Inspector General Audit Report

United States Department of the Interior

OFFICE OF INSPECTOR GENERAL
Washington, D.C. 20240

MAY 10 2000

INDEPENDENT AUDITORS REPORT

Memorandum

To: Assistant Secretary for Policy, Management and Budget and Chief Financial Officer

Subject: Independent Auditors Report on Department of the Interior Annual Report for Fiscal Year 1999 (No. 00-I-429)

SUMMARY

In our audit of the Department of the Interior's (DOI) annual report for fiscal year 1999, we found the following:

- The principal financial statements were fairly presented in all material respects. The Department of the Interior's principal financial statements consist of the Consolidated Statement of Financial Position as of September 30, 1999; the Consolidated Statement of Net Cost of Operations, Consolidated Statement of Changes in Net Position, and Consolidated Statement of Custodial Activity for the fiscal year ended September 30, 1999; and the Combined Statement of Budgetary Resources and Statement of Financing for the fiscal year ended September 30 1999.

- Our tests of the internal controls identified weaknesses in the following areas that we consider to be material: U.S. Fish and Wildlife Service (FWS) and Bureau of Indian Affairs (BIA) construction-in-progress accounts; BIA property, plant and equipment accounts, automated information systems, and financial information integrity reviews; Minerals Management Service (MMS) financial management and accounting processes; BIA and Bureau of Reclamation (BOR) financial information related to lands; DOI and bureau trading partner data and intra-Departmental eliminations; BIA, U.S. Geological Survey (USGS), and FWS unliquidated obligations; and USGS and BOR accrued liabilities. In addition, we believe that the weaknesses in the following areas are reportable conditions: Departmental and bureau management and reporting of deferred maintenance and summarizing transactions as Government or non-Government and FWS Federal aid grants to states.

- Our tests of compliance with laws and regulations identified specific noncompliance issues for the Department and certain bureaus that are required to be reported concerning the Chief Financial Officers Act of 1990, the Debt Collection Improvement Act of 1996, the Prompt Payment Act of 1990, the Government Management Reform Act of 1994, and the Federal Financial Management Improvement Act of 1996. In addition, our tests of compliance with laws and regulations identified noncompliance with Statement of Federal Financial Accounting Standards No. 4, "Managerial Cost Accounting Standards," by BIA, USGS, and the Bureau of Land Management (BLM).

Our conclusions are detailed in the sections that follow. At the Department's request, the Department's responses to each finding are presented verbatim.

OPINION ON PRINCIPAL FINANCIAL STATEMENTS

In accordance with the Chief Financial Officers Act of 1990, we audited DOI's principal financial statements for the fiscal year ended September 30, 1999 as contained in DOI's accompanying 1999 Annual Report. DOI is responsible for these principal financial statements, and we are responsible for expressing an opinion, based on our audit, on these principal financial statements. We did not audit the information contained in Note 17 relating to Indian Trust Funds. The information in this note was audited by a certified public accounting firm, whose report has been provided to us. The information contained in Note 17 is based solely on the report of the other auditors.

Our audit was conducted in accordance with the "Government Auditing Standards," issued by the Comptroller General of the United States, and with Office of Management and Budget Bulletin (OMB) 98-08, "Audit Requirements for Federal Financial Statements," as amended, and was completed on April 20, 2000. These audit standards require that we plan and perform the audit to obtain reasonable assurance as to whether the accompanying principal financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the principal financial statements and the accompanying notes. An audit also includes assessing the accounting principles used and the significant estimates made by management. We believe that our audit work provides a reasonable basis for our opinion.

In our opinion, based on our audit and the report of the other auditors on the Indian Trust Funds, the principal financial statements (pages 89-120) present fairly, in all material respects, the consolidated statement of financial position of DOI as of September 30, 1999, its consolidated statement of net cost, consolidated statement of changes in net position, and consolidated statement of custodial activity for the fiscal year ended September 30,1999, and the combined statement of budgetary resources and statement of financing for the fiscal year ended September 30, 1999 on the basis of accounting described in Note 1 to the principal financial statements.

Our audit was conducted for the purpose of forming an opinion on the consolidated and combined principal financial statements taken as a whole. The accompanying consolidating and combining information is presented for purposes of additional analysis of the consolidated and combined principal financial statements. The consolidating and combining information for fiscal year 1999 (pages 121-133) was subjected to the auditing procedures applied in the audit of the consolidated and combined principal financial statements and, in our opinion, is fairly stated in all material respects in relation to the consolidated and combined principal financial statements taken as a whole.

