

SEMIANNUAL REPORT  
TO CONGRESS

*April 1, 2007 to September 30, 2007*



Smithsonian Institution  
Office of the Inspector General

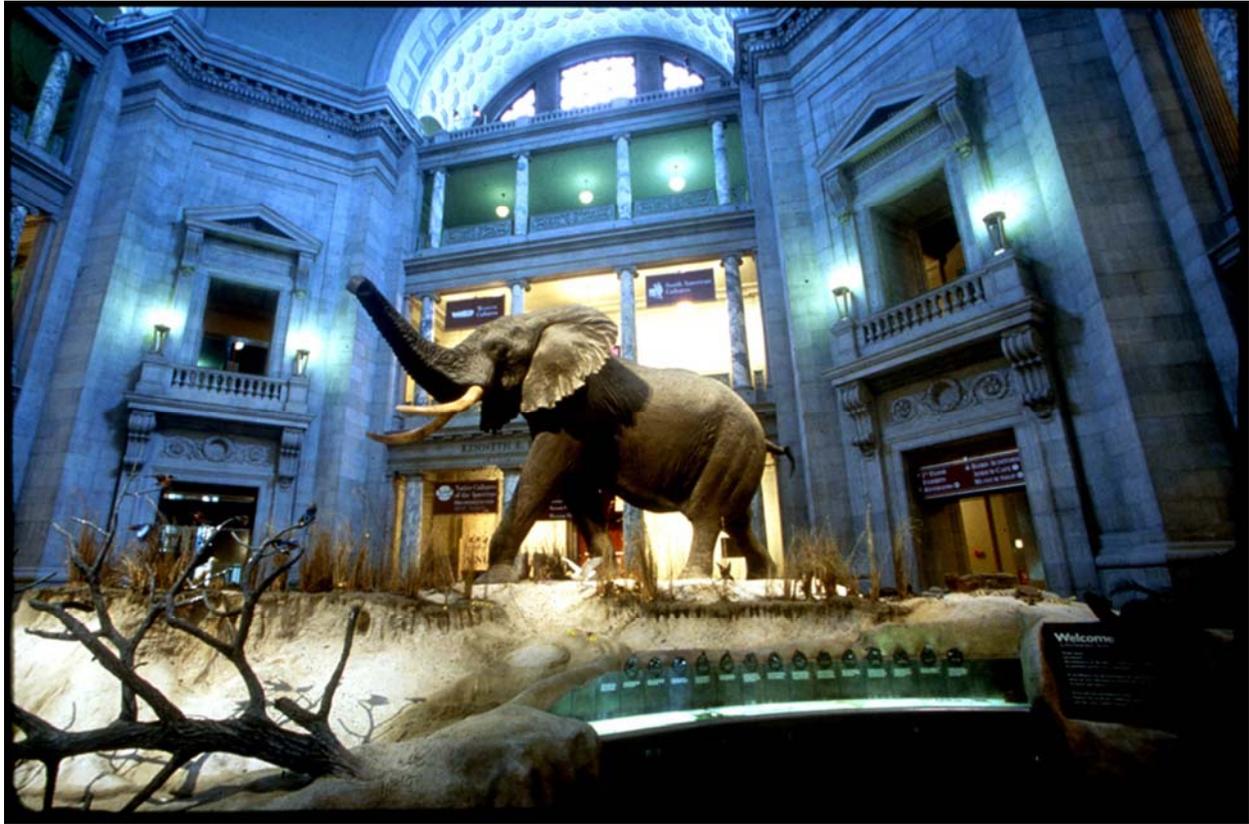
The cover depicts West Mexican/Shaft Tombs dog figures from Colima, Mexico. They were part of the “Mexican Treasures of the Smithsonian” exhibition at the Dillon S. Ripley Center in September 2007. The Smithsonian Latino Center, in partnership with the Mexican Cultural Institute and other organizations, is offering a series of public programs in Washington, D.C., that highlight different aspects of Mexican and Mexican American culture and heritage.

***Photo courtesy of the Smithsonian's National Museum of the American Indian***

***Other photos in this report are by Stuart A. Metzger unless otherwise noted.***

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An African bull elephant greets visitors in the rotunda of the National Museum of Natural History.

Photo courtesy of the Smithsonian Institution

# Message to Congress

On behalf of the Smithsonian Office of the Inspector General (OIG), I am pleased to submit this report summarizing the work of our office for the semiannual period ending September 30, 2007. In it, we highlight our efforts to improve the economy, efficiency, and effectiveness of Smithsonian Institution programs and operations, and to prevent and detect waste, fraud and abuse.

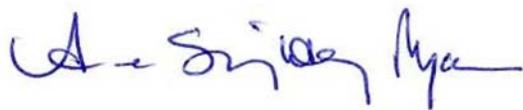
These six months have continued to be a challenging time for the Smithsonian. Congress and the media continued their scrutiny, and several senior executives have resigned or retired. The Regents and management, meanwhile, are working to reform the Institution's governance. We are pleased that many of the issues and problems we identified in our reports, reviews and congressional testimony have become key targets of the reform efforts, such as the impediments to effective oversight by the Regents; the disparities between federal and trust executive compensation; and those instances when the Institution should have been more sensitive to its stewardship responsibilities as a trust and a nonprofit entity. The Regents' Governance Committee and the Independent Review Committee issued comprehensive reports with thoughtful recommendations to change the Institution's governance for the better. We will assist these efforts by monitoring their implementation and continuing to fulfill our responsibilities under the Inspector General Act.

This has been an exceptionally busy semiannual period for the OIG as well. We issued three substantial audit reports and reviews. In addition, we issued a letter report covering our oversight of the Institution's annual financial statement audit and oversaw and issued four reports on external reviews of the Institution's information security practices. I testified before two congressional committees. On the investigative side, during this period we received 27 new complaints, opened 6 cases, and closed 33 complaints and 3 cases. We completed this work despite 2 staff vacancies – our current staff numbers 14.

