U.S. Department of the Interior
Office of Inspector General

AUDIT REPORT

INTERNAL CONTROLS OVER THE ACCOUNTING SYSTEM, FINANCIAL MANAGEMENT BRANCH, MINERALS MANAGEMENT SERVICE

REPORT NO. 00-I-333
MARCH 2000

EXECUTIVE SUMMARY

**Internal Controls Over the Accounting System,
Financial Management Branch, Minerals Management Service
Report No. 00-I-333
March 2000**

BACKGROUND

The financial activities of the Minerals Management Service (MMS) are managed by MMS's Financial Management Branch, located in Herndon, Virginia. In fiscal year 1998, the Branch accounted for appropriated funds of approximately $208 million. The accounting system used by MMS is the Advanced Budget/Accounting Control and Information System (ABACIS), which provides for recording, processing, and transmitting MMS's financial transactions; supporting the financial planning and budgeting activities; and preparing MMS's financial statements. The ABACIS also provides the accounting details for the Department of the Interior-established Interior Franchise Fund. The Government Management Reform Act (Title 31, United States Code) established the Franchise Fund Pilot Program. Pursuant to the Act and as part of the pilot program, the Department established the Fund to offer services such as personnel management, payroll, procurement, and automated data processing for customers outside the Department. Office of Management and Budget guidance requires Federal agencies to design and implement effective controls over financial accounting and over program and administrative operations.

RESULTS IN BRIEF

Overall, MMS's Financial Management Branch did not have financial data that were accurate, complete, and timely for fiscal year 1998. Office of Management and Budget Bulletin No. 98-08, "Audit Requirements for Federal Financial Statements," states that internal controls are designed to provide reasonable assurance that transactions are properly recorded, processed, and summarized to permit the preparation of financial statements in accordance with Federal accounting standards. Office of Management and Budget Circular No. A-123, "Management Accountability and Control," states that managers are responsible for the quality and timeliness of program performance and for ensuring that programs are managed with integrity and in compliance with applicable laws. However, control deficiencies occurred because MMS personnel did not follow established internal controls, such as performing account reconciliations and providing management oversight of the financial management accounting processes, and MMS did not establish adequate internal controls to ensure that transactions were properly classified during the conversion to the new standard general ledger required by the Federal Financial Management Improvement Act of 1996. In addition, MMS did not have sufficient internal control procedures to ensure proper accounting of the Interior Franchise Fund. As a result, MMS's financial statements were adversely affected; for example, it was necessary for MMS to make adjusting journal entries totaling $24.5 million to correct the differences between the general ledger cash balance and the Department of the Treasury cash balance. Also, funds in the Interior Franchise Fund were commingled with its Fedsim fund (a nonappropriated fund) to supplement the Interior Franchise Fund.

RECOMMENDATIONS

We recommended that the Director of MMS establish an internal control structure that provides assurance that assets are safeguarded; transactions are processed in accordance with applicable laws and regulations and are recorded, reconciled, processed, and summarized to permit the preparation of reliable financial statements; and accountability for assets is maintained. We also recommended that a cost accounting system be developed to accumulate separately all expenses and revenues associated with the Interior Franchise Fund and that the accrual accounting method of transaction reporting be applied to the Fund so that it is in accordance with generally accepted accounting standards.

AUDITEE COMMENTS AND OIG EVALUATION

MMS concurred with the report's three recommendations. Based on the response and subsequent information, we considered two recommendations resolved and implemented and one recommendation resolved but not implemented.

United States Department of the Interior

OFFICE OF INSPECTOR GENERAL
Washington. D.C. 20240

MAR 3 1 2000

AUDIT REPORT

Memorandum

To: Assistant Secretary for Land and Minerals Management

From: Roger La Rouche Roger La Rouche
Acting Assistant Inspector General for Audits

Subject: Audit Report on Internal Controls Over the Accounting System, Financial Management Branch, Minerals Management Service (No. 00-I-333)

INTRODUCTION

This report presents the results of our review of the internal controls over the financial data managed by the Minerals Management Service's (MMS) Financial Management Branch. We performed this review as part of our audit of MMS's financial statements for fiscal years 1998 and 1997. During fiscal year 1998, we began a review of MMS's financial data; however, we were unable to complete the audit because the financial data were not accurate, were incomplete, and were not timely.

BACKGROUND

The financial activities of MMS are managed by the Service's Financial Management Branch, located in Herndon, Virginia. In fiscal year 1998, the Branch accounted for appropriated funds of approximately $208 million. The accounting system used by MMS is the Advanced Budget/Accounting Control and Information System (ABACIS), which provides for recording, processing, and transmitting MMS's financial transactions; supporting the financial planning and budgeting activities; and preparing MMS's financial statements. Office of Management and Budget Circular No. A-127, "Financial Management Systems," states that appropriate internal controls "shall be applied to all system inputs, processing, and outputs" and that the financial management system "shall include a system of internal controls that ensure resource use is consistent with laws, regulations, and policies; resources are safeguarded against waste, loss, and misuse; and reliable data are obtained, maintained, and disclosed in reports." The Chief of Accounting Operations and the Chief of Accounting systems are responsible for ensuring that reliable data are obtained, maintained, and disclosed in MMS's reports.

The ABACIS also provides accounting details for the Interior Franchise Fund. The Government Management Reform Act (Title 31, United States Code) established the Franchise Fund Pilot Program. Pursuant to the Act and as part of the pilot program, the Department of the Interior established the Interior Franchise Fund to offer services such as personnel management, payroll, procurement, and automated data processing for customers outside the Department.

