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

AUDIT REPORT

COSTS RECOVERED THROUGH NET RECEIPTS SHARING DEDUCTIONS, MINERALS MANAGEMENT SERVICE AND BUREAU OF LAND MANAGEMENT

REPORT NO. 98-I-79
OCTOBER 1997

United States Department of the Interior

OFFICE OF INSPECTOR GENERAL
Washington, D.C. 20240

NOV 18 1997

MEMORANDUM

TO: The Secretary

FROM: Wilma A. Lewis
Inspector General

SUBJECT SUMMARY: Final Audit Report for Your Information - "Costs Recovered Through Net Receipts Sharing Deductions, Minerals Management Service and Bureau of Land Management" (No. 98-I-79)

Attached for your information is a copy of the subject final audit report. The objective of the audit was to determine whether the Minerals Management Service, the Bureau of Land Management, and the Department of Agriculture's U.S. Forest Service properly identified and allocated onshore mineral leasing costs and deducted the appropriate amounts from the states' mineral leasing receipts.

We found that the cost sharing deductions were computed efficiently and deducted from the states' mineral leasing receipts on a timely basis. However, we also noted that the methodologies used by the three agencies did not result in equitable distribution of mineral leasing program costs for fiscal years 1994 through 1996. As a result, net receipts sharing deductions were overstated by $8.8 million for this time period. We also noted that the Congressionally approved method for cost sharing deductions effective in fiscal year 1997 may not accurately compute the deductions. We recommended that the Minerals Management Service and the Bureau of Land Management establish consistent policies and procedures to guide the net receipt determination process and to improve communication with the states. We further recommended that the Bureau obtain a Solicitor's opinion on whether preleasing costs were allocable cost deductions to the states.

The Minerals Management Service and the Bureau concurred with Recommendation 1, which was addressed to both bureaus, and the Bureau agreed with Recommendation 2. Based on the responses, we considered Recommendation 1 resolved but requested that the Service provide additional information on target dates and responsible officials, and we considered Recommendation 2, which was addressed to the Bureau, resolved but not implemented.

If you have any questions concerning this matter, please contact me at (202) 208-5745 or Mr. Robert J. Williams, Assistant Inspector General for Audits, at (202) 208-4252.

Attachment

C-IN-MOA-002-96

United States Department of the Interior

OFFICE OF INSPECTOR GENERAL
Washington, D.C. 20240

OCT 22 1997

AUDIT REPORT

Memorandum

To: Director, Bureau of Land Management
Director, Minerals Management Service

From: Robert J. Williams
Assistant Inspector General for Audits

Subject: Audit Report on Costs Recovered Through Net Receipts Sharing Deductions, Minerals Management Service and Bureau of Land Management (No. 98-I-79)

INTRODUCTION

This report presents the results of our review of costs recovered through net receipts sharing deductions. The objective of this review was to determine whether the Minerals Management Service, the Bureau of Land Management, and the Department of Agriculture's U.S. Forest Service properly identified and allocated onshore mineral leasing program costs and deducted the appropriate amounts from the states' mineral leasing receipts.

BACKGROUND

Three Federal agencies are involved in administering the Federal onshore mineral leasing program as follows: the Bureau of Land Management issues leases, monitors production, and ensures compliance with lease terms for most Federal land, including certain Forest Service land; the Forest Service coordinates with the Bureau to monitor production and to ensure compliance with lease terms for Forest Service land; and the Minerals Management Service collects and distributes revenues generated under the program.

Net receipts sharing is an administrative process in which Federal and state governments share the cost of managing the Federal onshore mineral leasing program. The Service, the Bureau, and the Forest Service are responsible for identifying their respective program appropriation and allocating the identified amounts among the states. On a monthly basis, the Service deducts these amounts as the net receipts costs from the states' mineral leasing receipts.

Before fiscal year 1991, the Federal Government bore the full costs of administering the program, which have averaged about $120 million annually for the three Federal agencies. However, beginning in fiscal year 1991, the Congress required the states to pay a portion of these program costs. The Congress, with cost data provided by the three agencies, set the amount of the cost deductions at $33.4 million, $34.2 million, and $38.0 million, respectively, in the Department of the Interior's budget appropriation acts for fiscal years 1991, 1992, and 1993.

The Omnibus Budget Reconciliation Act of 1993 (Public Law 103-66, Title X, Subtitle C, Section 10201) legislatively instituted a multistep process for net receipts sharing and established, as of fiscal year 1994, the general methodologies for identifying and allocating the amount of the enacted appropriation to be deducted from the states' mineral receipts (the process is detailed in Appendix 1). These methodologies, which involved computing multiple cost pools,[1] were developed by the Service in consultation with the Congress and were reviewed and approved by a major public accounting firm. The program cost deductions for fiscal years 1994, 1995, and 1996 were $26.5 million, $25.7 million, and $23.7 million, respectively (cost deductions by individual state are in Appendix 2). The decrease in cost deductions beginning in fiscal year 1994 reflects the change in the methods required under the Act, as well as certain revisions in the Service's cost identification and allocation procedures (see the Results of Audit section).

In fiscal year 1995, the Service distributed $477.5 million in mineral leasing revenues to 37 states. Six western states accounted for 94 percent of these distributions as follows: Wyoming, 45 percent; New Mexico, 25 percent; Colorado, 7 percent; Utah, 7 percent; California, 5 percent; and Montana, 5 percent. The states' share of revenues is a percentage determined by statute and is based on land category, such as public domain or acquired lands, and also by the source of revenues, such as oil and gas lease rents, coal royalties, or other mineral bonuses. For example, the Mineral Leasing Act of 1920, as amended, provides for each state to receive 50 percent of revenues generated by Federal mineral leases located on public lands within the state. (Alaska is an exception; that is, under its Statehood Act, Alaska receives a 90 percent distribution of mineral leasing revenues in the State.) About 99 percent of mineral lease revenues are distributed under the Act. Other revenue distribution percentages ranging from 25 to 100 percent are stipulated in separate minerals legislation. For example, states receive 25 percent of mineral revenues derived from acquired National Forest lands (16 U.S.C. 499) and 75 percent of mineral revenues from lands administered by the U.S. Army Corps of Engineers (33 U.S.C. 701C-3).

---

[1]The cost pool is the accumulation of all identified costs associated with administering the Federal onshore program. Each Federal agency develops its own cost pool for the net receipts sharing process.

The Minerals Management Service, in its capacity as the lead agency for the net receipts sharing process, accumulates the cost pool data for the onshore program from the three Federal agencies, computes the cost deduction for each state, and subtracts the amount from each state's monthly distribution of mineral leasing receipts. Because the three agencies have separate budget processes and mineral-related responsibilities, they have established different methodologies for identifying costs associated with the Federal onshore program and for allocating these costs to the states (the methodologies used by each Federal agency for identifying and allocating costs are detailed in Appendix 3).

