Council financial statements.

We provided draft copies of our report to OCFO and ISS for review and comment. OCFO had no comments; however, ISS' response included several points of disagreement. We have addressed ISS' comments by separating them into two groups: the first, which we address immediately following our report, consists of substantive issues. The second group, which we address in table 1, starting on page 4, addresses minor factual issues brought up by ISS for which a detailed response is not necessary. We have omitted attachments 2 and 3 from ISS' response as they consisted of detailed tables and a brochure that were not necessary for the purpose of this memorandum.

We recommend that ISS review Financial Services Directive 02-03: *Guidelines for Accounting for Capitalized Property and Depreciation* to assist it in understanding the context of this issue.

OCFO and ISS have begun a joint project to remedy the control issues identified in our report. We will monitor this effort as it progresses.

attachments

OIG Assessment of ISS' Response

As steward of the Library's fixed asset subsidiary accounting system, Integrated Support Services (ISS) has primary responsibility for overseeing controls over fixed assets and ensuring the accuracy of the fixed asset financial accounting records.

ISS plays a critical role in the fixed asset lifecycle. It –

- receives most new fixed assets,
- identifies expenditures to be capitalized,
- conducts and reconciles fixed asset inventories, and
- controls fixed asset disposal.

Because it is the only participant at key times in the fixed asset lifecycle, ISS occupies the best position to recognize control breakdowns.

Notwithstanding its position and responsibility, ISS did not respond in a timely manner to breakdowns in fixed asset internal control that became evident by early 2007. As a result, a material internal control weakness in the Library's internal control system was cited in the independent auditor's report on the Library's fiscal year (FY) 2007 financial statements.

On March 14, 2008, the Director of ISS provided a response to OIG's draft memorandum dated February 27, 2008. Substantive areas addressed in the ISS Director's response include:

- responsibility for managing the Library's fixed assets, including reconciliation of the fixed asset subsidiary ledger with the Library's general ledger,
- the timeliness of ISS' notice to OCFO regarding the inventory variances included in the January 2007 inventory, and
- valuation of the fixed assets that could not be located.

Our assessments of the substantive areas addressed by ISS follow:

Fixed Asset Management Responsibility

No system of internal controls can function if ownership of key assigned responsibilities is not taken.

The ISS Director believes that ISS satisfactorily meets its fixed asset management responsibilities, including its responsibility to effectively manage fixed asset internal controls. The Director also claims that ISS is not responsible for reconciling the fixed asset subsidiary ledger with the Library's general ledger, does not have authority to adjust the subsidiary ledger to reflect variances in fixed asset inventories, and is not responsible for tracking and documenting fixed asset disposals.

We disagree with the ISS Director. Library guidance in Financial Services Directive 02-03, *Guidelines for Accounting for Capitalized Property and Depreciation*, makes it clear that ISS is responsible for reconciling the fixed asset subsidiary ledger with the Library's general ledger, is authorized and responsible for adjusting the subsidiary ledger to reflect all variances in fixed asset inventories, and is responsible for documenting the details of each fixed asset disposal.

Moreover, OIG believes ISS provided information to the Library's Management Control Program on internal controls for the Library's fixed assets that is in conflict with the January 2007 inventory findings. Specifically, from a rating of 65 for FY 2005 (high end of the medium risk level range), ISS management downgraded the risk level for fixed asset control twice to ratings of 46 for FY 2006 (low end of the medium risk level range) and 42 for FY 2007 (low risk level). ISS reported its FY 2007 risk assessment to the Management Control Program in March 2007 after the January 2007 inventory variances had come to light.

Timeliness of ISS' Notice Regarding Inventory Variances

A key feature of an internal control structure is timeliness. Breakdowns in the system must be caught, reported, and corrected on a timely basis.

The ISS Director claims that ISS advised OCFO of the fixed asset inventory variances prior to October 2007, stating "… OCFO had been notified each year for the past several years of the 'not found' assets on the annual inventory list." However, the Director's claim is not consistent with other information; specifically, the claim is in conflict with the January 31, 2008 memorandum that the Director and the Chief Financial Officer (CFO) sent to the Inspector General and a statement made by the Acting Head of Logistics.

The ISS/CFO memorandum advised the Inspector General that ISS first notified OCFO that significant fixed asset shortages were found in the fixed asset inventories when "… ISS/Logistics delivered the FY 2007 Inventory Report to OCFO toward the end of October 2007….Prior to FY 2007, ISS has completed and submitted to OCFO a Fixed Ssset (sic) Inventory report. Items found during the inventory were checked, **however items not checked were not directly communicated to OCFO as being not found (i.e. shortages)** and OCFO did not question ISS about the unchecked items" (emphasis added). Additionally, the Acting Head of Logistics and his staff told OIG in late November 2007 that they notified OCFO about the fixed asset shortages in October 2007.

Moreover, OCFO maintains that it was not advised about the inventory variances until October 2007.

Valuation of the Fixed Assets That Were Not Found

The ISS Director's response to OIG's draft report suggests that the missing assets had minimal value, and therefore the losses were of little consequence. The Director referred to an evaluation performed by an ISS-engaged engineer who assessed the current market value of a few arbitrarily selected assets that were not found. In all cases the engineer concluded that the assets' values were negligible.

Notwithstanding the ISS Director's opinion and the engineer's conclusions, the significant asset value in this context is the value an item had when it left the Library's possession – not its current value – and because ISS cannot identify when the missing assets left the Library, it cannot determine the assets' relevant values.

Furthermore, it is inappropriate to suggest that the Library has no custodial responsibility for taxpayer-funded assets because the value of the assets is unknown.

Other Issues Raised by ISS

Table 1, which follows, contains OIG remarks on specific ISS comments that were not substantive.

