

***U.S. DEPARTMENT OF COMMERCE***  
***Office of Inspector General***

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***OFFICE OF THE  
CHIEF FINANCIAL OFFICER  
AND ASSISTANT SECRETARY  
FOR ADMINISTRATION***

*OMB Bulletin 97-01 Implementation  
Requires Additional Efforts by the Department*

*Audit Report No. FPD-10876-8-0001 / September 1998*

*Office of Audits, Financial and Performance Analysis Division*





September 28, 1998

MEMORANDUM TO: W. Scott Gould  
Chief Financial Officer and  
Assistant Secretary for Administration

FROM: Johnnie E. Frazier  
Acting Inspector General

SUBJECT: *OMB Bulletin 97-01 Implementation Requires Additional Efforts  
by the Department*  
Final Audit Report No. FPD-10876-8-0001

This is our final report on the Department's efforts to implement the Office of Management and Budget (OMB) Bulletin 97-01, *Form and Content of Agency Financial Statements*. OMB Bulletin 97-01 defines the form and content of financial statements for the fiscal year (FY) ending September 30, 1998. Our limited scope audit disclosed that appropriate attention had not been devoted to implementation of the Bulletin because Department and bureau financial management resources had been concentrated on the FY 1997 financial statements.

The Deputy Chief Financial Officer (CFO) and Director for Financial Management expressed general agreement with our recommendations stating that corrective actions will be taken. Since our June 17, 1998, discussion of audit results with the Director for Financial Management and Deputy CFO, the Office of Financial Management (OFM) has undertaken a number of actions to address our concerns and recommendations. This includes the Director for Financial Management and Deputy CFO's July 2, 1998 issuance of *Department of Commerce Supplementary Guidance for FY 1998 Financial Statements* and the August 24, 1998 issuance of the memorandum, *Documentation of Cost Accounting Activities, Processes, and Procedures that Relate to the Statement of Net Cost*. On September 16, 1998, the Deputy CFO issued *Department of Commerce Second Supplemental Guidance for the FY 1998 Financial Statements*. We are aware that OFM staff have been meeting with the bureaus on OMB Bulletin 97-01 and have provided commentary on bureau-prepared interim statements. While these activities are responsive to our recommendations, it is essential that OFM continue to provide bureaus with assistance as needed.

We would appreciate receiving your audit action plan addressing our recommendations within 60 calendar days, in accordance with Department Administrative Order 213-5. The plan should be in the format specified in Exhibit 7 of the DAO. Should you have any questions regarding the preparation of the audit plan, please contact Chris Rose, Director, Financial & Performance Analysis Division, on (703) 603-0301.

## **INTRODUCTION**

Section 304 of the Chief Financial Officers Act of 1990, as amended by the Government Management Reform Act of 1994, requires an audit be performed of the Department of Commerce's consolidated financial statements. The Department's approach to the consolidated financial statements is to prepare financial statements for each of the individual bureaus, and then combine the financial information and elimination entries into consolidated financial statements. The Department received a disclaimer of opinion on its FY 1997 consolidated financial statements due to management's inability to support certain account balances and deficiencies noted in the Department's internal controls.

For the FY 1998 financial statements, the Department and its bureaus need to address not only identified audit deficiencies, but also the complex financial reporting requirements of OMB Bulletin 97-01. Implementing OMB Bulletin 97-01 will present substantial challenges to the Department and other federal agencies as it (1) substantially modifies the presentation of financial information, requiring six statements to be prepared as opposed to the two statements previously required under OMB Bulletin 94-01, and (2) implements several new standards issued by the Federal Accounting Standards Advisory Board. A revised OMB Bulletin 97-01 is to be issued in the near future. We believe that the Statement of Net Cost, which requires the reporting of costs by responsibility segments and programs, will prove to be the most challenging new statement. The Statement of Net Cost (1) implements the concepts of full costing and (2) links to two other new statements, the Statement of Changes in Net Position and the Statement of Financing.