SCOPE OF AUDIT

To accomplish our audit objective, we evaluated the methodologies used by the Service, the Bureau, and the Forest Service to identify and allocate cost deductions for fiscal years 1994 through 1996. We obtained and analyzed Service, Bureau, and Forest Service work sheets and other data that detailed the agencies' computations and accounting methodologies. We verified that cost and enacted budget appropriation data were supported by the agencies' respective accounting systems. We also visited or conducted telephone interviews with Federal and state officials knowledgeable of the net receipts sharing process at the following locations: (1) the Service's administration and budget offices in Washington, D.C., and its Royalty Management Program offices in Lakewood, Colorado; (2) the Bureau's budget and accounting offices and its Resource Use and Protection Directorate in Washington, D.C., and its National Business Center (formerly the Denver Service Center) in Lakewood, Colorado; (3) the Forest Service's minerals and geology management offices in Washington, D.C.; and (4) the appropriate offices in the States of Alaska, California, Colorado, Missouri, Montana, New Mexico, North Dakota, Utah, and Wyoming.

Our review was made in accordance with the "Government Auditing Standards," issued by the Comptroller General of the United States. Accordingly, we included such tests of records and other auditing procedures that were considered necessary under the circumstances. In addition, we reviewed the Secretary's Annual Statement and Report to the President and the Congress, which is required by the Federal Managers' Financial Integrity Act, for fiscal years 1993 through 1995 and determined that there were no reported weaknesses related to the objective and scope of our audit.

PRIOR AUDIT COVERAGE

The Office of Inspector General has not issued any reports during the past 5 years on the net receipts sharing process, but the General Accounting Office has issued one report during this period. The report "Minerals Management, Costs for Onshore Minerals Leasing Programs in Three States" (No. GAO/RCED-97-31), issued in February 1997, compared the mineral leasing program costs incurred by the three Federal agencies for the States of California, New Mexico, and Wyoming with the costs incurred by these states' minerals management offices. The report included an explanation of the net receipts sharing process but did not make any recommendations.

Additionally, other organizations have examined selected aspects of the net receipts sharing process as follows:

- In 1991, the Service contracted with a major public accounting firm to evaluate the methodology used to allocate the Federal onshore program costs to the states. The firm issued two reports in November 1991 which stated that the Service's cost accounting methodology and cost distribution computations were reasonable. The Service used the same methodology upon passage of the Omnibus Budget Reconciliation Act of 1993.

- In August 1995, the Associate Director for Royalty Management, Minerals Management Service, formed a peer review group consisting of Service personnel and a representative from the Office of Inspector General to determine whether the cost identification and cost allocation methodologies were valid and resulted in equitable cost deductions for the states. This review was limited to an examination of the fiscal year 1995 cost deductions. The group concluded that the fiscal year 1995 cost deductions were overstated because the Service used inappropriate cost identification and allocation procedures for the Audit Divisions[2] and the Systems Management Division (see the Results of Audit section). The group recommended that the Service: (1) use a more accurate basis to identify and allocate costs among onshore, Indian, and offshore mineral leases and (2) replace the separate cost pools used for the revenue and cost methods with a single cost pool based on actual onshore program costs. Both recommendations had been implemented for the net receipts sharing computations for fiscal year 1997.

RESULTS OF AUDIT

We found that the cost sharing deductions were computed efficiently and deducted from the states' mineral leasing receipts on a timely basis. However, the methodologies used by the three agencies to determine the amount of cost deductions for fiscal years 1994 through 1996 did not result in an equitable distribution of mineral leasing program costs. Specifically, we found that the three agencies inaccurately identified and allocated certain mineral leasing program and related general administrative costs to their respective cost pools for deduction purposes. Additionally, the cost pools for the Bureau and the Forest Service included preleasing costs that may not be an allocable cost to the states. The Omnibus Budget Reconciliation Act of 1993 established general methodology requirements for the development of cost deductions to the states' mineral leasing receipts. However, in the 3 years after passage of the Act, the three agencies had not adopted policies or operating

[2] The Audit Divisions consist of the Dallas Compliance Division, the Houston Compliance Division, and the Lakewood Compliance Division.

procedures to ensure that the process provided equitable cost deductions. As a result, the costs of $75.9 million that were deducted from the states' mineral leasing receipts during fiscal years 1994 through 1996 were overstated by $8.8 million, or 11.6 percent (see Appendix 4).

Minerals Management Service

To comply with the net receipts sharing provisions of the Act, the Minerals Management Service has refined its practices since fiscal year 1996 to better identify the amount of cost deductions charged to the states. Specifically, the actions taken as a result of the peer review group formed by the Associate Director for Royalty Management (see Prior Audit Coverage section) should result in substantially better identification of cost deductions for fiscal year 1997. However, for fiscal years 1994 through 1996, the Service inaccurately identified certain program and related general administrative costs as allocable deductions and did not initiate timely actions to correct the inaccuracies. The overstated cost deductions relating to these issues totaled $7,627,403. The amounts presented below are not an itemized breakdown of this total but are presented for illustrative purposes as follows:

- The Service allocated the portion of its appropriation that related to the onshore program to the states by using different cost pools for the revenue and the cost allocation methods. We found that a disparity resulted because the cost pools developed for the revenue method were significantly higher than those developed for the cost method ($54.9 million versus $44.5 million for fiscal year 1994, $56.8 million versus $45.7 million for fiscal year 1995, and $59.7 million versus $32.8 million for fiscal year 1996). We determined that the cost pools for the revenue method were overstated and that the cost pools for the cost method were generally accurate. Since the net receipts cost deductions for most states were based on the revenue allocation method (see Appendix 2), the overstated cost pools caused an overcharge of cost deductions to these states. In our opinion, only one cost pool should have been developed for the program regardless of whether the revenue or the cost allocation method was used to determine the cost deductions. Moreover, the Act did not stipulate that a unique cost pool be established for each allocation method. Service officials maintained that since the Service established the two cost pool methodology in consultation with the Congress, any change would require Congressional approval. Nevertheless, the methodology resulted in an overallocation of program costs to most states. To illustrate the effect on the cost deductions, the amounts of overstated deductions for five states for fiscal year 1996 are presented in Table 1.

Table 1. Overstated Cost Deductions for Fiscal Year 1996

State	Costs Charged	Audited Amount	Overstated Costs
Alaska	$266,833	$146,719	$120,114
California	799,487	439,602	359,885
Colorado	1,126,917	619,641	507,276
Montana	78 1,742	429,845	351,897
Utah	989,344	543,996	445,348

Service officials said that they had recognized the inequity of using separate cost pools and obtained Congressional approval to use one pool for the Service's fiscal year 1997 net receipts computations. However, for fiscal years 1994 through 1996, the use of separate cost pools resulted in excess cost allocations to the states and excess deductions from the states' royalty receipts.

