TERMINAL SERVICE
COST ACCOUNTING PRACTICES

Federal Aviation Administration

Report Number: FI-2003-013
Date Issued: January 21, 2003

Memorandum

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

Subject:	ACTION: Report on Terminal Service Cost Accounting Practices, FAA FI-2003-013	Date:	January 21, 2003
From:	Alexis M. Stefani Principal Assistant Inspector General for Auditing and Evaluation	Reply to Attn. of:	Meche: x61496
To:	Federal Aviation Administrator		

This report is one in a series on implementation of the Federal Aviation Administration (FAA) cost accounting system. This report presents our audit results on cost accounting practices being implemented for the Terminal Service, a service within Air Traffic Services, which is one of five FAA lines of business. FAA's Terminal Service provides air traffic control services to aircraft arriving at and departing from airport facilities. As required by the Wendell H. Ford Aviation Investment and Reform Act for the 21st Century (AIR-21), we will be issuing a summary report in the near future assessing FAA's overall efforts in developing and implementing its cost accounting system.

INTRODUCTION

Terminal Service facilities include airport air traffic control towers, terminal radar approach control centers, and other types of facilities. FAA has 291 terminal and tower facilities, 194 contract towers where air traffic services are performed by private companies, and 1,118 terminal facilities without air traffic control services, such as radars and unmanned control facilities.

An effective cost accounting system is fundamental to measuring the cost of FAA activities and provides the basis for setting benchmarks and measuring performance. It represents the underpinning for FAA's operation as a performance-based organization through the development of good cost information for effective decisionmaking. FAA has spent about $38 million over the last 7 years developing its cost accounting system. Producing and reporting accurate and reliable cost accounting information and using the information for cost and performance management has been a difficult challenge for FAA.

The new FAA Administrator has a significant opportunity to overcome these difficulties and implement an effective cost accounting system. Having good cost information is more important now that FAA is facing critical issues involving increasing capacity in the National Airspace System, carrying out cost-effective and timely acquisitions, and improving business operations by controlling costs. In essence, FAA needs to act more like a business, particularly in view of the steep declines in projected Aviation Trust Fund revenues.

Our audit objectives were to evaluate the appropriateness of cost accounting practices used for the assignment and allocation of costs to, and within, the Terminal Service, and to ensure that costs were accurately reported in the cost accounting system in accordance with applicable Federal accounting standards.

RESULTS IN BRIEF

FAA reported that implementation of its cost accounting system for the Terminal Service was completed in Fiscal Year (FY) 2001. To determine the adequacy of the cost accounting practices for the Terminal Service, we analyzed the FY 2001 costs because FAA would not report its final FY 2002 costs until calendar year 2003. We verified that costs reported in the FAA cost accounting system were the same as reported in the Department's financial accounting system. However, we identified significant deficiencies with the cost accounting practices for the Terminal Service. We found that FAA did not (1) report costs for each facility location, (2) use appropriate cost assignment methods, and (3) allocate overhead costs properly. Specifically,

- FAA reported $2.4 billion of costs for the Terminal Service in FY 2001; however, about $1.3 billion was reported in lump-sum totals and not by individual facility as required. FAA cannot effectively manage its Terminal Service unless it knows the cost to operate individual facilities.

- FAA distributed $203 million in costs, such as equipment acquisition cost, to the Terminal Service using cost assignment methods that are not in accordance with Federal accounting standards. Because FAA used inappropriate methods to assign cost, it could not determine if the assigned amounts were accurate. FAA needs to improve its source data collection methods and develop processes for assigning each activity's cost to individual facility locations to determine the actual cost of each facility.

- FAA used an inappropriate method to assign FY 2001 overhead costs to the Terminal Service. FAA used total employee labor cost as its basis to assign overhead costs instead of the total cost of Air Traffic Services. If FAA had used total cost, it would have assigned about $38 million more overhead costs to the Terminal Service.