Department Organization Order 20-27, effective December 14, 1995, assigns OFM the responsibility to develop and implement policies and procedures for departmental financial management and accounting requirements, and provide policy guidance and oversight of departmental financial management personnel, activities, and operations. OFM is also responsible for planning and coordinating the preparation of annual financial statements.

Recognizing the challenges associated with effective implementation of OMB Bulletin 97-01, we briefed the Department of Commerce's CFO Council at its April 22, 1998, meeting. We also have been providing briefings to senior management at the various bureaus on the requirements and challenges associated with the implementation of the OMB Bulletin 97-01.

## **PURPOSE AND SCOPE OF AUDIT**

The purpose of this limited scope audit was to assess the Department's early efforts to comply with the requirements of OMB Bulletin 97-01. We discussed implementation efforts with the OFM's Office of Financial Policy and Assistance (OFPA) officials, and also met with bureau financial management representatives to discuss their efforts to date. We reviewed pertinent

documentation related to OFM guidance provided to facilitate the Department's efforts to prepare consolidated financial statements. We also analyzed documents related to efforts by individual bureaus to prepare the FY 1998 financial statements.

Our fieldwork was conducted from April 9, 1998, to May 29, 1998. On June 17, 1998, we met with the Director for Financial Management and Deputy CFO and his staff to discuss our concerns with the Department's implementation of OMB Bulletin 97-01 and our recommendations for improvement. On June 23, 1998, we forwarded to OFM issues and concerns that had been identified in our discussions with individual bureaus on the implementation of OMB Bulletin 97-01. We subsequently reviewed the *Department of Commerce Supplementary Guidance for FY 1998 Financial Statements* issued on July 2, 1998.

We conducted our review in accordance with generally accepted government auditing standards. As a limited scope audit, we did not test compliance with significant laws and regulations or evaluate controls over computer generated data. The limited scope audit was performed under the authority of the Inspector General Act of 1978, as amended, and Department Organization Order 10-13, dated May 22, 1980, as amended.

## **FINDINGS**

### **Additional Efforts Are Necessary for OMB Bulletin 97-01 Implementation**

At the initiation of our review, the Department and bureaus were generally in the early stages of implementing OMB Bulletin 97-01. Sufficient attention had not been provided to planning for the challenges of implementing the bulletin, as the Department and its bureaus had generally concentrated their efforts on the FY 1997 financial statements. We found that:

1. Commerce bureaus were unclear on the preparation of the Statement of Net Cost.
2. The Department had not provided comprehensive written guidance on the FY 1998 statements to the bureaus.
3. Some bureaus were uncertain about the Department's request to prepare interim statements.
4. Cost accounting systems and processes were not documented.

While OFM had taken steps to prepare bureaus for implementing the new form and content guidelines, comprehensive training on the new accounting standards and reporting requirements had not been received. Subsequent to our discussions with the bureaus and OFM, written guidance was provided to the bureaus that addressed the Statement of Net Cost and interim statements. Comprehensive training sessions on the bulletin and new accounting standards were held in May and June of 1998. In the coming months, it is essential that OFM continue to work with bureaus in the implementation of OMB Bulletin 97-01.

### Bureaus Are Unclear on Preparation of Statement of Net Cost

OMB Bulletin 97-01 requires that the Statement of Net Cost and related supporting schedules classify revenue and cost information by suborganization or responsibility segments and, to the extent practicable, within each classification by major programs. We found that individual bureaus were unclear on what constitutes a responsibility segment and had been left on their own to determine what should be reported as programs. This resulted in bureaus taking diverse approaches to presenting cost data in the Statement of Net Cost, which may make preparation of consolidated financial statements difficult.

The then Acting Chief Financial Officer and Assistant Secretary for Administration had requested in a memorandum dated July 28, 1997, that each bureau provide a listing of the responsibility segments against which the bureaus would track costs beginning in FY 1998; however, no feedback on the appropriateness of responsibility segments was provided to the bureaus. We identified bureaus that were struggling with defining or were improperly identifying responsibility segments. Without specific guidance on how to identify programs in the Statement of Net Cost, some bureaus planned to report strategic goals as programs, while other bureaus planned to define programs differently (e.g., funding source).