In addition, the deferred maintenance and supplementary stewardship information that follows the supplemental financial statements (pages 135-152) is not a required part of the principal financial statements but is supplementary information required by the Federal Accounting Standards Advisory Board. We have applied certain limited procedures, including discussions with management, on the methods of measurement and presentation of the supplementary information to ensure compliance with the OMB guidance and consistency with the financial statements. However, we did not audit the information and therefore do not express an opinion on this supplementary information.

REPORT ON INTERNAL CONTROLS

Our audit was conducted in accordance with the "Government Auditing Standards," issued by the Comptroller General of the United States, and with OMB Bulletin 98-08.

Management of DOI is responsible for establishing and maintaining an internal control structure which provides reasonable assurance that the following objectives are met:

- Transactions are properly recorded, processed, and summarized to permit the preparation of the principal financial statements and required supplementary stewardship information in accordance with Federal accounting standards.

- Assets are safeguarded against loss from unauthorized acquisition, use, or disposition.

- Transactions are executed in accordance with laws governing the use of budget authority and other laws and regulations that could have a direct and material effect on the principal financial statements or required supplementary stewardship information and any other laws, regulations, and Governmentwide policies identified by the OMB.

- Transactions and other data that support reported performance measures are properly recorded, processed, and summarized to permit the preparation of performance information in accordance with criteria stated by management.

Because of inherent limitations in any internal control structure, errors or fraud may occur and not be detected. Also, projections of any evaluation of the internal controls over financial reporting to future periods are subject to the risk that the internal controls may become inadequate because of changes in conditions or that the degree of compliance with the policies or procedures may deteriorate.

In planning and performing our audit, we considered DOI's internal controls over financial reporting by obtaining an understanding of DOI's internal controls, determining whether these internal controls had been placed in operation, assessing control risks, and performing tests of controls to determine our auditing procedures for the purpose of expressing an opinion on the principal financial statements and not to provide assurance on the internal controls over financial reporting. Accordingly, we do not provide an opinion on internal controls.

Our consideration of the internal controls over financial reporting would not necessarily disclose all matters in the internal control structure over financial reporting that might be reportable conditions. Under standards established by the American Institute of Certified Public Accountants and by OMB Bulletin 98-08, reportable conditions are matters coming to our attention relating to significant deficiencies in the design or operation of the internal controls that, in our judgment, could adversely affect DOI's ability to record, process, summarize, and report financial data consistent with the assertions made by management in the financial statements. Material weaknesses are reportable conditions in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted matters involving the internal controls and their operation that we consider to be reportable conditions as described by the American Institute of Certified Public Accountants and OMB Bulletin 98-08.

Material Weaknesses

We discovered material weaknesses as discussed in the paragraphs that follow.

A. BIA and FWS Need Improved Controls Over the Construction-in-Progress Account

BIA did not have sufficient internal control procedures to ensure that the general ledger control account for construction-in-progress was accurately stated and properly supported. Our test on the completeness of the account showed that BIA did not identify and record all projects that should have been included in the account, timely transfer completed projects from the account, or remove invalid projects from the account. We brought this deficiency to the attention of BIA management, and as of September 30, 1999, net adjustments totaling $69.2 million had been made to the construction-in-progress account.

In addition, FWS did not have sufficient internal control procedures to ensure that the general ledger control account for construction-in-progress was accurately stated and properly supported. Our test of the reasonableness of the account indicated that the account was overstated by approximately $114.5 million. This condition occurred because FWS did not implement procedures to ensure that the charges to the account were reviewed promptly and that the charges were for FWS building and structure assets (real property) that would meet the FWS capitalization threshold of $50,000. When we brought this deficiency to the attention of FWS management, they made the proper adjustments.

Departmental Response: The Department concurs with this finding. BIA is currently implementing a plan to improve controls over Construction-in-Progress (CIP) including the issuance of a new CIP Manual during the first quarter of FY 2000. In addition, BIA has completed a new physical inventory of CIP projects and will conduct a bureauwide training program for individuals involved in Construction-in-Progress activities in June, 2000.

FWS implemented several corrective actions during fiscal year 1999 to improve procedures over CIP. In the fall of 1999, FWS issued a second set of procedures to improve CIP practices. The Department believes that the implementation of these new procedures will resolve this issue.

B. BIA Needs Improved Controls Over Management of its Property, Plant and Equipment Accounts

BIA did not have sufficient internal control procedures to ensure that the buildings subsidiary ledger, other structures and facilities subsidiary ledger, and equipment subsidiary ledger were stated in accordance with Statement of Federal Accounting Standards No. 6, "Accounting for Property, Plant and Equipment." For example, we identified items that had incorrect acquisition costs, items that had been demolished but not removed from the ledgers, and items that had not been included in the ledger.

When these deficiencies were brought to the attention of BIA management, adjustments were made totaling $82.1 million to acquisition costs, accumulated depreciation, depreciation expense general ledger control accounts, other related control accounts, and the subsidiary ledgers.