Air Traffic Services has facilities located throughout the United States and spends about $7 billion for operating costs. However, FAA cannot effectively manage such large operations unless it knows the actual cost of its activities and services by location. A credible cost accounting system should track the cost of specific activities and services so managers can make informed decisions, identify best practices, set benchmarks, eliminate inefficiencies, and maximize efficiency.

To improve FAA's cost accounting system for its Terminal Service, we recommended that FAA distribute its costs to each terminal facility location, establish cost assignment bases that allocate costs using methods required by Federal accounting standards, and allocate overhead cost pools using a total cost basis. FAA concurred with our recommendation to allocate costs using methods required by Federal accounting standards, and partially concurred with our recommendations to distribute costs to each terminal location and to allocate overhead costs. FAA estimates it will have the necessary accounting systems and financial data to properly allocate and report its cost by September 30, 2004.

In its response to our draft report, FAA stated that it does not believe that the nature of our audit results can substantiate the classification as "significant deficiencies," and our reporting could falsely suggest that the cost accounting system does not produce credible data. In a separate action, FAA's Air Traffic Service recently decided to eliminate essential internal controls and requirements to report time by specific activity from its Cru-X labor distribution system used to track labor costs of about 8,700 air traffic controllers working in the Terminal Service. When we brought this to her attention, the new FAA Administrator directed that appropriate internal controls for recording time be incorporated into the Cru-X system. FAA needs to identify specific action plans to implement the Administrator's direction and provide milestones for starting and completing its corrective actions.

The FAA cost accounting system reported $1.3 of $2.4 billion of Terminal Service costs as lump-sum totals rather than by individual facilities, did not allocate costs on appropriate bases, and used outdated FY 1999 and FY 2000 appropriation and budget data to compute FY 2001 costs. In our view, not assigning and reporting actual and current costs by facility represents a significant deficiency and impacts the credibility of the reported data.

Over the years, FAA's efforts have reflected the lack of sufficient management commitment to design and build a credible cost accounting system, as evidenced by its continuing to push significant milestones further into the future for implementing a fully compliant cost accounting system. We are requesting that FAA reconsider its action plans and its implementation schedule.

In our view, FAA's response is symbolic of much larger issues. FAA will need credible cost accounting and labor distribution systems to effectively operate as a performance-based organization. Shortly, we will address these overall issues in a separate report to the new FAA Administrator and Congress as part of our annual assessment of FAA's cost accounting system and practices.

BACKGROUND

The Federal Aviation Reauthorization Act of 1996 (Act) requires FAA to develop a cost accounting system that accurately reflects the asset values, operating and overhead cost, and other financial measurement and reporting aspects of its operations. The Statement of Federal Financial Accounting Standards (SFFAS) Number 4, Managerial Cost Accounting Standards, also requires that Federal entities establish managerial cost accounting practices, effective October 1, 1997.

The Federal Accounting Standards Advisory Board developed managerial cost accounting standards for the Federal Government. These standards are basically the same as used by private industry businesses for (1) setting budgets for services; (2) establishing cost targets for controlling cost and measuring performance; (3) computing cost targets for controlling cost and programs; (4) evaluating programs; and (5) making business decisions. Congress and Federal executives need accurate cost information on agencies' programs and services to make decisions and allocate resources. Accurate cost accounting data also alert Government managers to potential waste and inefficiency.

During FY 1997, FAA purchased commercial off-the-shelf software to design and implement a cost accounting system in its individual lines of business. FAA is designing its cost accounting system in phases. The cost accounting system was originally scheduled to be implemented in October 1998 but now the schedule for full implementation in all lines of business is September 2003.

The Wendell H. Ford Aviation Investment and Reform Act for the 21st Century (AIR-21) requires that the Department of Transportation (DOT) Office of Inspector General (OIG) perform an independent assessment of the adequacy and accuracy of FAA's cost data and cost allocations. In conducting the assessment, the OIG is to assess the reliability of source documents and the data collection process; the system for tracking assets; the basis for establishing asset values and depreciation rates; the indirect cost pools and allocation bases; and the progress FAA is making in cost and performance management. AIR-21 also requires OIG to submit a report to Congress no later than December 31, 2000, and every year thereafter through 2004. Our audit work on the Terminal Service cost accounting practices will be used to satisfy some OIG reporting requirements under AIR-21.

