

# Section V

Report of the Office of Inspector General





## V. Report of the Office of Inspector General



U.S. Department of Agriculture

Office of Inspector General  
Financial & IT Operations

### Audit Report

#### U.S. Department of Agriculture's Consolidated Financial Statements for Fiscal Years 2005 and 2004

Report No. 50401-56-FM  
November 2005



UNITED STATES DEPARTMENT OF AGRICULTURE  
OFFICE OF INSPECTOR GENERAL  
Washington, D.C. 20250




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REPLY TO  
ATTN OF: 50401-56-FM

TO: Patricia E. Healy  
Acting Chief Financial Officer  
Office of the Chief Financial Officer

ATTN: Kathy Donaldson  
Senior Program Analyst  
Office of the Chief Financial Officer  
Planning and Accountability Division

FROM: Phyllis K. Fong   
Inspector General

SUBJECT: U.S. Department of Agriculture's Consolidated Financial Statements for  
Fiscal Years 2005 and 2004

This report presents the results of our audit of the U.S. Department of Agriculture's consolidated financial statements for the fiscal years ending September 30, 2005 and 2004. The report contains an unqualified opinion and the results of our assessment of the Department's internal control structure and compliance with laws and regulations.

In accordance with Departmental Regulation 1720-1, please furnish a reply within 60 days describing the corrective action taken or planned, including the timeframes, on our recommendations. Please note that the regulation requires a management decision to be reached on all findings and recommendations within a maximum of 6 months from report issuance.

We appreciate the courtesies and cooperation extended to us during the audit.

## ***Executive Summary***

***U.S. Department of Agriculture's Consolidated Financial Statements for Fiscal Years 2005 and 2004 (Audit Report No. 50401-56-FM)***

### **Purpose**

Our audit objectives were to determine whether (1) the consolidated financial statements present fairly, in all material respects, in accordance with generally accepted accounting principles, the assets, liabilities, and net position, net costs, changes in net position, budgetary resources, and reconciliation of net costs to budgetary obligations; (2) the internal control objectives were met; (3) the Department complied with laws and regulations for those transactions and events that could have a material effect on the consolidated financial statements; and (4) the information in the Performance and Accountability Report was materially consistent with the information in the consolidated financial statements.

We conducted our audit at the financial offices of various U.S. Department of Agriculture (USDA) agencies and the Office of the Chief Financial Officer (OCFO) located in Washington, D.C., and its National Finance Center located in New Orleans, Louisiana. We also performed site visits to selected agencies' field offices.

### **Results in Brief**

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of USDA as of September 30, 2005 and 2004; and its net costs, changes in net position, reconciliation of net costs to budgetary obligations, and budgetary resources for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

We have also issued reports on our consideration of USDA's internal control over financial reporting and its compliance with certain provisions of laws and regulations.

For internal controls over financial reporting, we identified three reportable conditions.

- Improvements needed in overall financial management across USDA,
- improvements needed in information technology security and controls, and
- improvements needed in certain financial management practices and processes.

We believe the first two conditions are material weaknesses. Our report on compliance with laws and regulations discusses two instances of noncompliance relating to the Federal Financial Management Improvement Act and the Anti-Deficiency Act.

**Key Recommendations** OCFO has immediate and long term plans to address most of the weaknesses in its financial management systems. The key recommendations in this report were limited to additional improvements in financial management.