Departmental Response: The Department concurs with this finding. The BIA completed a new physical inventory as of March 31, 2000. In addition to this inventory, BIA is currently photographing all real property; these photographs will be loaded into a database that will be linked to the Fixed Asset System.

C. BIA Needs Improved General Controls Over its Automated Information Systems

BIA continued to have ineffective general controls over the automated information systems of its Operations Service Center and was not in compliance with OMB Bulletin 98-08. Specifically, BIA did not (1) have an effective system security program and had not enforced personnel policies and procedures to ensure adequate system security, (2) classify its resources to determine the level of security needed, (3) monitor visitor activities and perform adequate housekeeping to safeguard computer hardware, (4) perform periodic reviews to ensure that users' access levels were appropriate, (5) ensure that the proper version of an application was used in production, (6) have segregation of duties for the system support functions, (7) have controls over system software to effectively detect and deter inappropriate use, and (8) have an effective means of recovering or of continuing computer operations in case a system fails.

Departmental Response: The Department concurs with this finding. As a result of the 1999 management control assessment process, the Department identified inadequate general controls over automated systems in BIA and has a plan to resolve these inadequate general controls.

D. MMS Needs Improved Controls Over Financial Management and Accounting Processes

MMS's Financial Management Branch did not have financial data that were accurate, complete, and timely for fiscal year 1999. OMB Bulletin No. 98-08, "Audit Requirements for Federal Financial Statements," states that internal controls are designed to provide reasonable assurance that transactions are properly recorded, processed, and summarized to permit the preparation of financial statements in accordance with Federal accounting standards. OMB Circular No. A-123, "Management Accountability and Control," states that managers are responsible for the quality and timeliness of program performance and for ensuring that programs are managed with integrity and in compliance with applicable laws. However, control deficiencies occurred because MMS personnel did not follow established internal controls, such as performing account reconciliations and providing management oversight of the financial management and accounting processes. Also, MMS did not establish adequate internal controls which ensured that transactions were properly classified during the conversion to the new standard general ledger required by the Federal Financial Management Improvement Act of 1996.

Departmental Response: The Department concurs with this finding, and as a result of the 1999 management control assessment process, identified inadequate internal controls over financial operations and data managed by the Financial Management Branch (MMS) as a new material weakness. MMS is working to improve internal controls through organizational changes, improved procedures, and better oversight.

E. BIA Needs Improved Controls Over Financial Information Integrity Reviews

BIA did not have sufficient internal control procedures to ensure that errors and invalid transactions contained in its general and subsidiary ledgers, listings, and reports were timely identified and corrected at September 30, 1999. This occurred because BIA had not developed and implemented an effective financial information integrity review, reconciliation, and correction process.

Departmental Response: The Department concurs with this finding. The BIA has implemented a two level review process for all journal vouchers that are to be entered into the accounting system. This change, along with management changes currently underway, should result in improved controls over financial information.

F. BIA and BOR Need Improved Controls Over Financial Information Related to Land

BIA did not have sufficient internal controls to ensure that errors and omissions related to the land improvements and the land rights subsidiary ledgers were timely identified and corrected. This occurred because BIA had not developed and implemented an effective financial information integrity review, reconciliation, and correction process. Our tests disclosed the following: one land improvement totaling $676,000 was erroneously recorded in the ledger; three land improvements totaling $465,000 were recorded in the ledger with no useful lives; three parcels of land were erroneously recorded in the ledger; and five athletic fields and seven parcels of land were not recorded in the ledger.

BOR did not have a complete and accurate inventory system to account for land and land rights data. This occurred because BOR's land and land rights subsidiary ledger had not been reconciled with the individual project plat books and land purchase contracts. During our audit, we found that the inventory system used to account for the $1.7 billion in land and land rights contained costs for lands that were previously transferred to project beneficiaries and/or other Federal agencies, project plat maps that did not include all related costs and acres, and project plat maps that were not reconciled to BOR's financial accounting system.

Departmental Response: The Department concurs with this finding. The BIA has completed a comprehensive physical inventory of all bureau property, including land, and is testing the inventories that were taken at their Regional Offices. BIA land amounts to less than .04% of total BIA Property, Plant and Equipment.

Reclamation agrees with the findings that some of its land records were not current and that reconciliations with the financial accounting system were not performed. To address this problem, Reclamation will develop an action plan by September 30, 2000, that will contain milestones and actions to: 1) conduct reconciliations and research to validate the accuracy of its land records; 2) populate its new real property system (FIRM) with such data; 3) develop and issue policy and procedures to ensure future quality, accuracy and completeness of data captured in the lands and finance systems; and 4) conduct an initial and periodic reconciliations between the detailed land data maintained in FIRM and the financial accounting system to ensure the quality of information contained in both systems.