SCOPE OF AUDIT

During our review of MMS's financial statements for fiscal year 1998, we reviewed the internal controls in place for that fiscal year. During fiscal year 1998, MMS instituted internal controls under the new standard general ledger that were the subject of this review. MMS is responsible for establishing and maintaining an internal control structure which provides assurance that transactions are properly recorded and processed, assets are safeguarded, and financial transactions are executed in accordance with applicable laws and regulations. We evaluated MMS's internal controls over the ABACIS general ledger and the ability of the Chief of Accounting Operations and the Chief of Accounting Systems to provide accurate and reliable financial data. We also reviewed the internal controls over accounts payable, the reconciliation process, and the Interior Franchise Fund.

Our audit was conducted in accordance with the "Government Auditing Standards," issued by the Comptroller General of the United States. We found that significant internal control weaknesses existed because procedures were either not followed or not established. As a result, MMS's internal controls were not sufficient to provide reasonable assurance that the amounts reported in the general ledger were accurate and reliable.

PRIOR AUDIT COVERAGE

During the past 6 years, the Office of Inspector General has issued six audit reports on MMS's financial statements as follows: for fiscal years 1996 and 1997, Report No. 98-I-382, issued in March 1998; for fiscal years 1995 and 1996, Report No. 97-I-445, issued in February1997; for fiscal years 1994 and 1995, Report No. 96-I-631, issued in March 1996; for fiscal years 1993 and 1994, Report No. 95-I-405, issued in January 1995; for fiscal years 1993 and 1992, Report No. 94-I-715, issued in June 1994; and for fiscal year1991, Report No. 93-I-369 (combined statement of financial position only), issued in December 1992. For all six audits, we issued unqualified opinions that the financial statements were fairly presented. The audit reports also stated that MMS's internal control structure met established internal control objectives and that it was in compliance in all material respects with applicable laws and regulations. Internal controls were applicable for these fiscal years; however, the internal control environment during fiscal year 1998, which is the subject of our review, changed. Specifically, the new standard general ledger was implemented, and the accounting activity for the General Services Administration and for the Interior Franchise Fund became fully operational. Management of MMS is responsible for establishing and maintaining an internal control structure that provides reasonable assurance that transactions are properly recorded, processed, and summarized. Because of inherent limitations in any internal control structure, errors or fraud may occur and not be detected. Also, projections of the internal controls over financial reporting to future periods are subject to the risk that the internal controls may become inadequate because of changes in conditions or that the degree of compliance with the policies or procedures may deteriorate.

RESULTS OF AUDIT

MMS's Financial Management Branch did not have financial data that were accurate, complete, and timely for fiscal year 1998. Office of Management and Budget Bulletin No. 98-08, "Audit Requirements for Federal Financial Statements," states that internal controls are designed to provide reasonable assurance that transactions are properly recorded, processed, and summarized to permit the preparation of financial statements in accordance with Federal accounting standards. Office of Management and Budget Circular No. A-123, "Management Accountability and Control," states that managers are responsible for the quality and timeliness of program performance and for ensuring that programs are managed with integrity and in compliance with applicable laws. However, control deficiencies occurred because MMS personnel did not follow established internal controls, such as performing account reconciliations and providing management oversight of the financial management accounting processes, and MMS did not establish adequate internal controls to ensure that transactions were properly classified during the conversion to the new standard general ledger. In addition, MMS did not have sufficient internal control procedures to ensure proper accounting of the Interior Franchise Fund. As a result, MMS's financial statements were adversely affected, and funds in the Interior Franchise Fund were commingled with MMS funds.

Account Reviews and Reconciliations

MMS did not review or reconcile financial data to ensure that accounting transactions were recorded and reported accurately during fiscal year 1998. In addition, the values in the property system did not support the general ledger balance. Office of Management and Budget Circular A-34, "Instruction on Budget Execution," states that each agency "shall maintain systems of accounting and internal controls that provide reasonable assurance that transactions are properly recorded and accounted for to permit the preparation of reliable financial reports." However, the Chief of Financial Management Branch said that they did not have sufficient time to perform the reviews and reconciliations.

General Ledger. During our interim testing of the accounts payable line item in the financial statements, we determined that the amount for each accounts payable transaction was not recorded in the subsidiary ledger. Therefore, we could not verify the general ledger account balance with the amounts in the detailed subsidiary ledger. The Chief of Accounting Operations stated that the Financial Management Branch did not review or reconcile the general and subsidiary ledgers on a monthly basis during fiscal year 1998 because management did not assign responsibility for these duties. According to the Chief of Accounting Operations and the Chief of Accounting Systems, they were not aware that the ledgers were not balanced monthly until we reviewed the accounts payable line item in

August 1998. However, the accounting system generated a monthly general ledger report, which indicated that the general ledger and the subsidiary ledger did not balance. We found that the Chief of Accounting Operations disposed of the monthly general ledger reports. The Chief, however, said that he was not aware that he was responsible for reconciling these reports. After we found that the general ledger did not balance, the Chief of Accounting Systems researched the general ledger accounts and determined that data were not converted properly during the conversion to the new standard general ledger in October 1997. The Chief of Accounting Systems made adjustments to the ABACIS in August 1998 for 595 accounts payable transactions, which totaled approximately $10.9 million.

If the general ledger had been reviewed and reconciled monthly, the Chief of Accounting Operations and the Chief of Accounting Systems would have found that their accounting information was recorded improperly in the subsidiary ledger. The accounting system indicates whether a line item should have a debit or a credit balance. For example, the accounts payable line item is identified as having a credit balance because it represents the amount the organization owes others (a liability), while the accounts receivable line item is identified as having a debit balance because it represents the amount the organization should receive from others (an asset). Thus, if the accounts payable has a debit balance, it would indicate an unnatural balance. During our review of the September 30, 1998, preclosing general ledger, we determined that 25 of the 42 general ledger accounts had unnatural balances. Of the 25 unnatural general ledger account balances, 14 balances pertained to budgetary accounts,[1] such as reimbursements and other earned income, and to undelivered orders, and 11 balances were proprietary accounts,[2] such as fund balance with Treasury, accounts payable, and unexpended appropriations. The Chief of the Financial Management Branch, the Chief of Accounting Operations, and the Chief of Accounting Systems said that they were unaware of the unnatural balances until we brought the matter to their attention. We noted during our testing that one of the reasons for the unnatural balances was that accounting activities for fiscal year 1998 were not closed properly, resulting in expenses being charged to the improper fiscal year and fund in the ABACIS.