RESULTS

FAA did not report costs for all Terminal Service locations, use appropriate cost assignment methods, and allocate its overhead costs properly. The details of our results follow.

Costs Not Reported for Facility Locations

FAA reported $2.4 billion of costs for the Terminal Service in FY 2001. However, about $1.3 billion of those costs were reported as lump-sum totals, not by individual facility location as shown in Table 1.

Table 1
Costs Not Reported for Individual Facility Locations or Activities

Type of Activity or Cost	Number of Facilities	Facilities Not Reporting Cost Individually	Cost Not Individually Reported	Percentage of the Total Terminal Service Cost
FAA Air Traffic Control Terminals	291	240	$824 million*	34
Contract Towers	194	194	$127 million	5
Non-controlled locations (no air traffic control)	1,118	1,118	$ 94 million	4
Equipment implementation	1,603	1,552	$115 million	5
Post-retirement employee benefits	1,603	1,552	$107 million	4
Depreciation	1,603	1,552	$ 56 million	2
Flight inspection	1,603	1,552	$ 15 million	1
Total	**-**	**-**	**$1.3 billion**	**55**

*FAA's system collects the cost by site, but does not report it by terminal facility.

Federal accounting standards require that FAA define and establish areas of responsibility where managerial cost accounting can be performed. FAA has identified its Terminal Service facility locations as areas of responsibility. To effectively manage the Terminal Service, FAA needs to collect and report cost by facility location to the greatest extent practical.

Specific cost information for each facility location is necessary for managers to compare performance among Terminal Service locations. After several years of developing its cost accounting system, FAA still is not reporting about $1.3 billion of Terminal Service costs to its individual facilities. A credible cost accounting system should track the cost of specific activities and report the costs by facility location so managers can identify best practices, set benchmarks at facilities, and make informed business decisions.

Inappropriate Cost Assignment Methods

FAA did not appropriately assign $203 million of FY 2001 costs in accordance with Federal accounting standards. As a result, FAA could not accurately determine the Terminal Service's appropriate share of the costs. FAA assigned the $203 million of costs using appropriation and budgetary data rather than by using an acceptable method of cost assignment, as shown in Table 2.

Table 2
Inappropriate Cost Assignment Methods Used

Activity	Basis Used	Amount
Equipment Acquisition	Funding/Obligations/Budgetary	$ 66 million
Research, Engineering, and Development	Appropriation Funding	$ 22 million
Gains and Losses	Direct Labor and Benefits Cost	$ 75 million
Environmental Liability	Funding Amounts	$ 40 million
Total	**-**	**$203 million**

FAA needs to develop proper methods for assigning each activity's cost to facility locations. In accordance with SFFAS Number 4, costs should be assigned through the tracing of costs to activities or services, assignment of costs on a basis that reflects the reason for the cost, or allocation of costs on a reasonable and consistent basis according to Federal accounting standards. Appropriation and budgetary data are not adequate allocation bases because they are estimates and forecasts, not actual costs. Using budget data to allocate costs prevents managers from making essential comparisons of variances between budgets and actual costs and making improvements in operations. FAA needs to develop better source data collection methods to trace costs to activities or services, or develop an adequate allocation basis that reflects the reason for the cost.

Overhead Costs Not Properly Allocated

FAA used an allocation base of direct labor and benefits cost that is not appropriate to allocate the administrative overhead cost pools to the Terminal Service. Although we found that the Air Traffic Services headquarters, the Air Traffic Operations, and the Airway Facilities Operations overhead pools had properly collected general and administrative costs in compliance with Federal accounting standards, FAA did not properly allocate these costs. Federal accounting standards require that overhead costs be allocated using an appropriate allocation base to ensure that costs are distributed properly.

In our opinion, the appropriate allocation base should be total cost because it better represents the activity of the Terminal Service. For example, using a total cost basis, FAA would have allocated about $232 million of overhead cost to the Terminal Service, or $38 million more than by using the direct labor and benefit cost basis. The direct labor and benefits cost basis understates the actual cost the Terminal Service should receive based on its activities.