***Abbreviations Used in This Report***

C&A	Certification and Accreditation
CCC	Commodity Credit Corporation
CFO	Chief Financial Officer
FACETS	Federal Agencies' Centralized Trial Balance System
FFIS	Foundation Financial Information System
FFMIA	Federal Financial Management Improvement Act
FFMSR	Federal Financial Management Systems Requirements
FISMA	Federal Information Security Management Act
FS	Forest Service
FSA	Farm Service Agency
GAO	U.S. Government Accountability Office
IT	Information Technology
ITS	Information Technology Services
JFMIP	Joint Financial Management Improvement Program
NIST	National Institute of Standards and Technology
OCFO	Office of the Chief Financial Officer
OCIO	Office of the Chief Information Officer
OIG	Office of the Inspector General
OMB	Office of Management and Budget
RSSI	Required Supplemental Stewardship Information
SFFAS	Statement of Federal Financial Accounting Standard
SOF	Statement of Financing
SV	Standard Voucher
USDA	U.S. Department of Agriculture

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UNITED STATES DEPARTMENT OF AGRICULTURE  
OFFICE OF INSPECTOR GENERAL  
Washington, D.C. 20250



## *Report of the Office of Inspector General*

To: Patricia E. Healy  
Acting Chief Financial Officer  
Office of the Chief Financial Officer

We have audited the accompanying consolidated balance sheets of the U.S. Department of Agriculture (USDA) as of September 30, 2005 and 2004, and the related consolidated statements of net cost, changes in net position, and financing, and the combined statements of budgetary resources (hereinafter referred to as the "consolidated financial statements") for the fiscal years then ended. The consolidated financial statements are the responsibility of USDA's management. Our responsibility is to express an opinion on the consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 01-02, "Audit Requirements for Federal Financial Statements." Those standards and OMB Bulletin No. 01-02 require that we plan and perform the audits to obtain reasonable assurance that the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the USDA as of September 30, 2005 and 2004; and its net costs, changes in net position, reconciliation of net costs to budgetary obligations, and budgetary resources for the years then ended, in conformity with accounting principles generally accepted in the United States of America..

The information in the Performance and Accountability Report (see exhibit B) is not a required part of the consolidated financial statements, but is supplemental information required by accounting principles generally accepted in the United States of America or by OMB Circular No. A-136, "Financial Reporting Requirements." We attempted to apply certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of this information. However, the Department did not provide its final analysis in time for

us to complete our review. Therefore, we can provide no assurance on the reliability of the information. In addition, we did not audit this information and, accordingly, we express no opinion on it.

We have also issued reports on our consideration of USDA's internal control over financial reporting and its compliance with certain provisions of laws and regulations. These reports are an integral part of an audit performed in accordance with Government Auditing Standards, and, in considering the results of the audit, should be read in conjunction with this report. For internal controls over financial reporting, we identified three reportable conditions.

- Improvements needed in overall financial management across USDA,
- improvements needed in information technology security and controls, and
- improvements needed in certain financial management practices and processes.

We believe the first two conditions are material weaknesses. Our report on compliance with laws and regulations discusses two instances of noncompliance relating to the Federal Financial Management Improvement Act and the Anti-Deficiency Act.

This report is intended solely for the information of the management of USDA, OMB, and Congress, and is not intended to be and should not be used by anyone other than these specified parties.



Phyllis K. Fong  
Inspector General

November 10, 2005



UNITED STATES DEPARTMENT OF AGRICULTURE  
OFFICE OF INSPECTOR GENERAL  
Washington, D.C. 20250



## ***Report of the Office of Inspector General on Internal Control Over Financial Reporting***

To: Patricia E. Healy  
Acting Chief Financial Officer  
Office of the Chief Financial Officer

We have audited the accompanying consolidated balance sheets of the U.S. Department of Agriculture (USDA) as of September 30, 2005 and 2004, and the related consolidated statements of net cost, changes in net position, and financing, and the combined statements of budgetary resources (hereinafter referred to as the "consolidated financial statements"), and have issued our report thereon dated November 10, 2005. We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 01-02, "Audit Requirements for Federal Financial Statements."