We are pleased to report that the Institution generally accepted our audit findings and recommendations and is implementing or planning appropriate corrective actions to the extent allowed by current resource levels. However, we note that many corrective actions recommended in two audits from the semiannual period that ended a year ago, and which are critical to security

at the Institution, require significant further investments, investments the Institution cannot make without obtaining additional funding or cutting other priority programs. Their importance is underscored by the Government Accountability Office's recent report on the facilities maintenance backlog at the Institution and the vexing problem of obtaining sufficient resources to address that backlog.

**W**e are proud to be part of an Institution dedicated to the increase and diffusion of knowledge. As always, we are grateful to Smithsonian management, especially Acting Secretary Samper, whose efforts contributed to the results we are reporting. We also appreciate the continuing interest of the congressional oversight committees with whom we work. Finally, we thank the Audit and Review Committee and the entire Board of Regents for their commitment and support.



Anne Sprightley Ryan  
Inspector General

# Profiles

## Smithsonian Institution Profile

The Smithsonian Institution is a trust instrumentality of the United States created by Congress in 1846 to carry out the provisions of the will of James Smithson, an English scientist who left his estate to the United States of America to found “an establishment for the increase and diffusion of knowledge.” Although a federal entity, the Smithsonian does not exercise governmental powers or executive authority, such as enforcing the laws of Congress or administering government programs. It functions essentially as a nonprofit institution dedicated to the advancement of learning.

Since its inception in 1846, the Smithsonian has expanded from the lone castle building to an extensive museum and research complex that today includes 19 museums and galleries, the National Zoological Park, and research centers around the nation’s capital, in eight states, and in the Republic of Panama. The Institution is the steward of nearly 137 million collection items, which form the basis of world-renowned research, exhibitions, and public programs in the arts, history, and the sciences.

Federal appropriations provide the core support for the Smithsonian’s science efforts, museum functions and infrastructure; and trust resources, including external grants and private donations, supplement that. This combination of support has allowed the Smithsonian to produce scientific research that is flexible, independent, and capable of exploring potentially high-risk areas of inquiry. Today, the Smithsonian is the largest museum and research complex in the world.

## Strategic Direction

To support its overall mission to increase and diffuse knowledge, the Smithsonian has developed a five-year strategic plan for FY 2006-2011 that encompasses four broad strategic goals for enlarging its role in American society and succeeding as a complex enterprise in the 21<sup>st</sup> century:

- ***Increased Public Engagement*** - *Enlarge the Smithsonian's audiences, expand its degree of engagement with the public in Washington and throughout the country, and improve the quality of the Smithsonian impact on its audiences, both through its public programs and science research.*
- ***Strengthened Scientific Research*** - *Pursue scientific advances and discovery by focusing resources in areas in which the Institution has recognized strengths due to staff, research platforms, and collections.*
- ***Enhanced Management Excellence*** - *Modernize Smithsonian management systems by bringing each of them to a level of quality and sophistication appropriate to an organization of the size and complexity of the Institution.*
- ***Greater Financial Strength*** - *Provide the financial support essential to achieving the Institution's goals.*

# Office of the Inspector General Profile

The Inspector General Act of 1978, as amended, created the OIG as an independent entity within the Institution to detect and prevent fraud, waste, and abuse; to promote economy and efficiency; and to keep the head of the Institution and the Congress fully and currently informed of problems at the Institution. The OIG reports directly to the Smithsonian Board of Regents and to the Congress. As of the end of the reporting period, the OIG had 14 employees.

## **Audit Division**

The Audit Division independently audits the Smithsonian's programs and operations, including financial systems, guided by an annual Audit Inventory that identifies high-risk areas for review to provide assurance that the Institution's programs and operations are working efficiently and effectively. The Audit Division also monitors the external audit of the Institution's financial statements and contracts out the annual reviews of the Institution's information security practices. The Audit Division includes the Assistant Inspector General for Audit, three project managers, five auditors (two positions remain vacant), and one analyst.

## **Investigation Division**

The Investigation Division investigates allegations of waste, fraud, abuse, gross mismanagement, employee and contractor misconduct, and criminal and civil violations of law that have an impact on the Institution's programs and operations. It refers matters to the U.S. Department of Justice whenever the OIG has reasonable grounds to believe there has been a violation of federal criminal law. It also identifies fraud indicators and recommends measures to management to improve the Institution's ability to protect itself against fraud and other wrongdoing. Two Senior Special Agents make up the Investigations Division.

## **Counsel**

The Counsel to the Inspector General provides independent legal advice to the Inspector General and the audit and investigative staff.

# Audits and Reviews

Our audits and reviews focus on two of the Institution's four performance goals: ***Enhanced Management Excellence*** and ***Financial Strength***. Specifically, we address the following high-risk areas:

- Modernization of financial management and accounting operations
- Budget performance and integration
- Management of capital assets
- Modernization and security of the IT infrastructure
- Profitability of revenue operations and collection of revenues
- Contract administration
- Security and care of the national collections
- Safety and environmental management
- Human resource management

To this end, during the past semiannual period we completed 8 audits and reviews; worked with management to close 26 recommendations; provided formal oversight of the Institution's annual financial statement audit, the annual information security evaluations, and an agreed-upon-procedures review of the compensation and expenses of the Smithsonian Business Ventures Chief Executive Officer; completed substantial work on ongoing audits; and developed and published an audit inventory for fiscal year 2008.

# Summary of Audit Accomplishments

## **Transmittal Letter and Independent Accountant's Report on Applying Agreed-Upon Procedures to a Review of the Compensation and Expenses of the Chief Executive Officer of Smithsonian Business Ventures, 2000-2005**

At the request of the then-Secretary and the Audit and Review Committee of the Board of Regents, we contracted with an independent accountant to perform an agreed-upon procedures review of the compensation and expenses of the Chief Executive Officer (CEO) of Smithsonian Business Ventures (SBV). For the period covering fiscal years 2000 through 2005, the independent accountant reviewed the CEO's compensation and verified that, with few exceptions, he was paid in accordance with his employment agreement.