G. DOI and Bureaus Need Improved Controls Over Trading Partner Data and Intra-Departmental Eliminations

DOI's and the bureaus' internal controls were not sufficient to provide reasonable assurance that transactions with other Federal agencies and within DOI were properly summarized as required by the Treasury Financial Manual and that the intra-Departmental transaction amounts were accurately identified. In addition, DOI and the bureaus did not adequately reconcile the trading partner data to the eliminations data. The intra-Departmental trading partner amounts should be the same as the intra-Departmental eliminations amount; thus, after the elimination of intra-Departmental transactions and the reconciliation of intra-Departmental trading partner data, the balances should be zero. An analysis by DOI showed that differences in individual bureaus ranged from minimal differences to over $60 million. We also observed a number of differences between these two data segments. For example, BIA showed $66.7 million in expenses with its trading partner, USGS, but the elimination data between the two bureaus was only $3.7 million.

Departmental Response: The Department concurs with this finding. In fiscal year 1999, the Department did not rely on trial balance trading partner data to identify intra-departmental transactions to be eliminated in reporting consolidated financial statement information. Bureaus followed alternative procedures to identify and certify the accuracy of intra-departmental transactions. This data was used in preparing the Department's consolidated financial statements. Beginning in fiscal year 2000, the Department expects to base intra-departmental elimination information on trial balance trading partner information to ensure the accuracy and consistency of trading partner data.

H. BIA, USGS, BOR, and FWS Need Improved Controls Over Their Respective Unliquidated Obligations Account and/or Accrued Liabilities

BIA, USGS, and FWS did not have adequate controls to ensure that unliquidated obligations were timely deobligated and adequately supported. In general, this occurred because management of the respective bureaus either did not (1) implement adequate policies and procedures to ensure that periodic assessments of the validity and accuracy of the unliquidated obligation transactions were conducted, (2) have procedures to update the general ledger undelivered orders account, or (3) timely remove or deobligate the unliquidated obligation. During our testing, we found that the unliquidated obligations balance at September 30, 1999 was overstated for all three bureaus by a total of about $46.6 million. Once informed, management of the three bureaus made the necessary adjusting entries.

In regard to accrued liabilities, BOR did not properly estimate or record its year-end accruals for liabilities owed others for fiscal years 1998 and 1999. This occurred because BOR's procedures did not include a complete analysis of payments, which may have affected the liability amount at year end but occurred after year end; its regional offices did not follow existing procedures or lacked the understanding of the procedures; and its management did not provide sufficient oversight. As a result, BOR failed to identify liabilities totaling approximately $14 million attributable to fiscal year 1999. Once informed of our conclusions, BOR management made the proper adjustments. USGS failed to establish adequate internal control procedures to ensure that its accrued expenses were valid. This occurred because USGS management had not enforced the existing bureauwide policy on when to realize an accrued liability. When we informed USGS of our finding, management conducted a review and made a $70 million adjustment to accrued liabilities and unexpended appropriations.

Departmental Response: The Department recognizes the need to continue to improve controls over unliquidated obligation accounts. Building on the review process instituted as a result of the FY 1999 financial statement audits, the Department will continue to review unliquidated obligations periodically during the year and at year end to support the preparation of annual financial statements and to ensure that the data is reliable.

Reclamation and USGS agree with the finding that they did not properly estimate or record year-end accruals for some liabilities owed to others. To preclude this from occurring again, these bureaus will re-emphasize the need to properly accrue liabilities, and continue to address these procedures in the year-end closing guidance. Moreover, to ensure that liabilities are properly accrued, the bureaus will perform year-end analytical reviews. The FWS is addressing Federal Aid Grant Program unliquidated obligation accounts in the context of a comprehensive review of Federal Aid accounting. In addition, FWS has taken steps to develop additional grant accounting expertise within its finance operation.

Reportable Conditions

We discovered the reportable conditions discussed in the paragraphs that follow.

I. DOI and Bureaus Need Improved Controls Over Deferred Maintenance Management and Reporting

In accordance with OMB Bulletin 98-08, we reviewed the internal controls related to transactions and other data that support the reported information on deferred maintenance in the bureaus to determine whether the transactions were properly recorded, processed, and summarized. We found that formal policies and procedures for conducting periodic condition assessment surveys and for computing, compiling, and reporting deferred maintenance funding estimates needed to be established by DOI and the bureaus to promote consistency and accuracy. In addition, the supervisory and monitoring controls over deferred maintenance reporting requires strengthening to ensure that deferred maintenance estimates are accurate, complete, and supported by adequate documentation.

