



United States Department of the Interior

OFFICE OF INSPECTOR GENERAL
Washington, D.C. 20240

May 31, 2001

Memorandum

To: Assistant Secretary for Policy, Management and Budget

Subject: Independent Auditors Report on Departmental Offices Financial Statements for Fiscal Year 2000 (No. 01-I-407)

We found that the Departmental Offices (DO) principal financial statements¹ for fiscal year 2000 were fairly presented in all material respects. We also found that the DO was in compliance with applicable laws and regulations. Our tests of the DO's internal controls, however, identified four material weaknesses. Our detailed findings are in the independent auditors report.

We identified material weaknesses related to Tribal and Other Special Trust Funds, costs charged to construction in progress, undelivered orders, and Interior Franchise Fund (IFF) financial reporting as follows:

- **Tribal and Other Special Trust Funds.** The Office of Trust Funds Management, within the Office of the Special Trustee for American Indians, lacked effective internal controls over managing and accounting for Tribal and Other Special Trust Funds and did not have dependable accounting systems and reliable accounting information.
- **Construction in Progress.** The DO's internal controls over costs charged to construction in progress under the Central Utah Project Completion Act were inadequate to ensure the reliability and accuracy of the construction-in-progress and other related accounts. We identified expenditures of nearly \$66 million that should have been recorded in other general ledger accounts.
- **Undelivered Orders.** The DO did not establish policies and procedures to ensure that the year-end undelivered orders balance was accurate and reliable, requiring the DO to decrease the undelivered orders balance by \$7.6 million for accrued accounts payable and deobligate \$8.2 million for invalid undelivered orders.

¹The DO's principal financial statements consist of the Consolidated Balance Sheet as of September 30, 2000; the Consolidated Statement of Net Cost and Consolidated Statement of Changes in Net Position for the fiscal year ended September 30, 2000; and the Combined Statement of Budgetary Resources and Combined Statement of Financing for the fiscal year ended September 30, 2000.

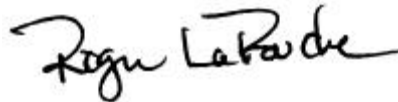
- **IFF Financial Reporting.** The IFF's financial reporting process lacked key controls, including monitoring relationships with and disbursements to service providers and adequately controlling check receipts, deposits, and accounts receivable balances. In addition, there is doubt as to whether the IFF will continue after its authorizing legislation expires on October 1, 2001.

We made seven recommendations to address the weaknesses identified in our tests of the DO's internal controls. The DO concurred with the seven recommendations. Based on the DO's response to our draft report (Appendix 3), we consider the recommendations resolved but not implemented. Accordingly, the recommendations will be referred to the Assistant Secretary for Policy, Management and Budget for tracking of implementation.

Since the recommendations are considered resolved, no further response to the Office of Inspector General is required (see Appendix 4).

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.

The independent auditors report, which includes the DO's Annual Report, is intended for the information of management of the Department of the Interior, the Office of Management and Budget, and the Congress. The report, however, is a matter of public record, and its distribution is not limited.



Roger La Rouche
Assistant Inspector General
for Audits

[CONTACT THE ASSISTANT SECRETARY FOR POLICY, MANAGEMENT AND BUDGET FOR INFORMATION ON THE DEPARTMENTAL OFFICES=FINANCIAL STATEMENTS FOR FISCAL YEAR 2000, WHICH ARE NOT INCLUDED.]

Independent Auditors Report Departmental Offices Financial Statements Fiscal Year 2000

We have audited the Departmental Offices (DO) principal financial statements for the fiscal year ended September 30, 2000. The DO's principal financial statements consist of the Consolidated Balance Sheet as of September 30, 2000; the Consolidated Statement of Net Cost and Consolidated Statement of Changes in Net Position for the fiscal year ended September 30, 2000; and the Combined Statement of Budgetary Resources and Combined Statement of Financing for the fiscal year ended September 30, 2000. These financial statements are the responsibility of DO, and our responsibility is to express an opinion, based on our audit, on these principal financial statements.