Table 1: Detailed Table of ISS Assertions and OIG Comments

ISS Ref	ISS Assertion	OIG Comment
1	ISS does not prepare a quarterly reconciliation between the fixed asset control system and the general ledger fixed asset control accounts maintained by OCFO.	a) LOC FSD 02-03, *Guidelines for Accounting for Capitalized Property and Depreciation*, Sec. 3.1.2 states that Logistics (ISS) is responsible for periodic reconciliations. b) The ICP Vulnerability Assessment Worksheet prepared by ISS on 3/7/07 states that "fixed asset records are maintained in IBCFAS(AIS) with manual reconciliation with the Library Financial Accounts."
2	The original amount for the assets that were not found in the initial FY07 inventory was $29,796,304, not $31 million.	The ISS Director's January 31, 2008 reply to OIG questions states that "[i]n FY 07…after reviewing the 30.7 million originally unlocated assets, 161 items totaling $24.8 million were disposed of and removed from the book(s)."
3	The requested disposal records were beyond NARA's (and the Library's) records retention requirements.	FSD 02-03 states in Sec. 3.2: "Logistics shall maintain a file of supporting documents and data for each capitalized PP&E item. The file shall contain the following information: …Disposition paperwork."
4	ISS disagrees in general that "some … fixed assets may continue to have value. [M]ost, if not all of the IT equipment [has] no appreciable market value."	The issue is the value of the item at the time it was removed from the Library's possession. ISS cannot determine this because it does not know when the assets were removed. In some cases, there may be a significant difference between book value (because of depreciation) and market value.
5a	a) ISS advised OCFO of inventory variances before October 2007 and b) The Library did not have a written policy or procedure for removing inventory shortages from the financial ledgers.	In late November 2007 the Acting Head of Logistics and his staff advised OIG that they first notified OCFO about the fixed asset shortages in October 2007. In a memo dated January 31, 2008 Levering and Page advised OIG that ISS had not specifically advised OCFO of shortages until October 2007. OCFO has repeatedly advised OIG that ISS did not advise it about fixed asset inventory variances before October 2007. The Library policy for removing inventory shortages from financial ledgers is stated in FSD 02-03 and places this responsibility on Logistics. FSD 02-03 Sec. 3.6 prescribes Logistic's responsibility for adjusting the subledger for disposals and lost and stolen assets.

ISS Ref	ISS Assertion	OIG Comment
5b	ISS asserts it made no statements to the auditors concerning financial adjustments having been made to the Library's financial records as a result of physical inventories. ISS states that only OCFO can make adjustments to the Library's financial records.	Memoranda describing the fixed asset cycle were presented to ISS management for approval during the Library's financial audit. These memos, approved by ISS management, indicated that adjustments were made for inventory variances. Additionally, FSD 02-03 clearly requires Logistics to make such adjustments.
7	ISS asserts it did not write off $24 million in fixed assets because it did not have the authority or ability to do so.	Although factually correct, this response does not address the issue, which was that assets had to be written off by the Library in order to avoid a qualified opinion on its FY 2007 financial statements.
9	ISS maintains it advised OCFO of the variances in the January 10, 2007 inventory.	See 5a above.
10	ISS disagrees with the comment that Logistics personnel were inadequately trained and unaware of the primary internal control objectives for the system.	The material weakness cited by the independent public accountants reveals various breakdowns in ISS. Despite the management changes cited by the Director in 2004 and 2005, ISS did not fulfill its duties as required by FSD 02-03. ISS management also erroneously downgraded the area's risk level in the internal control program review for FY2007.
11	ISS disagrees with the statement that it did not recognize the objectives for controlling the disposal of fixed assets.	Logistics did not comply with FSD 02-03 and did not include the required disposal documentation in the subsidiary system. This makes it appear that ISS did not, in fact, recognize critical objectives for this process cycle.
12	ISS contends that the SU/su senior managers' certification accounts for the $17.5 million of questioned assets for which disposal paperwork could not be found.	This response makes it clear that ISS did not recognize critical objectives for this cycle. Management certifications without supporting documentation in no case could account for over $17 million in questioned assets.
Ctl Pt 1	ISS agrees with the IG's comment in general but disagrees that integration is necessary between the subsidiary ledger and the general ledger.	Integration means the systems should interface. We believe the Director is improperly defining integration. Additionally, her comment that the subsidiary ledger and general ledger should not be a common system in order to maintain data integrity of each shows a lack of system knowledge. Data integrity will be enhanced if the systems are in common and there will be greater operating efficiencies.
Ctl Pt 2	ISS maintains that there is centralized receiving of newly purchased assets.	During the search for missing assets the auditors found that significant quantities of newly purchased assets were shipped directly to the Culpeper audio visual center and to the Madison building. Logistics was unaware of these new assets and did not record them as newly purchased fixed assets.

ISS Ref	ISS Assertion	OIG Comment
Ctl Pt 3	ISS disagrees that assets are frequently transferred or disposed of without its knowledge.	ISS acknowledges in its reply that transfers were missed and unlocated assets in the inventory exceeded 35% of the asset base.
Ctl Pt 7	ISS asserts that the ISS/OCFO quarterly reconciliations have identified missed capitalizations of many new assets.	This assertion is not supportable in view of the independent public accountant's statement in its FY 2007 report that "the Library incorrectly recorded $20.3 million of expenditures that should have been capitalized…the Library initially recorded $48.9 million of non-capitalized equipment expenditures." The ratio of assets not properly capitalized to total expenditures is over 41%.

UNITED STATES GOVERNMENT

Memorandum

LIBRARY OF CONGRESS

Integrated Support Services

TO: Karl Schornagel
Inspector General

DATE: March 14, 2008

FROM: Mary Levering
Director, Integrated Support Services Mary Levering

SUBJECT: ISS Comments on Draft IG Report on the Library's Fixed Asset Control System

This is in response to your memo of February 27, 2008, requesting comments from Integrated Support Services on the Draft Report on "The Fixed Asset Control System at the Library of Congress." Robert Williams, Acting Head of Logistics, Quincy Allen, Assistant Head of Logistics and I have reviewed the draft carefully and we have collaborated in preparing the attached comments for your consideration. Because this is such an important matter to the Library and to ISS as well, we have given this a great deal of time and attention to be as accurate and thorough as possible.