RECOMMENDATIONS

We recommend that FAA:

1. Distribute costs to each Terminal Service facility location and report the results to FAA management.

2. Change the cost accounting system to assign costs using an acceptable method as required by Federal accounting standards.

3. Allocate the Air Traffic Services headquarters, Air Traffic Operations, and Airway Facilities Operations administrative overhead cost pools using a total cost basis.

MANAGEMENT COMMENTS AND OIG RESPONSE

A draft of this report was provided to the FAA Administrator on November 14, 2002. FAA concurred or partially concurred with each of our recommendations. FAA's comments and our response follow.

FAA General Comment: FAA does not believe that the nature of the audit results can substantiate the classification as "significant deficiencies." In addition, reporting that the system has "significant deficiencies" could falsely suggest that the cost accounting system does not produce credible data.

OIG Response: We disagree with FAA. The FAA cost accounting system reported $1.3 of $2.4 billion of costs as lump-sum totals rather than by individual facilities, did not allocate costs on appropriate bases, and used outdated FY 1999 and FY 2000 appropriation and budget data to compute FY 2001 costs. In our view, not assigning and reporting actual and current costs by facility represents a significant deficiency and impacts the credibility of the reported data.

Recommendation 1: FAA partially concurred. FAA currently distributes costs to all FAA-staffed terminal facilities. Air Traffic Services (ATS) elected to initially produce and distribute monthly cost reports for only the top 50 airports and a few lower level facilities. FAA is currently in the process of implementing a new reporting tool, the Report, Analysis and Distribution System (RADS), which will provide ATS with access to reports for all FAA-staffed Terminal facilities.

FAA also is in the process of replacing the Departmental Accounting and Financial Information System (DAFIS) with a new financial accounting system, Delphi, which should increase the level of detail associated with financial transactions. RADS also should enable ATS to readily obtain costs for any FAA-staffed Terminal facility.

FAA will perform a study of any remaining service level costs to determine the most logical, relevant and suitable cost assignment method and basis for reporting the costs. FAA plans to complete the study by the end of FY 2003 and will provide implementation dates by December 31, 2003.

OIG Response: Actions planned by FAA should improve the cost accounting system and data. However, these improvements are limited to FAA staffed facilities. FAA's reporting system must include the costs for all Terminal Service facilities by location, including individual contract towers and facilities that do not have air traffic control services, such as radars and unmanned control facilities.

We agree that Delphi should provide better detail for financial transactions. However, FAA needs to ensure that Delphi is properly programmed to collect the necessary level of detail so the cost accounting system can electronically retrieve the data and allocate the cost in accordance with Federal accounting standards. Consistent with proper implementation of Delphi, FAA also needs to ensure that the Cru-X labor distribution system is developed with adequate internal controls and time reporting categories so that FAA can use it to manage and allocate its air traffic controller resources in an efficient and effective manner.

Recommendation 2: FAA concurred. FAA stated it used the best available information as the bases for allocating costs to ATS services for cost accounting implementation in the ATS Terminal Service and used a method in accordance with Federal accounting standards. FAA used budgetary data because no other data had a direct relationship with the cost pool and the data were available at the necessary level of detail. After FAA implements Delphi, the cost accounting system will be able to trace most costs directly to Terminal facilities. FAA will review its current business processes, and where possible, develop or use more reasonable data as bases when using the cost allocation method. FAA will provide implementation dates by December 31, 2003.

OIG Response: Although FAA concurred with the recommendation, we do not agree that it used the best available information nor did it use a method in accordance with Federal accounting standards. FAA used FY 1999 and FY 2000 appropriation and budgetary data to compute the Terminal Service's FY 2001 costs. Not only did FAA use outdated information, but appropriation and budgetary data are not reasonable allocation bases because they are estimates and forecasts, not actual costs. FAA's plan to review its business processes and to develop methods for accurate assignment of costs is appropriate.