The independent accountant also reviewed over \$202,000 of the CEO's business expenses for fiscal years 2001 through 2005, and found that \$165,484 (over 81%) of these expenses were unsupported, inadequately supported, or unauthorized.

In our letter transmitting the independent accountant's report to the Audit and Review Committee, we made several observations and recommendations. Based on our additional analysis, we adjusted the amount of unsupported, inadequately supported, and unauthorized expenses and concluded the total for these expenses to be \$149,320.58 (over 73% of the reviewed expenses). We also noted \$5,000 of unreimbursed personal expenses, an amount subsequently paid by the CEO. We observed that most of the CEO's expenses were likely incurred for Smithsonian purposes, but that the documentation available failed to meet Smithsonian and Internal Revenue Service requirements for business expenses. We recommended that the Regents seek to ensure appropriate reimbursements for the unsupported and unauthorized expenses as well as revised tax filings to reflect the inadequately supported expenses as income to the CEO.

We noted ambiguity in the Institution's travel and expense policies. We recommended revisions to these policies to clarify that all employees should take the most economical and appropriate means of transportation under the circumstances; to specify that car service may be used only in exceptional circumstances and be justified and authorized in writing in advance; and to establish stricter standards for when actual expenses, rather than per diem, may be authorized for travel.

We also observed weak internal controls over SBV's business expenses. For example, SBV exercised lax recordkeeping in violation of Smithsonian policy, had no written business expenses policies or procedures for over 6 years, and often failed to adhere to or enforce Smithsonian travel card policies. We questioned these practices, especially in light of the Smithsonian's nonprofit and trust status. Moreover, the Institution failed to guard its limited resources by its inattention to these questionable practices. Among other things, the Institution allowed the CEO to use repeatedly his business travel card for personal use and paid off his travel card statements with commingled business and personal expenses without complete documentation and often by lump-sum payments.

The Audit and Review Committee accepted our findings and recommendations, with the exception of \$2,625 of parking expenses they deemed to be a non-taxable qualified benefit and a \$990 offset to correct a calculation error in the CEO's bonus for FY 2001.

### **Administration of Relocation and Recruitment Payments**

During our audit of executive compensation at the Smithsonian, which we described in our last semi-annual report, we observed that the Smithsonian had no consistent, Institution-wide method for processing or documenting relocation or recruitment payments, and that central oversight of such payments was lacking. In this audit, we sought to assess if the Institution has adequate policies and procedures to govern the granting and recording of relocation and recruitment payments; whether the Institution made payments in accordance with these policies and procedures; and whether the Institution addressed all associated tax liabilities.

We found that the Smithsonian in many instances did not ensure proper reporting to the IRS of employee taxable income arising from relocation and recruitment payments. In the 5-year period covered by our audit, the Smithsonian generally reported lump-sum payments to employees correctly on IRS W-2 forms. However, when the Smithsonian reimbursed employees for moving expenses, or when it paid third parties directly for temporary housing or other non-deductible expenses, the Smithsonian generally did not report taxable income or other required information accurately to the IRS.

For the period 2002 through 2006, the Smithsonian reported employee income associated with these payments of approximately \$1.2 million when, according to the transactions we reviewed, it should have reported employee income of about \$1.4 million. We identified a number of factors that contributed to the inaccurate processing of these transactions, including the Institution's decentralized organizational structure, weak guidance on proper processing procedures, and a lack of adequate training for data entry and reporting.

We also found that the Smithsonian did not maintain required employee service agreements for relocation and recruitment payments. Service agreements spell out employees' responsibility to repay relocation or recruitment amounts if they leave the Smithsonian prior to serving a minimum period, such as one year. While we found instances where units followed up to recover payments from employees when they left the Smithsonian before fulfilling the terms of their service agreements, we also identified cases where management failed to recover payments from breached agreements.

Examples included:

- A Smithsonian Business Ventures (SBV) executive was authorized moving and temporary living expenses of nearly \$100,000 without signing a service agreement. SBV reimbursed the employee for temporary living expenses of over \$40,000. The executive left SBV within a year of his start date and SBV never required the employee to reimburse the Institution for any portion of the payments.
- Two Office of Protection Services employees received recruitment payments of \$5,000 each. Neither employee fulfilled the required six-month terms of employment set out in their service agreements and neither reimbursed the Institution.

We made five recommendations to strengthen oversight of relocation and recruitment payments. We recommended that management amend policies and procedures, improve user training, report corrected information to the IRS, and maintain a central file of all approved service agreements in the Office of Human Resources.

Management concurred with the report's findings and recommendations and proposed corrective actions that will resolve all the recommendations.

## **Friends of the National Zoo Revenue Operations**

Friends of the National Zoo (FONZ) is a nonprofit organization governed by a member-elected Board of Directors. FONZ has an agreement with the Smithsonian to operate the concessions at the National Zoological Park (Zoo), the net proceeds from which are to be used exclusively for the benefit of the Zoo.

In response to a request from the Zoo's Deputy Director, we evaluated FONZ's revenue operations. Our objectives were to determine whether FONZ is managing the Zoo's revenue operations in the most efficient and profitable manner.

FONZ has made significant contributions to the Zoo. It promotes quality educational programs for the public, generates profits from its concessions and parking operations, and marshals hundreds of volunteers who help support many important functions for the Zoo. Nonetheless, we identified numerous areas where FONZ can improve its revenue-generating operations

FONZ could increase sales and reduce expenses in its merchandise operations by strengthening its inventory management practices, increasing retail square footage, and streamlining its management and staffing structures. Further, the FONZ Board of Directors and the Zoo should explore all options, including the feasibility of outsourcing merchandise operations, to enhance profitability.