Attachments:
1. ISS Responses to Draft IG Report, 3/14/08
2. Copies of Email Communications to SU/SU re Unlocated Assets (Jan-Feb 2007)
3. Additions/Corrections to Oct. 2007 Asset Reconciliation, 2/15/08
4. Computers For Learning, ISS Brochure, 6/06

cc w/copy of attachments:
Jo Ann Jenkins, COO
Lucy Suddreth, LIBN
Jeff Page, OCFO
Mary Levering, ISS
Robert Williams, ISS/LOG
Quincy Allen, ISS/LOG

File: ISS Audits — Fixed Assets Report 2-08

ATTACHMENT #1

Integrated Support Services/Logistics Services Response to Draft Report on Fixed Asset Control System, Dated February 27, 2008 March 14, 2008

1. <u>IG Statement</u>: Page 1, para 2 states:
ISS also prepares the quarterly reconciliation between the fixed asset control system and the general ledger fixed asset control accounts.

<u>ISS response</u>: ISS disagrees with this as stated.

ISS does not prepare a quarterly reconciliation between the fixed asset control system (i.e. sub-ledger) and the general ledger fixed asset control accounts maintained by the Office of the Chief Financial Officer (OCFO). OCFO had a process on a quarterly basis through which OCFO provided the ISS Property Control Unit with a list of expenditures during the previous quarter. OCFO requested that ISS attempt to determine, from the expenditure documents provided, whether the items identified on the expenditure document should be categorized as "Capitalized", "Funds Expended", "Funds Not Verified", or "Other Government Capitalized Expenditure". The ISS Property Control Unit provided this requested information to OCFO in an Excel spreadsheet by the categories cited. The ISS Property Control Unit validated the items categorized as "Capitalized" or "Other Government Capitalized Expenditure" to determine whether these items should be included in the IBCFACS database. However this OCFO process did not actually reconcile the ISS-managed fixed asset sub-ledger, maintained in the IBCFACS database, against the OCFO-managed general ledger.

2. <u>IG Statement</u>: Page 1, para 3 states:
During the audit ISS advised the Office of the Chief Financial Officer (OCFO) and Kearney & Company (Kearney), the Library's independent public accountants, that it could not locate approximately $31 million or 43%, of the Library's $72 million in fixed assets (at original cost), representing approximately $47 thousand in net book value.

<u>ISS response</u>: ISS agrees with the IG statement in principle but disagrees with the amounts cited.

According to ISS calculations, the original amount for the assets that were not found by OSS or Service Units in the initial FY07 inventory was $29,796,304 (not $31 million). This actually represents 41% (not 43%) of the Library's $72 million in assets (at original acquisition cost).

3. <u>IG Statement</u>: Page 1, para 4 states:
Further research by ISS and OCFO reduced the initial inventory variance by approximately $13 million. ISS also claims that it has been notified by service units that the remaining assets, mostly computer equipment, with a cost of $18 million have been disposed of. Neither it, nor the service units, however could find satisfactory records of these disposals.

<u>ISS response</u>: ISS agrees with sentence 1 and 2; however, ISS maintains that sentence 3 needs clarification because the disposal records were beyond NARA's (and the Library's) federal records retention requirements.

According to the National Archives and Records Administration's (NARA) General Record Schedule (GRS) 4, "Property Disposal Records" for transactions over $25,000 are to be destroyed after 6 years. This particular section (Item 3) of GRS 4 refers to the "sales and surplus personal property". Item 3 specifically is concerned with case files on sales of surplus personal property, comprised of invitations, bids, acceptances, lists of materials, evidence of sales, and related correspondence. ISS Office Systems Services/Records Management Section (OSS/RMS) has written one Records Disposition Authorization (RDA) for Property Disposal Records (PDR). RDA/PDR #1 is listed in the Library of Congress Records Schedule. PDR#1 states that original and duplicate records pertaining to equipment returned to Logistics for disposal (not sale) which has been declared as excess, obsolete and/or damaged equipment to the NLS/BPH program shall be destroyed when 3 years old. This PDR is applicable to any office of the Library that is disposing of this type of property, and is not limited to NLS/BPH. The Library expects service units to follow the records destruction schedule as published so that critical storage space is not used for non-essential records that should have been destroyed. It is most probable that key documentation that the IG expected service units to produce to verify disposal(s) was destroyed in accordance with the Library's established records destruction schedule. Therefore, documenting records of these particular disposals would not be available to the IG for review at this time.

Although ISS recognizes the applicability of the NARA federal records retention requirement as the probable reason disposal authorization documentation by service/Support units to account for the questioned $17.5 million, ISS also acknowledge its own critical process "gaps" for the timely updating of the fixed asset subsidiary ledger by Property Control Unit staff. The Property Control Unit has experienced two major office moves in the past several years, one from Landover to the Adams Building in 2000 when it was a part of the Contracts and Logistics division, then in August 2006 from the Adams Building to the Madison building for better management. In preparation for the whole C&L division 2000 move from Landover, there was a massive clean out of old out-dated documents and material, and ISS believes that some disposal documents not yet recorded in IBCFACS may have been inadvertently destroyed at that time. The adverse impact of both moves caused poor document control and poor system control and management.

4. <u>IG Statement</u>: Page 1, para 4 states:
The market value of these assets is not known. Most have been fully depreciated for accounting purposes, but some may continue to have value; assets often continue in service for periods far exceeding their depreciable lives.

<u>ISS response</u>: ISS disagrees in general that "some may continue to have value." ISS and ITS maintain that most, if not all of the IT equipment is obsolete with no appreciable market value.

According to federal statute [P.L. 107 - 217 Aug 21, 2002, para 527] the Administrator of the General Services Administration (GSA) may authorize the abandonment or destruction of property, or the donation of property to a public body if -

(1) the property has no commercial value; or
(2) the estimated cost of continued care and handling exceeds the estimated proceeds from sale.