Recommendation 3: FAA partially concurred. FAA excluded certain cost elements, such as equipment acquisition cost, from the total cost allocation basis used to allocate overhead cost to the Terminal Service. Using this method, FAA would have assigned $33 million more in overhead costs to the Terminal Service rather than the $38 million reflected in the draft report. According to FAA, the use of total cost basis versus personnel costs and benefits merely shifts the amount of overhead costs between ATS services. The total cost basis reduces overhead cost allocated to Enroute and Flight Service Station services and increases the amount assigned to Terminal services.

FAA believes that personnel costs and benefits represent a more consistent basis for monthly ATS overhead allocations. FAA plans to wait until it implements Delphi to make any changes to the ATS overhead allocation basis. FAA plans to conduct analyses and implement appropriate changes by September 30, 2004.

OIG Response: In our opinion, all cost elements of Terminal Service facilities, such as equipment acquisition costs, should be included in the total cost allocation basis because these are costs of FAA operations. In addition, last year, in response to a similar recommendation concerning flight service stations, FAA agreed that by March 2002 it would analyze each FAA Headquarters administrative overhead cost pool and determine the most appropriate base to use in allocating overhead cost to lines of business. This did not happen. Now, FAA plans to analyze its costs to determine the overall impact of converting from a personnel cost and benefits base to a total cost base by September 30, 2004, or about 2½ years after its original estimated completion date.

Rather than fix the previously identified deficiencies, FAA continues to push significant milestones further into the future for implementing a fully compliant cost accounting system. FAA should complete its analysis before September 2004 to ensure the proper allocation of overhead costs among the Air Traffic Services.

ACTION REQUIRED

In accordance with DOT Order 8000.1C, we are requesting that FAA reconsider its position and provide, within 30 days, specific action plans and estimated completion dates to address our recommendations and the implementation schedule for the cost accounting system. The complete text of management comments is in the Appendix.

We appreciate the courtesies and cooperation of FAA representatives. If we can answer any questions, please call me at (202) 366-1992 or John Meche at (202) 366-1496.

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EXHIBIT A. SCOPE AND METHODOLOGY

We evaluated the reasonableness of the Terminal Service's cost accounting practices for the assignment and allocation of cost. We evaluated and performed detailed tests of the accuracy and validity of the allocations, and determined whether costs were accurately reported for the Terminal Service in the cost accounting system in accordance with Federal accounting standards. We also verified that the costs in the Air Traffic Operations overhead cost pool reported in the cost accounting system were the same as reported in the Department's financial accounting system.

We evaluated the allocations of Terminal Service costs totaling $2.4 billion for FY 2001. The analyses we performed of internal controls provided an understanding of the design of the internal controls, whether the internal controls had been placed in operation, and whether they were sufficient to assess the control risk associated with the Terminal Service portion of the cost accounting system.

The scope of our examination reflects our assessment of control risk and includes tests of compliance with applicable laws and regulations. Our assessment of control risk reflects that we have not specifically examined all internal controls that may be applicable to FAA's cost accounting system because the system still is under development.

Our audit work on the Terminal Service's cost accounting practices was not an audit of FAA's compliance with the overflight fee statute. Therefore, our audit results should not be used as a basis to evaluate FAA's overflight fees.

We performed our audit from April through October 2002 at FAA headquarters in Washington, D.C. The audit was conducted in accordance with Government Auditing Standards prescribed by the Comptroller General of the United States.

EXHIBIT B. MAJOR CONTRIBUTORS TO THIS REPORT

THE FOLLOWING INDIVIDUALS CONTRIBUTED TO THIS REPORT.

Name	Title
Keith Cosper	Program Director
Paul Barry	Project Manager
Michael Veverka	Senior Auditor

APPENDIX. MANAGEMENT COMMENTS

U.S. Department
of Transportation
Federal Aviation
Administration

Memorandum

Subject: **ACTION:** Draft Report on Terminal Service Cost Accounting Practices, FAA

Date: December 4, 2002

From: Assistant Administrator for Financial Services and Chief Financial Officer

Reply to
Attn. of:

To: Assistant Inspector General for Financial and Information Technology Audits

We have attached to this memorandum our response to the subject Draft Audit Report. We concurred or partially concurred with all findings and recommendations, and indicated the specific actions that we plan to take for each recommendation and target dates for completion.