In May 1998, the Deputy Chief Financial Officer issued preliminary guidance to bureaus on the preparation of FY 1998 financial statements in a memorandum, *Department of Commerce Preliminary Guidance for FY 1998 Financial Statements*. The guidance states that the major programs and activities listed on the Statement of Net Cost should link directly to the entity's goals and objectives in the Department's Strategic Plan. Most bureaus do not currently capture financial data by strategic goal. If the Department had provided guidance on how it expected the Statement of Net Cost to be prepared prior to FY 1998, bureaus could have made arrangements to capture cost information in a manner to facilitate preparation of statements in accordance with the Department-specified format. Many bureaus must now, well into FY 1998, develop an approach to allocate costs by strategic goal.

### Bureaus Are Unclear on the Preparation of Interim Financial Statements

The May 1998 guidance directs the bureaus to prepare six-month financial statements as of March 31, 1998. The preparation of interim financial statements is a useful exercise as it will provide hands-on experience needed for the successful implementation of the new bulletin. Prior to the CFO Council meeting on April 22, 1998, some bureaus had not been informed of the Department's intention to prepare interim financial statements using financial data as of March 31, 1998. Even after the meeting, it was not clear what level of information was needed by the Department to prepare consolidated interim statements. The first clear guidance on interim statements came with the May 8, 1998, request by the Deputy Chief Financial Officer for complete financial statements, with the exception of the overview, by July 15, 1998. OFM

prepared consolidated financial statements based on this information. We are concerned that the late date provides little time for the Department to address problems identified during the mock financial statement process.

#### Cost Accounting Activities, Processes, and Procedures Were Not Well Documented

Our efforts to assess the implementation of the new reporting guidelines were made difficult by a lack of available documentation. Bureaus generally did not have documented procedures on such routine issues as allocation of overhead costs or how they plan to prepare the Statement of Net Cost. Statement of Federal Financial Accounting Standard No. 4, *Managerial Cost Accounting Standards*, states that all managerial cost accounting activities, processes, and procedures should be documented by a manual, handbook, or guidebook of applicable accounting operations. This need for well-documented cost accounting activities, processes, and procedures is necessitated by the inadequate cost accounting systems within the Department.

#### **RECENT OFM ACTIONS TO IMPLEMENT OMB BULLETIN 97-01**

On June 17, 1998, we met with the Director for Financial Management and Deputy Chief Financial Officer and his staff to discuss our concerns with the Department's implementation of OMB Bulletin 97-01. On June 23, 1998 we forwarded to OFM, issues and concerns that had been identified in our discussions with individual bureaus on the implementation of OMB Bulletin 97-01. On July 2, 1998, the Director for Financial Management and Deputy Chief Financial Officer (CFO) issued the *Department of Commerce Supplementary Guidance for FY 1998 Financial Statements*. On August 24, 1998, the Deputy CFO issued *Documentation of Cost Accounting Activities, Processes, and Procedures that Relate to the Statement of Net Cost*. On September 16, 1998, the Deputy CFO issued *Department of Commerce Second Supplemental Guidance for the FY 1998 Financial Statements*. The supplemental guidance and the August 24, 1998 memorandum address many of our concerns and recommendations raised with OFM and our recommendation regarding the documentation of cost accounting activities, processes, and procedures. However, continued efforts are necessary to implement our remaining recommendations.

With respect to specific issues we raised with OFM, the supplementary guidance issued on July 2, 1998 requires that all entities that collect non-exchange revenue for the General Fund of the Treasury prepare a Statement of Custodial Activity that is audited; provides general guidance on cost assignment for preparation of the Statement of Net Cost; defines responsibility segments and discusses how bureaus should identify programs in the Statement of Net Cost; and reminds bureaus of the importance to document their methodologies for cost assignment and allocation. Also, bureaus are encouraged to discuss with OFM any concerns or questions they have regarding the implementation of new accounting standards and departmental guidance (e.g., cost allocation and identification of responsibility segments).