Departmental Response: The Department recognizes the need to continue to improve controls over deferred maintenance management and reporting. The Department has identified inadequate maintenance management capability as a material weakness through out the Department. Progress is being made to correct the material weakness. The Department issued comprehensive facilities condition assessment guidelines in December, 1999 and bureaus are in the process of developing programs to implement these guidelines. Work is also in progress on new maintenance management systems, including a pilot system at the National Park Service. The Department has instituted a five-year capital planning process to improve facilities maintenance and construction planning and ensure that high priority deferred maintenance needs are addressed.

J. DOI and Bureaus Need Improved Controls Over Summarizing Transactions as Government or Non-Government

DOI and the bureaus did not properly summarize transactions as Government or non-Government. This occurred because internal controls were not sufficient to provide reasonable assurance that transactions were properly summarized as Federal (Government) or Public (non-Government) in the general ledger accounts, as required by OMB Bulletin 97-01, "Form and Content of Agency Financial Statements," as amended.

Departmental Response: The Department agrees that it needs to continue to improve internal controls over the classification of transactions as Federal or Public. Additional training is scheduled for staff managing these transactions and quarterly reviews of these accounts will be performed in 2000.

K. FWS Needs Improved Controls Over its Federal Aid Grants to States

FWS did not have adequate controls to ensure that grantee-approved drawdown amounts were for costs incurred. The draft "Grant Financial System Requirements Manual," published by the Joint Financial Management Improvement Program, requires an agency's grant financial management system to include documentation on the timing of a grantee's cash flow, the amounts disbursed to the grantee during the year, and the amounts actually expended by the grantee. FWS did not establish a system to obtain documentation from grant recipients to support costs incurred during the year. Thus, FWS could not verify that the drawdowns were for costs that the grantee incurred during fiscal year 1999.

Departmental Response: The Department and FWS recognized the existence of inadequate management controls and audit follow-up in the Federal Aid Program in fiscal year 1999, and reported it as a new material weakness under the Federal Managers' Financial Integrity Act (see page 59, Compliance with Legal and Regulatory Financial Requirements). To address the material weakness, the FWS Director established five Federal Aid Process Improvement Teams to review every aspect of the program and provide recommendations to enhance program accounting compliance and strengthen overall program accountability and management. The findings and recommendations were reported to the Department on February 15, 2000, and have been incorporated into a comprehensive correction action plan with appropriate milestones and target dates.

STEWARDSHIP AND PERFORMANCE MEASURES

We reviewed DOI's internal controls over the required supplementary stewardship information (pages 135-152) by obtaining an understanding of DOI's internal controls relating to the preparation of the required supplementary stewardship information, determining whether these internal controls had been placed in operation, assessing control risk, and performing tests of these controls as required by OMB Bulletin 98-08. However, providing assurance on these internal controls was not an objective of our audit, and accordingly, we do not provide assurance on such controls.

With respect to the internal controls related to the performance measures reported in DOI's Management Discussion and Analysis section (pages 1-68), we obtained an understanding of significant internal controls related to the existence and completeness assertions as required by OMB Bulletin 98-08. Our procedures were not designed to provide assurance on the internal controls over reported performance measures, and accordingly, we do not provide an opinion on such controls.

We also identified other issues that, in our judgment, were not required to be included in this audit report but that should be communicated to management. We will report these issues in a separate management letter.

REPORT ON COMPLIANCE WITH LAWS AND REGULATIONS

We conducted our audit in accordance with the "Government Auditing Standards," issued by the Comptroller General of the United States, and with OMB Bulletin 98-08.

Management of DOI is responsible for complying with applicable laws and regulations. As part of obtaining reasonable assurance as to whether DOI's principal financial statements are free of material misstatement, we performed tests of DOI's compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of amounts contained in the principal financial statements and certain other laws and regulations specified in OMB Bulletin 98-08, including the requirements referred to in the Federal Financial Management Improvement Act of 1996. However, providing an opinion on compliance with certain provisions of laws and regulations was not an objective of our audit, and accordingly, we do not express such an opinion.

The results of our tests of compliance with laws and regulations discussed in the preceding paragraphs, exclusive of the Federal Financial Management Improvement Act, disclosed instances of noncompliance that are required to be reported under "Government Auditing Standards" and/or OMB Bulletin 98-08 as follows:

- Chief Financial Officers Act of 1990. BIA did not effectively establish and implement general and financial management practices and improve its systems of accounting, financial management, and internal controls to ensure the issuance of financial information related to the production of complete, reliable, timely, and consistent financial reports. As such, BIA was not in compliance with the Act.

Departmental Response: The Department concurs with this finding. The National Association of Public Administration (NAPA) undertook a study of BIA administrative operations. The bureau has implemented the recommendations included in the NAPA Report and is reorganizing the Division of Accounting Management to include professional positions to improve its financial information systems and internal controls. Implementation of these recommendations should substantially improve the management over financial management practices and internal controls.