You requested that we comment on the reasonableness of the $38 million related to the appropriate allocation of Air Traffic Service administrative overhead. We do not agree with all cost elements that you included in the total cost basis used for the allocation of the ATS overhead costs. Specifically we believe that the acquisition costs, gains and losses, imputed post retirements benefits, change in environmental liabilities and change in FECA actuarial liability should be excluded from the total cost basis. Based on our computation, the use of total cost basis versus personnel costs and benefits will result in an increase of $33 million of fiscal year 2001 Terminal service overhead costs.

We appreciate the courtesy and professionalism of your audit staff. If you have any questions, please call Ray Morris at (202) 267-7580.

Chris Bertram

Attachment

FAA RESPONSE TO OFFICE OF INSPECTOR GENERAL (OIG) DRAFT REPORT
TERMINAL SERVICE COST ACCOUNTING PRACTICES
PROJECT NO. 02F3001F000

November 29, 2002

General Comments. We generally concur with the OIG recommendations on Terminal Service Cost Accounting Practices. However, we believe the following changes to the Draft Report will provide a fairer representation of the Terminal services cost accounting practices.

Specific Comments. Our specific comments follow:

Page 1, Results in Brief section, first paragraph, fourth sentence:

OIG Draft Report: "However, we identified significant deficiencies with the cost accounting practices for the Terminal Service."

FAA Comment: The FAA does not believe that the nature of the audit results documented in this report can substantiate their classification as "significant deficiencies." Our responses to the OIG recommendations will support our position. In addition, reporting that the system has "significant deficiencies" could falsely suggest that the CAS does not produce credible data. Therefore, we recommend the removal of the word "significant" from the audit report.

Page 2, Results in Brief section, second bullet, first sentence:

OIG Draft Report: "FAA distributed $203 million in costs, such as equipment acquisition cost, to the Terminal service using cost assignment methods that are not in accordance with Federal Accounting Standards."

FAA Comment: FAA used "allocation on a reasonable and consistent basis" as the method to assign selected ATS costs to the Terminal service. This method is in accordance with Federal Accounting Standards. The report confused the allocation method with the basis for making the allocations. While the report took issue with the method, in fact the OIG questioned the appropriateness of the basis used to make allocations. In determining the basis, the FAA used the best data available. We believe that the OIG should eliminate the reference to "not in accordance with Federal Accounting Standards." The report should state, "For distribution of $203 million in costs, such as equipment acquisition cost, to the Terminal service, FAA did not use the most relevant bases."

Page 2, Results in Brief section, third bullet, first two sentences:

OIG Draft Report: "FAA used an inappropriate method to assign FY 2001 overhead costs to the Terminal Service. FAA used total employee labor cost as its basis to assign overhead costs instead of total cost of Air Traffic Services."

FAA Comment: FAA believes that using labor versus total costs, as the basis to allocate the ATS overhead costs to ATS services is an appropriate method. Again, the report confused the allocation method with the basis for making the allocations. While the report took issue with the method, in fact the OIG questioned the appropriateness of the basis used to make allocations. We recommend the removal of the first sentence and the revision of this section as follows: "To assign the FY 2001 overhead costs to the Terminal Service, FAA used total employee labor cost as its basis to assign overhead costs instead of total cost of Air Traffic Services."

OIG Recommendations.

OIG Recommendation: Distribute costs to each Terminal Service facility location and report the results to FAA management.

FAA Response: Partially Concur.

Air Traffic Control (ATC) Terminals. FAA currently distributes costs to all FAA-staffed terminal facilities. In accordance with ATS management direction, ATS elected to initially produce and distribute monthly cost reports for only the top 50 airports and a few lower level facilities (for system validation purposes only). Please note that a quick ad-hoc query can provide cost data for any FAA-staffed Terminal facility. FAA is currently, in the process of implementing a new reporting tool. This tool is the Report, Analysis and Distribution System (RADS). ATS will soon have FAA-wide access to RADS. This will eliminate the need for specific query requests, and will provide ATS with access to monthly reports for all FAA-staffed Terminal facilities. The finding on ATC Terminals represents $824 million (63 percent) of the $1.3 billion that the OIG categorized as costs not individually reported.

