



Memorandum

U.S. Department of
Transportation

Office of the Secretary
of Transportation

Office of Inspector General

Subject: INFORMATION: Report on Financial Statements
for Fiscal Years 2002 and 2001, Highway Trust Fund
FI-2003-015

Date: January 24, 2003

From: Kenneth M. Mead
Inspector General

Reply To
Attn. of: Meche:x61496

To: The Secretary

I respectfully submit the Office of Inspector General (OIG) report on the Highway Trust Fund (HTF) Financial Statements for Fiscal Years (FY) 2002 and 2001. This report is required by the Chief Financial Officers Act of 1990, as amended by the Government Management Reform Act of 1994.

This report presents our unqualified opinion on the HTF Consolidated Balance Sheet, Statement of Net Cost, Statement of Changes in Net Position, and Statement of Financing, and the Combined Statement of Budgetary Resources as of, and for the years ended, September 30, 2002, and September 30, 2001.

The unqualified, or "clean," opinion did not come without extraordinary effort by HTF agencies and OIG auditors. This report identifies significant financial issues. However, with the effective leadership of the Department of Transportation (DOT) Chief Financial Officer and the Federal Transit Administrator, and the hard work by DOT employees to address these issues timely, the clean opinion was attained.

The HTF Financial Statements are the responsibility of the Federal Highway Administration (FHWA), Federal Transit Administration (FTA), National Highway Traffic Safety Administration, Federal Railroad Administration, and the Federal Motor Carrier Safety Administration. FHWA is the lead agency for preparing financial statements for the HTF agencies.

To assist us, the Department of the Treasury (Treasury) Office of Inspector General audited the schedule of assets and liabilities, and the related schedule of activity for the HTF accounts (referred to as the Corpus account) administered by the Treasury Bureau of Public Debt. The Treasury OIG issued an unqualified opinion on these schedules. The General Accounting Office (GAO) performed agreed-upon procedures on tax revenue receipts at the Internal Revenue Service and distributions to the HTF Corpus account, and identified no material discrepancies.

We identified one material weakness affecting the HTF Financial Statements. As required by the Federal Managers' Financial Integrity Act of 1982, the following material weakness was reported in DOT's 2002 report to the President and Congress.

- Last year, we reported that a headquarters account created by former FTA employees existed to hold obligations which were adjusted using inappropriate accounting procedures. This account had a negative \$77 million obligation balance as of September 30, 2001. While addressing this issue during FY 2002, FTA discovered that this account contained the remaining balance of what at one time was a \$562 million overobligation that had occurred 19 years earlier.

Rather than report the Antideficiency Act violation in FY 1984, former FTA employees engaged in inappropriate actions, such as (1) using funds from other appropriations, some of which had expired for obligation purposes; (2) maintaining records outside the accounting system; and (3) manipulating financial information on reports to Treasury and the Office of Management and Budget (OMB) to prevent detection.

After a thorough review of its financial records, FTA found that the remaining balance of the FY 1984 overobligation was about \$29 million and the deficiency involved non-HTF accounts as of September 30, 2002. This labor-intensive effort identified a material internal control weakness involving many areas of FTA financial practices. For example, about \$7 billion of adjustments were needed to correct the FY 2002 HTF Financial Statements. FTA is taking or plans to take corrective actions.

We also identified the following key issues involving internal control weaknesses and compliance with laws and regulations. While they are important, they did not affect our audit opinion.

- An interface deficiency existed between FHWA's grants management system and the DOT accounting system, which underreported valid obligations by about \$388 million. FHWA corrected its financial records and financial statements.
- FHWA needed to do more to determine whether obligations on inactive projects were needed. We identified about \$118 million of obligations that were no longer needed on inactive projects. FHWA and the states agreed, and these funds were made available for other projects or returned to the U.S. Treasury.
- The HTF agencies were not in compliance with the Federal Financial Management Improvement Act of 1996 because DOT's accounting system did not (1) provide the data for preparing the HTF Financial Statements, (2) comply with the U.S. Government standard general ledger, and (3) comply with requirements for implementing managerial cost accounting standards. The HTF

agencies also need to enhance computer security over the financial information systems. DOT and the HTF agencies plan to have compliant and secure financial systems by September 2004.