- The peer review group found that the Service overstated cost deductions for fiscal year 1995 because of inaccurate methods of identifying and allocating the costs under the cost allocation method for the Audit Divisions and the Systems Management Division. Specifically, the group determined that, under the cost method, onshore program costs for the Audit Divisions were based on the number of producing leases and that the costs for the Systems Management Division were based on the number of report lines processed. Neither of these bases represented an accurate measure of the work performed and the costs incurred on behalf of the Royalty Management Program for the states. However, the Service corrected this situation for the net receipts computations for fiscal year 1996. The Audit Divisions currently allocate costs based on revenues generated by the leases, whereas the Systems Management Division allocates costs based on the number of on-line users of the Royalty Management Program's automated systems. As a result of these changes, the cost allocations for both divisions are currently representative of the work performed.

- General administrative costs pertaining to the fiscal year 1996 cost pool under the revenue method were overstated by $2 million, resulting in a $114,000 overcharge to the states. The overstatement was the result of a mathematical error in computing general support service costs. The error could have been prevented had the Service established and implemented a formal procedure to independently verify its computations.

- The Service did not make timely adjustments to correct certain deficiencies in the net receipts process. For example, the Service did not revise its methodology for identifying and allocating the fiscal year 1994 cost deductions, even though the cost pool under the revenue method ($54.9 million) and the cost method ($44.5 million) showed a wide disparity.

Additionally, the peer review group's recommendations in fiscal year 1995 to improve the cost identification and allocation procedures for the Audit Divisions and the Systems Management Division and to use a single cost pool for the revenue and cost methods were not implemented until 1 and 2 years, respectively, after the deficiencies were identified.

We also noted that the Service's procedures adopted for fiscal year 1996 for identifying and allocating general administrative costs to the Royalty Management Program under the cost method were complex and time-consuming. Specifically, the Service attempted to identify, with a high degree of precision, the cost components of administrative operations, general support services, policy and management improvements, and executive direction. Although we acknowledge that the Service made efforts to identify these costs and that the Service's process did result in accurate cost determinations, we believe that indirect costs could be allocated through a standard overhead rate based on agency direct costs without the desired level of precision being lost. A standard overhead rate is administratively simple to compute and is an accepted cost accounting practice.

Bureau of Land Management

The Bureau of Land Management consistently followed a cost accounting methodology for its computations for fiscal years 1994 through 1996. Although we found that the Bureau was reasonably effective in allocating its appropriation to the states, the Bureau did not accurately identify certain program and general administrative costs. The overstated cost deductions caused by these issues totaled $1,206,563. The amounts presented are not an itemized breakdown of this total but are presented for illustrative purposes as follows:

- The Bureau did not accurately estimate its appropriation associated with Indian lease management on the net receipts computation work sheets. To identify the states' share of allocable costs in the Energy and Minerals Management budget activity, the Bureau had to exclude all amounts associated with Indian lease management. This required the Bureau to estimate the amounts because Indian mineral leasing activities were not identified separately in the Bureau's budget system. In addition, at the time that cost deductions were computed and submitted to the Minerals Management Service for a particular fiscal year, only about 10 to 11 months of cost data were available. As such, the Bureau determined Indian mineral leasing costs for the remaining 1- to 2-month period based on an estimated percentage of the Bureau's yearly expenditures for Indian mineral leasing costs. However, we found that the percentages were not accurate relative to historical cost data, which could have been used to more accurately project these year-end costs. Specifically, using historical data, we determined that the Bureau overestimated the Indian lease management costs in its computations by $261,000 (6.7 percent) for fiscal year 1994 and by $142,000 (4.7 percent) for fiscal year 1996 and that it underestimated the costs by $579,000 (19.4 percent) for fiscal year 1995. The overall effect was a net overstatement of onshore program costs, which resulted in an overcharge of cost deductions to the states.

- The Bureau did not correctly allocate its support costs to the states. Specifically, costs associated with the following areas were allocated primarily to the states: personnel leave surcharge; Bureauwide permanent changes of station; and general administration and operation of the Bureau's National Training Center, National Business Center, and Washington Office. Instead, an appropriate share of these support costs should have been allocated to the program areas of Indian lease management and mineral material sales management. The effect of not allocating costs to the Bureau programs was an overcharge of the cost deductions to the states.

- The Bureau used an overhead rate of 19 percent instead of 18 percent in its computations for fiscal years 1994 through 1996, which resulted in an overcharge of the cost deductions to the states. The Bureau's billing rate for cost-recoverable and cost-reimbursable projects was 18 percent during fiscal years 1994 through 1996, a rate that we believe should have been used for cost deduction purposes.

During our review, we noted that the Bureau had not corrected the cost accounting deficiencies cited in this section for establishing its cost deductions for fiscal year 1997.

U.S. Forest Service

The U.S. Forest Service used a methodology in fiscal years 1994 and 1995 and initially in fiscal year 1996 that did not equitably allocate costs to the states. The methodology was based on each state's respective percentage of national forest acreage less national wilderness and national recreation area acreage. Forest Service officials said that they used this method because the Forest Service's accounting system did not record costs by national forest until fiscal year 1995 and that therefore acreage was the best available allocation basis. However, the method did not allocate costs equitably because mineral leasing costs are not the result of the amount of acreage of public land holdings but of the amount of mineral leasing activity. The effect of this issue was an understatement of cost deductions that totaled $43,670 for fiscal years 1994 through 1996.

Additionally, the Forest Service had not established adequate policies or procedures for the net receipts sharing process. In a March 1996 letter, the Royalty Policy Committee requested the Forest Service to provide an explanation of the agency's cost allocations.[3] To respond to the Committee's request, the Forest Service had to reconstruct the process, as key individuals had left the agency and the cost allocation methodology was not documented. As a result, the Forest Service reexamined its process and initiated improvements to its methodology. However, because of uncertainties regarding the accuracy of the 1996 cost

[3] The Royalty Policy Committee was formed in July 1995 by the Department of the Interior to provide advice on the Department's management of Federal and Indian mineral leases, revenues, and other mineral-related issues. The Committee includes representatives from Federal, state, and tribal governments; allottee organizations; and mineral industry associations.

deductions, the Forest Service revised its original computations twice. Each of the three schedules used a different cost allocation basis, which resulted in substantially different deductions to the states. We concluded that the final schedule used by the Forest Service, which incorporated its recently enhanced accounting system to accumulate costs by individual national forest, represented an accurate method of identifying each state's share of program costs.

Preleasing Costs

We found that costs associated with preleasing activities were included in the cost pools of the Bureau of Land Management and the Forest Service for fiscal years 1994 through 1996. However, neither the budget nor the accounting systems of the Bureau and the Forest Service specifically identified the amount of preleasing costs incurred for fiscal years 1994 through 1996. In fiscal year 1992 (the latest year that actual data were available), the Bureau incurred preleasing costs of $855,000. Bureau budget officials stated that preleasing costs were fairly stable from year to year.