Our audit was conducted in accordance with generally accepted auditing standards; "Government Auditing Standards," issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin 01-02, "Audit Requirements for Federal Financial Statements." These standards require that we plan and perform the audit to obtain reasonable assurance as to whether the accompanying principal financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures contained in the principal financial statements and the accompanying notes. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation.

We believe that our audit work provides a reasonable basis for our opinion. The objectives, scope, and methodology of our work are discussed in Appendix 1. Previous Office of Inspector General reports with significant unresolved or unimplemented recommendations related to DO's financial statements or internal controls are summarized in Appendix 2.

We did not audit the financial statements of the Interior Franchise Fund (IFF), which reflect total assets and expenses constituting 7 percent and 11 percent, respectively, of the consolidated totals of DO. In addition, we did not audit the amounts included by the Office of the Special Trustee for American Indians in the Fund Balance with Treasury, Treasury Securities, Other Government Securities, and Public Securities accounts, which represent 15 percent of the total consolidated assets of DO. Our opinion as it relates to amounts included for IFF and for accounts included by the Office of the Special Trustee for American Indians is based solely on the work of other auditors.

The Office of Inspector General is not entirely independent with respect to amounts pertaining to its financial operations that are included in DO's consolidated financial statements. The fiscal year 2000 financial amounts for the Office of Inspector General represent less than 1 percent of the DO's consolidated assets and less than 3 percent of its operating expenses. The Office of Inspector General, however, is considered organizationally independent with respect to all other aspects of DO's financial management activities.

Opinion on Principal Financial Statements

In our opinion, the principal financial statements appearing on pages 43 to 65 present fairly, in all material respects, the consolidated financial position of DO as of September 30, 2000 and its consolidated net cost and changes in net position and combined budgetary resources and financing activities for the fiscal year ended September 30, 2000 in conformity with generally accepted accounting principles.

Our audit was conducted to form an opinion on the principal financial statements taken as a whole, and our opinion relates only to the principal financial statements. The supplemental financial and management information contained in DO's Annual Report is presented for additional analysis and is not a required part of the principal financial statements but is supplementary information required by the Federal Accounting Standards Advisory Board or OMB Bulletin 97-01, "Form and Content of Agency Financial Statements," as amended. We have applied limited procedures, including discussions with management, on the methods of measurement and presentation of this information to ensure compliance with OMB guidance and consistency with the financial

statements. We did not subject this information, however, to the auditing procedures applied in our audit of the principal financial statements, and we therefore do not express an opinion on the information.

DO prepared the accompanying consolidated financial statements and supplemental consolidating statements assuming that the IFF will continue. As discussed in Note 1A to the consolidated financial statements, the expiration of IFF's authorizing legislation on October 1, 2001 creates an uncertainty about IFF's ability to continue. Management plans regarding this matter are also described in Note 1A. The financial statements do not include any adjustments that might be necessary if IFF did not continue.

Report on Internal Controls

Our audit was conducted in accordance with generally accepted auditing standards; "Government Auditing Standards," issued by the Comptroller General of the United States; and OMB Bulletin 01-02. In planning and performing our audit, we obtained an understanding of DO's internal controls to determine whether the controls had been placed in operation. We also assessed control risks and tested the controls to determine our auditing procedures to express an opinion on the principal financial statements. We limited our internal control testing to those controls necessary to achieve the objectives described in OMB Bulletin 01-02. We did not test all internal controls relevant to operating objectives as broadly defined by the Federal Managers' Financial Integrity Act 1982. The objective of our audit was not to provide assurance on internal controls, and we therefore do not provide an opinion on the internal controls.

Our consideration of the internal controls over financial reporting would not necessarily disclose all matters in these controls that might be reportable conditions (matters that in our judgment should be communicated to agency management). These matters relate to significant deficiencies in the design or operation of the agency's internal control structure that could adversely affect the agency's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. There are basically two levels of reportable conditions: those that are considered significant enough to affect the fair presentation of the financial statements (material weaknesses) and those that, while not material, are significant matters that merit management's attention. We noted certain matters involving the

internal controls and their operation that we considered to be material weaknesses.