- DOT spent about \$37 million obtained from Treasury miscellaneous receipts accounts between FYs 1998 and 2001, rather than using appropriated funds. DOT had no authority to spend Treasury's money. When the erroneous transactions were corrected during FY 2002, FHWA appropriations were overobligated by about \$5 million. We recommended corrective actions in a separate report. DOT is in the process of reporting the Antideficiency Act violation to OMB and Congress.
- FHWA's accounting treatment for recovery of prior year funds was not in accordance with OMB reporting requirements. FHWA was combining recovered prior year funds with current year funds. FHWA plans to propose a revision to the Transportation Equity Act to permit this accounting treatment. Notwithstanding, FHWA needs to obtain OMB approval to deviate from its accounting and reporting requirements.
- The performance measures presented in the Management Discussion and Analysis did not provide information about the cost-effectiveness of programs nor relate to the Statement of Net Cost. Of the 20 FY 2002 performance measures, 9 were based on FY 2001 rather than FY 2002 performance data. None of the measures was linked to the cost of achieving targeted results.

We are making two recommendations concerning FTA implementing internal controls and reporting of the FY 1984 Antideficiency Act violation and FHWA's accounting for prior year funds. DOT and the HTF agencies have ongoing corrective actions to address the internal control and compliance issues. Issues that are common to HTF and other DOT agencies will be addressed in our report on the DOT Consolidated Financial Statements.

A draft of this report was provided to the DOT, FHWA, and FTA Chief Financial Officers on January 21, 2003. They agreed with the report.

We appreciate the cooperation and assistance of representatives of DOT and the HTF agencies. If we can answer any questions, please call me at (202) 366-1959, or John Meche at (202) 366-1496.

Attachments

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DEPARTMENT OF TRANSPORTATION
INSPECTOR GENERAL'S INDEPENDENT AUDIT REPORT
ON THE HIGHWAY TRUST FUND FINANCIAL STATEMENTS
FOR FISCAL YEARS 2002 AND 2001

To the Federal Highway Administrator,
Federal Transit Administrator,
National Highway Traffic Safety Administrator,
Federal Railroad Administrator, and
Federal Motor Carrier Safety Administrator

The Department of Transportation (DOT), Office of Inspector General (OIG), audited the Highway Trust Fund (HTF) Financial Statements and accompanying notes as of, and for the years ended, September 30, 2002, and September 30, 2001. In our audit of the HTF Financial Statements for Fiscal Years (FY) 2002 and 2001, we found:

- the financial statements are fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles;
- a material internal control weakness in the Federal Transit Administration (FTA) accounting and financial reporting; and reportable conditions concerning recorded obligations, prior year recoveries, and performance measures;
- noncompliance with the Federal Financial Management Improvement Act of 1996 (FFMIA) regarding: (1) DOT's accounting system, (2) financial system interfaces, (3) computer security over financial information systems, (4) managerial cost accounting standards, and (5) overobligation of funds;
- financial information in the Management Discussion and Analysis was materially consistent with the financial statements, except 9 of 20 performance measures were based on FY 2001 rather than FY 2002 performance data; and
- supplementary and stewardship information was consistent with management representations and the financial statements.

We performed our work in accordance with U.S. generally accepted government auditing standards and Office of Management and Budget (OMB) Bulletin 01-02, *Audit Requirements for Federal Financial Statements*. The following sections discuss these conclusions. Our audit objectives, scope, and methodology are discussed in the Exhibit. We believe that our audit provides a reasonable basis for our opinion.

A. UNQUALIFIED OPINION ON FINANCIAL STATEMENTS

In our opinion, the Consolidated Balance Sheet, Statement of Net Cost, Statement of Changes in Net Position, and Statement of Financing, and the Combined Statement of Budgetary Resources, including accompanying notes, present fairly, in all material respects, in conformity with U.S. generally accepted accounting principles, the HTF assets, liabilities, and net position; net costs; changes in net position; budgetary resources; and reconciliation of net costs to budgetary obligations as of September 30, 2002, and September 30, 2001.