Preleasing activities consisted primarily of preparing environmental impact statements and environmental assessments to determine the suitability of an area for mineral leasing operations. The two agencies conducted these evaluations to comply with the environmental protection mandates of the National Environmental Policy Act of 1969. However, these costs may not be an allocable cost deduction. The Omnibus Budget Reconciliation Act amended the Mineral Leasing Act (30 U.S.C. 191, Section 35) and stipulated that net receipts deductions consist "of the portion of the enacted appropriation allocable to the administration of all laws providing for the leasing of any onshore lands or interest in land owned by the United States for the production of the same types of minerals leasable under this [Mineral Leasing] Act or of geothermal steam, and to enforcement of such laws." Since environmental work is completed before the land is leased and leasing may not occur in areas considered unsuitable for mineral operations, some of the state government officials we interviewed said that the Omnibus Budget Reconciliation Act precludes these costs from being included in the cost pools. As such, we believe that the Bureau should obtain legal advice on whether preleasing costs should be allocated to the states through the net receipts sharing process.

State Involvement

During our visits and contacts, we found that state government officials strongly opposed the concept of net receipts sharing. These officials were concerned that program costs may be "excessive" in relation to the benefits the states receive, and some questioned the authority of the Federal Government to assess the cost deductions. In addition, state government officials told us that they were not sufficiently informed about the decision-making and cost-methodology processes and expressed concern about the accuracy of the cost deduction computations and the Federal Government's responsiveness to their requests for detailed explanations of the computations. However, Minerals Management Service and Bureau officials stated that the Federal Government has maintained an open line of communication with the states and has fully responded to the states' requests for information concerning net receipts. In view of the differences of opinion concerning communications, we believe that the Federal Government should ensure that the methodologies used by the three agencies are communicated frequently and clearly to the states.

Conclusion

We concluded that the three agencies essentially complied with their responsibilities to implement the net receipts sharing provisions of the Omnibus Budget Reconciliation Act. However, we further concluded that the agencies did not develop the administrative procedures required to accurately identify and allocate the onshore mineral leasing program costs. We recognize that determining these costs is particularly difficult because the agencies' budgeting processes and accounting systems were not designed for accumulating costs in the detail required for net receipts sharing purposes. In view of this difficulty, we believe that the three agencies should establish written policies and procedures which facilitate the accumulation and computation of the states' cost deductions.

Recommendations

We recommend that the Directors of the Minerals Management Service and the Bureau of Land Management:

1. Establish policies and procedures which effectively and consistently guide the net receipts sharing process consistent with the findings outlined in this report. The Forest Service should be invited to participate in this effort, and all of the agencies should improve communications with the affected state governments.

We recommend that the Director, Bureau of Land Management:

2. Request an opinion from the Office of the Solicitor on whether preleasing costs are an allocable cost deduction to the states.

Minerals Management Service Response and Office of Inspector General Reply

In the July 15, 1997, response (Appendix 5) to the draft report from the Director, Minerals Management Service, the Service concurred with Recommendation 1, stating that it would "coalesce and update its existing net receipts sharing policies and procedures into a single document and provide [the document] to the Bureau of Land Management and the Forest

Service," as well as provide the document to the states. However, additional information is requested for the recommendation (see Appendix 7).

Service's Additional Comments on Audit Report

In its response, the Minerals Management Service stated that our report would benefit from "some clarification of the facts" and that our report "suggests" that the Service did not take timely action to correct inequities in the net receipts process once they were identified. The Service also stated that it "took action . . . on the one item that it had the authority to change (i.e., allocations of system and audit costs based on lease counts)" and that the "other change (i.e., use of one cost pool) required the concurrence of Congress."

Our report addressed the identified inequities of two separate cost pools and the effect that those inequities had on net receipts sharing deductions during fiscal years 1994 through 1996. To correct these inequities, the Service requested and received approval for the use of one cost pool in its fiscal year 1997 Senate appropriations subcommittee report. While we do not take issue with the Service's contention that Congressional approval was required to effect the changes, the fact remains that, although discovered in fiscal year 1995, the inequity was not corrected until fiscal year 1997. The result was that for fiscal years 1994 through 1996, the states were overcharged as set forth in Appendix 4.

In its response to the draft report, the Service also stated that if the cost deductions for fiscal years 1994 through 1996 are to be recalculated, the recalculation should include the costs of audits pertaining to Section 205 of the Federal Oil and Gas Royalty Management Act. The Service said that it had excluded audit costs from its net receipts cost pools but that the audit costs were an allocable charge to the Federal onshore mineral leasing program and therefore should have been included in the cost pools for the 3 years included in our review. The Service further stated that "including these costs would significantly mitigate the 'overcharges' and in some instances may result in undercharges."

We used the Service's cost allocation methodology as it existed from fiscal years 1994 to 1996 in computing the overcharges to the states. This methodology, as described by the former Director of the Service in written testimony to the Congress in 1993, did not include audit costs, which the Service previously and currently recovers through cost sharing agreements with the states. In its response, the Service stated that the new methodology approved by the Congress in fiscal year 1997 should include audit costs. The Service's contention in this regard confirms our position that the Service needs to articulate and document what costs should be allowable as cost deductions and how those costs are to be allocated before such a methodology is submitted to the Congress for its approval.

The Service also said that our draft report "implie[d]" that it "failed to keep State government officials sufficiently informed on net receipts sharing decisions and processes." The Service further stated that it maintained an “open line of communication” with the states and that it had many meetings on the subject.

Our report stated that “state government officials told us that they were not sufficiently inforrned about the decision-making and cost-methodology processes and expressed concern about the accuracy of the cost deduction computations.” We also stated that “Minerals Management and Bureau officials stated that the Federal Government has maintained an open line of communication with the states and has fully responded to the states’ requests for information concerning net receipts.” The apparent difference of opinion regarding the sufficiency of the information that the Service provided to the states, combined with the Federal Government’s responsibility to keep the states informed, led to our recommendation to “improve communications with the affected state governments.”

The Service also said that it believes it should continue to use its established procedures regarding the identification and allocation of general administrative costs instead of a general administrative overhead rate. While we acknowledge that a change is not required, we believe that, instead of the complex and cumbersome method currently used, the Service should explore more efficient methodologies, such as the development of a standard overhead rate based on direct costs, for distributing general administrative expenses.

Bureau of Land Management Response and Office of Inspector General Reply

In the July 16, 1997, response (Appendix 6) to the draft report from the Deputy Director, Bureau of Land Management, the Bureau indicated concurrence with the two recommendations directed to it. Based on the response, we consider Recommendation 1 resolved and implemented and Recommendation 2 resolved but not implemented (see Appendix 7).

