



U.S. Department of Agriculture  
Office of Inspector General  
Northeast Region  
Audit Report

FISCAL YEAR 2001  
RURAL DEVELOPMENT FINANCIAL  
STATEMENT AUDIT – PENNSYLVANIA



**Report No.  
85401-01-Hy  
April 2002**



UNITED STATES DEPARTMENT OF AGRICULTURE

OFFICE OF INSPECTOR GENERAL

Northeast Region

Suite 2-2230

5601 Sunnyside Avenue, Stop 5300

Beltsville, Maryland 20705-5300



DATE: April 26, 2002

REPLY TO

ATTN OF: 85401-01-Hy

SUBJECT: Fiscal Year 2001 Rural Development, Financial Statement Audit –  
Pennsylvania

TO: Byron E. Ross  
State Director  
Rural Development

This report presents the results of the subject audit. Your written response, dated April 11, 2002, has been incorporated into the Findings and Recommendations section of the report. We also made the two corrections your reply noted in Finding No. 3. The complete text of the response is included as exhibit B.

We agree with your management decision for each recommendation in the report. Please follow your internal agency procedures when forwarding final action correspondence to the Office of the Chief Financial Officer.

We appreciate the assistance you and your staff provided to us during our review.

/s/

REBECCA ANNE BATTS  
Regional Inspector General  
for Audit

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## EXECUTIVE SUMMARY

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### RESULTS IN BRIEF

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This report presents the results of our audit of internal controls over Rural Development programs in the State of Pennsylvania. This audit was performed as part of the Office of Inspector General's (OIG's) audit of Rural Development's fiscal year (FY) 2001 Financial Statements. The objectives of this audit were to determine if Pennsylvania's Rural Development's system of internal control provides reasonable assurance that agency control objectives were met, and that Rural Development has complied with laws and regulations for transactions and events that may have a material effect on its financial statements.

Our review of controls over various loan and grant programs, collection activities, accountable property, and the Purchase Card Management System (PCMS) disclosed no issues that would have a material effect on Rural Development's FY 2001 financial statements. Generally, we found controls were in place and functioning to ensure only eligible borrowers were approved for loans and grants, collections were accounted for accurately, property existed, and PCMS reviews were being performed.

Although Pennsylvania Rural Development had established sufficient internal controls over various programs, activities, and systems, some of these controls need to be strengthened. The Property Inventory Management System (PROP) inventory listing for the State office and three of the six area offices visited was not updated when property was transferred or otherwise disposed of. We found 7 of 32 property items at the State office and 11 of 27 items at three area offices had been transferred or disposed of and the PROP inventory listing had not been updated. As a result, personal property, valued at \$39,249 was not properly accounted for in the PROP.

The State office did not adequately manage access to its computer systems. Employees who retired, died, or left the Agency had not been timely removed from the systems. During our review, the State Information Resource Manager removed the user identification from the systems for all non-current Rural Development employees.

Our review of eight water and waste loans closed in FY 2001 in four area offices identified one area office that had not performed the required civil rights compliance review on a loan totaling \$9,611,800 for a sewage collection and treatment system. According to Rural Development instructions, a compliance review is required to be performed on water and waste loans and grants before the loan or grant closing or before construction begins, whichever ever occurs first. Although procedures were in place to ensure that loans and grants met eligibility requirements and were approved in accordance with agency criteria, they were not always followed. Officials of the Pennsylvania Rural Development Lehigh Area Office could not explain why the review was not performed. Also, the State office officials were not aware that the review had not been conducted. Rural Development has no assurance that the borrower did not subject any person to discrimination on the grounds of race, color, or national origin.

During our review, State officials instructed the Lehigh Area Office officials to immediately complete the compliance review. The compliance review was completed on November 6, 2001.

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## **KEY RECOMMENDATIONS**

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We recommend Rural Development perform a physical inventory for the State, reconcile all missing items, and update the PROP Inventory Management System as necessary.

Rural Development should issue accountable property management procedures that document the responsibilities of State accountable property officers. The State office should remove all unauthorized users from Rural Development systems and implement controls to ensure that only authorized users have access. In addition, State office personnel should ensure that a civil rights compliance review is performed, as required, for the water and waste loans and grants.