B. CONSIDERATION OF INTERNAL CONTROLS

In planning and performing our audit, we considered HTF agencies' internal controls over financial reporting and compliance with laws and regulations. We do not express an opinion on internal controls and compliance because the purpose of our work was to determine our procedures for auditing the financial statements and to comply with OMB Bulletin 01-02 audit guidance, not to express an opinion on internal controls.

For the controls we tested, we found a material weakness concerning FTA's accounting and financial reporting. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce, to a relatively low level, the risk that errors, fraud, or noncompliance that would be material to the financial statements, may occur and not be detected promptly by employees in the normal course of performing their duties. Our internal control work would not necessarily disclose all material weaknesses or reportable conditions.

Our work also identified the need to improve internal controls over financial reporting and compliance in two other areas. These reportable weaknesses in internal controls, although not considered material weaknesses, represent significant deficiencies in the design and operation of internal controls, which could adversely affect the HTF Financial Statements.

Material Weakness

The following section describes a material weakness concerning FTA's accounting and financial reporting. On December 26, 2002, as required by the Federal Managers' Financial Integrity Act of 1982, the Secretary of Transportation reported this material weakness to the President and Congress.

Accounting and Reporting of FTA Financial Transactions

Last year, we reported that a headquarters account created by former FTA employees existed to hold obligations which were adjusted using inappropriate accounting procedures. This account had a negative \$77 million obligation balance as of

September 30, 2001. While addressing this issue during FY 2002, FTA discovered that this account contained the remaining balance of what at one time was a \$562 million overobligation that had occurred 19 years earlier.

Rather than report the Antideficiency Act violation in FY 1984, former FTA employees engaged in inappropriate actions, such as (1) using funds from other appropriations, some of which had expired for obligation purposes; (2) maintaining records outside the accounting system; and (3) manipulating financial information on reports to OMB and Treasury to prevent detection. After a thorough review of its financial records, FTA found that the remaining balance of the FY 1984 overobligation was about \$29 million and the deficiency involved non-HTF accounts as of September 30, 2002. This issue will be addressed in our report on the DOT Consolidated Financial Statements.

When this was brought to the current FTA Administrator's attention, she directed that a comprehensive review be made of FTA financial accounting and reporting. This labor-intensive effort identified a material internal control weakness involving many areas of FTA financial practices as the following examples indicate.

- About \$7 billion of adjustments were needed to correct the HTF Financial Statements.
- Interface deficiencies between the new DOT accounting system (Delphi) and FTA's financial feeder systems (TEAM and ECHO) prevented FTA from electronically processing transactions. For example, about \$350 million in ECHO payments had to be manually processed into Delphi.
- Until July 2002, FTA was not reconciling financial data between the DOT accounting system (DAFIS) and FTA's financial feeder system, TEAM. Differences between the two systems totaled about \$200 million as of September 30, 2002.
- In June 2002, when FTA implemented Delphi, significant obligation and expense transactions were not electronically transferred to Delphi. For example, when FTA manually processed transactions, about \$64 million in valid obligations were not entered into Delphi.

FTA corrected its financial records and provided accurate amounts for the financial statements. FTA also is in the process of implementing new internal control policies and procedures to address the material weakness.

Recommendation 1. We recommend that FTA report the Antideficiency Act violation that occurred in FY 1984 to OMB and Congress and ensure new internal control policies and procedures are implemented.

Reportable Conditions

Internal control weaknesses existed because of an electronic interface deficiency between the Federal Highway Administration (FHWA) grants management system and the HTF agencies' accounting system, and insufficient reviews by FHWA and states to identify inactive obligations that were no longer needed.

FHWA's Grants Management System

Last year, we reported an electronic interface deficiency between FHWA's Fiscal Management Information System (FMIS) and DAFIS, and recommended corrective action. FMIS records initial obligations for Federal-aid grants to states. However, when FMIS interfaces with DAFIS, all obligations are not electronically transferred into DAFIS. This occurs due to problems resulting from upgrades and changes that were made to the FMIS system. FHWA also did not reconcile obligated balances between FMIS and DAFIS. As of September 30, 2002, valid obligations totaling \$388 million were understated.