- Debt Collection Improvement Act of 1996. BIA was not in compliance with the Debt Collection Improvement Act, which requires that all receivables delinquent for more than 180 days be referred to the U.S. Treasury for collection. BIA had accounts receivable of about $22.8 million that were delinquent for more than 180 days and were eligible for referral at September 30, 1999.

Departmental Response: The Department concurs with this finding. The BIA is referring delinquent debt to Treasury as required by the Debt Collection Improvement Act and expects to be current with the transfer of eligible receivables, including power and irrigation receivables, by the end of the fiscal year 2000.

- Prompt Payment Act. BIA was not in compliance with the Prompt Payment Act, which requires that Federal agencies pay their bills on time, pay interest penalties when payments are made late, and take discounts only when payments are made within the discount period and are advantageous to the Government. A January 24, 2000 quality control report prepared by the Chief, Accounting Operations Branch, National Business Center, for the fourth quarter of fiscal year 1999 stated that the overall accuracy of BIA's prompt pay report was not acceptable because of the number of payment processing errors found.

Departmental Response: The Department recognizes that the BIA needs to continue to improve its prompt payment performance. As part of this process, the BIA conducts periodic quality assurance reviews of payment packages prepared in the field and paid under the BIA Remote Payment Process. BIA is making progress in the internal auditing of payment packages and currently reports that over 90% of all potential errors are corrected at the Regional Offices before payment is made. The Department realizes that this performance needs to continue to improve, and we are working with BIA to achieve an accuracy rate that approaches 100%.

- Government Management Reform Act of 1994. DOI was not in compliance with the Government Management Reform Act, which requires that Federal agencies submit audited financial statements to OMB no later than March 1 of the following year. DOI did not comply with this requirement because it was unable to complete the analyses of all accounts necessary for the preparation of the financial statements in a timely manner. Since the primary financial statement analyses occurred after the fiscal year-end and the closing of the bureaus' general ledgers, more than 750 financial data adjustments totaling over $120 billion were required to be posted for DOI's consolidated financial statements to be presented fairly.

Departmental Response: The Department concurs with this finding. In Fiscal Year 1999, the Department focused its attention on resolving known issues related to specific detail accounts, such as Property Plant and Equipment, Construction in Progress and Undelivered Orders. Further, the Department required bureaus to record all adjustments in the consolidated financial statement data base to enable the Department and the Office of the Inspector General to improve the analysis of bureau level adjustments. This process delayed the completion of the final financial statements. In Fiscal Year 2000, the Department will begin preparing quarterly financial statements, which will allow analytical reviews to be performed prior to fiscal year end. Further, the system capabilities established in Fiscal Year 1999 will be expanded in Fiscal Year 2000 to ensure consistent application of accounting principles and standards.

- Under the Federal Financial Management Improvement Act (FFMIA), we are required to report whether DOI's financial management system is in substantial compliance with requirements for Federal financial management systems, Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level. To meet these requirements, we performed tests of compliance using the implementation guidance for the Act included in Appendix D of OMB Bulletin 98-08. We identified instances in BLM where the bureau did not comply with the requirements for Federal financial management systems and Federal accounting standards in processing assembled land exchanges.

Departmental Response: The Department does not concur with this finding. After analysis, BLM identified several instances totaling less than $4.5 million for FY 1999 where cash used in assembled land exchanges was determined to be public money that should have been properly deposited in the U.S. Treasury and recorded in the BLM accounting system. Instead, these funds were held by custodians in financial institutions that were not designated as depositories of the Secretary of the Treasury. BLM is modifying its policies and procedures related to assembled land exchange transaction to improve this process. The Department does not believe this represents a substantial non-compliance with requirements for Federal financial management systems, Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level.

OIG Reply: Although DOI disagreed with the finding, BLM management concurred with the finding in its April 24, 2000 response to the BLM report and has developed a corrective action plan to address the issue. Executive agencies are required by 31 U.S.C. § 3512b to establish and maintain systems of accounting that provide "complete disclosure of the financial results of the activities of the agency, adequate financial information the agency needs for management purposes, effective control over and accountability for assets for which the agency is responsible, and reliable accounting results that will be the basis for . . . suitable integration of the accounting of the agency with the central accounting and reporting responsibilities of the Secretary of the Treasury." In addition, custodians of public money are required by 31 U.S.C. § 3302 to deposit monies with the U.S. Treasury or with a depository designated by the Secretary of the Treasury. At the end of fiscal year 1999, we identified $4.3 million of cash held in escrow accounts or by other third parties that was used in assembled land exchanges but was not recorded in BLM's financial management system. The $4.3 million was reflected in BLM's financial statements. However, because BLM has been designated as a custodian of this public money but did not deposit the cash in the U.S. Treasury or in a designated depository of the Secretary of the Treasury, the Bureau was not in compliance with the requirements for Federal financial management systems.