Bureau’s Additional Comments on Audit Report

In its response, the Bureau noted that our report stated that “the three agencies had not adopted policies or operating procedures to ensure that the process provided equitable cost deductions”; that the Bureau “consistently followed a cost accounting methodology for its computations”; and that "[t]his would seem to imply that the Bureau of Land Management had adopted an [acceptable] operating procedure.” The Bureau disagreed that the process did not provide equitable cost deductions because we calculated the overcharges related to the Bureau at only $1,206,563 of over $200 million. Therefore, according to the Bureau, our report should have shown the "1- percent difference” to be “an estimation that deserves positive comment.” The Bureau also stated:

> While the OIG [Office of Inspector General] contends that a portion [of the cost deductions charged] should be prorated to Indian minerals management in general, employees are not hired to work solely on Indian lease management. In many cases, such work is only a minor part of their job and

> would result in a small deduction. Having said this we nevertheless believe that the OIG did point out a methodological flaw with respect to mineral material sales.

We concluded that the Bureau consistently followed a cost accounting methodology for its computations for fiscal years 1994 through 1996. As such, we believe that the report (page 7) adequately presents the Bureau's efforts. However, the fact that the Bureau was consistent in identifying and allocating costs does not obviate the need for improvements in the methodology. Although the $1.2 million in overcharges may not be material to the Bureau, the individual amounts may be significant to the states that were overcharged.

In regard to the overcharges resulting from Indian lease management costs, the Bureau stated that the effect of the overcharges is "virtually insignificant." As stated in our report (page 7), using historical cost data readily available to the Bureau, the states were overcharged by as much as $579,000 in the cost pool for fiscal year 1996. We do not consider any overcharges to the states to be insignificant. In addition, we disagree with the Bureau's statement that charges for support costs were "appropriate." Support costs allocable to Indian lease management and mineral material sales are not, as the Bureau states, "part of the operations of a mineral leasing program" because these efforts (permanent change-of-station transfers; leave surcharges; and administrative costs for training, finance, and headquarters operations) do not solely benefit the states and should not be included in net receipts deductions.

The Bureau disagreed with our statement that it had not corrected the cost accounting deficiencies cited when establishing its deductions for fiscal year 1997, stating that it had not started work on its 1997 cost deductions. However, our report said that the Bureau had not corrected the deficiencies <u>for</u> establishing its fiscal year 1997 deductions; that is, the corrections should be made before the work on the fiscal year 1997 calculations was started. We had explained and clarified this issue at our exit conference with Bureau officials.

In accordance with the Departmental Manual (360 DM 5.3), we are requesting the Mineral Management Service's written comments to this report by November 24, 1997. The response should provide the information requested in Appendix 7.

The legislation, as amended, creating the Office of Inspector General requires semiannual reporting to the Congress on all audit reports issued, the monetary impact of audit findings, actions taken to implement audit recommendations, and identification of each significant recommendation on which corrective action has not been taken.

We appreciate the assistance of officials from the Minerals Management Service and the Bureau of Land Management in the conduct of our audit.

NET RECEIPTS SHARING PROCESS

Under the Omnibus Budget Reconciliation Act of 1993, each state's cost deduction for net receipts sharing is computed in a multistep process as follows:

Step 1 Prior year appropriation for the Federal Onshore Mineral Leasing Program times 50 percent equals one-half of the appropriation.

COST ALLOCATIONS

Step 2 **Revenue Method**
One-half of the appropriation[1] (from Step 1) times (mineral revenues disbursed to a state divided by total mineral revenues disbursed to all states) times the state's share of mineral revenues as established by law (averages about 50 percent) equals the cost deduction.

Step 3 **Cost Method**
One-half of the appropriation[2] (from Step 1) attributable to a state as determined by the cognizant agency times the state's share of mineral revenues as established by law (averages about 50 percent) equals the cost deduction.

The actual cost deduction is the lower of the amounts computed under the revenue method or the cost method. The Minerals Management Service deducts the full year amount of cost deductions in approximately 12 equal amounts from each state's monthly distribution of mineral receipts.

[1]The Minerals Management Service used the percentage of onshore leases in the producing lease universe to identify the amount of the appropriation attributable to the onshore program.

[2]The Minerals Management Service used cost accounting procedures to identify the amount of the appropriation attributable to the onshore program.

NET RECEIPTS SHARING COST DEDUCTIONS TO STATES FOR FISCAL YEARS 1994, 1995, AND 1996

Fiscal Year 1994

State	Cost Method	Revenue Method	Revenue Distribution Percentage	Cost Deduction
Alabama	$265,263	$135,028*	46.0618	$62,196
Alaska	1,008,190	588,786*	90.7221	534,159
Arizona	841,391	12,530*	50.0000	6,265
Arkansas	909,229	259,113*	43.1727	111,866
California	3,757,364	3,464,262*	50.0258	1,733,026
Colorado	7,130,684	5,528,293*	49.9979	2,764,031
Florida	78,411	15,742*	50.0229	7,875
Georgia	42,779	31*	25.0162	8
Idaho	795,206	343,087*	49.9827	171,484
Illinois	21,997*	22,527	62.9072	13,837
Indiana	1,872	29*	25.0085	7
Kansas	789,774	204,057*	50.0029	102,034
Kentucky	311,145	13,240*	46.9535	6,217
Louisiana	487,764	168,318*	35.4983	59,750
Maryland	11,324	0*	0.0000	0
Michigan	427,123	136,198*	41.2845	56,229
Minnesota	38,868	0*	0.0000	0
Mississippi	547,922	217,396*	26.1236	56,792
Missouri	268,074	145,144*	25.1178	36,457
Montana	4,746,209	3,511,310*	50.0000	1,755,655
Nebraska	146,596	3,187*	49.5993	1,581
Nevada	1,108,229*	1,280,490	50.0000	554,114
New Hampshire	0	0	0.0000	0
New Mexico	15,377,818*	20,767,197	49.9993	7,688,803
New York	6,987	0*	0.0000	0
North Carolina	16,321	312*	24.9992	78
North Dakota	1,900,658	509,922*	50.0260	255,094
Ohio	250,352	32,714*	72.0331	23,565
Oklahoma	1,778,415	428,796*	50.3723	215,994
Oregon	873,353	11,800*	50.0000	5,900
Pennsylvania	205,744	1,995*	73.1965	1,460
South Carolina	2,765	94*	30.5399	29
South Dakota	210,390	70,861*	50.0000	35,431
Tennessee	37,146	168*	43.0284	72
Texas	364,993	90,114*	29.4162	26,508

*The cost deduction represents the lower amount of the cost or revenue **method** multiplied by the state's revenue distribution percentage (rounded to four decimal places in this schedule).