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## **AGENCY RESPONSE**

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In its April 11, 2002, response to the official draft report, Rural Development officials agreed with the findings and recommendations as presented. Applicable portions of the response are incorporated, along with our position, in the Findings and Recommendations section of the report. The full text of the agency's response is included as exhibit B of the report.

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# INTRODUCTION

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## BACKGROUND

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Rural Development is the credit agency for rural development in the United States, Puerto Rico, the Virgin Islands, and trust territories. Rural Development provides loans and grants

and extends loan guarantees for housing, community development, and electric and telecommunication programs. The Rural Development mission area consists of three program agencies, the Rural Housing Service, the Rural Utilities Service, and the Rural Business-Cooperative Service.

Nationwide, Rural Development has an outstanding loan portfolio of \$82.4 billion. The loan programs are delivered through each agency's national office, 47 State offices, 266 area offices, and 686 local offices. At the State level, Rural Development provides guidance and oversight of field office activities and administers program activities. A State office program specialist is assigned to each program. As part of its oversight function, the State office performs reviews of program areas and field offices. At a minimum, State offices are required to perform a review of each field office once every five years. In Pennsylvania, there are 11 field offices.

Before granting a loan, Rural Development must ensure the applicant is eligible. Eligibility determinations vary by loan program. For housing loans, repayment of the loan is dependant on the applicant having stable income and no significant outstanding debt. Rural Development will verify the applicant's income by contacting the applicant's employer and will verify existing debt by obtaining a credit report. Rural Development generally has first lien on the subject property and in case of default, the house must be of sufficient value to cover the amount of the loan. An appraisal of the subject property must be completed prior to loan approval with only properties appraised at or above the loan amount being considered. Community development and rural utility loans are made only to municipalities where repayment of the loan is dependent on the tax base of the community or the use of the facility.

The management of the three Rural Development agencies is responsible for establishing internal controls and for ensuring compliance with laws and regulations applicable to its programs. During the course of our review, we tested compliance with a number of these laws and regulations, including the Anti-Deficiency Acts of 1906 and 1950; Rural

Utilities Service Instruction 1780; Single-Family Housing Instruction HB-1-550; and Rural Development Instructions 4279A, 4279B, 1980-A, 1980-D, 1980-I, 1944-E, 1901-E, and 2024-H.

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## **OBJECTIVES**

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The overall objective of the nationwide audit is to determine whether Rural Development's financial statements present fairly, in all material respects, the financial results in accordance with prescribed accounting principles. In Pennsylvania, we determined if the State system of internal controls provided reasonable assurance that agency control objectives were met, and that it complied with laws and regulations for transactions and events that might have a material effect on its financial statements.

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## **SCOPE**

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The audit control point, OIG Midwest Region, selected the State of Pennsylvania for our review. We performed audit work at the Pennsylvania State office, and at the Lehigh, Butler, York, Lycoming, Westmoreland, and Juniata Area Offices. At these sites we reviewed controls over borrower eligibility determinations and loan approval functions for the direct single-family housing, community programs, water and waste programs and multi-family housing loan programs. We also reviewed similar controls over the guaranteed single-family housing and business and industry loan programs. In addition, we reviewed internal controls over accounting for personal property, use of the government purchase card, computer security, graduation of direct single-family borrowers to outside credit, collection of payments and fees, and disbursements of grant funds. We performed fieldwork from June 2001 through October 2001.

In Pennsylvania, Rural Development's loan portfolio consisted of 13,518 single-family housing direct borrowers with an outstanding unpaid principal balance of over \$583 million; 5,417 single-family housing borrowers with loan guarantees of over \$405 million; 332 multi-family housing borrowers with an outstanding balance of over \$350 million; 59 borrowers with guaranteed or direct business and industry loan balances of over \$152 million; 217 water and waste borrowers with direct loan balances of over \$188 million; and 93 borrowers with guaranteed or direct community facilities loan balances of over \$77 million.

Our universe consisted of loans closed in FY 2001 as follows.