Cash. MMS did not perform monthly cash reconciliations for any of its 13 funds during fiscal year 1998. The Treasury Financial Manual, Part 2, Chapter 3300, Section 3330, requires cash to be reconciled on a monthly basis and reported to the Department of the Treasury on Standard Form 224, "Statement of Transactions." Any differences in the cash balances between MMS's general ledger and the Department of the Treasury's balances are to be reported in the Statement of Differences section of Form 224. The Chief of the Branch said that the Branch was aware that cash needed to be reconciled monthly but that it did not have sufficient time to perform this task during fiscal year 1998. Instead, an MMS

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[1]Budgetary accounts are used for fund control. Such accounts maintain the appropriation, apportionment, allotment, obligation, and other budget-related accounts and ensure that the agency complies with the provisions of the Antideficiency Act.

[2]Proprietary accounts track, record, and state the financial condition of the entity and provide profit or loss information.

accountant said that the Branch assumed that the Treasury balances were correct and adjusted the general ledger to these amounts. For example, if the Treasury records reported a cash balance lower than the cash balance in MMS's general ledger, an adjusting journal entry was made to reduce MMS's amount by crediting the cash account and debiting the accounts payable account. The Chief of Accounting Operations said that he was not aware that the adjustments were incorrect, and the Chief of the Branch stated that he was not aware that the adjustments were made only to the two accounts instead of all of the differences reconciled. In October 1998, MMS began to determine, by fiscal year and fund, the differences between the general ledger cash balance and the Department of the Treasury cash balance. In November 1998, MMS made adjusting journal entries totaling $24.5 million to correct the differences.

A cash reconciliation should be performed on a transaction basis so that it provides the information needed to adjust specific transactions in the subsidiary ledger. For example, Schedule No. 8H9134, paid in September 1998, was posted to the subsidiary ledger in the amount of $634.72, while the Department of the Treasury recorded the schedule in the amount of $1,421.92. The differences could have occurred for reasons such as posting errors and timing differences. Thus, a transaction-level analysis had to be performed to determine the correct amount and the reason for the differences. A determination then could be made as to whether MMS's subsidiary ledger or Department of the Treasury records needed to be adjusted. As a result of not performing proper cash reconciliations, inaccurate information on the Form 224 was submitted to the Department of the Treasury, and the balances for the cash account and the accounts payable account in the general ledger were incorrect. In addition, when cash reconciliations are not performed, the potential exists for an antideficiency situation or for funds to be misappropriated.

Year-End Closeout. We found that fiscal year 1998 transactions were included in the fiscal year 1999 subsidiary account balances in the ABACIS. We randomly selected 40 fiscal year 1999 transactions that were posted on November 6, 1998, and found that 6 transactions (15 percent) were fiscal year 1998 transactions. MMS prepared adequate year-end procedures; however, the accounting staff did not follow these procedures. As a result, fiscal year 1998 transactions were posted incorrectly to the fiscal year 1999 accounts.

We also statistically tested 327 fiscal year 1998 expenses and determined that the information recorded in the ABACIS contained either the incorrect appropriation fund code or the incorrect fiscal year. For example, on February 3, 1998, expenses for aircraft services totaling $33,140 were incurred using 1-year money (98MM fund); however, the purchase order indicated that no-year money (98MD fund) was to be used. We also found that a fiscal year 1996 oil spill research account (96MO fund) had charges for an environmental test tank totaling $276,782 for which the purchase order indicated that fiscal year 1992 1-year money (92MM fund) should have been used. A projection of the sample results to the total expense population resulted in the most likely error of misclassified financial data in the ABACIS to be $6.6 million. In addition, while auditing the 327 operating expense transactions, we found the following discrepancies:

- One hundred twenty five invoices were not date stamped, resulting in a projection of $82 million of invoices that could not be reviewed for compliance with the Prompt Payment Act. The Prompt Payment Act requires that a payment be made within at least a 30-day time frame. Therefore, if an invoice is not date stamped when it is received, the payment due date cannot be tracked, and the invoice may not be paid timely.

- Fifteen account numbers in the ABACIS did not agree with the account numbers on the purchase order, resulting in a projection of as much as $9.9 million that may have been charged to the incorrect fund. For example, a state and Indian compliance review was charged to a no-year fund (98MD fund) in the ABACIS but should have been charged to the annual appropriation (98MM fund).

- Nine paid invoices were not approved. Based on our sample results, we projected unapproved paid invoices of $5.9 million. When payments are not reviewed, the potential exists for funds to be misappropriated.

We believe that the existence of these discrepancies increases the potential for an antideficient situation because available funds may be depleted before all valid expenses are identified and paid or because funds may be misappropriated if controls are not followed.

Conversion. During October 1997, MMS converted to the new standard general ledger, as required by the Federal Financial Management Improvement Act of 1996. However, the conversion did not properly include all of the general ledger account balances. Consequently, MMS created a balancing account (Account 0000) that had a $69 million balance as of September 30, 1998, to capture the remaining activities. Because MMS did not reconcile the $69 million to identify the adjustments needed in the ABACIS records, we found, in August 1998, that the fiscal year 1997 ending balances audited were not equal to the fiscal year 1998 opening balances. This occurred because MMS did not compare the ending balances with the opening balances after the conversion to the new standard general ledger. The Chief of the Financial Management Branch, the Chief of Accounting Operations, and the Chief of Accounting Systems stated that they were not aware of the differences until we informed them of the discrepancies. After fiscal year 1998, MMS made 12 adjustments, totaling $91.3 million, to the fiscal year 1998 beginning balances so that they were the same as the audited ending balances for fiscal year 1997.