Fiscal Year 1994 (Continued)

State	Cost Method	Revenue Method	Revenue Distribution Percentage	Cost Deduction
Utah	$5,141,541	$4,794,391*	50.0237	$2,398,329
Virginia	314,756	22,178*	50.5249	11,205
Washington	115,984	39,433*	50.0000	19,717
West Virginia	792,370	48,588*	40.4480	19,653
Wisconsin	33,957	468*	24.9995	117
Wyoming	15,629,523*	29,096,628	50.0000	7,814,762
TOTAL	$66,788,487	$71,964,427		$26,550,300

Fiscal Year 1995

State	Cost Method	Revenue Method	Revenue Distribution Percentage	Cost Deduction
Alabama	$225,958	$58,174*	40.8741	$23,778
Alaska	1,013,608	426,921*	91.2947	389,756
Arizona	736,450	10,006*	50.0000	5,003
Arkansas	828,802	199,654*	43.6701	87,189
California	3,795,418	3,102,943*	49.6722	1,541,299
Colorado	7,056,622	4,923,915*	50.0006	2,461,986
Florida	92,173	11,762*	50.0292	5,884
Georgia	30,803	14*	25.0174	4
Idaho	806,226	354,925*	49.9012	177,112
Illinois	32,361	25,553*	57.4877	14,690
Indiana	872	28*	25.0091	7
Kansas	857,293	153,887*	50.0021	76,947
Kentucky	317,881	16,117*	31.2310	5,034
Louisiana	610,598	102,403*	38.3354	39,257
Maryland	8,747	0*	0.0000	0
Michigan	357,719	93,562*	50.0003	46,781
Minnesota	18,142	7,518*	25.0000	1,880
Mississippi	561,053	136,683*	26.3840	36,062
Missouri	111,778*	168,139	25.0948	28,050
Montana	4,790,936	3,418,814*	50.0000	1,709,407
Nebraska	131,009	2,645*	55.2231	1,461
Nevada	1,166,067	1,074,563*	49.9894	537,168
New Hampshire	0	0	0.0000	0
New Mexico	15,885,221*	19,996,343	49.9997	7,942,559
New York	203,359	0*	0.0000	0
North Carolina	11,160	304*	25.000	76
North Dakota	1,747,064	352,498*	50.3606	177,520
Ohio	301,980	22,560*	67.9202	15,323
Oklahoma	1,839,025	277,834*	51.2388	142,359
Oregon	773,946	7,776*	49.7517	3,869
Pennsylvania	172,745	1,772*	73.1083	1,295
South Carolina	3,718	310*	25.0016	77
South Dakota	206,815	53,583*	50.0000	26,791
Tennessee	26,506	20*	33.4655	7
Texas	392,737	94,331*	38.1049	35,945
Utah	5,386,867	4,429,058*	50.0390	2,216,256
Virginia	240,062	17,276*	49.1917	8,498
Washington	129,517	45,478*	50.0320	22,754
West Virginia	544,162	38,285*	48.6944	18,643
Wisconsin	30,965	120*	25.0042	30
Wyoming	15,744,869*	33,152,841	50.0000	7,872,434
TOTAL	$67,191,234	$72,778,615		$25,673,191

Fiscal Year 1996

State	Cost Method	Revenue Method	Revenue Distribution Percentage	Cost Deduction
Alabama	$214,706	$65,283*	45.8388	$29,925
Alaska	1,009,506	694,100*	90.6888	629,471
Arizona	279,439	12,958*	50.0000	6,479
Arkansas	697,624	128,735*	46.1553	59,418
California	4,041,405	3,768,323*	50.0485	1,885,989
Colorado	5,568,497	5,316,737*	50.0006	2,658,402
Florida	49,306	12,747*	50.0428	6,379
Georgia	17,596	0*	0.0000	0
Idaho	760,600	354,233*	49.9913	177,086
Illinois	67,803	15,282*	71.1214	10,869
Indiana	1,340	0*	0.0000	0
Kansas	575,546	132,749*	50.0874	66,491
Kentucky	408,286	10,845*	42.5646	4,616
Louisiana	466,676	107,467*	48.6393	52,271
Maryland	5,408	0*	0.0000	0
Michigan	291,029	130,496*	46.3063	60,428
Minnesota	3,458	2,817*	25.0000	704
Mississippi	493,311	85,917*	27.4979	23,625
Missouri	454,915	145,919*	25.1729	36,732
Montana	4,009,854	3,688,250*	50.0000	1,844,125
Nebraska	114,041	2,113*	50.0000	1,056
Nevada	1,144,291*	1,212,844	49.9986	572,130
New Hampshire	11,343	0*	0.0000	0
New Mexico	11,693,715*	17,780,815	50.0000	5,846,857
New York	5,738	0*	0.0000	0
North Carolina	30,906	141*	24.9982	35
North Dakota	1,564,529	384,375*	50.1040	192,587
Ohio	304,134	36,198*	72.4541	26,227
Oklahoma	1,506,563	278,950*	53.3792	148,901
Oregon	676,996	6,549*	50.0000	3,275
Pennsylvania	180,020	3,380*	74.2821	2,511
South Carolina	21,185	0*	0.0000	0
South Dakota	178,035	115,848*	50.0000	57,924
Tennessee	29,725	0*	0.0000	0
Texas	675,503	68,804*	41.5150	28,564
Utah	4,694,588	4,663,976*	50.0398	2,333,842
Virginia	126,804	13,662*	64.8499	8,860
Washington	143,477	55,212*	50.0000	27,606
West Virginia	654,498	30,213*	50.2811	15,191
Wisconsin	46,060	141*	24.9982	35
Wyoming	13,778,619*	31,098,010	50.0000	6,889,310
TOTAL	$56,997,075	$70,424,089		$23,707,921

COST ALLOCATION METHODOLOGIES BY FEDERAL AGENCY

Minerals Management Service

From fiscal years 1994 through 1996, the Service developed the net receipts sharing cost deductions by computing two separate cost pools. First, for the cost method, the Service calculated the Federal onshore mineral leasing program cost pool by subtracting the costs to administer offshore and Indian leases from the prior year's Royalty Management Program appropriation for its separate divisions and by adding the prior year's general administrative costs. The Service then allocated the costs to the states using a method keyed to each division's specific work load. Second, for the revenue method, the Service determined a separate onshore program cost pool by multiplying the prior year's Royalty Management Program appropriation by the percentage of onshore producing leases. The Service then allocated the costs based on each state's percentage of onshore mineral leasing receipts. Beginning in fiscal year 1997, the revenue allocation method used the same cost pool developed for the cost allocation method. The Service accounts for about 32 percent of the Federal agencies' total onshore program costs.

Bureau of Land Management

Since fiscal year 1994, the Bureau has computed a single cost pool by subtracting Indian lease management costs, reimbursements for filing fees, and mineral material sales program costs from the prior year's Energy and Minerals Management appropriation. Allowances are added to the cost pool for the leave surcharge; Bureauwide permanent changes of station; and costs for general administration and operation of the National Training Center, the National Business Center, and the Washington Office. Under the cost method, the Bureau allocates the cost pool to the states based on the budgeted cost targets for the Bureau's state offices. For state offices serving multiple states, the cost pool is further allocated using a weighted average based on the number of producing leases in each applicable state office. Under the revenue method, the Bureau allocates the cost pool in the same manner as the Service. The Bureau accounts for about 58 percent of the Federal agencies' total onshore program costs.