In planning and performing our audits, we considered USDA's internal control over financial reporting by obtaining an understanding of the internal controls, determining whether the internal controls had been placed in operation, assessing control risk, and performing tests of controls in order to determine our auditing procedures for the purpose of expressing our opinion on the consolidated financial statements. We limited our internal control testing to those controls necessary to achieve the objectives described in OMB Bulletin No. 01-02 and Government Auditing Standards. We did not test all internal controls as defined by the Federal Managers' Financial Integrity Act of 1982. The objective of our audit was not to provide assurance on USDA's internal control. Consequently, we do not provide an opinion on internal control over financial reporting.

Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be reportable conditions. Under standards issued by the American Institute of Certified Public Accountants, reportable conditions are matters coming to our attention relating to significant deficiencies in the design or operation that, in our judgment, could adversely affect the agency's ability to record, process, summarize, and report financial data consistent with the assertions by management in the consolidated financial statements. Material weaknesses are reportable conditions in which the design or operation of one or more internal control components do not reduce to a relatively low level the risk that misstatements, in amounts that would be material in relation to the consolidated 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. Because of inherent limitations in any internal control, misstatements due to error or fraud may occur and not be detected.

We noted certain matters described in the “Findings and Recommendations” involving the internal control over financial reporting and its operation that we consider to be reportable conditions.

- Improvements needed in overall financial management across USDA (Section 1),
- improvements needed in information technology security and controls (Section 1), and
- improvement needed in certain financial management processes and practices (Section 2).

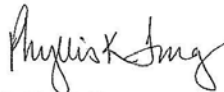
We believe that the first two conditions are material weaknesses.

#### **Additional Other Procedures**

As required by OMB Bulletin No. 01-02, we considered USDA’s internal controls over Required Supplemental Stewardship Information (RSSI) by obtaining an understanding of the internal controls, determining whether these internal controls had been placed in operation, assessing control risk, and performing tests of controls. Our procedures were not designed to provide assurance on internal controls over such RSSI; accordingly, we do not provide an opinion on such controls.

As further required by OMB Bulletin No. 01-02, with respect to internal control related to performance measures determined by management to be key and reported in the Management’s Discussion and Analysis section of the Performance and Accountability Report, we obtained an understanding of the design of significant internal controls relating to the existence and completeness assertions. Our procedures were not designed to provide assurance on internal control over reported performance measures; accordingly, we do not provide an opinion on such controls.

This report is intended solely for the information and use of the management of USDA, OMB, and Congress, and is not intended to be and should not be used by anyone other than these specified parties.



Phyllis K. Fong  
Inspector General

November 10, 2005



UNITED STATES DEPARTMENT OF AGRICULTURE  
OFFICE OF INSPECTOR GENERAL  
Washington, D.C. 20250



## ***Report of the Office of Inspector General on Compliance with Laws and Regulations***

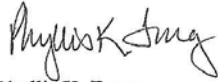
To: Patricia E. Healy  
Acting Chief Financial Officer  
Office of the Chief Financial Officer

We have audited the consolidated balance sheets of the U.S. Department of Agriculture (USDA) as of September 30, 2005 and 2004, and the related consolidated statements of net cost, changes in net position, and financing, and the combined statements of budgetary resources (hereinafter referred to as the "consolidated financial statements"), and have issued our report thereon dated November 10, 2005. We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 01-02, "Audit Requirements for Federal Financial Statements."

The management of USDA is responsible for complying with laws and regulations applicable to it. As part of obtaining reasonable assurance about whether the consolidated financial statements are free of material misstatement, we performed tests of USDA compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of the consolidated financial statement amounts, and certain provisions of other laws and regulations specified in OMB Bulletin No. 01-02, including certain requirements referred to in the Federal Financial Management Improvement Act of 1996 (FFMIA). We limited our tests of compliance to the provisions described in the preceding sentence and did not test compliance with all laws and regulations applicable to USDA. However, providing an opinion on compliance with 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 disclosed one instance of noncompliance with laws and regulations discussed in the second paragraph of this report, exclusive of FFMIA, that are required to be reported under Government Auditing Standards and OMB Bulletin No. 01-02. (See Findings and Recommendations, Section 3, "Compliance With Laws and Regulations.")