Contract Towers. The contract tower program manager uses contractual data to centrally manage contract tower costs. The financial system records these costs at an aggregate level. However, the CAS provides additional level of details and distributes costs to contract towers at the regional level. The finding on contract towers represents $127million (9 percent) of the $1.3 billion that the OIG categorized as costs not individually reported.

Non-controlled locations. At non-towered locations (without FAA paid controllers) FAA maintains equipment. The standard ATS cost reports aggregate all costs related to equipment maintenance at non-towered locations into one SDP. However, ATS management is interested in the cost to maintain equipment at each site. The "site" data element is associated with all transactions and as a result the cost to maintain individual systems is available in a site report. The finding on non-controlled locations represents

$94 million (7 percent) of the $1.3 billion that the OIG categorized as costs not individually reported.

Other. FAA distributes some costs at the service level only. These cost include those that do not have enough detail to permit their assignment to SDPs; and those that ATS decided to report at the service level because of the nature of the cost. The finding on other costs represents $293 million (approximately 22 percent) of the $1.3 billion that the OIG categorized as costs not individually reported.

FAA is in the process of replacing the Departmental Accounting and Financial Information System (DAFIS) with a new financial system, DELPHI. DELPHI will increase the level of detail associated with financial transactions. Users will be able to directly assign most costs to SDPs. Further, as indicated above, RADS will enable ATS to readily obtain costs for any FAA-staffed Terminal facility. In addition, FAA will perform a study of any remaining service level costs to determine the most logical, relevant and suitable cost assignment method and basis for reporting the costs at the SDP level.

We plan to complete the study by the end of Fiscal Year (FY) 2003 and implement appropriate changes at a later date. We will schedule the implementation dates based on the results of the study, and provide them to the OIG by December 31, 2003.

OIG Recommendation: Change the cost accounting system to assign costs using an acceptable method as required by Federal accounting standards.

FAA Response: Concur. FAA used the best available information as the bases for allocating costs to ATS services for cost accounting implementation in the ATS Terminal Service. FAA used budgetary data as the basis for allocating $128 million (63 percent) of the $203 million that the OIG identified as not appropriately assigned. No other data had a direct relationship with the cost pool and was available at the necessary level of detail. For the remaining amount of $75 million (37percent) representing gains and losses, FAA used personnel costs and benefits as the allocation basis. We believe that after the FAA implements DELPHI, the CAS will be able to trace most costs directly to Terminal facilities. In addition, FAA will review its current business processes, and where possible develop and/or use more reasonable data as bases when using the cost allocation method.

We plan to complete the review by the end of Fiscal Year (FY) 2003 and implement appropriate changes at a later date. We will schedule the implementation dates based on the results of the study, and provide them to the OIG by December 31, 2003.

OIG Recommendation: Allocate the Air Traffic Service headquarters, Air Traffic Operations, and Airway Facilities Operations administrative overhead cost pools using a total cost basis.

FAA Response: Partially Concur. The use of total cost basis versus personnel costs and benefits merely shifts the amount of overhead costs between ATS services. The total cost basis reduces overhead cost allocated to Enroute and Flight Service Station services and increases the amount assigned to Terminal services. FAA processes various year-end adjusting entries that affect the expense and property, plant and equipment accounts. Therefore, we believe that PC&B represents a more consistent basis for ATS overhead allocation in producing monthly ATS cost reports. Since DELPHI, will require routine posting of capitalized costs, we plan to wait until FAA implements DELPHI to make any changes to the ATS overhead allocation basis. Once we have DELPHI data for a complete year, including year-end adjustments, we will analyze the overall impact of converting from a PC&B basis to a total cost basis and make changes as warranted.

We plan to implement appropriate changes by the end of FY 2004.