- As discussed in the Report on Internal Controls section of this report, we believe that the material internal control weaknesses concerning the ineffective general controls over BIA's automated information systems and MMS's financial management and accounting processes are instances of noncompliance with FFMIA.

Departmental Response: The Department concurs with this finding. Both BIA and MMS are taking steps to improve general controls over automated information systems. BIA is in the process of implementing several NAPA recommendations related to computer operations. These changes should result in improved general controls over automated information systems. In addition, MMS is taking steps to improve controls over its automated financial accounting operations.

- Our tests of compliance with laws and regulations disclosed that DOI was not in full compliance with managerial cost accounting standards. This occurred because DOI (1) did not, in all cases, have support for the assignment of costs to responsibility segments when two or more responsibility segments shared resources and (2) did not report the costs of outputs and unit costs of outputs. Statement of Federal Financial Accounting Standards No. 4 requires agencies to establish responsibility segments and to measure and report the full costs of resources consumed by the segment in producing each segment's outputs. Appendix E to the Statements of Federal Financial Accounting Concepts and Standards defines outputs as "a tabulation, calculation, or recording of activity or effort that can be expressed in a quantitative or qualitative manner. They shall have two characteristics: (1) they shall be systematically or periodically captured through an accounting or information management system, and (2) there shall be a logical connection between the reported measures and the program's purpose." The full costs of outputs produced by a responsibility segment are to be assigned by the following methods listed in order of preference: directly tracing costs wherever feasible and economically practicable; assigning costs on a cause-and-effect basis; and allocating costs on a reasonable and consistent basis. Full costs include the direct and indirect costs that contribute to the output regardless of funding sources. Standard No. 4 further provides that in cases where resources are shared by two or more activities, the common costs are to be assigned to activities either on a cause-and-effect basis, if feasible, or through reasonable allocations. BIA did not allocate over $114 million in indirect costs (shared resources) to its segments. BLM allocated about $470 million in indirect costs based on percentages supported by "professional judgement," which we do not consider a reasonable or consistent basis for assigning costs because the percentages were not verifiable.

According to Standard No. 4, "outputs produced by responsibility segments should be accumulated and, if practicable, measured in units [and] the full costs . . . should be assigned to outputs . . .." However, DOI has not identified the costs of all outputs and the costs per unit. For example, one of the performance measures reported by DOI is the number of acre-feet of water delivered by BOR (an output); however, no information is presented on the cost per acre-foot of water delivered.

Departmental Response: The Department does not concur with this finding. During fiscal year 1999, the Department took aggressive steps to align cost information with GPRA information to comply with the Managerial Cost Accounting Standard, SFFAS No. 4. Specifically, the Department required that the responsibility segments identified by bureaus be directly related to the GPRA Program Activities and aligned with the mission goals of the Department. This correlates with the Managerial Cost Accounting Standard requirement which defines a responsibility segment as a component of a reporting entity that is responsible for carrying out a mission, conducting a major line of activity, or producing one or a group of related products and services. The Department reported full cost for individual responsibility segments and presented performance measures for each GPRA Program Activity which align with these responsibility segments. These performance measures are an appropriate reflection of the results or outputs of the GPRA Program Activity for which the costs are reported. Both positive and negative results were reflected.

The official cost records for responsibility segments are the core accounting records of the bureaus and are reflected in the data used to prepare the Department's consolidated financial statements. In cases where costs accumulated in the core accounting records relate to more than one responsibility segment, such costs were assigned to the appropriate responsibility segments. As permitted by SFFAS No. 4, the cost assignments were made by directly mapping accounting data to responsibility segments or by other "cost finding" techniques; for example, by assigning costs to segments on a percentage basis.

All bureaus followed the Department's guidance to report full cost by responsibility segment as described above. The Department is committed to continue improving this process to meet financial statement reporting and management objectives.

***OIG Reply*:** The OIG agrees that DOI took steps to align cost information with Government Performance and Results Act (GPRA) information in order to comply with Standard No. 4. We disagree, however, that DOI has fully complied with the standard because, according to the standard, "the purpose of cost accounting by a responsibility segment is to measure the costs of its outputs." Although DOI has assigned full costs to responsibility segments and aligned the responsibility segments with GPRA program activities, it has not fully identified all the outputs of the responsibility segments or the costs of those outputs, as shown in the BIA, BLM and BOR examples discussed in the finding paragraph.