Accordingly, each item disposed was determined by the service unit or the Property Control Unit to have met the criteria for destruction by GSA. The decision to dispose is not based on available utility value of the item according to Public Law; however it is based strictly on financial value based on commercial value or cost to maintain.

To address the IG's concern about possible residual value of old IT equipment disposed of by

LC/Information Technology Services (ITS), ITS consulted an engineer for ESE, a computer electronics firm, to sample the computer items disposed of for a determination of any residual value that could exist for the ITS items listed that were part of the $17.5 million of capitalized assets reviewed (see attached spreadsheet dated 2/15/08, "Additional corrections to October 2007 Asset Reconciliation"). The following statements were provided by this consultant, concerning subject computer equipment:

Example 1. EMC Integrated cached disk arrays. These are typically "traded in"as part of a technical refresh. After a period of typically 3 years, the residual value is less than 10% of the purchase price. This covers entries on the 2/15/08"Additions/Corrections to October 2007 Asset Reconciliation" list #50, 55, 56, 57, and 58. This is consistent with broad industry trends. The first hard disk sub-system, a part of IBM RAMAC, had a capacity of 5 MB and a cost of $150,*000*. A recent mid-range EMC SATA disk purchase was $4,000/TB, equivalent to about 2 cents for 5 MB.

Example 2. STK Tape Robot Library. This hardware uses 3 GB tapes with a mainframe data connection. LC no longer has a mainframe, and current tape technology uses 300 GB tapes, in a different format. The current value of this equipment is "NIL." LC had to pay to get it hauled off the floor. Item #71, a "Additions/Corrections to October 2007 Asset Reconciliation" list.

Example 3. CISCO routers. This covers items #90, 105 and 91 of the "Additions/Corrections to October 2007 Asset Reconciliation" list. A current fair value purchase price for CISCO 7206 equipment is $1,586. What LC would get selling them is far less. As the original acquisition cost was over $25,000, the residual value is less than 6 cents on the dollar.

Example 4. Product Name: IBM 3480-B22 Tape Drive Unit Mfg: IBM Mfg Part #: 3480-B22. Today's average price for each: $500 re-conditioned. Each 3480-B22 module contains two drives . These devices were produced from 1984 thru 1990. These drives were "BUS and TAG" connected. Bus and Tag connections were replaced by "ESCON" connectivity many years ago. Each 3480 tape held 100 megabytes and a modification to the drive allowed the tapes to contain 200 megabytes. Today's tape capacity is rated in gigabytes (1000mb). There is nothing in the market place that holds such a small amount as 200 megabyte. Today LOC uses magnetic tapes and tape drives (LTO4) rated at 800 gigabytes and they are 1/4 the size of the old 3480 200 megabyte cartridges. This addresses items #33 through #42 of the "Additions/Corrections to October 2007 Asset Reconciliation" list.

General Considerations.

There are three factors governing ITS' capital equipment disposal.

(1) **Mission.** For instance, the decision to retire the bulk of the outdated token-ring network.

(2) **Economic end of life.** In many cases, such as the EMC cached disk arrays, it is cheaper to trade in than to pay maintenance because of the enhanced performance at a reduced cost. The fact of economic end of life is generally accepted by the practice of depreciating computer equipment over five years. In many cases, this overstates the current value.

(3) **Vendor End of Life.** Vendors, such as CISCO, cease supporting and repairing equipment. This date is well known in advance. In order to provide high available service, it is important to stay withing vendor-supported configurations.

5a. **<u>IG Statement</u>:** Page 1, para 5 states:

We determined that the Library acquired the majority of these fixed assets over the last twenty years, most of the assets were fully depreciated, and a significant number of them were identified as missing in prior ISS inventories. (*Footnote 1*) ISS advised us that the Acting Head

of Logistics questioned the significant number of missing fixed assets in January 2007. However, ISS did not advise OCFO or any other Library organization of these major variances.

<u>ISS response</u>: ISS agrees with sentence 1 and 2 but disagrees with sentence 3.

It is a correct statement that the Library had acquired the majority of the subject $17.5 million disposed assets over the last twenty years. It is also accurate that the vast majority of these assets was electronic computer equipment, acquired prior to 1998. It is also true that many of these items were identified on previous ISS inventories and annotated as such to OCFO. ISS management actually began questioning in late 2006 and early 2007 (January-March) the FY06 inventory results, by notifying each service/support unit's property control Point of Contact to verify and validate the list of "not found" assets assigned to their service/support unit. Sample emails of these communications are attached, dated January and February 2007 (Attachment 2). Each service unit with unlocated assets was contacted at that time with a list of "unlocated" assets and asked to do further research on each unlocated item. Thereafter during the spring of 2007, ISS began in earnest redrafting processes and procedures for conducting the fixed asset inventory and annual inventory reconciliation to include a process of notifications and approvals through the LC Police and LC Chief Operating Officer for any items still considered "unfound". During informal inquiries by ISS to OCFO during the summer of 2007, inquiring about how to account for assets that are unlocated, it was determined by ISS and OCFO that the Library of Congress did not have a written policy or procedure for removing inventory shortages from the financial ledgers. At the conclusion of the FY2007 fixed asset inventory, as was done in previous years, ISS provided OCFO with the inventory results and more formally raised the issue again of how to remove "not found" items from the financial ledgers since carrying these totals was overstating the Library's financial accountability. However, OCFO had been notified each year for the past several years of the "not found" assets on the annual inventory list.

5.b <u>IG Footnote 1</u>: Page 2, Footnote 1

In FY2007 and prior, the OCFO and ISS had incorrectly asserted to the auditors that adjustments had been made to the Library's financial records as a result of physical inventories.

<u>ISS response</u>: ISS disagrees.

ISS made no assertions to the auditors concerning financial adjustments having been made to the Library's financial records as a result of physical inventories. Only OCFO can make adjustments to the Library's financial records, not ISS.

6. <u>IG Statement</u>: Page 2, para 1.