Capitalized Equipment. MMS did not have sufficient internal control procedures to ensure that the general ledger control balance for Property, Plant and Equipment was accurately stated and supported by detailed subsidiary information. The official property records are maintained in MMS's Property Management System, which is not integrated with the ABACIS. During our testing of the Property, Plant and Equipment line item in the financial statements, we found that MMS did not periodically reconcile the property management records to MMS's general ledger control account. Office of Management and Budget Circular A-127 states that each agency should establish and maintain a single integrated financial management system that requires reconciliations between subsystems to ensure the accuracy of the data. During the audit, we identified 11 capitalized equipment property items, totaling $182,206, that were in the Property Management System but that were not in the subsidiary ledger. Overall, there was a $3.8 million difference between the two systems for capitalized equipment. To ensure that the accounting system balance is the same as the Property Management System balance for capitalized equipment, the general ledger would have to be adjusted by $3.8 million and individual property items updated in the subsidiary ledger.

Inadequate Procedures

MMS did not have adequate procedures to ensure that accounting transactions were recorded and reported properly during fiscal year 1998, as described in the paragraphs that follow.

Federal or Public Transactions. MMS did not have adequate internal controls to ensure that transactions were properly classified as Federal (government) or Public (nongovernment) in the general ledger accounts. Office of Management and Budget Bulletin 97-01, "Form and Content of Agency Financial Statements," requires liabilities to be separated between Federal and Public. Because the MMS did not develop and implement procedures which ensured that accounts were properly defined as either Federal or Public, accounting employees judgmentally selected the designation when posting each transaction. We reviewed 327 operating expense transactions and found 22 transactions, totaling approximately $1.2 million, that were classified as Federal (government) but that should have been classified as Public (nongovernment). For example, 15 purchase orders relating to six states (California, Colorado, Montana, Oklahoma, Utah, and Wyoming) were entered as Federal; however, they should have been entered as Public.

Interior Franchise Fund. MMS did not have sufficient internal control procedures to ensure the proper accounting of the Department of the Interior's Franchise Fund. Specifically, MMS did not (1) develop a cost accounting system to determine whether the pricing structure was adequate to recover full costs; (2) implement accrual accounting procedures to record expenses incurred or revenues received in accordance with accounting standards; and (3) provide oversight over the Fund by establishing written accounting procedures or reviewing accounting data. As a result of these deficiencies, MMS used its Fedsim fund (a nonappropriated fund) to supplement the Interior Franchise Fund.

MMS did not develop a cost accounting system to facilitate compliance with the Department of the Interior and Related Agencies Appropriation Act of 1997 (Public Law 104-208), which requires that established pricing rates recover all expenses of operations. In addition, the Government Management Reform Act (Public Law 103-356) and the Department of the Interior and Related Agencies Appropriation Act of 1997 (Public Law 104-208) require that the Interior Franchise Fund recover the full costs associated with the products and services provided and an amount necessary to maintain operating reserves. The Acts also allow the Interior Franchise Fund to retain up to 4 percent of gross revenues for the acquisition of capital equipment and for the improvement and implementation of Departmental financial management, automated data processing, and other support systems.

MMS's Chief of Financial Management Branch stated that MMS did not establish a cost accounting system because MMS personnel believed that their ABACIS could accommodate the additional activities for the Interior Franchise Fund transactions. However, the Interior Franchise Fund did not account for all the expenses and revenues such as overhead costs. Instead, the overhead costs were allocated to a revolving fund established to account for procurement activity conducted with the General Services Administration. For example, overhead costs of approximately $42,000 for the Cooperative Administrative Support Unit were charged to the General Services Administration Fund. We informed MMS that overhead expenses associated with the Interior Franchise Fund had been commingled with other funds in the ABACIS. MMS's Financial System Team Leader stated that the overhead charges were posted to the revolving fund because the Interior Franchise Fund account did not have sufficient funds to cover these expenses. Until MMS properly accounts for the overhead charges, revenues from Department of the Interior activities may be supplementing MMS's appropriation, or conversely, MMS's appropriation may be supplementing non-Department of the Interior transactions.

MMS did not implement accrual accounting procedures to record expenses and revenues for the Interior Franchise Fund. Accounting standards require expenses to be recognized when goods and services are received and revenues to be recognized when earned. However, MMS recorded revenues before all of the goods or services were received. This resulted in MMS's collecting at least $2.2 million from the Interior Franchise Fund during fiscal year1998 that had not been earned.

MMS did not provide proper oversight over fiscal year 1998 accounting activities for the Interior Franchise Fund. The Fund subcontracts with MMS for the billing and collection functions and for delivering goods and services and with the U.S. Geological Survey for financial accounting and reporting. The Interior Franchise Fund is reported as part of the financial statements of the Office of the Secretary's Departmental Offices. We determined that the Fund's subsidiary account balances were not supported by the accounting records and that the subsidiary ledger was not reconciled to Interior Franchise Fund accounting activities. These deficiencies occurred because accounting procedures for the Interior Franchise Fund were not documented and monthly account reconciliations were not performed. Specifically, MMS did not have written procedures for year-end closeouts of expenses, and the informal procedures to close the books as of September 30, 1998, were not followed. For example, we found that the fiscal year 1998 Interior Franchise Fund subsidiary ledger remained open for financial activities through November 1998. Because the ledger was updated 2 months after the close of the fiscal year, fiscal year 1999 expenditures of approximately $1.6 million were recorded in the fiscal year 1998 subsidiary ledger. In addition, we found that monthly billing documents were processed by MMS without being reconciled to the source documents. MMS officials stated that they did not have the time to reconcile the billing documents to the source documents because there was only one staff member assigned to that function. During our testing, we attempted to reconcile January billings with source documents; however, MMS was unable to provide the necessary documentation for us to perform the reconciliation.

