



Department of Energy
Washington, DC 20585

June 26, 2006

MEMORANDUM FOR THE CHIEF FINANCIAL OFFICER

FROM:


Rickey R. Hass

Assistant Inspector General
for Financial, Technology and Corporate Audits
Office of Audit Services
Office of Inspector General

SUBJECT:

INFORMATION: Review of Actions to Correct Financial Control
and Reporting Weaknesses; Audit Report No.: OAS-FS/CA-06-04

BACKGROUND

On May 9, 2006, we issued our third report on our *Review of Actions to Correct Financial Control and Reporting Weaknesses* (OAS-FS/CA-06-03). This series of reports has discussed our assessment of the actions taken by the Financial Management Project Management Office (FM PMO) and others to address the material weakness described in our *Report on the Department of Energy's Fiscal Year 2005 Financial Statements* (OAS-FS-06-01). The objective of this series of reports was to determine whether the Department of Energy's (Department) planned and completed corrective actions adequately address critical control weaknesses in its financial management and reporting process.

In our third report, we found that while progress was being made, a great deal of work remained to be completed. In many cases, the Department had completed policies and procedural guidance to address critical weaknesses and had initiated work to address those weaknesses. However, a number of key reconciliations had not been completed and information was not available for us to initiate our test work. We also found that planned completion dates for some corrective actions had slipped and that, in certain instances, deliverables for the implementation of revised policy guidance had not been developed. Given the limited amount of time available to resolve the remaining control weaknesses, we suggested that the Office of the Chief Financial Officer consider refocusing its efforts on the most critical areas and ensure that deliverables had been developed for all critical corrective actions. Management concurred with our suggestions, accelerated certain corrective actions and indicated that other actions to correct reported weaknesses had been completed.

This is our final report in this series. Remaining tests of control deficiencies that led to last year's material weakness will be accomplished during the Fiscal Year (FY) 2006 Consolidated Financial Statement Audit that is now underway.

RESULTS

While the Department has reported that it has made substantial progress, significant and sustained effort will be required to fully resolve remaining financial control and reporting weaknesses. Actions to address differences between integrated contractor (IC) trial balances and the Standard Accounting and Reporting System (STARS), a critically important issue, are well on their way to completion. As of June 15, 2006, the FM PMO reported that

reconciliations of most IC trial balances had been completed and are ready to be tested. The FM PMO also reported significant improvement in funds control through the reconciliations of all eight budget feeder systems to STARS with only minor unresolved differences. Progress has also been reported in resolving balancing edit errors, with the outstanding balance having been reduced by approximately \$46 billion.

Even though the Department is nearing resolution on a number of important issues, much remains to be done. In particular, reconciliation of the Accounts Payable and other STARS system modules must be completed soon. Unresolved edit errors, even though reduced significantly, currently amount to about \$8 billion, an amount that could have a material impact on the financial statements. Correction of these remaining issues is essential if the Department is to avoid negative impacts on the FY 2006 Financial Statement Audit.

Testing and Verification

Since our last report, tests of the reconciliation of budget feeder systems, IC trial balances, and certain system modules have begun. Even though progress has been made on reconciling system modules, it has been slow and has delayed certain audit tests. Additionally, it has been necessary to modify the testing approach for obligations because of system deficiencies identified early in the testing process. Specific information about each of the nine findings that we consider most critical to the FY 2006 Consolidated Financial Statement Audit is included below. The status of corrective actions and Office of Inspector General (OIG) verification work, as well as management's assertions regarding progress and additional issues or testing contemplated, are summarized in Attachment B.

Recording of Obligations (Finding 1): Status of Corrective Actions and Audit Tests – Being Operationalized.

Actions to correct issues regarding the recording of obligations remain in process. A memorandum that will be issued to field offices reinforcing good funds control business practices has been drafted and is in the review process. The FM PMO reports that all eight field sites using budget feeder systems have reconciled April data to STARS and only insignificant differences remain for six of the eight field sites involved. The April budget feeder system reconciliation for Oak Ridge is currently being tested.

Budget Execution and Control (Finding 2): Status of Corrective Actions and Audit Tests – In Process.

Progress in the development of training and procedural guidance has been noteworthy, and efforts to resolve differences between contractors' data and STARS are underway. Training programs for STARS and the I-MANAGE Data Warehouse have been completed and training is taking place. The review guide, STARS reports, and policies and procedures designed to facilitate the correction of data differences between STARS and contractor systems have also been completed. Testing of required STARS reports and reconciliation of contractor trial balances and related certifications began in May 2006. Efforts to reconcile unresolved differences at 5 of the 29 ICs are expected to be completed by June 2006. Additional information on the progress made in reconciling ICs trial balances is provided under Finding 12 below.

**Insufficient Supporting Documentation – Obligations and Undelivered Orders
(Finding 5): Status of Corrective Actions and Audit Tests – Being Operationalized**

Progress continues to be made in correcting system and reporting deficiencies related to obligations. We are in the process of reviewing supporting documentation for our sample of obligations transactions for four of the five field sites we selected for review. We also found that, with minor exceptions, obligations data were accurately reported in the Statement of Budgetary Resources. As previously noted, we revised our testing approach because of systems issues related to specific transaction details. Using the contracts selected, all obligations will be tested in selected months. Separate test work on the posting of obligations will be performed to test the accuracy of general ledger posting. Financial Statement Audit test work has, preliminarily, identified some transactions at a few sites that do not appear to have been entered into STARS in a timely manner. Feeder system reconciliations have been prepared with minor exceptions noted. Work on undelivered orders has begun and testing is expected to be conducted on the undelivered orders balance as of June 30.

Unrecorded Accounting Transactions (Finding 7): Status of Corrective Actions and Audit Tests – Completed.

