Part 4.
Audit
Section

United States Department of the Interior

OFFICE OF INSPECTOR GENERAL
Washington, D.C. 20240

November 15, 2004

Memorandum

To: Secretary

From: Earl E. Devaney
Inspector General

Subject: Independent Auditors' Report on the Fiscal Year 2004 Annual Report on Performance and Accountability of the U.S. Department of the Interior (Report No. X-IN-MOA-0054-2004)

INTRODUCTION

We contracted with KPMG LLP (KPMG), an independent certified public accounting firm, to audit the financial statements of the U.S. Department of the Interior (DOI) for fiscal years 2004 and 2003. The contract required that KPMG perform its audit in accordance with the Comptroller General of the United States of America's *Government Auditing Standards,* the Office of Management and Budget's (OMB) Bulletin 01-02 *Audit Requirements for Federal Financial Statements*, and the Government Accountability Office/President's Council on Integrity and Efficiency's *Financial Audit Manual*.

FINDINGS

In its audit report dated November 15, 2004 (Attachment 1), KPMG issued an unqualified opinion on DOI's financial statements for fiscal years 2004 and 2003. As discussed in KPMG's report and Note 17 to the financial statements, DOI's fiscal year 2004 consolidated statement of net cost is not comparable to its fiscal year 2003 consolidated statement of net cost. This occurred because, in fiscal year 2004, DOI revised the presentation of costs and revenues to match the *Government Performance and Results Act* strategic plan applicable to fiscal year 2004, which is different from the plan applicable to fiscal year 2003. Also, as discussed in Note 20 to the financial statements, DOI changed its method of accounting for the liability related to the U.S. Park Police Pension Plan effective October 1, 2003, based upon guidance received from OMB.

In its report, KPMG also stated, based upon the limited procedures performed, that the required supplemental information for deferred maintenance and the required supplemental stewardship information for stewardship assets and investments are not presented in conformity with accounting principles generally accepted in the United States of America. In addition, the report noted that DOI did not reconcile intra-governmental transactions with its trading partners as required by OMB.

The report identified 14 internal control weaknesses over financial reporting, 2 internal control weaknesses over required supplementary information and required supplementary stewardship information, and 4 instances of noncompliance with laws and regulations, as detailed below.

✓ *INTERNAL CONTROLS OVER FINANCIAL REPORTING*

Deficiencies in internal controls are described as reportable conditions, with the most serious conditions identified as material weaknesses.

Material weaknesses are significant deficiencies in the design or operation of one or more components of internal controls which do not reduce to a relatively low level the risk that a material misstatement to the financial statements could occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. KPMG identified material internal control weakness in the following areas:

A. Controls over property, plant, and equipment
B. Process for year-end closing
C. Reconciliation of intra-governmental transactions and balances
D. Controls over Indian Trust funds

Reportable conditions are significant deficiencies in the design or operation of the internal control over financial reporting that could adversely affect an organization's ability to record, process, summarize, and report financial data consistent with the assertions by management in the financial statements. KPMG identified reportable conditions in the following areas:

E. Application and general controls over financial management systems
F. Controls over accruals
G. Controls over legal and environmental contingencies
H. Financial management at the Bureau of Indian Affairs
I. Controls over the revenue process and other financing sources
J. Controls over grants
K. Controls over payments in lieu of taxes
L. Controls over budgetary transactions
M. Controls over charge cards
N. Controls over benefit programs

✓ *INTERNAL CONTROLS OVER REQUIRED SUPPLEMENTARY INFORMATION AND REQUIRED SUPPLEMENTARY STEWARSHIP INFORMATION*

KPMG identified significant deficiencies in internal control over required supplementary information and required supplementary stewardship information, which it believes could adversely affect DOI's ability to collect, process, record, and summarize information pertaining to the following:

O. Deferred maintenance reporting
P. Stewardship reporting

✓ *NONCOMPLIANCE WITH LAWS AND REGULATIONS*

KPMG identified noncompliance with the following laws and regulations:

Q. Single Audit Act Amendments of 1996
R. Debt Collection Improvement Act of 1996
S. Prompt Pay Act
T. Federal Financial Management Improvement Act (FFMIA) of 1996

KPMG is responsible for the auditors' report and for the conclusions expressed in the report. We do not express opinions on the financial statements of DOI, conclusions on the effectiveness of internal control, conclusions on whether DOI's financial management systems substantially complied with FFMIA, or conclusions on compliance with laws and regulations.

DOI CORRECTIVE ACTIONS

In its response (Attachment 2), DOI indicated general concurrence with the findings and recommendations. However, DOI did not concur that application and general controls over financial management systems constituted a reportable condition in internal controls. In its comments on this matter, KPMG acknowledged that DOI has made improvements in the security and controls over information systems. However, KPMG also indicated that it identified a number of conditions that could have affected DOI's ability to detect unauthorized changes to financial information, control electronic access to sensitive information, and protect its information. Therefore, KPMG concluded that the control weaknesses identified constitute a reportable condition.

REPORT DISTRIBUTION

The legislation, as amended, creating the Office of Inspector General (5 U.S.C.A. App. 3), requires semiannual reporting to Congress on all audit reports issued, actions taken to implement audit recommendations, and recommendations that have not been implemented. Therefore, this report will be included in our next semiannual report. The distribution of the report is not restricted and copies are available for public inspection.

We appreciate the cooperation and assistance of DOI personnel during the audit. If you have any questions, please contact me at (202) 208-5745.

Attachments (2)