After the close of fiscal year 1998, MMS began its first reconciliation of Interior Franchise Fund activities. The reconciled data were provided to the Office of the Secretary for inclusion in the Departmental Offices financial statements for fiscal year 1998. We reviewed the subsidiary ledgers and compared the data with the amounts in the Interior Franchise Fund's financial statements for fiscal year 1998. We identified $2.2 million in Advances From Customers that should have been included in the Interior Franchise Fund but that was recorded as Fund Balance with Treasury, which we believe indicates that the cash was available to MMS. When we informed MMS and Office of the Secretary officials of the error, they adjusted the financial statements to reflect the correct information. In addition, year-end expenses of approximately $1.3 million and revenues of approximately $704,000 were not reported because year-end accruals[3] were not recorded. The Chief of Financial Management Branch agreed that the revenues should have been recognized when earned and that expenses should have been recognized when the goods and services were received. During our review, MMS officials began to develop accounting procedures to ensure that the accrual accounting method is used in future accounting periods.

Recommendations

We recommend that the Director of MMS implement internal control procedures which ensure that:

1. An adequate internal control structure, including management oversight, is established to provide reasonable assurance that assets are safeguarded; transactions are processed in accordance with applicable laws and regulations; transactions are recorded, reconciled, processed, and summarized to permit the preparation of reliable financial statements; and accountability for assets is maintained. At a minimum, MMS should ensure the following:

- Responsibilities are assigned to specific individuals and officials are held accountable for not complying with established internal controls.

- Year-end closeout procedures are followed for general ledger activities and are documented and followed for Interior Franchise Fund activities.

- Accounting transactions are defined properly in the ABACIS as either Federal or Public.

2. A cost accounting system is developed which will accumulate separately all expenses and revenues associated with the Interior Franchise Fund.

3. The accrual accounting method of transaction reporting is applied to the Interior Franchise Fund to be in accordance with generally accepted accounting standards.

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[3]Accrual-based accounting ensures that financial activity is recorded in the proper reporting period.

MMS Response and Office of Inspector General Reply

In the February 29, 2000, response (Appendix 1) to the draft report from the Director of MMS, MMS "agree[d]" with all three recommendations. Based on the response, we consider Recommendations 2 and 3 resolved and implemented. MMS also provided additional comments, which we incorporated into the report as appropriate.

For Recommendation 1, MMS, in subsequent correspondence, said that the recommendation would be implemented by December 31, 2001, and that the Chief, Budget and Finance Division, was responsible for implementation. Accordingly, the recommendation will be referred to the Assistant Secretary for Policy, Management and Budget for tracking of implementation.

Since the report's recommendations are considered resolved, no further response to the Office of Inspector General is required (see Appendix 2).

Section 5(a) of the Inspector General Act (5 U.S.C. app. 3) requires the Office of Inspector General to list this report in its semiannual report to the Congress. In addition, the Office of Inspector General provides audit reports to the Congress.

United States Department of the Interior

MINERALS MANAGEMENT SERVICE
Washington, DC 20240

FEB 29 2000

Memorandum

To: Assistant Inspector General for Audits

Through: Sylvia V. Baca Shayla Freeman Simmons
for Acting Assistant Secretary, Land and Minerals Management MAR - 3 2000

From: Walt Rosenbusch W Rosenbusch
Director, Minerals Management Service

Subject: Office of Inspector General Draft Audit Report, "Internal Controls Over the Accounting System, Financial Management Branch, Minerals Management Service"

Thank you for the opportunity to respond to the draft audit report on our accounting system's internal controls. We are providing to you our general comments on the audit findings, specific ones on the recommendations, and a detailed table listing specific findings and our actions taken or planned.

Please contact Bettine Montgomery at (202) 208-3976 if you have any further questions.

Attachment

Minerals Management Service Response to Draft Audit Report "Internal Controls Over the Accounting System, Financial Management Branch, Minerals Management Service"

Audit Agency: Office of the Inspector General (OIG)

Audit Number: E-IN-MMS-009-98

We welcome the opportunity to comment on this draft report. We generally concur with the report's findings and recommendations, and we have already taken corrective actions to resolve many of the deficiencies noted in the report. We offer the following comments to document our efforts to date, and also to explain our plans for additional corrective actions.

General Comments

We acknowledge that the Minerals Management Service (MMS) did not have accurate, complete, and timely financial data in FY 1998. During 1999 and 2000, we have and are implementing new accounting policies and procedures to improve the quality of our financial information. We have taken steps to correct FY 1998 and improve FY 1999 information. However, despite a yearlong focus on resolving FY 1998 accounting discrepancies, we were unable to resolve them with existing resources. Accordingly, we assembled a multi-Bureau Annual Financial Report Team (AFR Team) to resolve remaining general ledger inconsistencies and to reconcile MMS cash balances with Treasury. This was the opening phase in a longer term plan to ensure that MMS financial data relating to all fiscal years will once again be accurate and reliable. While the AFR Team has been successful in satisfying information requirements for the Department's Consolidated Financial Statements, we intend to carry our efforts to more detailed levels.

We acknowledge that the internal control system relating to our administrative accounting operations was not adequate to ensure that transactions were properly recorded, processed, and summarized to permit the preparation of financial statements in accordance with Federal accounting standards. Many of the actions taken during 1999 to enhance the quality of our financial data involved improvements to internal controls. However, we understand that a thorough review of the entire internal control environment is in order. Accordingly, we are arranging for a comprehensive review of the system and procedural controls relating to all MMS administrative accounting activities. This review will be performed by an organization outside of MMS to ensure complete objectivity of the review.