U.S. Forest Service

For fiscal years 1994 and 1995 and initially in fiscal year 1996, the Forest Service's onshore program cost pool consisted of the prior year's Leasable Minerals Program appropriation with an allowance for general administration. Under the cost method, the Forest Service allocated the cost pool to the states based on each state's national forest acreage less national wilderness and national recreation area acreage. Beginning in fiscal year 1996, the cost pool and the allocation to states were based on onshore program costs recorded for each national forest. Under the revenue method, the Forest Service allocated the cost pool in the same manner as the Service. The Forest Service accounts for about 10 percent of the Federal agencies' total onshore program costs.

NET RECEIPTS SHARING
OVERCHARGED COST DEDUCTIONS FOR
FISCAL YEARS 1994-1996*

State	FY 1994	FY 1995	FY 1996	Total
Alabama	$5,107	$4,844	$6,210	$16,161
Alaska	43,858	79,398	130,610	253,866
Arizona	514	1,019	1,344	2,877
Arkansas	9,185	17,761	12,334	39,280
California	142,292	313,979	391,300	847,571
Colorado	226,944	501,533	551,562	1,280,039
Florida	647	1,199	1,334	3,180
Idaho	14,080	36,080	36,731	86,891
Illinois	830	2,993	2,239	6,062
Kansas	8,378	15,675	13,805	37,858
Kentucky	511	1,025	950	2,486
Louisiana	4,906	7,997	10,858	23,761
Michigan	4,617	9,530	12,532	26,679
Minnesota	0	383	153	536
Mississippi	4,663	7,346	4,904	16,913
Missouri	2,993	(1,929)	7,621	8,685
Montana	144,150	348,224	382,611	874,985
Nebraska	130	298	217	645
Nevada	34,825	109,427	91,553	235,805
New Mexico	41,549	2,187,180	100,645	2,329,374
North Dakota	20,945	36,163	39,948	97,056
Ohio	2,029	3,121	5,452	10,602
Oklahoma	17,734	29,000	30,898	77,632
Oregon	484	788	692	1,964
Pennsylvania	120	264	540	924
South Dakota	2,909	5,458	12,009	20,376
Texas	2,176	7,322	5,925	15,423
Utah	196,918	451,475	484,205	1,132,598
Virginia	920	1,731	1,835	4,486
Washington	1,619	4,635	5,735	11,989
West Virginia	1,614	3,798	3,149	8,561
Wyoming	54,238	1,171,543	89,250	1,315,031
TOTAL	$991,885	$5,359,260	$2,439,151	$8,790,296

*This schedule does not include any adjustments for preleasing costs. Also, six states (Georgia, Indiana, North Carolina. South Carolina, Tennessee, and Wisconsin) were excluded because they had overcharged cost deductions totaling less than $35 each for the 3-year period.

United States Department of the Interior

MINERALS MANAGEMENT SERVICE
Washington, DC 20240

JUL 15 1997

Memorandum

To: Assistant Inspector General for Audits

Through: FOR Bob Armstrong Piet deWitt JUL 15 1997
Assistant Secretary, Land and Minerals Management

From: Cynthia Quarterman C Quarterman
Director, Minerals Management Service

Subject: Office of Inspector General Draft Audit Report C-IN-MOA-002-96, "Costs Recovered Through Net Receipts Sharing Deductions, Minerals Management Service and Bureau of Land Management'

I appreciate the opportunity to respond to this draft report on our costs recovered through the net receipts sharing deductions program with the States. We are in agreement with Recommendation 1 of the report; Recommendation 2 does not apply to Minerals Management Service.

We're sending you our general comments on the audit findings and specific ones on Recommendation 1.

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

Attachment

MINERALS MANAGEMENT SERVICE RESPONSE TO DRAFT AUDIT REPORT - "COSTS RECOVERED THROUGH NET RECEIPTS SHARING DEDUCTIONS MINERALS MANAGEMENT SERVICE AND BUREAU OF LAND MANAGEMENT"

Audit Agency: Office of Inspector General (OIG)

Audit Number: C-IN-MOA-002-96

GENERAL COMMENTS

We generally agree with the recommendations of this draft report. However, we believe some clarification of the facts would be beneficial and offer the following comments.

The draft report suggests that the Minerals Management Service (MMS) was remiss in not initiating timely actions to correct net receipt sharing inequities once they were identified by an internal review. MMS took action commencing in FY 1996 on the one item that it had the authority to change (i.e., allocations of system and audit casts based on lease counts). The other change (i.e., use of twa cost pools) required the concurrence of Congress. After extensive briefings, the Senate Appropriations Subcommittee for Interior and Related Agencies included specific language in their FY 1997 Subcommittee report authorizing the change. Therefore, beginning with FY 1997 payments, MMS eliminated the dual cost pool methodology. Earlier application of this new methodology without Congressional approval, as implied in the draft report, would have been ill-advised.

If the new methodology is to be applied to net receipt share deductions made in FY 1994 through 1996 as shown in Appendix 4, it should be recalculated to include costs of audits under Section 205 of the Federal Oil and Gas Royalty Management Act of 1982. These costs were never included in the reimbursement formula for those years, even though they clearly were costs incurred in the States. Including these costs would significantly mitigate the "overcharges" and in some instances may result in undercharges. In addition, there may be other categories of costs, such as MMS audit, where we have understated our cost to States. We will reevaluate those allocations in FY 1998.

The draft report implies that MMS failed to keep State government officials sufficiently informed on net receipts sharing decisions and processes. We understand the States oppose net receipts sharing. Nonetheless, we believe MMS has made considerable efforts to ensure States are familiar with our methodology. Not only did we maintain an open line of communication with the States and fully respond to their questions, as acknowledged in the report, but we briefed the State and Tribal Royalty Audit Committee on our approach in May 1995, and again met with State representatives in July 1995 to walk them through the entire net

JUL-15-97 10:11 FROM:POLICY & MANAGEMENT IMPROVEMENT

receipts sharing process. As a followup to that meeting, we also requested comments from the States on the changes MMS was proposing ta its methodologies for calculating net receipts sharing costs. At the request of the States, we extended the deadline for comments which delayed the timing of our Congressional briefings. Later in the same year, we invited Wyoming and New Mexico staff groups to visit the Royalty Management Program to review our casts and procedures. Over several days, we provided comprehensive briefings on virtually all Royalty Management issues of interest to the State representatives.

We would concur with OIG's observation that our 1996 procedures for identifying and allocating general administrative costs were complex and perhaps time consuming. However, the draft report also acknowledges that our process did result in accurate cost determinations. We understand our approach is consistent with most private sector cost accounting systems, and because it is generally accepted to be a more accurate method of assessing casts than using a standard overhead rate, we believe it should be continued.