The Deputy CFO's August 24, 1998 memorandum serves as a reminder to bureaus on the Department-specified format for the Statement of Net Cost and the need to document cost accounting activities, processes, and procedures. We are aware and encouraged that OFM has been interacting with the bureaus on OMB Bulletin 97-01 issues, including issuance of comments on interim statements prepared by the bureaus.

The supplemental guidance issued by the Deputy CFO on September 16, 1998 provides additional information to assist the bureaus in the form and content of their financial statements. In this memorandum, the Deputy CFO provides updated guidance on such issues as financial statement preparation and the consolidation process. The updated guidance is based on discussions with OMB, Treasury, and the Federal Accounting Standards Advisory Board about pending guidance.

While recently undertaken activities demonstrate OFM's efforts to provide the leadership essential to preparing consolidated financial statements, it is essential that OFM continue to assist bureaus as needed. OFM must continue to work with the bureaus in order to ensure that the financial information used to prepare the consolidated financial statements is complete, reliable, and in the Department-specified format.

## **CONCLUSION**

We believe that OFM must provide vigorous leadership if the Department is to successfully implement OMB Bulletin 97-01. To ensure effective implementation of OMB Bulletin 97-01, OFM should have provided training and guidance on the principal financial statements, and requested interim financial statements prior to or shortly after the beginning of FY 1998. In recent months, OFM has been demonstrating the leadership essential to preparing consolidated financial statements. However, in our discussions with bureaus, we found a number of other issues outstanding that still need to be addressed (e.g., how to allocate overhead costs, whether to prepare a Statement of Custodial Activity, and how to handle deferred maintenance). OFM needs to ensure that the bureaus fully understand OMB Bulletin 97-01 requirements and are capable of providing the information in the departmental-specified format. This will require constant dialogue between OFM and the bureaus. The Department must continue to meet with individual bureaus on issues such as cost allocation for the Statement of Net Cost.

## **RECOMMENDATIONS**

We recommend that the Chief Financial Officer and Assistant Secretary for Administration take the necessary actions to ensure that:

1. OFM immediately follows up with bureaus to determine how the bureaus plan to prepare the Statement of Net Cost and provide assistance as needed.
2. OFM evaluates the interim financial statements for compliance with OMB Bulletin 97-01 reporting requirements and the Department's guidance. In addition, OFM should provide timely written feedback on the interim financial statements. The feedback should identify deficiencies in the information provided and direct bureaus to address concerns (e.g., cost allocation methodology) with auditors.
3. The Deputy Chief Financial Officer issues a written memorandum to bureaus reminding them of the need for documenting cost accounting activities, processes, and procedures that relate to the preparation of the Statement of Net Cost. This should include selected methodologies for allocation of costs.



## **DEPUTY CHIEF FINANCIAL OFFICER RESPONSE AND OIG COMMENTS**

In an August 24, 1998, memorandum, the Deputy CFO and Director for Financial Management responded to our draft report stating that there was agreement on many of the observations in our draft report and that they had addressed most of them. Also, the Deputy CFO stated that there was general agreement with the recommendations and he plans to implement them. We are pleased to learn that certain actions have already been undertaken and that there are plans to implement our recommendations.

The Deputy CFO's response requested that we make certain modifications to the report. A summary of the suggested modifications along with our comments follows. A complete copy of the Deputy CFO's response is attached.

The response requested that we indicate in our report that (1) other federal agencies are having problems implementing OMB Bulletin 97-01, and that this is a complex and complicated issue and (2) that form and content of the financial statements are an evolving subject for the entire federal government. We have added language to the report to emphasize the complexities surrounding OMB 97-01 implementation and to indicate that a revision to the bulletin is expected in the near future. While we do not feel that we are in a position to characterize other federal agency efforts relating to implementing OMB Bulletin 97-01, we modified our report to acknowledge that other agencies are facing similar challenges on this issue.