<b>Program</b>	<b>Loan Universe</b>	<b>Dollar Value of Loans (Millions)</b>	<b>No. of Loans Reviewed</b>	<b>Dollar Value of Loans Reviewed (Millions)</b>
Direct Single Family	482	\$37.8	23	\$ 2.7
Guaranteed Single Family	861	\$64.1	5	\$ .8
Guar. Bus & Industry	10	\$33.3	5	\$20.5
Multi-Family Housing	4	\$ 2.4	3	\$ 1.4
Water & Waste	15	\$25.4	8	\$15.9
Community Facility	10	\$ 3.7	4	\$ 2.1

We conducted this audit in accordance with government auditing standards.

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To accomplish the audit objectives we:

## **METHODOLOGY**

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- Reviewed applicable regulations;
- Examined case files and case file documents;
- Reviewed online history screens from Rural Development's accounting systems;
- Conducted interviews with applicable Rural Development personnel at the offices visited;
- Confirmed disbursements with grant recipients; and
- Performed a physical inventory of accountable property.

We judgmentally selected the loans, grants, and transactions related to loan collections, included in our review based on dollar value and availability of loan files. We randomly selected graduation projects for review and reviewed purchase card controls at all offices visited.



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## FINDINGS AND RECOMMENDATIONS

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<b>CHAPTER 1</b>	<b>ACCOUNTABILITY OF PERSONAL PROPERTY NEEDS IMPROVEMENT</b>
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### FINDING NO. 1

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The State office did not establish an effective property management system. State officials relied on an informal arrangement between the Information Resource Manager (IRM) and the Accountable Property Officer (APO) to share Information Technology acquisition, transfer and disposal information. In addition, property transfer documents submitted by area office personnel were not used by the APO to update the property management system. We found 7 of 32 property items at the State office and 11 of 27 items at three of six area offices had been transferred or disposed of and the Property Management Information System (PROP) inventory listing had not been updated. As a result, personal property, valued at \$39,249 was not properly accounted for in the PROP.

All property acquired by Rural Development is required to be recorded in the PROP.<sup>1</sup> Accountable personal property is defined by Rural Development's procedures<sup>2</sup> as all furniture and equipment with an acquisition cost of \$5,000 or more, including Information Technology equipment as well as sensitive and leased property, regardless of acquisition cost. Sensitive personal property is further defined as personal property, with an acquisition cost of less than \$5,000, that is highly susceptible to loss or theft and includes camcorders, cameras, laptop computers, and cell phones.

The State office completed a physical inventory of all accountable personal property in all offices on September 14, 2000. State office officials certified the inventory on hand as of the close of business September 14, 2000. This certification was made on inventory reports for the State office and area offices.

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<sup>1</sup> National Finance Center Procedures, Title IV, "Central Accounting System Manual," Chapter 6, "Property Management Information System", Section 4, "Personal Property System (Prop)," Pg. 4, Agency Responsibilities, dated March 1998.

<sup>2</sup> Rural Development Instruction 2024-H, Custody, Control, Utilization, and Disposal of Accountable Personal Property, subsection 2024.352, dated May 2001.

We obtained the PROP inventory report of accountable personal property for the State office and the six area offices visited. The inventory report listed a total of 73 personal property items for the seven sites. These items were valued at \$246,179. We performed a physical inventory and validated property serial numbers.

At the State office, we physically located 25 of the 32 items. According to the Management Control Officer 4 of the 7 remaining items were transferred to the Pennsylvania Farm Services Agency (FSA), two were reassigned to an area office, and the last item was deemed excess in 1999. The items not accounted for were laptop computers. Although there was documentation to show that the State office transferred or exceeded the laptops, the National Finance Center PROP system was not updated.

We could not locate 11 of 27 personal property items at three of the six area offices. We were, however, able to locate all 14 reported personal property items at the other three area offices. At the Lehigh Area Office, we could not locate 7 of the 12 items on the personal property list. State officials told us that these items had been transferred but the PROP system was not updated. For the Westmoreland Area Office, 3 of the 4 items on their personal property list had been sent to the State office for reassignment. The State office did not update the PROP system. Further, we could not locate 1 of the 11 items on the personal property list for the York Area Office. According to area office officials the item was transferred to the State office. A transfer document had been completed but the PROP system was not updated.