*FONZ recently improved presentation at Zoo stores.*

We also noted that store presentation needed to be improved, and by the end of our audit, we observed that FONZ had made significant improvements in this area.

While FONZ's food and beverage revenues have generally been lower than those of other zoos we reviewed, FONZ has generated moderately higher net contributions owing to the

lower cost of its food sales. FONZ can grow net contributions from its food services and improve the quality of the visitor experience by expanding the use of its small permanent food and beverage locations as well as its portable carts. In addition, FONZ should explore using carts to expand the variety of food items offered.

We believe FONZ could also increase its net contribution to the Zoo by improving customer service in its merchandise and food service operations. To enhance the quality of the visitor experience, FONZ should continue to improve its efforts to assess customer satisfaction through visitor surveys and secret shopper reports. FONZ needs to place more emphasis on providing outstanding customer service in the training it provides to management and permanent staff as well as to seasonal employees.

Parking spaces at the Zoo are inadequate during peak months. FONZ and the Zoo, in consultation with the Secretary, should examine two options for increasing parking revenues: they should reevaluate the policy of allowing free parking for FONZ and Zoo employees and others, and reexamine the unlimited free parking currently enjoyed by FONZ members.

We observed two areas where governance over FONZ's operations can be improved. The first concerns the way policies and procedures are developed, approved, and documented. The second concerns how FONZ's Board monitors policy implementation.

Finally, looking to the future, we considered the Zoo's ten-year master plan, which it has been developing since early 2005. The master plan is essentially a blueprint for updating the Zoo's infrastructure and revitalizing its exhibits. Preliminary cost estimates range from \$500 million to \$600 million. We identified four areas that could dramatically increase future revenues and enhance the quality of the visitor experience: the expansion of retail facilities, the expansion of food and beverage operations, the expansion of parking facilities, and the addition of other entertainment amenities that have been proven revenue-producers at other zoos. It is critical that the Smithsonian fully explore these opportunities to maximize revenue for the Zoo. These facilities need to be included in the master planning process from the outset. Building large, sustainable revenue-generation into the design now will help maintain the Zoo at a world-class level well beyond the initial ten-year planning horizon.

During the course of our audit, FONZ management, working with its Board, adopted a new strategic plan that will focus on improving the visitor experience, enhancing partnerships with stakeholders, and achieving organizational excellence.

We made 16 recommendations to strengthen FONZ's revenue operations by improving financial performance, operational effectiveness, and the visitor experience. Except for investment policy oversight by the FONZ Board of Directors, management generally concurred with the report findings and recommendations. Based on improvements already implemented by FONZ's new Executive Director, we have already closed 8 of the 16 recommendations.

### **Quality Assurance Letter on External Audit of FY 2006 Annual Financial Statements**

As part of our oversight of the Institution's fiscal year 2006 annual financial statement audit, we issued a quality assurance letter to the Regent's Audit and Review Committee summarizing our observations on the audit process and suggesting improvements for future audits.

The Institution's independent public accountant, KPMG, issued an unqualified opinion on the Smithsonian's FY 2006 annual financial statements and found no matters involving internal control that it considered to be material weaknesses.

KPMG did, however, identify two reportable conditions related to (1) accounting resources and staff capacity and (2) valuation of alternative investments. Until corrective actions are taken, these conditions will potentially have an adverse affect on the Smithsonian's ability to record and report financial data. In addition, KPMG identified the following accounting and reporting deficiencies: (1) inadequate documentation of accounting policies and procedures; (2) over-reliance on manual spreadsheets to track and develop critical statement balances; (3) deficiencies in SBV accounting operations; (4) lack of evidence of review of bank account reconciliations as well as reconciliations of intra-company

accounts; (5) lack of supervisory review of journal entries; and (6) inappropriate granting of system access, which overrides segregation of duties.

KPMG's Management Letter contained 23 recommendations to correct accounting and reporting weaknesses. Smithsonian management agreed to take corrective action on all recommendations.

KPMG issued a qualified opinion on the Smithsonian's special-purpose financial statements. KPMG qualified its opinion because the Smithsonian had not previously recognized its Federal Employment Compensation Act (FECA) actuarial liability and had not recorded the expected costs and financing sources for employee benefit programs provided by the Office of Personnel Management. KPMG made five recommendations related to these reportable conditions and management agreed to correct the deficiencies.

In order to ensure more timely completion of future audits, we suggested that the external auditor and the Smithsonian's financial managers improve communications throughout the audit process. Additionally, KPMG should perform substantive interim testing of account balances and transactions, which will reduce the amount of year-end testing and provide time to resolve audit differences and other issues. Further, the Institution needs to develop a plan for interim account closings and producing financial statements quarterly, in accordance with best practices.

## **Federal Information Security Management Act Audits**

The Federal Information Security Management Act of 2002 (FISMA) directs the Office of the Inspector General to conduct annual evaluations of the information security program of the Institution, which is critical to protecting the Institution's mission. The Institution voluntarily complies with FISMA requirements because it is consistent with its strategic goals. FISMA sets forth federal information security compliance criteria, including annual assessments, certification and accreditation of systems, and system security plans.

During this semi-annual period, we oversaw the annual evaluation of the Institution's information security program, as well as audits of a subset of systems, as also required by FISMA.

### ***FY 2006 Information Security Practices Audit***

During this year's overall FISMA evaluation, we assessed (1) the effectiveness of the Institution's security program; (2) the Institution's compliance with FISMA guidelines; (3) the security of the general support system and the development and membership information system; and (4) progress made in correcting previously reported security weaknesses.

We concluded that while the Institution has made progress in complying with FISMA requirements, significant work remains to ensure adequate controls are in place and operating effectively. In addition, we noted that the Institution's decentralized IT environment makes the implementation and enforcement of policies and procedures limited or inconsistent. Without the centralization of IT operations and the assignment of responsibility within OCIO for ensuring compliance with Institution policy and procedures, management cannot ensure adequate controls are in place.