The response requested that we delete from page 1, paragraph 2, the statement "The bureaus were not provided with the *Department of Commerce Preliminary Guidance for FY 1998 Financial Statements* until May 8, 1998." The Deputy CFO concluded that the statement misleads the reader and cited several actions that had been taken to provide the bureaus with supplemental information. While we reaffirm our finding that we do not feel that OFM provided timely guidance on implementing the new form and content bulletin, we eliminated this particular statement.

The response requested that we delete from page 3, paragraph 4, the statement "In addition, there had been limited professional training on the new reporting requirements," stating that OFM had taken several steps to assure that the bureaus would be ready to carry out the new reporting and underlying cost accounting required by OMB Bulletin 97-01. We modified our report to reflect that OFM had taken steps to prepare the bureaus for implementing the new form and content guidelines, but that comprehensive training on the new reporting and accounting requirements was not received until May and June 1998.

The response requested that we modify the first of our three recommendations by eliminating the second sentence in the first recommendation relating to OFM determining whether the bureaus have developed reasonable approaches to the allocation of costs and to add the words “and provides assistance as needed” to the first sentence in the recommendation. The Deputy CFO stated that guidance has already been provided to bureaus and that the bureaus need to be responsible for a reasonable approach for the allocation of costs. While we agree that bureaus need to be responsible for establishing a reasonable approach for allocating costs, we feel it is imperative that OFM continue to work with bureaus on issues such as cost allocation as they arise. Due to the approach taken by the Department in its preparation of consolidated financial statements, i.e., reliance on individual prepared financial statements, it is important that OFM follow up with bureaus on important issues relating to financial statement preparation.



UNITED STATES DEPARTMENT OF COMMERCE  
Chief Financial Officer  
Assistant Secretary for Administration  
Washington, D.C. 20230

August 24, 1998

MEMORANDUM FOR George E. Ross  
Assistant Inspector General for Auditing

FROM: Anthony Musick *Anthony Musick*  
Deputy Chief Financial Officer  
Director for Financial Management

SUBJECT: Draft Audit Report No. FPD-10876-8-0001 (the Report)

In response to the report on the Department's efforts to implement Office of Management and Budget Bulletin 97-01 (OMB 97-01), I am providing the following comments. First, I want to thank you and your staff for all the hard work it took to prepare the report. We agree with many observations noted in the report and have already addressed most of them. However, as we discussed at the June 17, exit conference, we would appreciate you indicating in your report that other Federal agencies are having problems implementing 97-01, and that this is a complex and complicated issue since it is the first year some of these statements have been required.

I would like you to also point out that the form and content of the financial statements are an evolving subject for the entire Government. For example, members of my staff attended training sessions where four prominent officials of the Federal financial community provided four conflicting methods to prepare the Statements of Financing and Budgetary Resources. Therefore, the problems you noted are not unique to the Department of Commerce. The following comments are provided on specific parts of the report.

Page 1, paragraph 2. Delete the statements "The bureaus were not provided with the Department of Commerce Preliminary Guidance for FY 1998 Financial Statements until May 8, 1998."

The statement misleads the reader. One might believe that this was the first time the bureaus were aware of the new requirements when in fact the bureaus had been provided with supplemental information. More specifically:

- OFM distributed OMB Bulletin 97-01 to the bureaus on November 6, 1996, a month after OMB published it.
- On June 11, 1996, OFM updated the Department's Accounting Principles and Standards Handbook (the Handbook) for many FASAB standards including SFFAS No. 4 "Managerial Cost Accounting Concepts and Standards for the Federal Government."
- OFM also discussed the financial statement reporting requirements incorporating the cost standards for FY 1998 in last year's CFO Guidance for FY 1997 Financial Statements. It

noted that program performance measures should be coordinated between bureau finance officers, budget officials, and program managers and be consistent with the goals and objectives contained in the Commerce Strategic Plan. Bureau Finance Officers received their copy of this document on April 29, 1997.

Page 3, paragraph 4 delete the statement "In addition, there had been limited professional training on the new reporting requirements."