COMMENTS ON RECOMMENDATIONS

1. Establish policies and procedures which effectively and consistently guide the net receipts sharing process consistent with the findings outlined in this report. The Forest Service should be invited to participate in this effort, and the agencies should improve communications with the affected State governments.

AGREE- MMS will coalesce and update its existing net receipts sharing policies and procedures into a single document and provide it to the Bureau of Land Management and the Forest Service.

While MMS believes that it has always communicated openly, honestly, and frequently with States concerning the methods used to determine their deductions under Net Receipts Sharing, we also recognize that communications can always be improved. Therefore, as in the past, we will continue to apprise State officials of their deductions and the methodology used to derive them,, but this year we will also provide the States a copy of the consolidated policies end procedures for their information and use.

2. Obtain an opinion from the Office of the Solicitor on whether preleasing costs are an allocable cost deduction to the States.

(This recommendation does not apply to MMS.)

United States Department of the Interior

BUREAU OF LAND MANAGEMENT
Washington, D.C. 20240

In Reply Refer To:
1245 (WO-300)

JUL 16 1997

MEMORANDUM

To: Assistant Inspector General for Audits

Through: FOR Bob Armstrong Piet deWitt JUL 17 1997
Assistant Secretary, Land and Minerals Management

From: Deputy Director, Bureau of Land Management

Subject: Response to Draft Audit Report on Costs Recovered Through Net Receipts Sharing Deductions, Minerals Management Service and Bureau of Land Management, May 1997 (Assignment No. C-IN-MOA-002-96)

Thank you for the opportunity to respond to the subject draft audit report. In general, we believe that the report determined that the Bureau of Land Management's (BLM) process for calculating costs applicable to each State under the net receipts sharing program is sound.

The report indicates that improvements could be made in the methodology BLM uses to determine net receipts sharing costs. The statistics shown by the auditors indicate, however, that Over a 3-year period the discrepancies they cite amount to about $1.2 million out of over $200 million, subject to application of the law, or less than a 1-percent deviation. As the law requires only an estimate, we believe that a more positive statement should be made about the work we have done.

Attached is our response to the specific recommendations, along with our comments on specific points made in the report.

If you have any questions, please contact Michael H. Schwartz, Senior Program Analyst, at (202) 452-5198 or Gwen Midgette, BLM Audit Liaison Officer, at (202) 452-7739.

Attachments

COSTS RECOVERED THROUGH
NET RECEIPTS SHARING DEDUCTIONS,
MINERALS MANAGEMENT SERVICE AND
BUREAU OF LAND MANAGEMENT, MAY 1997
(Assignment No. C-IN-MOA-002-96)

Specific Comments

1. Page 5 - "However, in the 3 years after passage of the Act, the three agencies had not adopted policies or operating procedures to ensure that the process provided equitable cost deductions."

Comment: On page 7 the report states, "The Bureau consistently followed a cost accounting methodology for its computations . . . ." This would seem to imply that the Bureau of Land Management (BLM) had adopted an operating procedure. We disagree with the Office of Inspector General (OIG) that the process does not provide "equitable cost deductions." Our comments below will explain why we hold this belief.

[NOTE: Attached methodology not included by Office of Inspector General]

2. Page 7 - For Fiscal Years 1994-1996, "the Bureau did not accurately identify certain program and general administrative costs. The overstated cost deductions caused by these issues totaled $1,206,563." The OIG used as examples the amount of money spent on Indian minerals management (not chargeable to net receipts sharing), a 1-percent discrepancy in overhead rates, and an assertion that certain overhead charges such as personnel leave surcharges, Bureauwide changes of duty station, training center operations, and Washington Office should not have been charged.

Comment: The BLM believes that these charges are appropriate, subject to net receipts sharing, as they are part of the operations of a mineral leasing program. While the OIG contends that a portion should be prorated to Indian minerals management in general, employees are not hired to work solely on Indian lease management. In many cases, such work is only a minor part of their job and would result in a small deduction. Having said this, we nevertheless believe that the OIG did point out a methodological flaw with respect to mineral material sales. However, the net effect of this flaw is virtually insignificant.

We want to emphasize that the Act requires only an estimate of costs as the basis for net receipts sharing deductions computation. If the discrepancy over a 3-year period is about $1.2 million and total expenses applicable to net receipts sharing is over $200 million, a 1-percent difference is an estimation that deserves positive comment.

3. Page 8 - "During our review, we noted that the Bureau had not corrected the cost accounting deficiencies cited in this section for establishing its cost deductions for fiscal year 1997."

Comment: We do not do the net receipts sharing calculations until August of the fiscal year. Thus, we have not started the work for 1997.

-

'The BLM strongly believes that, since both land use pluming and National Environmental Policy Act compliance **must** be completed before a lease may be issued, there should be no question that such costs are deductible under net receipts **sharing**.

The responsible official for implementation is the Assistant Director for Minerals, Realty, and Resource Protection. A written request will be in the **Solicitor's** Office by July 31, 1997, asking that an opinion be provided to the BLM by the end of September 1997.

Attachment

STATUS OF AUDIT REPORT RECOMMENDATIONS

Finding/Recommendation Reference	Status	Action Required
Minerals Management Service		
1	Management concurs; additional information needed.	The Minerals Management Service should provide an action plan that includes target dates and titles of officials responsible for implementation.
Bureau of Land Management		
1	Implemented.	No further action is required by the Bureau of Land Management.
2	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 implementation.

ILLEGAL OR WASTEFUL ACTIVITIES SHOULD BE REPORTED TO THE OFFICE OF INSPECTOR GENERAL BY:

Sending written documents to: | Calling:

Within the Continental United States

U.S. Department of the Interior
Office of Inspector General
1849 C Street, N.W.
Mail Stop 5341
Washington, D.C. 20240

Our 24-hour
Telephone HOTLINE
l-800-424-5081 or
(202) 208-5300

TDD for hearing impaired
(202) 208-2420 or
l-800-354-0996

Outside the Continental United States

Caribbean Region

U.S. Department of the Interior
Office of Inspector General
Eastern Division - Investigations
1550 Wilson Boulevard
Suite 410
Arlington, Virginia 22209

(703) 235-9221

North Pacific Region

U.S. Department of the Interior
Office of Inspector General
North Pacific Region
238 Archbishop F.C. Flores Street
Suite 807, PDN Building
Agana, Guam 96910

(700) 550-7428 or
COMM 9-O11-671-472-7279

Toll Free Numbers:
1-800-424-5081
TDD 1-800-354-0996

FTS/Commercial Numbers:
(202) 208-5300
TDD (202) 208-2420

HOTLINE

1849 C Street, N.W.
Mail Stop 5341
Washington, D.C. 20240