CONSISTENCY OF OTHER INFORMATION

We reviewed the financial information presented in DOI's Management Discussion and Analysis section (pages 1-68) and Supplementary Information section (pages 135-152) to determine whether the information was consistent with the principal financial statements. Based on our review, we determined that the information in the management discussion and analysis and in the required supplementary information was consistent with the principal financial statements.

PRIOR AUDIT COVERAGE

Based on our review of prior Office of Inspector General audit reports, we found that the material internal control weaknesses for BIA identified in the Report on Internal Controls section of this report were also identified as internal control weaknesses in the following reports:

- The September 1999 report "Deferred Maintenance, National Park Service, U.S. Fish and Wildlife Service, U.S. Geological Survey, Bureau of Indian Affairs, Bureau of Land Management, and Bureau of Reclamation" (No. 99-I-874) stated that the bureaus needed to implement actions to ensure that deferred maintenance information is reliable for budgetary and accounting purposes.

- The June 1998 report "Followup of General Controls Over Automated Information Systems, Operations Service Center, Bureau of Indian Affairs" (No. 98-I-483) stated that the general control weaknesses and risks identified in our audit for fiscal year 1996 continued to exist during fiscal year 1997.

- The May 1997 report "Bureau of Indian Affairs Consolidated Financial Statements for Fiscal Years 1995 and 1996" (No. 97-I-834) stated that BIA's internal control structure was not sufficient to support the balances for the other buildings and structures.

- The April 1997 report "General Controls Over Automated Information Systems, Operations Service Center, Bureau of Indian Affairs" (No. 97-I-771) stated that BIA's general controls over its automated information systems at the Center were not effective. Specifically, according to the report, BIA did not (1) have an effective security program and had not enforced personnel policies and procedures to ensure adequate system security, (2) classify its resources to determine the level of security needed, (3) monitor visitor activities and perform adequate housekeeping to safeguard computer hardware, (4) perform periodic reviews to ensure that users' access levels were appropriate, (5) ensure that the proper version of an application was used in production, (6) have segregation of duties for the system support functions, (7) have controls over system software to effectively detect and deter inappropriate use, and (8) have an effective means of recovering or of continuing computer operations in case a system fails.

OBJECTIVE, SCOPE, AND METHODOLOGY

Management of DOI is responsible for the following:

- Preparing the principal financial statements and the required supplementary information referred to in the Consistency of Other Information section of this report in conformity with generally accepted accounting principles and for preparing the other information contained in the 1999 Annual Report.

- Establishing and maintaining an internal control structure over financial reporting. In fulfilling this responsibility, estimates and judgments are required to assess the expected benefits and related costs of internal control structure policies and procedures.

- Complying with applicable laws and regulations.

We are responsible for the following:

- Expressing an opinion on DOI's principal financial statements.

- Obtaining an understanding of the internal controls based on the internal control objectives in OMB Bulletin 98-08, which require that transactions be properly recorded, processed, and summarized to permit the preparation of the principal financial statements and the required supplementary information in accordance with Federal accounting standards; that assets be safeguarded against loss from unauthorized acquisition, use, or disposal; and that transactions and other data that support reported performance measures be properly recorded, processed, and summarized to permit the preparation of performance information in accordance with criteria stated by management.

- Testing DOI's compliance with selected provisions of laws and regulations that could materially affect the principal financial statements or the required supplementary information.

To fulfill these responsibilities, we took the following actions:

- Examined, on a test basis, evidence supporting the amounts disclosed in the principal financial statements.

- Assessed the accounting principles used and the significant estimates made by management.

- Evaluated the overall presentation of the principal financial statements.

- Obtained an understanding of the internal control structure related to safeguarding assets; compliance with laws and regulations, including the execution of transactions in accordance with budget authority; financial reporting; and certain performance measures reported in the section "Management Discussion and Analysis" of DOI's 1999 Annual Report.

- Tested relevant internal controls over the safeguarding of assets; compliance with laws and regulations, including the execution of transactions in accordance with budget authority; and financial reporting.

- Reviewed the internal controls related to the existence and completeness assertions for systems producing the performance measures information reported in the section "Management Discussion and Analysis" of DOI's 1999 Annual Report.

- Tested compliance with selected provisions of laws and regulations.

We did not evaluate all of the internal controls relevant to the operating objectives as broadly defined by the Federal Managers' Financial Integrity Act, such as those controls related to preparing statistical reports and ensuring efficient operations. We limited our internal control testing to those controls needed to achieve the objectives outlined in our report on internal controls.

Section 5(a) of the Inspector General Act (5 U.S.C. app. 3) requires the Office of Inspector General to list this report in its semiannual report to the Congress. In addition, the Office of Inspector General provides audit reports to the Congress.

This report is intended for the information of management of DOI and OMB and the Congress. However, this report is a matter of public record, and its distribution is not limited.

Earl E. Devaney
Inspector General