Before the start of FY 1998, OFM took several steps to assure that the bureaus would be ready to carry out the new reporting and underlying cost accounting required by OMB 97-01.

- In March 1997, at the NOAA audit conference, the Deputy Chief Financial Officer spoke to all of NOAA's financial management personnel. Among the topics he covered were the new reporting requirements under OMB 97-01 and full costing in accordance with SFFAS No. 4.
- On July 1, 1997, OFM held a conference, attended by the bureau's accounting and budget staffs, to explain in depth the new reporting formats, most notably the Statement of Net Cost. We emphasized the fact that the Statement of Net Costs requires the reporting of costs along responsibility segments (i.e., business lines) and full costing. During the discussion of full costing we specifically noted the requirement to allocate indirect costs (e.g., administration) to programs.
- On July 28, 1997, OFM issued a memorandum to the Department's budget and finance communities. The memorandum asked each bureau for its planned responsibility segments and performance measures, and for its plans to implement the cost accounting standards of SFFAS No. 4, to support the Statement of Net Cost. We received a response from each bureau concerning our inquiry. The budget offices gave us the responsibility segments and performance measures that they had developed for strategic planning (GPRA) purposes. The accounting offices also provided descriptions of their current costing capabilities and plans to develop costing methodologies by responsibility segments. All the accounting systems except NOAA stated that they could track costs along responsibility segments. NOAA stated that it was developing a Strategic Plan Reporting System (SPRS) to be implemented October 1, 1997, which would crosswalk costs to responsibility segments for both NOAA and BXA.

Generally, we agree with your recommendations and plan to implement them. However, we would like the second sentence of the first recommendation eliminated and the words "and provides assistance as needed" added to the end of the first sentence. Given the amount of effort needed to prepare consolidated statements and the guidance already provided the bureaus, we believe the bureaus need to be responsible for a reasonable approach for the allocation of costs. I believe this would be consistent with your third recommendation.

Should you have any questions, please contact Ted Johnson at (202) 482-0766.



**UNITED STATES DEPARTMENT OF COMMERCE**  
**Chief Financial Officer**  
**Assistant Secretary for Administration**  
Washington, D.C. 20230

August 24, 1998

MEMORANDUM FOR

SEE DISTRIBUTION

FROM:

*Anthony Musick*  
Anthony Musick  
Deputy Chief Financial Officer and  
Director for Financial Management

SUBJECT:

Documentation of Cost Accounting Activities, Processes, and Procedures  
that Relate to the Statement of Net Cost

In a recent review of the Department's efforts to implement OMB Bulletin 97-01, the Office of the Inspector General recommended that "The Deputy Chief Financial Officer issue[s] a written memorandum to bureaus reminding them of the need for documenting cost accounting activities, processes, and procedures that relate to the preparation of the Statement of Net Cost. This should include methodologies for allocation of costs." The following is a reminder on how to prepare the Statement of Net Cost along with allocation methodologies.

We stated in our Supplementary Guidance for the FY 1998 financial statements (see page 3 Paragraph III.A.) that the Department's Statement of Net Cost will use bureaus as responsibility segments. We also indicated that the strategic plan would be used to assign the costs of bureaus programs.

Costs of resources consumed by responsibility segments should be accumulated by type of resource (OMB object class). The cost assignments should be performed by one of the following methods, in order of preference: (a) directly tracing costs wherever feasible and economically practicable, (b) assigning costs on a cause-and-effect basis, or (c) allocating costs on a reasonable and consistent basis. Once you decide on a cost assignment method(s), it is extremely important to document your methods.

You also need to document how your costs are broken down. Documentation of your methodologies provides that timely, reliable data is obtained, maintained, and fairly disclosed in your reports. At a minimum these calculations need to be fully documented so that a clear audit trail is established. Further, the documentation is needed to prepare the reports in a consistent manner for future periods and support the Department's system of internal controls.

Should you have any questions, please contact Paul McEnrue at (202) 482-0623.