FHWA corrected its financial records and reported the appropriate amounts on the FY 2002 Statement of Budgetary Resources. FHWA plans to resolve this interface deficiency during the Delphi implementation process.

Inactive Obligations

Last year, we reported that FHWA and the states were not adequately reviewing obligated balances on inactive projects. As of June 30, 2002, FHWA had about \$37 billion in recorded obligations. About 39,000 obligations, totaling about \$5.6 billion, had no activity within 18 months. We compared obligations on inactive projects in DAFIS to closed projects in FMIS and identified \$118 million of obligations that were no longer needed on inactive projects. FHWA and the states agreed, and these funds were made available for other essential projects or returned to the U.S. Treasury.

C. COMPLIANCE WITH LAWS AND REGULATIONS

Our objective was not to express, and we do not express, an opinion on compliance with laws and regulations. Our work was limited to selected provisions of laws and regulations that would be reportable under U.S. generally accepted government auditing standards or under OMB guidance. Our work disclosed the following instances of noncompliance with FFMIA and other laws and regulations.

Federal Financial Management Improvement Act of 1996

Under FFMIA, we are required to report whether or not HTF financial management systems substantially comply with: (1) Federal financial management system requirements, (2) applicable Federal accounting standards, and (3) the U.S. Government standard general ledger at the transaction level. On January 4, 2001, OMB issued *Revised Implementation Guidance for the Federal Financial Management Improvement Act*, including factors for determining compliance and auditor reporting responsibilities. To meet the FFMIA audit requirement, we performed tests of compliance with the three FFMIA section 803(a) requirements and the revised OMB guidance, including financial management systems; the standard general ledger; and accounting standards.

The HTF agencies did not meet FFMIA requirements for financial management systems because: (1) DOT's accounting system, DAFIS, cannot produce auditable financial statements; (2) interface deficiencies exist between DAFIS and FMIS and between Delphi and FTA's financial feeder systems; (3) HTF agencies need to enhance computer security over financial information systems; (4) DAFIS does not use the U.S. Government standard general ledger; (5) HTF agencies have not implemented managerial cost accounting standards; and (6) a material weakness existed concerning FTA's accounting and financial reporting.

Financial Management System Requirements

FHWA and the Federal Motor Carrier Safety Administration (FMCSA), which account for about 75 percent of the HTF agencies' budgets, use DAFIS which cannot produce financial statements based on the information included within the system. For example, FHWA and FMCSA made about 300 adjustments, totaling about \$11 billion, outside DAFIS to prepare the financial statements. These adjustments were recorded in a financial statement module, a tool used to process the adjustments. However, these two HTF agencies did not use the financial statement module to prepare the financial statements and the adjustments were not recorded in DAFIS.

DOT plans to have Delphi fully operational for HTF agencies by March 2003. Although Delphi is being used by three of the five HTF agencies, the system is under development and does not yet fully meet all FFMIA requirements for financial management systems. Of the three HTF agencies on Delphi, none used the capabilities in Delphi to prepare its FY 2002 financial statements. Delphi compliance with FFMIA will be discussed in our report on the DOT Consolidated Financial Statements.

Interface deficiencies exist between DAFIS and FMIS, and between Delphi and FTA's financial feeder systems. The Joint Financial Management Improvement Program (JFMIP) *Core Financial System Requirements* and *Grant Financial System*

Requirements and OMB guidance require that, to be compliant with FFMIA, integrated financial management systems must maintain data accuracy between the core financial system and feeder systems. As discussed in Section B, an interface deficiency between DAFIS and FMIS resulted in recorded obligations in DAFIS being understated by \$388 million. Interface deficiencies between Delphi and FTA's financial feeder systems prevented FTA from electronically processing transactions. FHWA and FTA plan to resolve these deficiencies during the Delphi implementation process.

The HTF agencies also need to enhance computer security over financial information systems. One recommendation from a prior OIG report relating to data processing controls and safeguards has not been fully implemented. FHWA still needs to complete a security plan for its two major financial feeder systems and perform required certification and accreditation reviews as required by OMB Circular A-130. FHWA also needs to enhance security over network connections with industry associations and ensure that background checks are completed on contractor personnel working on financial systems. FHWA plans to complete corrective actions by March 2003. Computer security is a Departmentwide issue that will be addressed in our report on the DOT Consolidated Financial Statements.