We made 12 recommendations to ensure that existing policies requiring the use of standard configuration baselines are implemented and enforced; that Institution security configuration baselines are compared to industry-accepted baselines; and that system sponsors and users are properly trained. Except for weaknesses noted in placing major systems into production before going through a certification and accreditation process, management generally concurred with the report's findings and recommendations.

### ***FY 2006 Development and Membership Information System Audit***

This report evaluated the effectiveness of technical security controls over the Development and Information System (DMIS) and whether baselines had been adequately documented and implemented over DMIS operating systems and databases for fiscal year 2006.

DMIS is a commercial off-the-shelf information system application that is used by the Office of Development and staff across the Institution to support constituency research, gift recording, membership, and other related development services. The data in DMIS is confidential because it contains sensitive information relating to Smithsonian Institution donors, prospects, and members.

We identified several areas in which adequate controls have not been documented and put in place. Without adequate procedures to ensure that configuration baselines are in place over the Institution's major information systems or that account administration controls are implemented, the confidentiality, availability, and integrity of DMIS and the data it processes may be at greater risk than management is willing to accept.

We made recommendations to strengthen the confidentiality, availability, and integrity of the information on DMIS and to enhance audit trails and user accountability. Management fully concurred with the report findings and recommendations and has planned or taken actions that will mitigate the identified weaknesses.

### ***FY 2006 Smithsonian Institution Network Audit***

Another system we covered was the Smithsonian Institution Network (SInet), the Institution's general support system. We evaluated SInet management, operational, and technical security controls for fiscal year 2006.

We found that management, operational, and technical controls over SInet were not adequate. Our audit noted that the Institution operates in a decentralized environment where responsibility for both performing functions and enforcing IT controls has been assigned to the same individuals. Furthermore, because responsibility for administration and security of SInet has not been centralized under the Office of the Chief Information Officer (OCIO), IT security policies and procedures documented by OCIO have not been consistently implemented or followed.

Without adequate controls in place to enforce Institution policies, procedures, and practices over SInet, the confidentiality, availability, and integrity of Institution

information systems and related data may be at greater risk than management is willing to accept.

We made 17 recommendations to strengthen controls over SInet by enforcing Institution policies, procedures, and practices over network account administration, segregation of duties, and risk assessments. Management generally concurred with the report's findings and recommendations, with the exception of those relating to weaknesses in the development of the SInet risk assessment.

### ***FY 2007 Human Resources Management System Audit***

We also examined the Human Resources Management System (HRMS) for fiscal year 2007. We evaluated HRMS's management, operational, and technical security controls.

HRMS contains sensitive personnel data. Managers throughout the Institution use HRMS to manage core activities such as recruitment, electronic transmittal of personnel actions, benefits administration, training, and recording and reporting of workplace incidents and injuries.

Overall, we concluded that management has done a good job identifying, documenting, and implementing management, operational, and technical controls over HRMS. We did, however, note instances during our testing where policies and procedures were not being followed. Without adequate controls in place to enforce Institution policies, procedures, and practices over HRMS, the confidentiality, availability, and integrity of the system and its related data may be at greater risk than management is willing to accept.

We made five recommendations to strengthen controls over HRMS by enforcing Institution policies, procedures, and practices over user access request forms, segregation of employee duties, database logging and monitoring, system baselines, and interconnection agreements. Management concurred with the report's findings and recommendations and has planned or taken action that will resolve all recommendations.

\* \* \* \* \*

Table 1 lists the audit reports and reviews issued during the period.

**Table 1: List of Issued Audit Reports and Reviews**

| Report Number | Title   | Date Issued |
|---------------|---|-------------|
| A-06-03       | Quality Assurance Letter on the FY2006 Financial Statement Audits       | 4/17/2007   |
| A-06-05       | Federal Information Security Management Act (FISMA) Audit for FY 2006   | 4/20/2007   |
| A-06-08       | Development and Membership Information System Audit                     | 5/16/2007   |
| A-06-04       | Review of Smithsonian Business Ventures CEO's Compensation and Expenses | 7/19/2007   |
| A-06-07       | Smithsonian Institution Network (SInet) Audit                           | 8/10/2007   |
| A-06-01       | Friends of the National Zoo Revenue Operations                          | 8/28/2007   |
| A-07-06       | Human Resources Management System                                       | 9/19/2007   |
| A-07-04       | Administration of Relocation and Recruitment Payments                   | 9/28/2007   |



The 2007 Smithsonian Folklife Festival featured programs from Vietnam, Northern Ireland, and Virginia.

## Other Audit Activity

### Status of Open Recommendations

Smithsonian managers made a significant effort during the last six months to implement many of the recommendations from audit reports issued during prior semiannual reporting periods. As a result, we closed 26 recommendations during the semiannual period. These recommendations included strengthening IT and physical security practices, improving inventory control measures to safeguard the national collections, improving employee and contractor screening measures, and enhancing FONZ's revenue operations.

Table 2 summarizes audit recommendation activity.

**Table 2: Audit Recommendation Activity**

| Status of Recommendations           | Numbers |
|-------------------------------------|---------|
| Open at the beginning of the period | 33      |
| Issued during the period            | 57      |
| Subtotal                            | 90      |
| Closed during the period            | 26      |
| Open at the end of the period       | 64      |

Management actions regarding questioned costs are detailed in Table 3, below.

**Table 3: Reports with Questioned Costs**

| <b>Reports</b>   | <b>Number</b> | <b>Questioned</b> | <b>Unsupported</b> |
|--|---------------|-------------------|--------------------|
| Reports for which no management decision has been made by the commencement of the reporting period | 0             | \$0               | \$0                |
| Reports issued during the reporting period   | 2             | \$192,818*        | \$145,778**        |
| <b><i>Subtotal</i></b>   | 2             | \$192,818         | \$145,778          |
| Reports for which a management decision was made during the reporting period                       |               |                   |                    |
| • Dollar value of disallowed costs   | 1             | \$5,000           | \$0                |
| • Dollar value of costs not disallowed   |               |                   |                    |
| Reports for which no management decision has been made by the end of the reporting period          | 2             | \$187,818         | \$145,778          |

\*Of this amount, \$184,275 was taxable income paid to Smithsonian employees that was not properly reported to the Internal Revenue Service.