In conjunction with the review of the internal control system, we are in the process of reviewing and documenting all financial management functions performed in MMS. These reviews are drawing upon the resources of the Financial Management Branch staff, other MMS organizations, other Departmental resources, and outside consultants.

Current operating procedures, document flows, and data flows will be closely analyzed for ways of improving the efficiency and effectiveness of operations. Desktop guides are being developed covering all recurring operating procedures. This process is currently underway with a projected completion date of April 2000. During 1999, workload and accountability responsibilities were documented (including backup responsibilities) for each position in the Financial Management Branch. However, this is a living document which will be updated to account for the recent addition of new staff and the planned addition of future staff.

Comments on the Findings Presented in the Report

Account Reviews and Reconciliations

We concur with the report's general finding that inadequate reviews and reconciliations were performed to ensure that accounting transactions were properly recorded and reported in FY 1998. We also acknowledge that the values in the property system did not reconcile completely with the general ledger information in the MMS administrative accounting system (ABACIS). Following are summaries of MMS efforts relating to specific areas identified in the draft report.

General Ledger

The AFR Team devoted significant resources to resolving outstanding general ledger issues. Some of the particular areas addressed included:

- Improper journal vouchers,
- Errors relating to the Standard General Ledger conversion performed at the beginning of FY 1998,
- Discrepancies between budgetary and proprietary accounts,
- Errors resulting from improper posting models, and
- Unnatural general ledger balances.

All MMS funds were reviewed through FY 1999, and correcting general ledger entries completed. FY 2000 general ledger transactions are currently being reviewed on a monthly basis for any inconsistencies, including unnatural balances and differences between the summary and subsidiary ledgers, and necessary corrections are being made.

Cash

The task force performed a reconciliation of cash between ABACIS and Treasury. The reconciliation compared balances in each of 42 MMS funds. While a complex and difficult task, we recognized that it was necessary to ensure the integrity of MMS financial information. As a further recognition of the importance of this reconciliation, MMS will continue to work on cash even though the task force was successful in reconciling cash to acceptable materiality levels.

Cash reconciliations are now being performed monthly on a transaction basis. To facilitate the reconciliation process, new procedures were established during 1999 to better track cash receipts and OPAC transactions with MMS trading partners. However, we plan to review the entire reconciliation process again to identify approaches, formats, and procedures that will make the process more efficient.

Year-end Closeout

For fiscal year-end FY 1999, particular emphasis was placed on ensuring that transactions were recorded in the correct fiscal year. Improved year-end procedures were developed and subjected to discussion and comment by all Financial Management Branch staff. Accounting technicians also received training to augment the written closeout instructions.

The planned review and documentation of financial management operating procedures will specifically address year-end closeout activities. The review will focus on ensuring that transactions are recorded in the proper fiscal year, appropriation, and account code.

Conversion

The AFR Team analyzed the adjustments made after FY 1998 to resolve discrepancies between the closing general ledger balances in FY 1997 and the beginning balances in FY 1998. Adjustments have been made to validate and correct closing FY 1997 and beginning FY 1998 balances.

Capitalized Equipment

We recently hired a new staff member who has been assigned responsibility for performing monthly reconciliations with the existing property system. Since MMS has increased the capitalization threshold to $15,000 beginning in FY 1999, the number of items to be reconciled has decreased by more than 65%. Longer term, we are planning to replace the current property management system with one that will be integrated with ABACIS.

Inadequate Procedures

We generally concur that MMS did not have adequate procedures in place to ensure that accounting transactions were recorded and reported properly during FY 1998. Following are summaries of our efforts relating to specific areas identified in the draft report.

Federal or Public Transactions

At the beginning of FY 1999 we provided instructions to accounting technicians on how to review documents to ensure the Government/non-Government indicator is correct on ABACIS input screens. In addition, as part of the FY 1999 year-end closeout, we closely scrutinized accrual documents prepared by program staff for appropriate Government/non-Government designations. (Accrual documents were a major source of errors in FY 1998.)

Interior Franchise Fund

The MMS Interior Franchise Fund business line operations grew quickly during FY 1998. During that time, the Interior Franchise Fund was still developing as an entity with numerous accounting policy issues needing to be resolved. Some of these issues included the level of cost tracking detail required for the MMS lines of business, and the allocation of funds to operating and improvement reserves.

Recognizing that our existing accounting approaches were inadequate, in November 1998, we contracted with the accounting firm KPMG to review and make recommendations for improving the accounting practices relating to the Interior Franchise Fund lines of business operated by MMS. We implemented, or are working on their recommendations for accounting procedure improvements, cost accounting methods, cost accounting systems, and management report formats.

Based in part upon the implementation of the KPMG recommendations, the MMS Interior Franchise Fund cost accounting system, while operated within ABACIS, is able to track Interior Franchise Fund transactions separately from other MMS activities. The system records transactions, including overhead, in sufficient detail for MMS to determine whether the pricing structures for MMS business lines are adequate to recover full costs.

We worked closely with the Interior Franchise Fund staff during FY 1999 to address appropriate methods for accruing revenues and expenses. Revenues and expenses are now accrued on a monthly basis for all MMS Interior Franchise Fund business lines. This information is provided to the Interior Franchise Fund each month to be incorporated into monthly financial statements.

To improve oversight of MMS Interior Franchise Fund activities, we established a new position in early FY 1999 whose duties include reconciling MMS records with Interior Franchise Fund records. These reconciliations are now performed monthly. One of the steps remaining for us is the written documentation of the policies, procedures and staff responsibilities relating to MMS franchise operations. This effort is underway.

We take exception to the statement "the Service's appropriation used its revolving fund to supplement the cost of the Interior Franchise Fund." First, MMS does not have a revolving fund. Second, we did not use appropriated funds to supplement the cost of the

Interior Franchise Fund. At worst, we shared overhead costs for Interior Franchise Fund activities with overhead costs for similar lines of business not included in the Interior Franchise Fund. To avoid the appearance that MMS supplemented the cost of the Interior Franchise Fund lines of business from other funding, we have segregated Franchise Fund related activities from other lines of business not included in the Interior Franchise Fund.

