



**OFFICE OF  
INSPECTOR GENERAL**  
U.S. DEPARTMENT OF THE INTERIOR

August 8, 2012

Memorandum

To: Eric Eisenstein  
Division Chief, Internal Control and Audit Follow-up  
Office of Financial Management

Gregory Gould, Director, Office of Natural Resources Revenue  
Office of Policy, Management and Budget

From: Charles Haman  
Central Regional Manager for Audits, Inspections, and Evaluations

Subject: Verification Review of Recommendations from our May 25, 2010, "Final Audit Report: Minerals Management Service: Royalty-In-Kind Program's Oil Volume Verification Process (Report No. C-IN-MMS-0007-2008)"  
Report No. CR-VS-ONRR-0005-2012

The Office of Inspector General (OIG) has completed a verification review of the four recommendations presented in the subject audit report. The objective of the review was to determine whether the Office of Natural Resources Revenue (ONRR) and the Bureau of Ocean Energy Management, Regulation and Enforcement (BOEMRE) implemented the recommendations. Based on our verification, we concluded that all four recommendations are resolved and implemented.

**Background**

Our May 25, 2010 report, "Minerals Management Service: Royalty-In-Kind Program's Oil Volume Verification Process" (Report No. C-IN-MMS-0007-2008), made four recommendations designed to assist the Minerals Management Service (MMS) in ensuring proper royalty collection during the phase-out of the Royalty-In-Kind (RIK) program. After we issued our report, MMS was reorganized into BOEMRE.

The Director of BOEMRE responded to our report on July 8, 2010, agreeing with all four recommendations and planned actions, target dates, and responsible officials. Based on the response, we considered recommendation 1 resolved and implemented and 2 through 4 resolved and not implemented. On September 29, 2010, we referred recommendations 2 through 4 to the Office of Financial Management (PFM), Office of Policy, Management and Budget to track their implementation. ONRR was subsequently moved out of BOEMRE and under the Assistant Secretary, Policy, Management and Budget on October 1, 2010. ONRR acted on recommendations 2 and 4, and both ONRR and BOEMRE acted on recommendation 3, with BOEMRE taking 3a and ONRR taking 3b. On October 1, 2011, BOEMRE was split into the

Bureau of Ocean Energy Management (BOEM) and Bureau of Safety and Environmental Enforcement (BSEE).

PFM informed us that all three recommendations had been implemented in memoranda dated March 23, 2011, June 27, 2011, and September 28, 2011.

## **Scope and Methodology**

The scope of this review was limited to determining whether ONRR and BOEMRE implemented the four recommendations as reported to OIG and PFM. To accomplish our objective, we reviewed the supporting documentation submitted to PFM by ONRR and BOEMRE relating to each of the recommendations. We also reviewed additional supporting documentation provided by ONRR when we started this review. We did not need to contact BOEM or BSEE officials during this review because PFM and ONRR provided us with all the supporting documentation we needed.

We did not perform any site visits or conduct any detailed fieldwork to determine whether the underlying deficiencies that were initially identified have actually been corrected. As a result, this review was not conducted in accordance with the Government Auditing Standards issued by the Comptroller General of the United States.

## **Results of Review**

Our review found that ONRR and BOEMRE implemented all four recommendations and that the closure actions by PFM are valid.

**Recommendation 1:** RIK should establish a tracking system for each property to ensure timely and proper reconciliation and resolution of imbalances.

**Action Taken:** We considered this recommendation resolved and implemented on September 29, 2010, based on the July 8, 2010 response to the final report, which stated that BOEMRE agreed with our recommendation and developed and implemented a Microsoft Project tracking sheet that lists all imbalances by offshore facility measurement points (FMP) in the RIK program from April 2004 to the present. We also confirmed the full implementation of this recommendation by reviewing the final RIK Oil Cash-Out Tracking Sheet printed on June 25, 2012.

**Recommendation 2:** RIK should appropriately document royalty calculations and ensure procedures are in place for a verification review of these calculations, especially for those properties with various royalty rates, royalty relief, and in-value leases.