This report is intended solely for the information and use of the management of USDA, OMB, and Congress, and is not intended to be and should not be used by anyone other than these specified parties.



Phyllis K. Fong  
Inspector General

November 10, 2005

## ***Findings and Recommendations***

### ***Section 1. Internal Control Over Financial Reporting – Material Weaknesses***

Material weaknesses are reportable conditions in which the design or operation of one or more internal control components do not reduce to a relatively low level the risk that misstatements, in amounts that would be material in relation to the consolidated 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. Because of inherent limitations in any internal control, misstatements due to error or fraud may occur and not be detected. We believe that the findings discussed in this section are material internal control weaknesses.

#### **Finding 1                      Improvements Needed in Overall Financial Management Across USDA**

During fiscal year 2005, the Department continued to make significant improvements in its overall financial management. However, we noted areas where further improvements are needed. For example:

- In response to last year's audit report OCFO revised its methodology in fiscal year 2005 for compiling the consolidated statement of financing (SOF). However, as the OCFO did not timely engage Forest Service personnel in the process, the initial revised methodology did not correctly produce the SOF at the Forest Service level. For example, the USDA OCFO made assumptions that were not correct because of the uniqueness of certain Forest Service business processes.
- Abnormal balances existed at yearend without being fully researched and corrected. As of fiscal yearend, we noted that over 90 abnormal account balances existed, totaling over \$1 billion. According to the Department, the existence of an abnormal balance indicates that transactions or adjustments may have been posted in error to an account. Agencies reported that their abnormal balances were caused by a variety of reasons. Although the number of abnormal account balances had been reduced by about half, the dollar value had increased. When abnormal balances exist, immediate research should be performed to identify the cause and correct the condition.
- Our review disclosed that budgetary and proprietary accounts were sometimes forced to equal each other in order to pass the Federal

Agencies' Centralized Trial Balance System (FACTS) II edit checks. These accounting relationships should exist naturally; when they do not, immediate research should be performed to identify the cause and correct the condition.

- We also noted the lack of financial management systems and processes that were not always capable of fully monitoring and controlling budgetary resources for all programs. This occurred, primarily, because the Commodity Credit Corporation (CCC) and the Forest Service (FS) do not yet track and manage the status of obligations and administrative limitations established by legislation or agency policy and are dependent upon manual processes. This subjects overall funds control to significant risk. Funds control is a vital component of any Federal Government operation.
- We continued to identify deficiencies in the credit reform processes used by CCC and the Farm Service Agency (FSA) relating to their cash flow models. We have reported material internal control weaknesses relating to credit reform processes and practices for fiscal year 2001 and all subsequent years. The conditions described below were primarily caused by the lack of adequate management oversight and review.
  - FSA incorrectly entered the loan maturity range for one loan program. FSA's cash flow model for direct loans also did not calculate the weighted average interest rate correctly. We identified these situations and brought them to FSA's attention. FSA immediately corrected the model and re-ran the reestimates used for financial reporting.
  - CCC made errors in the development, implementation, and maintenance of cash flow models. Additionally, the data underlying the cash flow models were not always appropriately processed. Errors in the cash flow models and related data were corrected by CCC prior to finalizing the reestimates used for financial reporting.
  - Additionally, our review of the initial version of the footnotes found errors in disclosure relating to CCC's loans. Corrections totaling more than \$8 billion were subsequently made to the footnote.
- We also noted that FS and CCC yearend accrual processes need to be calculated accurately and posted prior to providing the financial statements for audit. CCC also inappropriately applied accounting



standards and erroneously determined no accrual was needed for one program, and the auditors proposed an adjustment and a liability in the amount of about \$7 billion was recorded.

**Recommendation No. 1**

Finalize supporting documentation for any required manual adjustments to the SOF. The SOF compilation should be supported by transactions and account balances that are traceable to the general ledger.