Comments on the Recommendations Presented in the Report

We concur with all of the recommended internal control procedures presented in the draft report and, as detailed in our comments on the report's findings, we have taken numerous actions to implement these procedures. Following is a summary of our corrective actions (completed or planned) relating to each recommendation. The Chief, Budget and Finance Division, is the responsible official for implementing the recommendations. We plan to submit targets dates by the fall of 2000 after reviewing KPMG's report.

Recommendation 1. **Implement an Adequate Internal Control Structure in MMS that:**

- **Assigns responsibilities to specific individuals and holds officials accountable for noncompliance with internal controls**
- **Establishes year-end closeout procedures for general ledger and franchise fund activities**
- **Ensures that Federal v. Public transactions are properly identified**

AGREE. An assigned responsibilities listing was developed and discussed with all staff during 1999. The purpose of this list was to identify and assign primary responsibilities in the Financial Management Branch to specific individuals and to identify and assign backups for these responsibilities. This listing also supports the identification of individuals accountable for internal controls. This listing is not a static document. It will be updated for the addition of new staff and will be revised as the Financial Management Branch's functions and workload are reviewed.

Improved year-end procedures were prepared for the FY 1999 closeout. All staff members were asked to comment on the revised procedures and each step was discussed in a series of meetings called to prepare for year-end.

Instructions were provided to staff early in FY 1999 on the correct classification of government vs. non-government transactions. Since that time, new procedures have been developed for verifying government vs. non-government data recorded in ABACIS.

Written desktop procedures are being developed for all staff to assure consistency of actions and to support more readily the ability of other individuals to perform backup functions.

The accounting firm of KPMG will perform a comprehensive review of our internal controls, and make recommendations on improvements to existing controls and the addition of new controls where appropriate. This review will strengthen our assigned responsibilities listing and the accountability of specific individuals for maintaining compliance with these controls.

Recommendation 2. **Develop a cost accounting system that accumulates separately all revenues and expenses associated with the Interior Franchise Fund.**

AGREE. In November 1998, we contracted with KPMG to review our operations and to make recommendations to improve our accounting practices for the Interior Franchise Fund lines of business operated by MMS. KPMG provided recommendations to improve our cost accounting procedures. As a result of these recommendations, spreadsheets have been set up to track the revenues and expenses of the MMS franchising activities by business line. This information is provided to the Interior Franchise Fund each month to be incorporated into its monthly financial statements.

We have implemented a cost accounting system, operated within ABACIS, that tracks MMS Interior Franchise Fund activities separately from other MMS activities. The system records transactions in sufficient detail to allow an assessment of whether the pricing structures for MMS business lines are adequate to recover full cost of operations.

Recommendation 3. **Apply the accrual method of transaction reporting to MMS Interior Franchise Fund activities in accordance with generally accepted accounting standards.**

AGREE. Again, in part as a result of the KPMG review of our operations and accounting practices for the MMS Interior Franchise Fund activities, we have implemented new procedures for tracking Interior Franchise Fund related transactions. Spreadsheets have been developed to track accruals and overhead fees earned for each business line. This information is now reported to the Interior Franchise Fund on a monthly basis. We will document these procedures as part of the planned documentation of all MMS financial management functions.

Conclusions

In summary, we concur with the majority of the OIG's findings. It is also important to note that although we did not receive this report on FY 1998 internal control issues until

October 1999, we had already recognized many of these problems and had taken steps to address them, e.g., bringing in KPMG to review our Interior Franchise Fund operations and make recommendations on improvements. Some improvement steps are ongoing, e.g., the written documentation of all procedures. Other improvement steps will be initiated in the next few months, e.g., having KPMG perform a comprehensive review of our accounting operations.

A more detailed listing of the OIG's findings follows. This list also identifies our concurrence or non-concurrence with each of these findings, and comments on the steps we have taken or plan to take to address the findings.

Detailed Listing of OIG Comments and

Actions Taken or Planned by the Minerals Management Service

OIG Comment	Where Found	Concur/ Non-Concur	Action Taken/Planned
"the financial data were not accurate, were incomplete, and were not timely."	Page 1, Paragraph 1	Concur	Contracted for accounting support from National Business Center (NBC). Assembled multi-bureau Annual Financial Report Team (AFR Team) to assist in resolving outstanding issues.
"control deficiencies occurred because Service personnel did not follow established internal controls, such as performing account reconciliations and providing management oversight of the financial management accounting processes, and the Service did not establish adequate internal controls to ensure that transactions were properly classified during the conversion to the new standard general ledger."	Page 3, paragraph 2 – Results of Audit	Concur	While a number of actions have been taken to improve internal controls, we also plan to utilize the services of KPMG to conduct a comprehensive review of our controls and our operations.

OIG Comment	Where Found	Concur/ Non-Concur	Action Taken/Planned
"did not have sufficient internal control procedures to ensure proper accounting of the Interior Franchise Fund…funds in the Interior Franchise Fund were commingled with Service funds."	Page 3, paragraph 2 – Results of Audit	Concur with one exception	In November 1998, we contracted with KPMG to review our operations and to make recommendations to improve our accounting practices for the Interior Franchise Fund lines of business operated by MMS. The MMS did not commingle appropriated funds with Interior Franchise Fund funded activities. At worst, overhead costs for Interior Franchise Fund funded activities were commingled with overhead costs for similar lines of business not funded by the Interior Franchise Fund. To more clearly delineate the separate funding of these overhead costs, MMS has segregated its Franchise Fund related activities from these other lines of business.
"did not review or reconcile financial data to ensure that accounting transactions were recorded and reported accurately during fiscal year 1998."	Page 3, paragraph 3 – Account Reviews and Reconcilia-tions	Concur	New procedures have been put into place to reconcile cash and are being put into place to reconcile other financial data on a regular basis.
"values in the property system did not support the general ledger balance."	Page 3, paragraph 3 – Account Reviews and Reconcilia-tions	Concur	We have hired a new staff member whose responsibilities include performing a monthly reconciliation of the property system and ABACIS.
"the amount for each accounts payable transaction was not recorded in the subsidiary ledger."	Page 3, paragraph 4 – General Ledger	Concur	New procedures are being developed to require monthly reviews and reconciliations of general and subsidiary ledgers. Responsibility for these reviews and reconciliations has been assigned to the Chief of Accounting Operations.