Furthermore, Kearney determined that ISS failed to capitalize over $18 million in asset expenditures during FY2007. Accordingly, we concluded that the Library's fixed asset control system had systemic breakdowns through the entire cycle:

- in the acquisition phase, by failing to properly capitalize expenditures.

- in the in-service phase, by failing to properly inventory and reconcile such inventories, and

- in the disposal phase, by failing to properly account for disposals.

<u>ISS response</u>: ISS agrees with the IG statement in principle.

The $18 million in asset expenditures during FY2007 referred to in this statement were actually expenditures uncovered by Kearney which needed further research for possible capitalization. ISS does not have access to the Library's expenditure records and, therefore ISS was not responsible for capturing additional expenditures beyond the actual asset cost reflected on the receiving documents for that asset. ISS does agree, however, that the Library's fixed asset control system, both financial and asset accounting, needs to be reviewed and overhauled. The ISS portion of this process – the in-service phase and the disposal phase – were identified by ISS as weak prior to FY2007 and new processes and procedures were being considered and drafted beginning in 2006-2007. From analyzing the processes and practices of the past, it was determined that inadequate training in the past, particularly of service/support unit property liaisons, poor source document management and control, and insufficient communication between the service units, ISS and OCFO were the primary cause for the breakdown of this system.

7. <u>IG Statement</u>: Page 2, bullet 5 states:
ISS concluded that there are no fixed asset shortages despite writing off over $24 million in fixed assets.

<u>ISS response</u>: ISS disagrees with this statement.
ISS did not write off $24 million in fixed asset shortages. ISS did work with the Library's Service and Support Unit directors, who had unlocateable items on their annual inventory, and who, after internal research in their service/support units, certified the disposal of 88 obsolete items, with an original acquisition cost of $17,552,982, and with a depreciated value of $6,525, for which disposal documents were no longer on file.

8. <u>IG Statement</u>: Page 2, bullet 6 states:
ISS failed to take a timely inventory for FY2006.

<u>ISS response</u>: ISS agrees.
The original due date of the FY2006 inventory was October 16, 2006. However, the ISS Property Control Unit staff, equipment, systems and records, had moved from the Adams Building to the Madison Building on August 30, 2006, so that ISS management could provide better oversight. This move, and the resulting efforts to ensure operability of the old IBCFACS system, and efforts by the team to get organized in a new physical location had a detrimental effect on PCU's ability to operate effectively on a timely basis during that period. ISS management met with the Inspector General's Office representative (Mary Harmison) in December 2006 and ISS was granted an extension to complete the 2006 physical inventory by January10, 2007. ISS submitted the inventory to OCFO on January 10, 2007, as agreed.

9. <u>IG Statement</u>: Page 2, bullet 7 states:
ISS did not advise OCFO of the large inventory variances found in the January 2007 inventory until October 2007. ISS' delay precluded OCFO from taking action that could have mitigated the effect on the Library's FY 2007 financial statements audit.

<u>ISS response</u>: ISS disagrees.
OCFO was provided the inventory results from the FY06 inventory on January 10, 2007 upon completion of the FY06 inventory. The FY06 inventory results reported unfound items to OCFO. ISS then provided the FY07 inventory results to OCFO in October 2007. ISS does not understand the relationship of the FY06 inventory completion date of January 10, 2007 and the effect on the FY07 financial statements audit as stated by IG. [It appears that the IG report may have confused two separate inventory reports – the FY06 inventory report, provided to OCFO on January 10, 2007, and the FY07 inventory report provided to OCFO in October 2007.]

10. <u>IG Statement</u>: Page 2, bullet 8 states:
The employees responsible for operating and managing the fixed asset system are inadequately

trained and are unaware of the primary internal control objectives for the system.

<u>ISS Response</u>: ISS disagrees.

ISS takes strong exception to this comment. *As a reminder*, ISS reiterates that it was the ISS managers and staff, who are directly responsible for the operation and management of the fixed asset system, who first raised the issue to OCFO, concerning the issues and the effect of the Library's continuing to maintain "not found" items on the OCFO's financial ledger. To ISS knowledge, this condition was not previously challenged by OCFO staff or the Library's independent auditor, Kearney and Company. While ISS concedes that in many cases, processes and procedures lacked the proper documentation, and that inadequate quality control by ISS was exercised; however, "inadequate of training" and an "unawareness of the primary internal control objectives for the fixed asset system" are not traits or characteristic of the current ISS managers and Property Control Unit staff. Each member of the ISS Property Control Unit, and all managers and supervisors up to and including the Acting Head of Logistics have attended, at a minimum, a 5-day course in *Basic Government Property Management*, within the last year, in addition to other relevant training in the past. In addition, PCU staff have been crossed-trained internally and a significant emphasis has been placed on accountability.

In fact, it was as a direct result of the Logistics manager's and Property Control Unit's comprehensive review of their policies and procedures prior to FY07 that significant gaps were uncovered and a corrective action plan was begun. These changes began to occur as a result of the appointment of Quincy Allen in 2004 as Assistant Head of Logistics and Robert Williams as Acting Head of Logistics in 2005, bringing new leadership and professional guidance to the entire Logistics Services operation. For the past three years, with ISS-funded support for a contractor and a technical writer to assist in the process, Logistics Services team has been reviewing and documenting all Logistics policies and procedures, identifying "gaps", determining training needed, drafting policy and procedure documents, and investigating various potential replacements for the stand-alone, DOS-based IBCFACS database.

11. <u>IG Statement</u>: Page 3, bullet 9 states:

ISS management did not fully recognize the objectives for controlling the disposal of fixed assets, including verifying and documenting that:

- **all computer hard drives are cleansed**
- **all hazardous materials (including radiological items) are properly disposed of,**
- **the Library obtains value for salvageable materials, and**
- **any gain or loss on disposal of assets is recorded.**

<u>ISS response</u>: ISS disagrees with the statement and the 4 bullets.