Material Weaknesses

We identified four internal control deficiencies that we believe constitute material weaknesses, as discussed in the following paragraphs.

A. DO Needs Improved Controls Over Tribal and Other Special Trust Funds

The Office of Trust Funds Management (OTFM) within the Office of Special Trustee lacked effective internal controls over managing and accounting for Tribal and Other Special Trust Funds and did not have dependable accounting systems and reliable accounting information.

The independent auditors report on trust funds concluded that (1) cash balances reflected in the combined financial statements were materially greater than balances reported by the U.S. Treasury; (2) inadequacies in DO's various Trust Fund historical accounting systems and subsystems, controls, and records caused the systems to be unreliable; and (3) various tribal organizations with financial assets held in trust by OTFM did not agree with certain accountings and balances recorded by OTFM and have filed or are expected to file claims against the United States. The internal control weaknesses may result in a potential liability to the U.S. Government that is not reasonably estimable. DO's corrective action plan for these weaknesses is in the High Level Implementation Plan.

Recommendation: We recommend that the Assistant Secretary, Policy, Management and Budget and the Office of Special Trustee implement the High Level Implementation Plan as revised and updated on February 29, 2000. DO agreed with our recommendation.

B. DO Needs Improved Controls Over Costs Charged to Construction In Progress

DO did not have adequate internal controls over costs charged to construction-in-progress (CIP) related to the Central Utah Project Completion Act to ensure that the September 30, 2000 account balances for CIP and other related accounts were accurate and reliable.

We identified expenditures for land and water rights (\$38.98 million), a completed project (\$2.67 million), projects in abeyance (\$12.63 million), and advance payments for acquiring water rights (\$11.44 million) in the CIP balance as of September 30, 2000. These costs should be recorded in other general ledger accounts, as appropriate. Because of a timing difference in the Central Utah

Water Conservancy District's (CUWCD) reporting of expenditures, the CIP account did not include \$7.13 million in construction costs for the fourth quarter of fiscal year 2000 (July through September). In addition, construction costs of \$7.05 million for the fourth quarter of fiscal year 1999 were not accrued in the fiscal year 1999 financial statements. The beginning balances were therefore incorrect, and a prior period adjustment was required for the September 30, 2000 statements. When informed of these deficiencies, DO made the adjustments necessary to reflect more accurate account balances.

Recommendations: We recommend that the Assistant Secretary, Policy, Management and Budget take the following actions:

1. **Related to land and water rights costs and advances for acquisition of water rights included in CIP:** (a) identify and transfer all land and water rights costs in the CIP account to the Land account; disclose those land costs in the property, plant, and equipment note to the financial statements; and record future land costs in the Land account and (b) identify and transfer all advance payments for water rights acquisition in the CIP account to the Advances to Others account and record future payments to the Advances to Others account.
2. **Related to projects in abeyance:** (a) reclassify construction costs for projects in abeyance from the CIP account to an appropriate asset account; (b) disclose the current status of projects in abeyance in a note to the financial statements; and (c) develop and implement policies and procedures to identify and remove projects in abeyance from the CIP account and reclassify project costs to the appropriate asset account.
3. **Related to completed projects:** (a) transfer the cost of completed projects to Other Structures and Facilities and record any applicable depreciation expense and (b) develop and implement policies and procedures to transfer completed CIP projects to the Other Structures and Facilities account in a timely manner.
4. **Related to CUWCD's fourth quarter costs:** (a) make an adjusting journal entry for CUWCD's fiscal year 2000 fourth quarter expenditures, (b) make a prior period adjustment for CUWCD's fiscal year 1999 fourth quarter expenditures, and (c) develop and implement policies and

procedures to account for CUWCD's fourth quarter costs in the proper accounts and in the proper period.