**Recommendation No. 2**

Provide additional training on the relationship of the SOF to the statements of budgetary resources and net cost.

**Recommendation No. 3**

Continue to assess the overall process used to compile the SOF in order to identify approaches and techniques that provide for a more efficient, accurate, and consistent compilation process. The compilation should be subjected to a secondary review by a trained manager who is independent of the financial statement preparation process. In addition to reviewing specific support for the compilation, the review should also include an analytical analysis of the relationships among balances.

**Recommendation No. 4**

Provide oversight to the lending agencies to ensure that cash flow models and data inputs as well as estimates and reestimates are subject to appropriate controls, including management oversight review.

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**Finding 2                      Improvements Needed in Information Technology (IT) Security and Controls**

Federal information security has been on the U.S. Government Accountability Office (GAO) list of high-risk areas since 1997. Federal agencies rely extensively on computerized information systems and electronic data to carry out their missions. The security of these systems and data is essential to preventing data tampering, disruptions in critical operations, fraud, and inappropriate disclosure of sensitive information.

Protecting federal computer systems and the systems that support critical infrastructures is a continuing concern.

The efforts of the Department's Office of the Chief Information Officer (OCIO) and OIG in the past few years have heightened program management's awareness of the need to plan and implement effective IT security. Agencies and the Department accelerated their efforts to comply with Federal information security requirements during the fiscal year. While progress has been made there is still much to be accomplished. Due to the significance of these weaknesses the Department cannot be assured that its systems and data are adequately secured. As a result, IT management and security remains a material weakness within the Department.

While individual agencies need to improve the management and security of their respective IT environments, the Department should retain accountability for the lack of adequate guidance, oversight, and management of the certification and accreditation efforts, and the general support system of the service center agencies<sup>1</sup> operated by Information Technology Services (ITS), a component of OCIO. These departmental weaknesses have had a significant impact on the integrity, confidentiality, and availability of the systems and data.

The results of our audit work throughout the year are highlighted in the paragraphs below.

#### **Certification and Accreditation**

The Department and its agencies have made progress in addressing the lack of compliance with OMB Circular No. A-130, Appendix III, but weaknesses continue to exist. While the Department's efforts were commendable, completion of the first accreditation process did not correct the Department's security weaknesses; rather, it was the first step in identifying controls, documenting and testing those controls, and ensuring that the process is integrated into each system's development life cycle as OMB intended.

We found that the Department certification and accreditation (C&A) process did not produce complete and reliable documentation to support the accreditation decisions. Agencies did not fully comply with the National Institute of Standards and Technology (NIST) guidance in preparing the necessary system documentation, misapplied Federal Information Processing Standards 199 in assessing system risk, and did not ensure that thorough and adequate independent testing was performed during the Security Testing and Evaluation stage of the process. Finally, our review disclosed that the agencies had not yet established effective configuration management or

<sup>1</sup> The service center agencies include Rural Development, FSA, and the Natural Resources and Conservation Service.

continuous control monitoring of their systems, an integral part of the C&A process. Additional details of the weaknesses we identified are available under separate cover.<sup>2</sup>

#### **Common Computing Environment Management and Security**

OCIO-ITS assumed the responsibilities over the general support system for the Department's service center agencies. Our audit identified many of the same weaknesses we had identified in prior audits of the service center agencies individually. While the service center agencies retained ownership and control over their own applications, weaknesses in the general support system had significant implications regarding the reliability of the data processed by those agencies.