U.S. Government Standard General Ledger

DAFIS does not comply with the U.S. Government standard general ledger (SGL) at the transaction level because it does not use all of the SGL accounts. As a result, about 300 adjustments, totaling \$11 billion, were made outside DAFIS and financial statements were prepared manually. Delphi is compliant with the SGL, and DOT plans to have Delphi fully operational in all HTF agencies by March 2003.

Federal Cost Accounting Standards

HTF agencies have not made progress implementing managerial cost accounting standards or using cost accounting practices to identify the costs of HTF programs. Statement of Federal Financial Accounting Standards (SFFAS) Number 4, *Managerial Cost Accounting Standards*, require that beginning in FY 1998, each reporting entity should accumulate and report the costs of its activities on a regular basis. DAFIS does not have the capability to capture full costs, including direct and indirect costs assigned to HTF programs. DOT plans to be compliant with cost accounting standards by September 2004. This is a Departmentwide issue that will be addressed in our report on the DOT Consolidated Financial Statements.

Accounting and Reporting of FTA Financial Transactions

OMB Circular A-123, *Management Accountability and Control*, requires that agencies establish organization, policies, and procedures to ensure that transactions are properly classified and accounted for, and that obligations and costs are recorded in compliance

with applicable laws and regulations. As discussed in Section B, a material internal control weakness exists in FTA's financial accounting and reporting practices. FTA has ongoing corrective actions to resolve the material weakness.

On December 26, 2002, as required by the Federal Managers' Financial Integrity Act of 1982, the Secretary of Transportation reported the material weakness in FTA's internal controls in DOT's 2002 report, and that DOT was taking remedial and progressive actions that will bring DOT into substantial compliance with FFMIA when its actions are successfully implemented.

Inactive Obligations

Title 31, United States Code, Section 1501 and Treasury Financial Management Bulletin 2002-07 state that obligations must be supported and that agencies only report valid obligations. As discussed in Section B, about \$118 million of obligations that were no longer needed were in the financial records. FHWA and the states agreed, and these funds were made available for other projects or returned to the U.S. Treasury.

Antideficiency Act Violations

Title 31, United States Code, Section 1341(a) provides that an officer or employee of the U.S. Government may not make or authorize an expenditure or obligation exceeding an amount available in an appropriation. As discussed in Section B, a \$562 million overobligation occurred in FY 1984, and FTA still needs about \$29 million to pay the remaining overobligation balance.

DOT also spent about \$37 million obtained from Treasury miscellaneous receipts accounts between FYs 1998 and 2001, rather than using appropriated funds. DOT had no authority to spend money from Treasury miscellaneous receipts accounts. When the erroneous transactions were corrected during FY 2002, FHWA prior-year appropriations were overobligated by about \$5 million. We made recommendations for corrective action in a separate report. This is a Departmentwide issue that will be addressed in our report on the DOT Consolidated Financial Statements. DOT is in the process of reporting the Antideficiency Act violations to OMB and Congress.

Prior Year Recoveries

Title 31, United States Code, Chapters 13 and 15, as implemented in OMB Circular A-11, *Preparation, Submission, and Execution of the Budget*, which replaced OMB Circular A-34 in June 2002, requires agencies to separately report deobligations of prior year funds and new obligations. FHWA's current practice combines current year obligations with prior year recoveries. This accounting treatment previously was allowed, but was disallowed in the revised OMB Circular A-34. Despite the change,

FHWA continued to administer the Federal-aid account based on the earlier requirement in OMB Circular A-34 and its operating legislation under Title 23, Section 118.

FHWA disclosed this noncompliance in the notes to the financial statements. Because of the conflicting guidance in Title 31 and Title 23, FHWA plans to propose a revision to the Transportation Equity Act for the 21st Century that would exempt FHWA from the accounting and reporting requirements in OMB Circular A-11. The noncompliance impacts the amounts reported for obligations incurred and adjustments on the Statement of Budgetary Resources, but an amount could not be determined.