Bullet 1: ISS disagrees with this statement. ISS maintains extensive records on the entire process of reviewing and cleaning of computer hard drives before disposal, and has done so for several years. The computers are tightly controlled in batches, all are listed by bar code number, and records maintained on each computer as well as the batches. All surplus CPU's are routed to the ISS Automation Team in controlled batches for cleaning. In accordance with the Library's computer security policy and ITS security directive, all excess computer hard disks are cleaned of all stored data before being moved to surplus for disposal if inoperable or donated through the Computers for Learning Program. When cleaning hard drives, ISS follows the DoD standard (DoD 5220.22-M) which provides baseline standards for the protection of classified information released or disclosed to industry. This standard has become the "de facto" data cleaning policy throughout the federal government. The DoD standard requires 6 times overwrite of the entire hard drive plus 1 verify process.

After cleaning each hard disk thoroughly, the ISS Automation Team staff lists the bar code number and serial number on a tag which is affixed to the individual unit that has been cleaned and is to be returned to Landover/Logistics. Once the computers are cleaned, the ISS Automation Team records the date the CPU was received, the bar code, the date the CPU was cleaned, the date the CPU was picked up and returned to Landover warehouse, and which CPUs have been determined un-repairable. This information is recorded in the PC Cleaning Database which was developed and is maintained by the ISS Automation Team. Each bar code is also recorded on a separate checklist and the checklist is given to the LM Receiving team member when the cleaned CPUs are collected by the Logistics staff. The checklist of bar code numbers are validated against the original Logistics manifest for the batch to ensure that the batch is complete and all CPUs are accounted for. Thus complete records are maintained of the cleaning of all computer hard drives before disposal.

Bullet 2: During the past three plus years, ISS with the expert advice and assistance of the Safety Services Office, and with other Library offices who have hazardous waste materials, have conducted several carefully controlled and monitored disposals of hazardous waster materials, including chemicals and other materials. ISS provided detailed documentation on all of these.

With the expert advice and assistance of the ISS Safety Services/Environmental Engineer, ISS Logistics has for the past several years also ensured that hazardous materials in electronic waste assets are properly disposed of. During 2007 Robert Williams completed arrangements with UNICOR for the pick up and proper disposal of all e-waste surplus equipment from the Library. Until that procedure and MOU was approved in April 2007, e-waste equipment was stored at the Landover warehouse for at least a few years, awaiting proper disposal.

ISS Property Control Unit rarely handles other (non-electronic) equipment containing hazardous materials. In the rare instances that equipment containing hazardous materials are scheduled for disposal by the Property Control Unit (such as batteries, refrigerators, etc), the ISS Property Control Unit contacts the ISS Safety Services Office for guidance. In cases where equipment with hazardous waste must be removed from Library facilities, the Safety Services Office, not ISS Logistics, coordinates with an expert hazardous waste handling contractor, Clean Harbors Inc, for this removal, carefully follows all regulatory requirements in disposing of hazardous waste, as required in the federal universal waste regulations set forth in 40 CFR part 273, to protect the environment. For example, most commonly used lead acid batteries in large industrial warehouse equipment and trucks. In FY07, a total of 2,800 libs of batteries went to the appropriate treatment or recycling facilities pursuant to the hazardous waste regulatory controls. ISS Property Control is implementing additional controls to document all actions taken concerning removal of any equipment containing hazardous substances to record that the disposal is handled properly.

Bullet 3: The Library ensures that all salvageable materials are turned over to GSA which is responsible for obtaining value for of these on behalf of the U.S. Government. However, unless the Library were to choose direct sale as the method of disposal, the Library would not see any financial return for such items. For the past many years, all salvageable items are turned over to GSA for sale action, and the proceeds are returned to the U.S. Treasury, not the Library of Congress. This includes disposal of scrap metal, surplus cable, etc. However, one exception is the Library's participation in the Computers for Learning Program whereby surplus, operable, personal computers and peripherals are made available for donation to eligible non-profit, educational institutions, as defined by Executive Order 12999.

Bullet 4: See previous response. The Library of Congress has never held a direct sale of surplus assets.

12. <u>IG Statement</u>: Page 3, para 1 states:
In its latest inventory reconciliation, ISS contends that the Library is not missing any fixed assets. Its conclusion is based on "confirmations" from the Service and Support units that the approximately $18 million in missing fixed assets were disposed of, although no documentation to support this assertion exists.

<u>ISS response</u>: ISS contends that the SU/SU senior managers' certification do account for the $17.5 million of questioned assets.

According to NARA records retention directives, documentation would not be available from Service and Support Units, concerning any action that occurred more than 3 years ago for destruction of an asset or 6 years ago for the sale of the asset. Each SU/SU senior manager which had unlocated, obsolete equipment listed on the corrected ISS February 15, 2008 spreadsheet (copy attached), has *certified* that these obsolete items were disposed of as surplus equipment, and that the disposal records are no longer on file. These certifications account for the disposition of the assets. Most, if not all, were for obsolete, outdated equipment for which parts and maintenance were no longer available to the Library.

<u>Control Point/Responsible Area/Noted Weakness -- Chart</u>

1. <u>IG Comment</u>:
***Budgetary/Accounting Obligation and Expenditure*: OCFO. There is no integration between Momentum and the fixed asset subsidiary system. There is inadequate identification and ISS notification for capital expenditures at the requisition, contract, obligation, and expenditure stages. Consequently, ISS has difficulty identifying and capturing fixed asset purchases.**

<u>ISS Response</u>: ISS agrees with the IG's comment in general but disagrees that *integration* is necessary.

While ISS agrees that some electronic *interface* between Momentum and the fixed asset subsidiary system is needed and would be beneficial; however, ISS strongly disagrees that these systems need to be, or even should be *integrated.* ISS maintains that the subsidiary ledger and the general ledger should not be in a common system in order to maintain the data integrity of each. Furthermore, the required functions of the financial accounting for fixed assets and the requirements for physical asset accountability are very different and a single *integrated* system is not needed and should not be used. Because of the different mission focus of each, the subsidiary ledger and the general ledger should be in different systems, but – ISS strongly agrees – they should be reconciled often.