We found that OCIO-ITS had not established effective policies and procedures covering its operations, established clearly defined roles and responsibilities, adequately prepared to take over the vulnerability scanning and mitigation process, established a reliable baseline inventory of all systems and network equipment, nor established effective physical or environmental controls over the network equipment in the offices we visited. Additional details of the weaknesses we identified are available under separate cover.<sup>3</sup>

#### **Federal Information Security Management Act Report (FISMA)**

Our FISMA report consolidated the results of our audits, and those conducted through contract auditors throughout the year. This year, those audits continued to disclose noncompliance with OMB Circular No. A-130, Appendix III, and NIST guidance. Our conclusion was arrived at primarily from the results of our audit of the Department's certification and accreditation efforts cited above; however, we noted other weaknesses that persisted within the Department. For instance, the Department was still unable to produce a reliable inventory of applications and general support systems, had not yet established a reliable inventory of Internet Protocol addresses, had not ensured that agencies reported complete and accurate Plan of Action and Milestone reports, and had not ensured that all Department personnel received security awareness training. Additional details of the weaknesses we identified are available under separate cover.<sup>4</sup>

The Department and its agencies are in the process of addressing the above weaknesses by implementing the recommendations we made in the cited

<sup>2</sup> Audit Report No. 50501-4-FM, "Review of the U.S. Department of Agriculture's Certification and Accreditation Efforts," dated October 21, 2005.

<sup>3</sup> Audit Report No. 50501-3-FM, "Office of the Chief Information Officer, Management and Security Over Information Technology Convergence – Common Computing Environment," dated October 24, 2005.

<sup>4</sup> Audit Report No. 50501-5-FM, "Fiscal Year 2005 Federal Information Security Management Act Report," dated October 6, 2005.

audit reports. Therefore, we are making no additional recommendations in this report.

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**Section 2. Internal Control Over Financial Reporting – Reportable Condition**


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Reportable conditions are matters coming to our attention relating to significant deficiencies in the design or operation that, in our judgment, could adversely affect the agency's ability to record, process, summarize, and report financial data consistent with the assertions by management in the consolidated financial statements.

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**Finding 3 Additional Financial Management Issues Warrant Attention**

Our review disclosed certain areas for which financial management processes and practices can be improved. For example:

- The Foundation Financial Information System (FFIS) uses standard vouchers (SV) to process adjustments to the general ledger. SVs use predefined debits and credits based on business rules. We reviewed 91 SVs processed for fiscal year 2005 prior to October 1, 2005. We noted that 26 of the SVs reviewed were processed to (1) correct a system weakness, (2) compensate for a control weakness, and/or (3) correct another SV. Additionally, our review disclosed that the supporting documentation was inadequate for 47 SVs. The types of problems that we found could have been reduced had the agencies effectively implemented the controls outlined in FFIS Bulletin 02-06, "Internal Controls Over Standard Vouchers in the FFIS," which establishes overarching guidance for developing proper internal controls.
- We reviewed 65 documents processed after the close of agency fiscal month 12. These were needed to correct account balances for financial reporting. Many of the documents reviewed impacted cash or budgetary accounts. We noted that 28 of the documents were processed to (1) correct a prior adjustment, (2) compensate for a control weakness, and/or (3) correct a system weakness.
- Our review of FFIS application controls disclosed that controls relating to agency approvals could be strengthened. For example, we found that significant documents such as manual adjustments, payment documents, and appropriation documents did not require approval at some agencies. This preventative measure would provide a basis for a good quality control structure within the accounting system.
- Our review disclosed that obligations were not always valid because agencies were not effectively reviewing all unliquidated (open or

active) obligations and taking appropriate actions (de-obligating).<sup>5</sup> Invalid obligations increase the risk that funds may be inappropriately diverted for purposes other than what Congress intended. Treasury's annual closing guidance (Bulletin No. 2005-06) requires the annual review of unliquidated obligations. Departmental Regulation 2230-1, "Reviews of Unliquidated Obligations," dated April 17, 2002, requires semi-annual reviews and annual certifications from agency Chief Financial Officers (CFO) that the semiannual reviews were performed and unliquidated obligations existing at yearend are valid based on the reviews. Both Treasury and USDA require appropriate records of the reviews to be retained for audit purposes. However, we noted the following exceptions.