Recommendation 2. We recommend that FHWA obtain OMB approval to deviate from the accounting and reporting requirements of OMB Circular A-11.

Performance Data

Under OMB Bulletin 01-02, our responsibility is to obtain an understanding of internal controls relating to the existence and completeness of performance data. The HTF agencies are responsible for establishing and maintaining adequate internal controls. The FY 2002 DOT Performance and Accountability Report contains 39 primary and 25 supplementary performance measures, of which 20 were in the HTF Financial Statements. The overall presentation of the 20 performance measures complied with OMB Bulletin 01-09, *Form and Content of Agency Financial Statements*, to report performance measures consistent with goals and objectives from agencies' strategic and performance plans.

Linking to Statement of Net Cost and Measuring Cost-Effectiveness

According to OMB Bulletin 01-09:

Entities should strive to develop and report objective measures that . . . provide information about the efficiency and cost effectiveness of programs. The discussion of performance . . . should be clearly linked to cost categories . . . featured in the Statement of Net Cost. . . . To further enhance the usefulness of the information, agencies should include an explanation of what needs to be done and what is planned . . . to improve financial or program performance.

The HTF agencies still do not have the systems in place to allocate costs by major program and the performance measures presented in the financial statements did not provide information about cost-effectiveness. Consequently, none of the performance measures was linked to the cost of achieving targeted results or to the Statement of Net Cost. DAFIS does not have the capability to accurately identify program costs. DOT

is in the process of replacing DAFIS, and plans to have Delphi in full operation in the HTF agencies by March 2003.

Assessing Internal Controls

We performed various procedures to assess internal controls relating to performance data. While our work disclosed no material internal control weaknesses, we were not required to, and we did not, test the validity or accuracy of performance data as part of the HTF Financial Statement audit. However, the HTF agencies are facing a significant challenge to ensure the incoming data are accurate and complete.

The HTF agencies rely on third-party organizations outside the Federal Government, such as states, grantees, and transit authorities, for most of the performance data. States report on a calendar-year basis, and HTF agencies did not receive some information in time to incorporate it into the financial statements. Of the 20 performance measures, 9 were based on FY 2001 rather than FY 2002 performance data.

Reporting of Planned Actions

To enhance the usefulness of performance information, OMB Bulletin 01-09 encourages entities to include an explanation of what is planned to improve financial or program performance. The Management Discussion and Analysis overview includes general comments on how to improve performance; however, specific plans to improve financial performance were not included.

Indirect Costs Charged to FHWA Grants

OMB Circular A-87, *Cost Principles for State, Local, and Indian Tribal Governments*, provides that to be allowable under Federal awards, costs must be allocable to a particular grant or contract in accordance with the benefits received. All activities, Federal and non-Federal, that benefit from indirect costs should receive an equitable share. We found that one state inappropriately billed FHWA grants for indirect costs. In some instances, the state assigned indirect costs only to selected FHWA grants, although the expenditures benefited other Federal and non-Federal projects. The state agreed to correct its billing practices and refund about \$3.5 million.

Intragovernmental Balances

OMB Bulletin 01-09 requires that reporting entities reconcile intragovernmental asset, liability, and revenue amounts by confirming balances quarterly with their trading partners. HTF agencies only partially confirmed or reconciled their intragovernmental balances. However, our testing found no material differences. This is a Departmentwide issue that will be addressed in our report on the DOT Consolidated Financial Statements.

D. CONSISTENCY OF OTHER INFORMATION

Management's Discussion and Analysis, required supplementary information (including stewardship information), and other accompanying information contain a wide range of data, some of which are not directly related to the financial statements. We are not required to, and we do not, express an opinion on this information. We compared this information for consistency with the HTF Financial Statements and discussed the methods of measurement and presentation with HTF agency officials. Based on this work, except for FY 2002 performance measures that were based on FY 2001 performance data (Part C of this report), we found no material inconsistencies with the HTF Financial Statements nor nonconformance with OMB guidance.