\*\*Of this amount, we recommended that the Smithsonian report \$65,235 as additional taxable income to an employee.

Management actions regarding funds that could be put to better use are detailed below.

**Table 4: Audit Reports with Recommendations that Funds Be Put to Better Use**

| <b>Reports</b>   | <b>Number</b> | <b>Funds Put to Better Use</b> |
|--|---------------|--------------------------------|
| Reports for which no management decision has been made by the commencement of the reporting period | 0             | \$0                            |
| Reports issued during the reporting period   | 0             | \$0                            |
| <b><i>Subtotal</i></b>   | 0             | \$0                            |
| Reports for which a management decision was made during the reporting period                       | 0             | \$0                            |
| • Dollar value of recommendations that were agreed to by management                                | 0             | \$0                            |
| • Dollar value of recommendations that were not agreed to by management                            | 0             | \$0                            |
| Reports for which no management decision has been made by the end of the reporting period          | 0             | \$0                            |
| Reports for which no management decision was made within 6 months of issuance                      | 0             | \$0                            |

While management made considerable progress in closing old recommendations, 27 recommendations made in prior semiannual periods remained open at the end of this reporting period. Of those recommendations, 1 is over 4 years old, 2 are over 3 years old, 4 are over 2 years old, 12 are over 1 year old, and the remaining 8 are less than 1 year old. We summarize these open recommendations from prior semiannual periods and their target implementation dates in the following table.

**Table 5: Prior Recommendations for which Corrective Actions Are Not Yet Complete**

| Audit Title and Date   | Number of Recs | Summary of Recommendations   | Target Date |
|--|----------------|--|-------------|
| National Museum of the American Indian Information Systems (January 17, 2003)              | 1              | The Director should replace the Registrar's Office Windows NT network.   | 9/30/2006   |
| Steven F. Udvar-Hazy Center Business Activities (August 25, 2004)                          | 1              | The CFO for Smithsonian Business Ventures (SBV) should ensure that his staff develops written procedures for monitoring contractor performance.  | 12/31/2007  |
| Information Systems Controls at the National Museum of Natural History (September 9, 2004) | 1              | The Director of the National Museum of Natural History should relocate web servers to a secure network location.   | 12/31/2007  |
| National Air and Space Museum Mall Simulators (February 25, 2005)                          | 3              | The CFO of SBV should develop and implement policies and procedures for contractor selection, and follow up on intra-institutional receivables; and, in coordination with the Director of the Office of Facilities Engineering and Operations (OFEO), refine responsibilities for payment of utilities expenses. | 12/31/2007  |
| Bank Reconciliations (September 28, 2005)  | 1              | The Comptroller, in collaboration with the units, should establish an oversight process for ensuring that revenues are accurately recorded and reviewed.   | 11/30/2007  |

| Audit Title and Date  | Number of Recs | Summary of Recommendations  | Target Date                  |
|---|----------------|---|------------------------------|
| Internal Control Weaknesses in Cash Management and Banking Activities (February 14, 2006)   | 2              | The CFO should verify that charges for banking services are valid and reasonable in accordance with the Institution's current agreements with the banks, ensure a provision is incorporated into future banking agreements to allow for a monthly analysis of bank fees, and formalize the controls recommended to OC into a written policy to ensure current and future OC employees have appropriate operating guidance and to better document controls over cash management and other financial management activities. | 11/30/2007                   |
| Review of Smithsonian Institution Information Security Practices (February 16, 2006)  | 1              | The CIO should require that employees who have significant computer responsibilities report their plans for meeting the specialized training requirements at the beginning of the fiscal year, and monitor employee progress during the year to ensure that training is completed.  | 1/31/2008                    |
| Employee and Contractor Screening Measures (August 21, 2006)  | 4              | The Deputy Secretary and COO should replace NACIS with a system that will better meet Institution requirements. The Director of OPS should ensure that background investigations are or have been completed for 936 individuals who had no record of an investigation; comply with Smithsonian Directives 212 and 213 by processing NACIs and FFIs when required; and work with the Director of OHR to revise SD 212 and 213.   | 3/31/2008<br>to<br>9/30/2008 |
| Physical Security and Inventory Control Measures to Safeguard the National Collections at the National Museum of Natural History (September 29, 2006) | 5              | The Director of OPS should prioritize the repair, replacement, and upgrading of security devices identified in the 2005 Assessment Report; and prepare a comprehensive budget and timeframe for correcting the cited weaknesses. The Director, NMNH should establish requirements for closer supervision of non-collections staff and other individuals allowed access to the collections; direct the Department of Mineral Sciences to conduct a complete inventory and develop a follow-up                              | 11/1/2007<br>to<br>1/1/2010  |