- We selected 60 unliquidated obligations from 4 agencies for which no activity had occurred for over 2 years. We found that 54 of 60 (90 percent) obligations reviewed were invalid and agencies indicated the items would be de-obligated.
- We also requested evidence of the March 31, 2005, reviews from seven agencies. Three were unable to provide complete evidence of their reviews.

The OCFO has immediate and long-term plans to improve its financial management systems. These actions include working with the business process owners to address the problems with the legacy feeder systems, with the objective to provide an improved integration of the financial management architecture within the Department.

#### **Recommendation No. 5**

Ensure that agencies adhere to FFIS Bulletin No. 02-06, "Internal Controls Over Standard Vouchers in the FFIS."

#### **Recommendation No. 6**

Ensure that agency approval of appropriate significant documents is required prior to processing.

#### **Recommendation No. 7**

Provide oversight to ensure that general ledgers reflect valid obligations and that agencies perform the required reviews of unliquidated obligations

<sup>5</sup>Obligation means a binding agreement that will result in outlays, immediately or in the future. Budgetary resources must be available before obligations can be incurred legally.

appropriately and effectively. Additionally, ensure that agencies maintain evidence of the reviews.

### **Section 3. Compliance With Laws and Regulations**

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The management of USDA is responsible for complying with laws and regulations applicable to it. As part of obtaining reasonable assurance about whether the consolidated financial statements are free of material misstatement, we performed tests of USDA compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of the consolidated financial statement amounts, and certain provisions of other laws and regulations specified in OMB Bulletin No. 01-02, including certain requirements referred to in the Federal Financial Management Improvement Act (FFMIA).

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#### **Finding 4 Substantial Noncompliance With FFMIA Requirements**

Under FFMIA, agencies are required to annually assess whether their financial management systems comply substantially with (1) Federal financial management system requirements (FFMSR), (2) applicable Federal accounting standards, and (3) the U.S. Government Standard General Ledger at the transaction level. In addition, FISMA requires each agency to report significant information security deficiencies, relating to financial management systems, as a lack of substantial compliance under FFMIA. FFMIA also requires auditors to report in their CFO Act financial statement audit reports whether the financial management systems substantially comply with FFMIA's systems requirements.

During fiscal year 2005, USDA agencies worked to meet FFMIA and FISMA objectives, and as a result, corrective actions were taken to mitigate several significant deficiencies; however, additional work remains. USDA's fiscal year 2005 Performance and Accountability Report reported that financial management systems continued to be out of substantial compliance with the three requirements of the FFMIA. Our audit work during fiscal year 2005 has identified the following significant system nonconformances with FFMIA.

- FSA/CCC financial auditors reported non-compliance with all three requirements of the FFMIA. They found that although CCC had issued policies and procedures to correct deficiencies previously reported in its budgetary accounting and accounting for accruals, CCC was not able to fully implement them in fiscal year 2005. Auditors reported the inability of CCC to properly assess the correct accounting treatment for certain budgetary transactions in accordance with generally accepted accounting principles. Additionally, it was reported that CCC inappropriately applied the accounting standards in



formulating the policies related to accrued program liabilities. Finally, auditors reported the lack of a complete information security management program that can be applied to its general support and financial systems, along with the need for establishing and maintaining sustainable and repeatable information security and contingency planning controls.

- IT control weaknesses, which include an unreliable certification and accreditation process and ineffective controls in the OCIO-ITS general control environment, have a material effect on the integrity, confidentiality, and availability of Rural Development's systems and data. Rural Development aggressively pursued accreditation of its major applications as required by OMB Circular No. A-130. However, our review of the C&A documentation supporting four applications disclosed that the documentation did not meet basic accreditation requirements, the security testing and evaluation were inadequate, and/or the systems were fully accredited without restriction or limitation before all components were fully operational. Additionally, our review of the common computing environment network and systems identified the same types of weaknesses that our prior audits identified in the Service Center Agencies individually, including inadequate controls over physical and logical access, inventory of systems and network equipment, effective policies and procedures, and vulnerability scanning and mitigation.