The State office officials stated that they did not have written procedures but they had an assigned accountable property manager to maintain the PROP database. The accountable property manager informed us that the State follows Rural Development property management procedures. However, State office personnel did not include all sensitive equipment on its PROP reports. They also did not record all in-state transfers of property or record property bought for the State via a national contract.

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**RECOMMENDATION NO. 1**

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Perform a physical inventory for the State based on current Rural Development instructions. Reconcile all missing items, and update the PROP Inventory Management System, as necessary.

**Rural Development Response**

A physical inventory will be conducted and all PROP Inventory items will be reconciled by September 30, 2002.

**OIG Position**

The action planned is sufficient for management decision.

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**RECOMMENDATION NO. 2**

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Develop and issue accountable property management procedures that document the responsibilities of State accountable property officers.

**Rural Development Response**

A group of Administrative Staff employees responsible for Property Management, Contracting/Procurement, Information Resources Management, and Management Controls, met to discuss the issuance of a State procedure which will document the responsibilities of all involved in the accountability of property. We anticipate issuing the procedure prior to July 30, 2002.

**OIG Position**

The action taken and planned is sufficient for management decision.

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**FINDING NO. 2**

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The Pennsylvania State office did not actively manage access to Rural Development field office production systems by removing user identification (IDs) as people left the agency or periodically reviewing the access list. The

State Information Resources Manager (IRM) stated that access was not updated due to workload and lack of staff. The Pennsylvania Rural Development list of user IDs contained valid user IDs for Rural Development employees who retired, died, or left the Agency as long ago as 1996. As a result, the Pennsylvania Rural Development State office had no assurance that production system information was safeguarded against unauthorized use.

Office of Management and Budget Circular A-123 requires that policies and procedures used by agencies reasonably ensure reliable and timely information is obtained, maintained, reported and used for decision making. Active management control of logon IDs is critical to ensure that inactive and unauthorized users are removed. Management controls should provide reasonable assurance that system information is safeguarded against unauthorized use.

National Institute of Standards and Technology Generally Accepted Principles and Practices for Securing Information Technology Systems requires organizations effectively manage user access to systems<sup>3</sup>. This is to include establishing user accounts, tracking user authorizations, and closing user accounts. Rural Development's Data Security Manual states that user IDs, when no longer required due to terminations, transfers, dismissals, or other valid reasons, are to be canceled or removed promptly.

We obtained a roster of employees for Pennsylvania (Report CULP0007) from the audit control point. We also obtained a listing of user IDs that have access to the Rural Development Kansas City production systems. We compared the two lists and identified 36 names of employees with user IDs who are no longer employed by Rural Development. Seventeen

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<sup>3</sup> National Institute of Standards and Technology, Generally Accepted Principles and Practices for Securing Information Technology Systems, dated September 1996.

user IDs were assigned to Pennsylvania Rural Development employees who died, retired or left the Agency. Nineteen other user IDs were assigned to employees who transferred to FSA as part of a Statewide reorganization in FY 1996.

The State IRM is responsible for maintaining the production user ID list. The IRM was not aware of the number of questionable user IDs on the production user ID list. The IRM stated that Rural Development instructions require that the IRM be notified immediately upon employee separation and their user IDs promptly removed from the systems. However, the IRM informed us that instructions do not provide guidance on conducting periodic reviews of the user ID list. The IRM acknowledged the production system user ID access list was not maintained as required.

We found instances where the IRM was notified when an employee separated but, the user IDs were not removed until audit work began. We also found that employees, separated in 1996, were not removed from the access list at the time of separation or during periodic reviews of the access list. The IRM stated that user IDs were not reviewed until we began audit work.

The State IRM told us that the Pennsylvania FSA employees with valid user IDs are kept out of Rural Development systems by an organization code. However, the codes as described by the IRM would not have kept FSA employees from accessing Rural Development systems since many of the codes allowed those employees access to both Rural Development and FSA systems. According to the responsible computer security official for the Pennsylvania FSA, there is no reason for FSA employees to be authorized users of Rural Development systems.

During our review, the IRM removed the user IDs for all non-current Rural Development employees.

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**RECOMMENDATION NO. 3**

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Immediately remove all unauthorized users from Rural Development systems.

**Rural Development Response**

All unauthorized users have been removed as noted in the draft report.