| Audit Title and Date   | Number of Recs | Summary of Recommendations   | Target Date                            |
|--|----------------|--|--|
|  |                | <p>plan to locate all missing objects; direct the Registrar to work with department chairs to develop a list of NMNH's most valuable objects and type specimens, and with the assistance of the Institution's statistician, determine the appropriate percentage or number of those objects to review for each cyclical inventory; and, instruct the Associate Director, Registrar, and Assistant Director for Information Technology to develop and implement a plan to update and convert electronic and paper records so they are consistent in documenting the status of the collections inventory.</p>  |  |
| <p>Executive Compensation at Smithsonian Business Ventures, Phase I (January 19, 2007)</p> | <p>8</p>       | <p>The CEO of Smithsonian Business Ventures should ensure that any payments of incentive bonuses based on exceptions from approved financial and operational goals are justified and documented in writing at the time of the award; ensure that managers establish operational goals at the beginning of the fiscal year and that incentive plan worksheets are properly documented with supervisor and employee signatures and dates; ensure that operational goals are specific and measurable and can be clearly linked to improved organizational results; ensure that managers approve performance plans at the beginning of each year and complete written summary performance appraisals for all individuals promptly at year's end; ensure that SBV develops a 3- to 5-year strategic plan for approval by the SBV Board of Directors and the Secretary; and, ensure that all out-of-period adjustments as well as unusual and nonrecurring items are tracked and accumulated for internal management purposes; ensure that an annual examination-level attestation engagement by an independent public accountant is performed</p> | <p>10/31/2007<br/>To<br/>3/31/2008</p> |

| Audit Title and Date | Number of Recs | Summary of Recommendations  | Target Date |
|----------------------|----------------|---|-------------|
|                      |                | <p>on SBV's net gain and other key financial measures to ensure that SBV's reported financial results are complete, accurate, and reliable for calculating annual incentive awards as well as for other Institution uses. The Secretary should re-examine whether market-based compensation is the appropriate strategy for SBV and, if so, whether the level and types of executive compensation provide the most effective incentives to achieve long-term net gain growth.</p> |             |

## Oversight of Financial Statement Auditors

Beginning with the FY 2006 audit, the OIG assumed responsibility for the oversight of the annual financial statement audit, which is currently conducted by KPMG. In prior years, KPMG was under the supervision of the Institution's Comptroller. Because of our organizational independence, OIG oversight of this audit engagement strengthens assurances that the external auditor's report and conclusions are reasonable. Because of our limited resources, we will continue to rely on external auditors for the audited financial statements, but will review the audit documentation and evaluate key judgments to provide added assurance that the auditor's work complies with professional standards.

## FY 2008 Audit Inventory

In September 2007, we published our FY 2008 Annual Audit Inventory, which is available on our website, <http://www.si.edu/oig>. In addition to our oversight of the Institution's financial statement auditors and FISMA contractor, we plan to initiate audits and reviews in FY 2008 that will address:

- Facility safety issues

- The former Secretary's and the former SBV CEO's FYs 2006-2007 expenses and compensation
- Capital project oversight
- Travel card oversight
- Purchase card oversight
- Expenses of Smithsonian executives, unit directors, Regents, and Advisory Board members.

## **Work in Progress**

### **SBV Oversight of Contractors**

We are conducting a performance audit of oversight of contractors at SBV. The objectives of this audit are to assess (1) whether SBV has adequate procedures for ensuring the accuracy of revenues and expenses reported by contractors; (2) SBV's practices for collecting and recording proceeds from contractors; and (3) whether SBV is adequately overseeing contractors to ensure compliance with key contract terms. The universe we are reviewing consists of revenue-generating contracts and contracts for services that directly support revenue generation that exceed \$75,000 for the period FY 2004 through early 2007.

### **Oversight of Information Security Program**

We have engaged an outside consultant to perform an evaluation of the Institution's information security program and compliance with the Federal Information Security Management Act (FISMA) as well as focused assessments of two of the Institution's major IT systems. The FISMA evaluation will address the Institution's information system inventory; certification and accreditation processes; security configuration policies and procedures; plans of action and milestones; computer security incident handling; and computer security awareness training. In accordance with Office of Management and Budget reporting guidelines for FY 2007, on September 27, 2007, we forwarded our completed Inspector General FISMA template to the Acting Secretary for inclusion in the Institution's reporting package due in early October.

The two major information systems we selected for review are the Human Resources and Management System (which we have already completed and summarize in the Summary of Audit Accomplishments section) and three components of the Institution's Security Management System: ID and Badging, C-Cure Central, and Central Monitoring systems. These three components of the Security Management System and their data are sensitive with clearly defined functions for which there are readily identifiable security considerations. We plan to issue a report on our overall FISMA assessment as well as a separate report on the Security Management System.

### **Workers' Compensation Program**

We have initiated a performance audit of the Smithsonian Institution's management of the workers' compensation program. We will evaluate whether the program has been operating in accordance with U.S. Department of Labor (DoL) regulations, policies and procedures under the Federal Employees' Compensation Act. The objectives will be to assess whether adequate procedures are in place for (1) timely reviewing and submitting claims; (2) monitoring claims to ensure that case files are accurate and up-to-date and that claimants return to work as soon as possible; and (3) reconciling charge-back costs and recovering overpayments promptly. The audit will cover a sample of cases from charge-back years (July 1 through June 30) 2005 through 2007. We will use data from the past five years for our analysis and comparison of trends, including information reported through DoL's Safety, Health and Return-to-Employment (SHARE) initiative.

### **Peer Review of the Federal Trade Commission's Office of the Inspector General**

Our office has performed a peer review of the Office of Audit of the Federal Trade Commission's Office of Inspector General in accordance with the guidelines of the President's Council on Integrity and Efficiency/Executive Council on Integrity and Efficiency. The objective of the peer review was to determine whether the office's quality control system was adequate to provide reasonable assurance that it met generally accepted government audit-

ing standards and established policies and procedures. We expect to issue our final report in November 2007.



The Arts and Industries Building has a special role among Smithsonian buildings—it opened in 1881 as the original home of the National Museum. In 2004, the building was closed due to a deteriorating roof and other infrastructure problems and remains closed indefinitely. In 2006, the Arts and Industries Building was listed as one of “America’s Most Endangered Places” by the National Trust for Historic Preservation.

# Investigations

During the reporting period, we received 27 complaints, opened 6 cases and closed 33 complaints and 3 cases, resulting in 1 resignation, 1 admonishment, and 1 suspension. Our investigators provided assistance to auditors in reviewing compensation, business expenses, relocation expenses, and travel.