**Action Taken:** We considered this recommendation resolved and not implemented on September 29, 2010, based on the July 8, 2010 response to the final report, which stated that BOEMRE agreed with our recommendation and enhanced its procedures to appropriately document and verify royalty calculations. Analysts were required to

complete spreadsheets demonstrating the calculations of royalty volumes, and supervisors would manually check samples of the calculations.

We considered this recommendation closed as of March 23, 2011, based on documentation provided by ONRR, including written procedures for the analysts and a template for the checklist required for every imbalance file. ONRR also provided the guidance requiring supervisory review of oil imbalance files for RIK phase-out.

We confirmed the full implementation of this recommendation after reviewing the documentation and ONRR's "RIK Imbalance Internal Management Review Report," completed on February 4, 2011. This report concluded that Asset and Sales Accounting (ASA) management has made a concerted effort to follow ASA policies and procedures for properly reconciling and resolving oil and gas volume imbalances; that ASA is reconciling volume imbalances according to the established policies and procedures; and that the issued case folders have all of the required documentation, signatures, and supervisory review.

**Recommendation 3:** MMS should establish a process to verify volume allocation methods used by companies on offshore leases.

**Action Taken:** We considered this recommendation resolved and not implemented on September 29, 2010, based on the July 8, 2010 response to the final report, which stated that BOEMRE agreed with our recommendation and would conduct a risk-based analysis to help determine the best method and tools available for verifying oil volume allocations for facility measurement points (FMP) with mixed royalty rate leases. Once the analysis was complete, BOEMRE would establish a process to verify volume allocation methods used by companies for offshore leases.

ONRR and BOEMRE addressed this recommendation jointly and split it into 3a, to be addressed by BOEMRE, and 3b, to be addressed by ONRR.

**Recommendation 3a:** PFM determined that BOEMRE met the intent of the recommendation and considered recommendation 3a as implemented and closed on September 28, 2011. BOEMRE reported that it and ONRR established a process to verify volume allocation methods used by companies on offshore leases with mixed royalty rates. ONRR conducts risk assessments and provides BOEMRE with an annual list of high-risk FMPs for BOEMRE to conduct well and lease allocation reviews. We considered this recommendation closed as of September 28, 2011, based on documentation provided by BOEMRE.

**Recommendation 3b:** PFM determined that ONRR met the intent of the recommendation and considered recommendation 3b as implemented and closed on June 27, 2011. PFM's determination was based on the process ONRR developed with BOEMRE to verify volume allocation methods and provide an annual list of high-risk FMPs for BOEMRE to review. We considered this recommendation closed as of June 27, 2011, based on documentation provided by ONRR.

We confirmed the full implementation of this recommendation after reviewing all the documentation regarding this recommendation.

**Recommendation 4:** RIK should update its “Royalty-In-Kind Operator Imbalance Phase Out Strategy & Procedures,” dated October 7, 2009, with additional process improvements, such as the threshold certification form, property checklist, and royalty calculation spreadsheet. This will ensure a comprehensive closeout strategy.

**Action Taken:** We considered this recommendation resolved and not implemented on September 29, 2010, based on the July 8, 2010 response to the final report, which stated that BOEMRE was in the process of updating its oil imbalance procedures to address recent improvements and provisions added since October 2009.

We considered this recommendation closed as of March 23, 2011, based on documentation provided by ONRR, including the “Revised Royalty-In-Kind Operator Imbalance Phase Out Strategy & Procedures,” updated August 5, 2010. ONRR also developed a checklist and certification forms for entitlements and write-offs.

We confirmed the full implementation of this recommendation after reviewing the documentation and the February 4, 2011 “RIK Imbalance Internal Management Review Report.” As with recommendation 2, the “Management Report” showed that ASA management and staff have worked to improve their processes and procedures and ensure proper documentation.

## **Conclusion**

We informed ONRR officials of the results of this review at an exit conference on July 25, 2012. The ONRR officials agreed with our results.

cc: Director, Bureau of Ocean Energy Management  
Audit Liaison Officer, Bureau of Ocean Energy Management  
Director, Bureau of Safety and Environmental Enforcement  
Audit Liaison Officer, Bureau of Safety and Environmental Enforcement