DO agreed with our recommendations and stated that it would coordinate with the Central Utah Project manager to develop plans for implementing the recommendations.

C. DO Needs Improved Controls over Undelivered Orders

DO did not establish policies and procedures to ensure that the year-end undelivered orders balance was accurate and reliable. DO did not liquidate obligations, accrue liabilities, or record expenditures for all goods or services received by September 30. In addition, invalid obligations existed for orders that should have been terminated and/or de-obligated because there had been no expenditures against the obligations for several years and/or the agreement period had expired.

When informed of the results of the our tests, DO analyzed its undelivered orders and corrected related account balances by accruing \$7.6 million in accounts payable and expenses, decreasing the undelivered orders balance by \$7.6 million for accrued accounts payable and expenses, and de-obligating \$8.2 million for invalid undelivered orders.

Recommendation: We recommend that the Assistant Secretary, Policy, Management and Budget establish and implement policies and procedures to review year-end undelivered orders to ensure that (1) liabilities and expenses for goods and services received but not paid are accrued and the undelivered orders balance reduced accordingly and (2) undelivered orders with funds remaining after the agreement period or with no activity or expenditures for 2 years are evaluated and de-obligated as appropriate.

DO agreed with the recommendation and responded that an automated program will be initiated to de-obligate undelivered orders with funds remaining after the agreement period and with no activity for more than 2 years. The exceptions to this automated process will be grants that have to be reviewed by the Office of Insular Affairs and Permanent Change of Station travel and contracts that have to be processed separately because of procurement policies and procedures. In addition, DO has initiated a review of undelivered orders to determine the validity of the outstanding balances, bring all orders over 2 years old with no recent activity to the attention of appropriate program personnel, and take immediate action to de-obligate invalid obligations upon notification by program personnel.

D. IFF Needs Improved Controls Over Financial Reporting

The independent auditors reported that the IFF financial reporting process lacked key controls, including monitoring relationships with and disbursements to service providers,¹ documentation of policies and procedures for year-end closing; adequate pricing knowledge; controls over check receipt, deposits, and accounts receivable balances; and risk assessments and controls for software changes by an IFF service provider.

In addition, the auditors noted that IFF's authorizing legislation is scheduled to expire on October 1, 2001, raising substantial doubt about IFF's ability to continue. Management plans in regard to these matters are described in Note 1A to the consolidated financial statements. The independent auditors made specific recommendations addressing each of the issues reported.

Recommendation: We recommend that the Assistant Secretary, Policy, Management and Budget implement any recommendation made by the independent auditors that would improve controls over IFF's financial reporting process.

DO agreed with our recommendation.

The Department reported the weaknesses related to Finding A as a material weakness in its fiscal year 2000 Accountability Report; the other three material weaknesses, however, were not reported in the Department's or DO's annual assurance statements required by the Federal Managers' Financial Integrity Act.

Stewardship and Performance Measures

We also considered DO's internal controls over the Required Supplementary Stewardship Information. We obtained an understanding of DO's internal controls, determined whether the controls had been placed in operation, assessed control risk, and tested the controls, as required by OMB Bulletin 01-02. Our objective, however, was not to provide assurance on these controls, and we therefore do not provide an opinion on the controls.

Finally, with respect to internal controls related to performance measures reported in the Overview, we obtained an understanding of the design of the significant internal controls relating to the existence and completeness assertions, as required by OMB Bulletin 01-02. Our procedures were not designed to provide

¹The IFF has established subcontracting relationships with other Department of the Interior bureaus (service providers) to deliver products and services to IFF customers.

assurance over these internal controls, however, and we do not provide an opinion on the controls.