**OIG Position**

The action taken is sufficient for management decision.

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**RECOMMENDATION NO. 4**

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Implement controls to ensure that the State office conduct periodic reviews of user ID access and remove unauthorized users from the system.

**Rural Development Response**

Presently, the IRM receives monthly reports from the St. Louis Security Staff to verify FH ID's and FOCUS ID's. The IRM verifies the accuracy, signs, dates and returns the report to the Security Staff. When an employee leaves the Agency, the IRM continues to receive Form AD-139 from Human Resources, and deletes the appropriate ID's and other accesses. The IRM has initiated an additional monthly review of IDMS ID's and NFC User ID's. Monthly, the IRM runs a User ID report from FOCUS, verifies the accuracy and files for reference.

A group of Administrative Staff responsible for Human Resources, Contracting/Procurement, Budget, Travel, Information Resources, Property Management and Management Controls, met and revised the process for ensuring all appropriate items are collected and destroyed, and all ID's and accesses have been deleted. A State procedure or management letter will be issued by July 30, 2002, which will ensure that these controls are identified in writing.

**OIG Position**

The action taken and planned is sufficient for management decision.

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**FINDING NO. 3**

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Our review of eight water and waste loans closed in FY 2001 in four area offices disclosed that one area office did not perform the required civil rights compliance review on a loan and grant totaling \$9,611,800 for a sewage collection and treatment system. Although Rural Development had procedures in place to ensure that loans and grants met eligibility requirements and were approved in accordance with Agency criteria, the Lehigh Area Office did not always follow them. Officials of the area office could not explain why the compliance review was not performed. As a result, Rural Development had no assurance that the borrower did not subject any person to discrimination on the grounds of race, color, or national origin.

Rural Development instructions provide that civil rights compliance reviews are to be performed on many types of loans. Compliance reviews are required to be performed on water and waste loans and grants before loan or grant closings or before construction begins, whichever occurs first. The results of the compliance review are to be sent to the State director and a copy filed in the borrower's area office docket. If the organization is found in noncompliance, any additional information that led to the finding will be sent with the form<sup>4</sup>.

We reviewed eight waste and water loans, closed in FY 2001, from four area offices throughout Pennsylvania to determine if the area offices complied with Rural Development requirements for loan closing. All eight loans met the requirements for loan closing except one in the Lehigh Area Office. This loan request was initially submitted in 1995 under the Rush Township project and was resubmitted in June 2000 and combined with the Northeastern Schuylkill Joint Municipal Authority. The total cost of the project was \$9,611,800 in loans and grants. We determined that the Lehigh Area Office did not follow Rural Development's procedures to ensure that the Northeastern Schuylkill Joint Municipal Authority loan was closed in accordance with agency criteria.

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<sup>4</sup> RD Instruction 1901-E, 1901.204(a), (d)(3), and (e), dated September 15, 1976.

State officials were not aware that the compliance review had not been performed. As a result of our audit, State officials instructed Lehigh Area Office officials to immediately complete the initial compliance review that was due prior to the closing of the loan or start of construction. The area office completed the review on November 6, 2001.

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**RECOMMENDATION NO. 5**

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Perform the compliance review on the Northeastern Schuylkill Joint Municipal Authority project. This review should be performed immediately and forwarded to the State office.

**Rural Development Response**

This loan was closed in June 2001. The compliance review was completed on November 6, 2001, as noted in the draft report. This office has been advised of the need to complete the compliance reviews at the proper time as required by the regulations.

**OIG Position**

The action taken is sufficient for management decision.



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**EXHIBIT A – SUMMARY OF MONETARY RESULTS**

<b>FINDING NO.</b>	<b>DESCRIPTION</b>	<b>AMOUNT</b>	<b>CATEGORY</b>
1	Personal Property Not Accounted For in PROP	\$39,249	FTBPTBU/ Improper Accounting

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## EXHIBIT B – RURAL DEVELOPMENT’S RESPONSE TO DRAFT REPORT

Page 1 of 2



Rural Development  
Mission Area  
Pennsylvania State Office  
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[Byron.Ross@pa.usda.gov](mailto:Byron.Ross@pa.usda.gov)