OIG Comment	Where Found	Concur/ Non-Concur	Action Taken/Planned
"did not perform monthly cash reconciliations for any of its 13 funds during fiscal year 1998."	Page 4, paragraph 3 – Cash	Concur	A new staff member was hired late in FY 1998 and trained during FY 1999 whose primary responsibility is the monthly reconciliation of cash. Written procedures are being developed to ensure that all steps necessary to reconcile cash fully are completed each month.
"fiscal year 1998 transactions were included in the fiscal year 1999 subsidiary account balances in the ABACIS accounting system…The Service prepared adequate year-end procedures; however, the accounting staff did not follow these procedures."	Page 5, paragraph 3 – Year-end Closeout	Concur	Year-end procedures were improved for FY 1999. All staff were asked to comment on the revised procedures and each step was discussed in a series of meetings called to prepare for the year-end closeout.
"One hundred twenty five invoices were not date stamped"	Page 6, bullet 1	Concur	Both a new scanning system and new procedures have been set up to ensure that information is properly recorded.
"Fifteen account numbers in the ABACIS accounting system did not agree with the account numbers on the purchase order"	Page 6, bullet 2	Concur	New desk procedures are being developed for all positions to ensure that all primary staff and all backup staff are aware of the responsibilities of their jobs.
"Nine paid invoices were not approved."	Page 6, bullet 3	Concur	New desk procedures are being developed for all positions to ensure that all primary staff and all backup staff are aware of the responsibilities of their jobs
"the conversion did not properly include all of the general ledger account balances. Consequently, the Minerals Management Service created a balancing account…Because the Service did not reconcile the $69 million to identify the adjustments needed in the ABACIS accounting system records, we found, in August 1998, that the fiscal year 1997 ending balances audited were not equal to the fiscal year 1998 opening balances."	Page 6, Paragraph 6, Conversion	Concur	This was one of the issues addressed by the NBC staff and the AFR Team. They have successfully reconciled the balancing account and corrected ending and opening balances.

OIG Comment	Where Found	Concur/ Non-Concur	Action Taken/Planned
"The Service did not have sufficient internal control procedures to ensure that the general ledger control balance for Property, Plant and Equipment was accurately stated and supported by detailed subsidiary information…the Service did not periodically reconcile the property management records to the Service's general ledger"	Page 6, paragraph 7 & page 7, paragraph 1 – Capitalized Equipment	Concur	We have hired a new staff member whose responsibilities include performing a monthly reconciliation of the property system and ABACIS.
"did not have adequate procedures to ensure that accounting transactions were recorded and reported properly during fiscal year 1998"	Page 7, paragraph 2 – Inadequate Procedures	Concur	While a number of actions have been taken to improve internal controls, we also plan to utilize the services of KPMG to conduct a comprehensive review of our controls and our operations.
"did not have adequate internal controls to ensure that transactions were properly classified as Federal (government) or Public (nongovernment) in the general ledger accounts."	Page 7, paragraph 3 – Federal or Public Transactions	Concur	Instructions were provided to staff early in FY 1999 on how to classify government vs. non-government transactions. New procedures have been developed to verify data in the system.

OIG Comment	Where Found	Concur/ Non-Concur	Action Taken/Planned
"did not have sufficient internal control procedures to ensure the proper accounting of the Department of the Interior's Franchise Fund...did not (1) develop a cost accounting system to determine whether the pricing structure was adequate to recover full costs; (2) implement accrual accounting procedures to record expenses incurred or revenues received in accordance with accounting standards; and (3) provide oversight over the Fund by establishing written accounting procedures or reviewing accounting data."	Page 7, paragraph 4 – Interior Franchise Fund	Concur	In November 1998, we contracted with KPMG to review our operations and to make recommendations to improve our accounting practices for the Interior Franchise Fund lines of business operated by MMS. Spreadsheets have been developed to track accruals and overhead fees earned. This information is submitted monthly to the Interior Franchise Fund. Revenues and expenses of the MMS franchising activities are tracked in another spreadsheet for each business line and provided to the Interior Franchise Fund to be incorporated into monthly financial statements. Procedures have been developed to improve the processing of documents.
"the Service's appropriation used its revolving fund to supplement the cost of the Interior Franchise Fund."	Page 7, paragraph 4 – Interior Franchise Fund	Non-Concur	(1) the Service does not have a revolving fund, (2) the Service did not use appropriated funds to supplement the cost of the Interior Franchise Fund, (3) at worst, the Service shared its overhead costs for the Interior Franchise Fund activities with overhead costs for similar lines of business not included in the Interior Franchise Fund. To ensure that improper supplementing of costs cannot happen in the future, the Service has segregated its Franchise Fund related activities from other lines of business not included in the Interior Franchise Fund.

STATUS OF AUDIT REPORT RECOMMENDATIONS

Finding/Recommendation Reference	Status	Action Required
1	Resolved; not implemented.	No further response to the Office of Inspector General is required. The recommendation will be referred to the Assistant Secretary for Policy, Management and Budget for tracking of the implementation.
2 and 3	Implemented.	No further action is required.

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