Report on Compliance with Laws and Regulations

We conducted our audit in accordance with generally accepted auditing standards; the “Government Auditing Standards,” issued by the Comptroller General of the United States; and OMB Bulletin 01-02. DO management is responsible for complying with applicable laws and regulations. As part of obtaining reasonable assurance as to whether DO’s financial statements were free of material misstatement, we tested DO’s compliance with (1) certain provisions of laws and regulations that if not complied with could directly and materially affect the determination of financial statement amounts and (2) certain other laws and regulations specified in OMB Bulletin 01-02, including the requirements referenced in the Federal Financial Management Improvement Act of 1996. We limited our tests of compliance to these provisions and did not test compliance with all laws and regulations applicable to DO.

The results of our tests of compliance with laws and regulations, exclusive of the Federal Financial Management Improvement Act, did not disclose any instances of noncompliance that are required to be reported under “Government Auditing Standards” or OMB Bulletin 01-02.

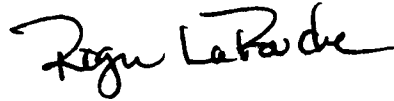
The Federal Financial Management Improvement Act requires that we report whether DO’s financial management systems substantially comply with (1) federal financial management system requirements, (2) applicable federal accounting standards, and (3) the U.S. Government Standard General Ledger at the transaction level. To meet this requirement, we tested compliance of DO’s financial management systems with Section 803(a) of the Act. The results of our tests disclosed no instances in which DO’s financial management systems did not substantially comply with the three requirements discussed above.

Providing an opinion on compliance with certain provisions of laws and regulations was not an objective of our audit, and, accordingly, we do not express such an opinion.

Based on DO's response (see Appendix 3), we consider all seven recommendations resolved but not implemented and will refer them to the Assistant Secretary for Policy, Management and Budget for tracking of implementation. Since the recommendations are considered resolved, you do not need to respond further to us (see Appendix 4).

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

The report is intended for the information of management of the Department of the Interior, Office of Management and Budget, and Congress. This report is a matter of public record, however, and its distribution is not limited.

A handwritten signature in black ink, reading "Roger LaRouche". The signature is fluid and cursive, with the first name "Roger" and last name "LaRouche" clearly distinguishable.

Roger La Rouche
Assistant Inspector General for Audits
February 14, 2001

Objective, Scope, and Methodology

DO management is responsible for the following:

- Preparing the principal financial statements and the required supplementary information in conformance with generally accepted accounting principles and other information contained in the Annual Report for fiscal year 2000.
- Establishing and maintaining an internal control structure over financial reporting. In fulfilling this responsibility, DO is required to assess the expected benefits and related costs of internal control structure policies and procedures.
- Complying with applicable laws and regulations.

We are responsible for the following:

- Expressing an opinion on DO's principal financial statements.
- Obtaining an understanding of internal controls based on the internal control objectives in OMB Bulletin 01-02, which require that (1) transactions be properly recorded, processed, and summarized to permit preparation of the principal financial statements and the required supplementary information in accordance with federal accounting standards; (2) assets be safeguarded against loss from unauthorized acquisition, use, or disposal; and (3) transactions and other data supporting reported performance measures be properly recorded, processed, and summarized to permit the preparation of performance information in accordance with criteria stated by management.
- Testing DO's compliance with selected provisions of laws and regulations that could materially affect the principal financial statements or the required supplementary information.

To fulfill these responsibilities, we took the following actions:

- Examined, on a test basis, evidence supporting the amounts disclosed in the principal financial statements.
- Assessed the accounting principles used and the significant estimates made by management.
- Evaluated the overall presentation of the principal financial statements.

- Obtained an understanding of the internal control structure related to safeguarding assets; compliance with laws and regulations, including the execution of transactions in accordance with budget authority; financial reporting; and certain performance measures information reported in the Annual Report.
- Tested relevant internal controls over the safeguarding of assets; compliance with laws and regulations, including the execution of transactions in accordance with budget authority; and financial reporting.
- Tested compliance with selected provisions of laws and regulations.

We did not evaluate all of the internal controls related to the operating objectives as broadly defined by the Federal Managers' Financial Integrity Act, such as those controls related to preparing statistical reports and ensuring efficient operations. We limited our internal control testing to those controls needed to achieve the objectives outlined in our report on internal controls.