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April 11, 2002

SUBJECT: Fiscal Year 2001 Rural Development, Financial Statement  
Audit - Pennsylvania

TO: Rebecca Anne Batts  
Regional Inspector General for Audit  
Northeast Region  
Suite 2-2230  
5601 Sunnyside Avenue, STOP 5300  
Beltsville, MD 20705-5300

The PA Rural Development State Office staff reviewed the official draft report for the subject review. The response outlining our corrective actions taken or planned on each audit recommendation and proposed completion dates follows:

Recommendation No. 1 - Perform a physical inventory for the State based on current Rural Development Instructions. Reconcile all missing items, and update the PROP Inventory Management, as necessary.

**RD RESPONSE:** A physical inventory will be conducted and all PROP Inventory items will be reconciled by September 30, 2002.

Recommendation No. 2 - Develop and issue accountable property management procedures that document the responsibilities of State accountable property officers.

**RD RESPONSE:** A group of Administrative Staff employees responsible for Property Management, Contracting/Procurement, Information Resources Management, and Management Controls, met to discuss the issuance of a State procedure which will document the responsibilities of all involved in the accountability of property. We anticipate issuing the procedure prior to July 30, 2002.

Recommendation No. 3 - Immediately remove all unauthorized users from Rural Development systems.

**RD RESPONSE:** All unauthorized users have been removed as noted in the draft report.

Recommendation No. 4 - Implement controls to ensure that the State Office conduct periodic reviews of user ID access and remove unauthorized users from the system.

**RD RESPONSE:** Presently, the Information Resources Manager (IRM) receives monthly reports from the St. Louis Security Staff to verify FH ID's and FOCUS ID's. The IRM verifies the accuracy, signs, dates and returns the report to the Security Staff. When an employee leaves the Agency, the IRM continues to receive Form AD-139 from Human Resources, and deletes the appropriate ID's and other accesses. The IRM has initiated an additional monthly review of IDMS

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Rural Housing  
Service

Rural Business-Cooperative  
Service

Rural Utilities  
Service

USDA Rural Development is an Equal Opportunity Lender, Provider, and Employer. Complaints of discrimination should be sent to:  
USDA, Office of Civil Rights, Washington, DC 20250-9410.

**ID's and NFC User ID's. Monthly, she runs a User ID report from FOCUS, verifies the accuracy and files for reference.**

**A group of Administrative Staff responsible for Human Resources, Contracting/Procurement, Budget, Travel, Information Resources, Property management and Management Controls, met and revised the process for ensuring all appropriate items are collected and destroyed (ID cards, credit cards, accountable property, etc.), and all ID's and accesses have been deleted. A State procedure or management letter will be issued by July 30, 2002, which will ensure that these controls are identified in writing.**

Recommendation No. 5 - Perform the compliance review on the Northeastern Schuylkill Joint Municipal Authority project. This review should be performed immediately and forwarded to the State office.

**RD RESPONSE: The RUS Program Director reviewed the information contained in the Finding No. 3 paragraph. The following changes should be made:**

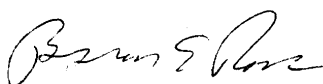
- The file reviewed was a loan and grant; therefore, the first sentence should read, "... the required civil rights compliance review on a loan **and grant** totaling \$9,611,800 ...".
- RD no longer has "county" offices; therefore, the second sentence in the second paragraph should read, "... State Director and a copy filed in the borrower's **area** office docket."

**This loan was closed in June 2001. The compliance review was completed on November 6, 2001 as noted in the draft report. This office has been advised of the need to complete the compliance reviews at the proper time as required by the regulations.**

Exhibit A - Summary of Monetary Results, Finding No. 1 - Amount \$39,249 for personal property not accounted for in PROP.

**RD RESPOSE: We agree with the findings and monetary amount. The items will be placed on the PROP report as required.**

If you have any questions, please contact Trudy S. Moore, Management Control Officer, at (717) 237-2266.



BYRON E. ROSS  
State Director

cc: Financial Management Division, Rural Development  
Management Control Officer, Rural Development, Pennsylvania  
Administrative Management Program Director, Rural Development, Pennsylvania  
RUS Program Director, Rural Development, Pennsylvania