ISS responsibility (in relation to the various financial requirements listed on the IG chart) relates <u>only</u> to the contract/acquisition stage. An effective *interface* between OCFO's Momentum financial system and the separate ISS fixed asset system would create a "asset receipt due" file, based on Library acquisition orders placed, according to specific criteria. This would enable ISS to track pending receipts of fixed assets and to trace them from the point of receipt. However, ISS is not responsible for, nor involved in, any other aspect of the financial accounting for the asset, such as "requisition, obligation or expenditure". These are SU/SU and OCFO responsibilities, and are not relevant to ISS property control of the actual asset itself. Of greater importance for ISS to fulfill its responsibilities is being able to adequately track the physical location of the asset throughout its entire life cycle through to disposal, including tracking and monitoring physical moves of the asset, and ensuring that these are all recorded on a timely basis in the ISS subsidiary system.

2 **IG Comment:**
***Receiving*: ISS. There is no centralized receiving of newly purchased assets. Therefore, newly received assets are not always identified and recorded.**

ISS Response: ISS disagrees with sentence 1 and agrees with sentence 2.
The Library does have centralized receiving. The primary receiving site is Logistics Services at the Landover Center Annex, though some smaller, non-capitalized items are occasionally received directly at the Madison Building by the ISS Logistics/Receiving team and receipt is properly recorded there. Logistics also serves as the receiving point of contact for LOC off-site centers as well. The operation at Fort Meade is one occasional exception to the general rule of ISS centralized receiving, and is a good example of how a limited but well-controlled instance of occasional decentralized receiving can be successful.

This requires adequate staffing and understanding by on-site SU/SU personnel to make the required notifications to ISS Property Control Unit so PCU can capture data about any fixed asset that is delivered directly to the off-site facility and that must be accounted for in the subsidiary ledger. This past year represented an anomaly with the set-up of NAVCC in Culpeper, VA. ISS acknowledges that there was poor coordination between ISS and MBRS concerning transfer of information on what NAVCC equipment was being sent directly to NAVCC and what equipment was coming to the Landover/Logistics. During the NAVCC construction phase, ISS Logistics met numerous times with the representatives of NAVCC (particularly Ruth Scovil, the project manager) and set up processes and procedures to record and report the receipt of equipment at the NAVCC facility that needed to be bar coded. During these planning discussions, ISS also expressed concern to NAVCC managers that the MBRS logistics staffing was inadequate and should be increased from only 1 GS-6 staff member to at least 5 staff members, but this recommendation was not implemented by MBRS. Hence problems resulted from inadequate communications between MBRS and Logistics when equipment deliveries actually occurred. As a result, several pieces of capitalized equipment were received and installed at the Culpeper facility, but the ISS Property Control Unit was not notified on a timely basis and the assets were not properly captured and recorded on the FY07 inventory as capitalized equipment.

3. **IG Comment:**
***Service Unit Custody*: ISS/Service Units. Documented requirements for service unit fixed asset custody and communication with ISS are weak. Assets are frequently transferred or disposed of without ISS' knowledge.**

ISS Response: ISS agrees with sentence 1 but disagrees with sentence 2.
ISS agrees that procedures and communications were weak in the past. ISS also agrees that some IT assets were sometimes (but not "*frequently*") traded in or exchanged without ISS knowledge. The detailed analysis by ISS in conjunction with the SU/SUs as represented on the February 15, 2008 spreadsheet, shows that this occurred for only nine (9) ITS assets or approximately .02 (or 2%) of the total capitalized assets in the fixed assets inventory (441) as of September 30, 2007. ISS has already designed a training course for implementation with all SU/SU property liaisons in early April 2008 that will address this specific issue. ISS also plans to provide specialized training to SU/SU funds managers and COTRs who monitor contracts that generally involved acquisition of fixed assets that must be accounted for in some cases, capitalized.

4. **IG Comment:**
***Inventory*: ISS/Service Units. Fixed asset inventory procedures are inadequately documented and communicated. Service unit liaisons are not fully informed of inventory procedures and the**

importance of inventory.

<u>ISS Response</u>: ISS agrees.

ISS agrees that much work needs to be done both by ISS and Service Units to address these issues properly. ISS recognized the need to define and document polices and procedures throughout the whole Logistics Services area as early as 2003. ISS funded consultants in FY04-05 and technical writers in FY06-07 to assist ISS Logistics to identify and scope this massive project into manageable pieces, and to begin defining and drafting the identified polices and procedures, with a view toward creating appropriate ISS/Logistics Directives as a result. Initial focus was on documenting all the warehousing, receiving and supply operations. Work began during 2006 - 07 on the property control aspects. Regrettably this project has not yet been completed. Documenting the ISS fixed asset inventory policies and procedures is now the number one priority in ISS/Logistics.

5. <u>IG Comment</u>:
***Inventory Reconciliation*: ISS. Inventory reconciliation procedures are not documented, reconciliation procedures are not comprehensive, and the fixed asset subsidiary ledger is not adjusted for inventory variances. Inventory variances (missing assets) are not resolved.**

<u>ISS Response</u>: ISS agrees with the statement but contends that this is a joint ISS/Service Unit responsibility, not a sole ISS responsibility.

Working in concert with OCFO, the inventory and the inventory reconciliation processes are being drafted to support the FY08 inventory. In addition to these processes, procedures are being drafted to provide for the process to adjust and reconcile the subsidiary ledger against the general ledger for inventory variances. Additionally, in conjunction with OCFO, ISS will publish an annual inventory plan which will specifically assign roles, responsibilities, establish time-lines and an inventory and reconciliation methodology for the annual inventory. This annual plan will make the necessary adjustments to incorporate any changes in process, procedures or technology developed during the year.