Prior Audit Coverage

Our review of Office of Inspector General and General Accounting Office audit reports did not disclose any General Accounting Office reports with significant unresolved or unimplemented recommendations related to DO's financial statements or internal controls. We found one Office of Inspector General report with significant unresolved or unimplemented recommendations that we considered to be material weaknesses, as follows:

Our May 2000 report "Independent Auditors Report on the Financial Statements for Fiscal Years 1998 and 1997 for the Office of the Special Trustee for American Indians Tribal and Other Special Trust Funds and Individual Indian Monies Trust Funds Managed by the Office of Trust Funds Management" (No. 00-I-434) issued qualified opinions because cash balances were materially greater than those reported by the U.S. Treasury, major deficiencies in accounting system controls and records caused the systems to be unreliable, and certain Trust Fund beneficiaries disagreed with balances recorded by the Office of Trust Funds Management and had filed or were expected to file claims against the Office. These conditions prevented the auditors from auditing the cash and Trust Funds balances and receipts and disbursements. In addition, a potential liability to the federal government existed because of the lawsuits filed by the Trust Fund beneficiaries. Of the 42 issues reported, 23 recommendations remained unimplemented as of September 30, 2000.



United States Department of the Interior

OFFICE OF THE SECRETARY
Washington, D.C. 20240

APR 13 2001

Memorandum

To: Roger La Rouché
Assistant Inspector General for Audits

From: Bob Lamb *Bob Lamb*
Assistant Secretary for Policy, Management and Budget

Subject: Response to the Auditors Report on Departmental Offices Financial Statements for Fiscal Year 2000

This memorandum is in response to the Draft Independent Auditors Report on the Departmental Offices Financial Statements for Fiscal Year 2000. We concur with the findings and recommendations.

The appropriate offices are aware of the material weaknesses and have been given the responsibility for actions necessary to increase internal controls as follows:

A. DO Needs Improved Controls Over Tribal and Other Special Trust Funds

Responsible Office(s) or Personnel: Office of Trust Funds Management

B. DO Needs Improved Controls Over Costs Charged to Construction in Progress

Responsible Office(s) or Personnel: Central Utah Mitigation Commission, Central Utah Project Manager, Bureau of Reclamation

C. DO Needs Improved Controls Over Undelivered Orders

Officials Responsible: Program, Budget, and Accounting Personnel

Note: An automated program to deobligate undelivered orders remaining after the agreement period and where there has been no activity for more than 2 years will be initiated. The exception to this process will be the grants that will have to be reviewed by the Office of Insular Affairs. PCS travel and contracts will be processed separately as well due to procurement policy and procedures.

The General Accounting Branch, Division of Financial Management, has initiated an ongoing review of undelivered orders to determine the validity of the outstanding balances. All documents that are over two years old with no recent activity are brought to the

attention of the appropriate program personnel for examination. Immediate action is taken to deobligate the invalid obligations upon notification by the program personnel.

The Operations Accounting Group, DOI Financial Officers Partnership, is reviewing department-wide policies and procedures relating to undelivered orders and accruals at the bureau levels. The group will be making recommendations for improved internal controls over undelivered orders and accruals for the Department of the Interior.

D. IFF Needs Improved Controls Over Financial Reporting

Officials Responsible: National Business Center, Products and Services

Note: Effective May 1, 2001, the Franchise Fund support is being transferred to the National Business Center, Products and Services, Denver, Colorado, which is aware of the audit findings.

cc: R. Schuyler Leshner, Director
Office of Financial Management

Timothy G. Vigotsky, Director,
National Business Center

Status of Audit Report Recommendations

Findings/Recommendations Reference	Status	Action Required
A, B, C, and D	Resolved; Not Implemented	No further response to the Office of Inspector General is required. We will forward the recommendations to the Assistant Secretary for Policy, Management and Budget for tracking of implementation. The target dates and titles of the officials responsible for implementation should be provided to the Office of Financial Management