## **Summary of Investigative Activity**

During this period, OIG special agents opened a number of investigations. The following descriptions summarize the more significant matters that they were able to close in the last six months.

### **Financial Mismanagement**

OIG special agents conducted an investigation into financial mismanagement at one of the Institution's facilities. The investigation revealed that an employee responsible for cash management had failed to make bank deposits of incoming cash and checks for a period of nearly ten months, totaling over \$85,000 in receipts. While no criminal misconduct occurred, the investigation revealed deficiencies in the system for safeguarding, depositing and tracking incoming funds and resulted in a complete revision of the policies and internal controls in place. Formal administrative action was taken against the employee and the employee's immediate supervisor.

## **Contract Implementation Improprieties**

The OIG investigated whether a contractor had an improper relationship with a Smithsonian employee and determined that allegation was unfounded. However, the OIG did substantiate the allegation that the employee violated the Smithsonian conflict of interest rules in that the employee improperly acted on behalf of the contractor and received a personal benefit while performing related professional services. Additionally, the investigation revealed that this Smithsonian unit violated portions of the contract, and that unit-level employees lacked necessary contract and procurement training. Administrative action against the employee and supervisor is pending.

## **Destruction of Documents**

OIG special agents conducted an investigation into the actions of an individual suspected of destroying documents in violation of a document retention order. The investigation substantiated that the official had destroyed, and had ordered subordinates to destroy, various documents covered by the order. The case was referred to the U.S. Attorney's Office, but prosecution was declined. The individual involved has since resigned.

## **Other Investigative Activity**

During the course of several investigations, the OIG learned of matters that were not necessarily within the scope of the respective investigative reports but required prompt management attention. To alert management, we issued separate investigative memorandums on the following:

- We found deficiencies in the system for depositing and tracking incoming funds at one Smithsonian unit as well as lack of management oversight in its Administration and Finance Office. We also identified the need for controls at that unit to (1) ensure currency and checks are deposited in the Smithsonian's bank accounts promptly and completely; and (2) ensure these amounts are promptly and accurately recorded into the ERP financial system.

- We identified contract violations at a Smithsonian unit and recommended corrections with regard to payment of royalties as required by the vendor’s contract. We also advised the unit to cease activities violating the vendor’s contract; recommended that the unit develop a consistent method for tracking work done by that unit requiring reimbursement from other SI units; and recommended that the Office of Contracting ensure employees assigned as the Contracting Officers’ Technical Representative have the requisite training.

OIG special agents are also working on several cases with other offices of Inspector General, including those at the U.S. Postal Service and the U.S. Department of Labor.

\* \* \* \* \*

The following table summarizes complaint activity for this reporting period:

**Table 6: Summary of Complaint Activity**

| Status                                    | Numbers |
|---|---------|
| Open at the start of the reporting period | 39      |
| Received during the reporting period      | 27      |
| Subtotal                                  | 66      |
| Closed during the reporting period        | 33      |
| Total complaints pending                  | 33      |

The following table summarizes investigative activity for this reporting period:

**Table 7: Summary of Investigative Caseload, Referrals, and Results**

| Investigations                                 | Amount or Number |
|--|------------------|
| <b>Caseload</b>                                |                  |
| Cases pending at beginning of reporting period | 5                |
| Cases opened during the reporting period       | 6                |
| <b>Subtotal</b>                                | 11               |
| Cases closed during the reporting period       | 3                |
| Cases carried forward                          | 8                |
| <b>Referrals for Prosecution</b>               |                  |
| Pending at the beginning of the period         | 3                |
| Referred for prosecution                       |                  |
| Pending at the end of the period               | 3                |
| <b>Successful Prosecutions</b>                 |                  |
| Convictions                                    |                  |
| Fines  |                  |
| Probation                                      |                  |
| Confinement                                    |                  |
| Monetary Recoveries and Restitutions           |                  |
| <b>Administrative Remedies</b>                 |                  |
| Terminations                                   |                  |
| Resignations                                   | 1                |
| Reprimands or admonishments                    | 1                |
| Reassignments                                  |                  |
| Demotions                                      |                  |
| Revocation of privileges                       |                  |
| Suspensions                                    | 1                |
| Monetary loss prevented                        |                  |
| Funds Recovered                                |                  |

# Other OIG Activities

## **Testimony**

During this period, the Inspector General testified before two congressional committees. In April, the IG testified before the Senate Committee on Rules and Administration in a hearing concerning governance at the Institution. The IG's testimony focused on impediments to effective oversight at the Institution, in particular the lack of information made available to the Regents, as well as on the role of the OIG at the Smithsonian. In August, the IG testified before the Committee on House Administration on ongoing reforms in governance that the Regents and the Institution are pursuing. Copies of the Inspector General's testimony to both Committees are available on our website.

## **Legislative and Regulatory Review**

The Inspector General Act mandates that our office monitor and review legislative and regulatory proposals for their impact on the Smithsonian's programs and operations and with an eye toward promoting economy, effectiveness, efficiency, and preventing fraud, waste, abuse and mismanagement.

During this period, we reviewed and commented on draft revisions to a number of Smithsonian Directives. For example, we provided comments on a preliminary draft Freedom of Information Act policy put forward by the Office of General Counsel. We also provided suggestions to the Office of the Chief Information Officer on strengthening controls on email access and developing appropriate safeguards to prevent unauthorized monitoring of employee email.

## **Involvement in Professional Organizations**

The Smithsonian OIG continues to participate in the work of professional organizations. Currently, we are involved with the PCIE/ECIE's Peer Review Guide Update Project. This project is being conducted under a working group of the Federal Audit Executive Council. Its goals are to (1) complete by December 31, 2008, an updated peer review guide for the 2009/2010 review cycle and (2) develop related training materials.

Our involvement focuses on updating the guide to reflect changes in audit standards, especially those that stem from the 2007 revisions to ***Government Auditing Standards*** since the guide's last revision in FY 2005.



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