6. <u>IG Comments</u>:
***Asset Disposal*: ISS/Service Units. Service units dispose of assets without following Library policies and procedures. ISS is unable to accurately adjust the subsidiary ledger for disposals. There is no assurance that asset disposals conform to laws and Library regulations.**
ISS is unable to assure that:
(1) hazardous materials have been properly handled,
(2) computer hard drives are cleansed,
(3) the Library recovers asset salvage value,
(4) assets are not misappropriated, and
(5) where applicable, charitable donation policies are followed.

<u>ISS Response</u>: ISS agrees.

ISS agrees in part with the first 3 sentences of the IG comment but only in relation to the limited instances exchange/sales handled in the past by ITS for some of its capitalized IT equipment. This problem did not occur in any other Service/Support Unit; it was limited only to a small amount of ITS computer equipment. ISS concurs that ITS had apparently disposed of some assets through exchange/trade-ins without following Library policies and procedures. This created a disparity between what ITS has in its possession and the assets listed in the subsidiary ledger. However, ISS management also acknowledges that in the past several years, ISS did not provide sufficient training and direction to all SU/SU property liaisons, including ITS.

ISS disagrees with the IG's last sentence in relation to all surplus equipment disposition by ISS. ISS <u>is</u> able to assure that:

(1) hazardous materials have been properly handled,
(2) computer hard drives are cleansed,
(3) the Library recovers asset salvage value,
(4) assets are not misappropriated, and
(5) where applicable, charitable donation policies are followed.

(1) The Library makes use of significant number of hazardous chemicals in a myriad of operations in support of its mission. Those operations include sophisticated research, testing and preservation laboratories; photoduplication services; printing; talking books for the blind (batteries) and film/recorded sound cleaning, preservation and reproduction operations. ISS has implemented numerous hazardous chemical and waste reduction initiatives. Over the last two-year reporting period, with Safety Services advice and expertise, the Library has reduced the number of hazardous chemicals in its inventory by thirty-eight per cent (38%). In addition, the Library has reduced the amount of hazardous and universal waste generated by forty-two per cent (42%). Even though the Library is considered a small quantity generator by U.S. Environmental Protection Agency regulations, significant reductions were achieved through management's commitment to the environment, internal chemical inventory reporting, sophistication in the SU/SU acquisition process (ordering only what is needed) and SU/SU selecting less hazardous chemical alternatives, when possible.

The Library carefully follows all regulatory requirements in disposing of hazardous waste, as required in the federal universal waste regulations set forth in 40 CFR part 273, to protect the environmental. The Library most commonly uses lead acid batteries in large industrial warehouse equipment and trucks. In FY 2007, a total of 2,800 libs of batteries went to the appropriate treatment or recycling facilities pursuant to the hazardous waste regulatory controls.

ISS Logistics does not routinely handle hazardous materials. In a case where an item is provided to ISS for disposal which may contain some hazardous material, ISS Logistics contacts ISS Safety Services Office for guidance. In the future, ISS Logistics will also require a written certification from the SU/SU that no hazardous materials are contained in the equipment requiring disposal.

(2) ISS has supported a program for several years of cleaning the hard-drives of <u>all</u> surplus computers before donation or disposal. ISS has written assurance from the ISS Automation Team that <u>all</u> computers listed by serial number sent to ISS Logistics for disposal have been properly and completely cleaned of data from the hard-drives either for donations or destruction for non-operable computers.

(3) The only time that the Library would recover asset salvage value would be if the Library conducted a sale to dispose of an item or an exchange sale. The Library has never conducted such a sale as a method of disposal. Exchange sales are "trade-ins", when the value of the disposed item is applied specifically towards the acquisition of a replacement item. In all other disposal cases when GSA is involved, i.e. scrap metal, surplus cable, etc. the proceeds are credited to the US Treasury, not the Library of Congress.

(4) All surplus fixed assets identified for disposal are carefully controlled by bar code by Logistics and every change of accountability is recorded and signed for, and paper records are retained until after final disposal is recorded in the system and the expiration of the records retention period.

(5) The Computers For Learning Program (CFL) is the only charitable donation program that ISS handles. This program was established several years ago at the Library of Congress under Executive Order 12999. The Computers For Learning Program is managed and administered in strict conformance with polices and program requirements cited on the CFL website <www.computer.f.ed.gov >. Logistics staff who receive applications must route these to the Acting Head of Logistics, for personal review of the eligibility of the requesting organization and approval/rejection. The approved applications for computers are logged into a log book maintained by the Acting Head of Logistics and then forwarded to the Property Control Unit for further processing. The Property Control Unit logs the status of each application as determined by the Acting Head of Logistics and notifies each applicant of this status. Quarterly, the PCU reconciles the log book entries against those of the Acting Head of Logistics. In June 2006, ISS revised the brochure of this program to state more clearly the eligibility criteria for schools (pre-K through 12) and educational non-profits serving Pre-K through grade students, located in the U.S. and its territories (along with other edits needed in the revision). ISS management therefore assures that all federal donation polices are followed for this program.

7. **IG Comment:**
***Reconciliation of Subsidiary System to General Control Accounts*: ISS/OCFO. Reconciliations have not identified missed capitalization of new assets, missing adjustments for inventory variances, and fully depreciated out-of-service assets on both systems.**

ISS Response: ISS disagrees with the statement as written. The ISS/OCFO quarterly reconciliations have identified missed capitalizations of many new assets.

While the former procedures followed by OCFO and ISS captured some assets – if these were identified in the expenditures lists provided by OCFO to ISS – that process was flawed because the expenditure reports did not provide sufficient detailed information in the past to identify costs that should be capitalized, e.g. design services, installation costs, etc. related to building improvements paid for by non-ISS Service and Support Units. Furthermore, that process did not provide a true reconciliation of the subsidiary system to the general ledger. Reconciliations could not have identified fully depreciated out-of-service assets on both systems.

The reconciliation process of the ISS Property Control Unit quarterly review of expenditures reported by OCFO does capture new assets *if* the expenditure report provides the specific data needed. If expenditures requiring capitalization were not listed for the asset/improvement on OCFO report, then this capitalization would likely be missed.