In addition, we noted other information security control weaknesses during our fiscal year 2005 Federal Information Systems Control Audit Manual reviews that should have been reported as FFMLA noncompliance by the Department and its component agencies. Those weaknesses are described in Finding No. 2 of this report. Unresolved information security weaknesses could adversely affect the ability of agencies to produce accurate data for decision making and financial reporting because such weaknesses could compromise the reliability and availability of data that are recorded in or transmitted by an agency's financial management system.

The Department continues its effort to achieve compliance with the FFMLA requirements. It has been working with the component agencies to accelerate completion of corrective actions previously estimated to extend into fiscal year 2006. Currently, all scheduled completion dates are targeted for fiscal year 2006, except for corrective actions relating to CCC funds control. CCC's funds control completion is scheduled for fiscal year 2009. Issues regarding modernization of systems continue to be and will remain significant challenges in fiscal year 2006. These are complex areas and significant efforts will be needed to accomplish the target dates without, again, extending timeframes. We believe correcting these deficiencies should be a primary concern and priority for the Department during fiscal year 2006.

Improving Federal financial management systems is critical to increasing the accountability of financial program managers, providing better information for decision-making, and increasing the efficiency and effectiveness of services provided by the Federal Government.

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**Finding 5**
**Anti-Deficiency Act Violation**

During fiscal year 2005, Rural Development reported a \$1 billion Anti-Deficiency Act violation. The violation occurred when a bond guarantee agreement and the related guarantee of payment were executed prior to the approval of the apportionment of funds.<sup>6</sup> Specifically, the initial note and guaranteed loan level was signed on June 14, 2005, and the apportionment was not approved by OMB until July 20, 2005.

OIG's review of this matter disclosed that controls existed to prevent an Anti-Deficiency Act violation from occurring; however, management circumvented those controls. Rural Development has stated that to prevent future violations, any unsigned note will be held in the Office of the Assistant Administrator for Electric Programs pending written verification that OMB has processed the Apportionment of Funds.

We are making no further recommendations because the Anti-Deficiency Act violation was appropriately reported to OMB and the President.

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<sup>6</sup> There is no budget authority associated with the \$1 billion bond guarantee. Section 6101 of the Farm Security and Rural Investment Act of 2002 (P.L. 107-171) directed the Secretary to guarantee Investment Grade Bonds issued by non-profit lenders if the proceeds were used for electric and telephone projects eligible for assistance under the Rural Electrification Act of 1936.

***Exhibit A – Audit Reports Related to the Fiscal Year 2005 Financial Statements***

<b>AUDIT NUMBER</b>	<b>AUDIT TITLE</b>	<b>RELEASE DATE</b>
05401-14-FM	Federal Crop Insurance Corporation/Risk Management Agency's Financial Statements for Fiscal Years 2005 and 2004	November 2005
06401-20-FM	Commodity Credit Corporation's Financial Statements for Fiscal Years 2005 and 2004	November 2005
08401-5-FM	Forest Service's Financial Statement Audit for Fiscal Years 2005 and 2004	November 2005
11401-22-FM	Fiscal Year 2005 Review of the National Finance Center General Controls	November 2005
15401-6-FM	Rural Telephone Bank's Financial Statements for Fiscal Years 2005 and 2004	November 2005
27401-1-FM	Food and Nutrition Service's Financial Statements for Fiscal Year 2005	November 2005
50501-3-FM	Management and Security Over IT Convergence	November 2005
50501-4-FM	Review of USDA's Certification and Accreditation Effort	November 2005
50501-5-FM	Fiscal Year 2005 Federal Information Security Management Act Report	October 2005
85401-12-FM	Rural Development's Financial Statements for Fiscal Years 2005 & 2004	November 2005
88501-2-FM	National Information Technology Center General Controls Review-Fiscal Year 2005	September 2005