E. PRIOR AUDIT COVERAGE

Our report on the HTF Financial Statements for FYs 2001 and 2000 expressed an unqualified opinion and included one recommendation that FHWA establish procedures to reconcile obligated balances in DAFIS and FMIS, and develop procedures for interfacing FMIS with Delphi. FHWA plans to resolve this issue during the Delphi implementation process.

This report is intended for information and use by the HTF agencies, DOT, OMB, GAO, and Congress. This report is a matter of public record, and its distribution is not limited.



Kenneth M. Mead
Inspector General

Exhibit. Objectives, Scope, and Methodology

Our audit objectives for the HTF Financial Statements for FYs 2002 and 2001 were to determine whether: (1) principal HTF Financial Statements and accompanying notes are presented fairly, in all material respects, in conformity with U.S. generally accepted accounting principles; (2) HTF agencies have adequate internal controls over financial reporting, including safeguarding assets; (3) HTF agencies have complied with laws and regulations that could have a direct and material effect on the HTF Financial Statements or that have been specified by OMB, including FFMIA; (4) financial information in the Management Discussion and Analysis is materially consistent with the information in the principal HTF Financial Statements; (5) internal controls ensured the existence and completeness of reported data supporting performance measures; and (6) supplementary and stewardship information is consistent with management representations and the HTF Financial Statements.

HTF agencies are responsible for (1) preparing the HTF Financial Statements for FYs 2002 and 2001 in conformity with U.S. generally accepted accounting principles; (2) establishing, maintaining, and assessing internal controls to provide reasonable assurance that broad control objectives of the Federal Managers' Financial Integrity Act are met; (3) ensuring that HTF's financial management systems substantially comply with FFMIA requirements; and (4) complying with applicable laws and regulations.

OIG is responsible for obtaining reasonable assurance about whether (1) the HTF Financial Statements for FYs 2002 and 2001 are presented fairly, in all material respects, in conformity with U.S. generally accepted accounting principles and (2) management maintained effective internal controls. The objectives of these controls are:

- Financial reporting: Transactions are properly recorded, processed, and summarized to permit the preparation of financial statements and stewardship information in conformity with U.S. generally accepted accounting principles, and assets are safeguarded against loss from unauthorized acquisition, use, or disposition.
- Compliance with laws and regulations: Transactions are executed in accordance with laws governing the use of budget authority and with other laws and regulations that could have a direct and material effect on the financial statements and any other laws, regulations, and Governmentwide policies identified by OMB audit guidance.

OIG also is responsible for (1) obtaining sufficient understanding of internal controls over financial reporting and compliance to plan the audit, (2) testing compliance with selected provisions of laws and regulations that have a direct and material effect on the financial statements and laws for which OMB audit guidance requires testing, and

(3) performing limited procedures with respect to certain other information appearing in the HTF Financial Statements for FYs 2002 and 2001.

To fulfill these responsibilities, we examined the amounts and disclosures in the financial statements; assessed accounting principles and estimates; evaluated internal controls, and evaluated the presentation of the financial statements. We also examined the validity of financial transactions and interviewed financial management officials.

We did not evaluate all internal controls relevant to operating objectives as broadly defined by the Federal Managers' Financial Integrity Act, such as those controls relevant to preparing statistical reports and ensuring efficient operations. We limited our internal control testing to controls over financial reporting and compliance. Because of inherent limitations in internal controls, misstatements due to error or fraud, losses or noncompliance may nevertheless occur and not be detected. We also caution that projecting our evaluation to future periods is subject to the risk that controls may become inadequate because of changes in conditions or that the degree of compliance with controls may deteriorate.

We did not test compliance with all laws and regulations applicable to HTF agencies. We limited our tests of compliance to those laws and regulations required by OMB audit guidance that we deemed applicable to the HTF Financial Statements for FY 2002 ended September 30, 2002, and FY 2001 ended September 30, 2001. We caution that noncompliance may occur and not be detected by these tests and that such testing may not be sufficient for other purposes. We also caution that our internal control testing may not be sufficient for other purposes.

We performed our work in accordance with U.S. generally accepted government auditing standards and OMB Bulletin 01-02, *Audit Requirements for Federal Financial Statements*.