While the Department has implemented controls over the Automated Standard Application for Payment (ASAP) system, procedures to ensure the proper posting of manual entries have not yet been developed. The addition of a cost flag and information in ASAP Exception Reports have made it easier for officials to correctly identify the transactions that require manual entries. However, written procedures for recording manual entries have not yet been established. We have completed our tests of both receipts and payments exceptions and found that manual entries were properly recorded.

Fund Balance with Treasury Reconciliation (Finding 9): Status of Corrective Actions and Audit Tests – In Process.

The Energy Finance and Accounting Service Center (EFASC) has assigned three people under a Team Leader to perform Fund Balance with Treasury (FBWT) reconciliations as it has been determined that the reconciliations are too cumbersome for one person. The Team Leader has indicated that it should take 30 to 60 days to identify and resolve the differences from one month's reconciliations. While the reconciliations have been prepared, they cannot be considered complete as there are differences from February through May that have still not been resolved. Timeliness of the completion of FBWT reconciliations remains a concern and the Team Leader hopes to have the February through May differences resolved by the end of July 2006.

Integrated Contractor Trial Balance Reconciliations (Finding 12): Status of Corrective Actions and Audit Tests – Being Operationalized.

Actions to address deliverables for correcting differences between IC trial balances and STARS are ongoing. Policies and procedures for reconciling and certifying IC trial balances have been updated and issued. As of June 15, 2006, the FM PMO reported that they have received all 29 of the April 2006 IC trial balance reconciliations. Officials indicated that 24 of the 29 reconciliations have been certified and are ready for audit test

work, while five ICs (Y-12, SNR, LBNL, SLAC, and Carlsbad) continue to have unresolved differences totaling \$729 million. Audit test work on the April 2006 reconciliation for Washington Savannah River Company has been completed and no exceptions were found. The five contractors with unresolved differences are receiving assistance in completing their reconciliations and expect that the differences will be resolved in June 2006.

Oracle Modules Reconciliations (Finding 13): Status of Corrective Actions and Audit Tests – In Process.

Differences continue to exist between certain systems modules and the STARS general ledger. With the exception of the Accounts Payable module, reconciliation procedures have been developed and implemented. The Fixed Asset module reconciliations for January through March 2006 have been tested and no exceptions were noted. For the Purchase Order module, testing has begun on variances identified during the March 2006 reconciliation. As of June 15, 2006, the FM PMO reported that remaining unresolved differences have been reduced to \$271 million. Efforts to reconcile the Accounts Payable module have an expected implementation date of July 2006. While progress continues for most modules, substantial work remains. Given these difficulties, we remain concerned that progress in this important area may not be sufficient to avoid negative impacts on the FY 2006 Financial Statement Audit.

Significant Balancing Edit Errors (Finding 14): Status of Corrective Actions and Audit Tests – Being Operationalized.

The Department has made progress in the implementation of processes and procedures to correct existing balancing edit errors and to prevent them from recurring in the future. The Deliverable Champion has indicated that EFASC has completed its research and has corrected five unresolved balancing edit errors from the FY 2005 Financial Statement Audit, totaling \$49.3 million. In addition, the Department also implemented new processes to prioritize the existing balancing and combination edit errors based upon the overall impact these transactions could have on the Department's financial statements. The new processes also transfer ownership of the edit errors to the field office that has the ability to resolve the errors in a timely and efficient manner. The Department is currently focusing on the edit errors they categorize as "critical" and "material" with significant progress noted in May. EFASC reported that the value of all unresolved edits has been reduced from \$54 billion to approximately \$8 billion. The Deliverable Champion's goal is to correct all existing "critical" edit errors and to reduce each "material" edit error to less than \$1 million by June 30. Overall dollar amounts have been reduced, however, remaining unresolved differences have the potential to materially impact the current audit.

Analysis of Budgetary/Proprietary Relationships (Finding 18): Status of Corrective Actions and Audit Tests – Completed.

Although reported as complete, actions to correct issues regarding the relationship between budgetary and proprietary accounts are still in process. Edit rules for the five items identified in the audit finding have been completed. Our review disclosed that

work has been completed on variance reports for three of the five items identified in the audit finding. The Deliverable Champion responsible for this area confirmed that the variance reports for Receivables and Payables have not yet been completed and estimated that it would be a couple of weeks before they were finished.

Deliverable Tracking

In our prior report, we noted that in some instances deliverables for monitoring and confirming that recently deployed policy guidance was properly implemented had not been developed. We suggested that the Office of the Chief Financial Officer develop deliverables to ensure that corrective actions are implemented and effective for all remaining critical findings. The FM PMO responded by developing its Critical Issue Tracking Report that includes due dates, measures and targets for all remaining critical findings. We consider this an important tool for tracking the full resolution of findings.

However, our review disclosed that planned completion dates for three critical actions have slipped. Based on our review of the latest version of the Updated Mapping report, dated June 5, 2006, two critical actions have slipped. Specifically, for Finding 2, deliverables for the development and testing of reports to be used for analyses of the third quarter financial statements have slipped by one month. Additionally, for Finding 9, deliverables for creating detailed desk procedures for preparing FBWT reconciliations have slipped by two months. Based on information provided by the FM PMO on June 12, 2006, for Finding 13, the deliverable for reconciling the Accounts Payable module has slipped by one month to July 2006. While we are encouraged by the progress made by the Department, these difficulties could pose significant risk to the completion of this year's audit.

Resolution of Remaining Weaknesses

Since our last report, the Department has increased the focus and tempo of its efforts to resolve control deficiencies and to provide information necessary to perform the FY 2006 Financial Statement Audit. In recent weeks, progress has been demonstrated in correcting the issues associated with budget feeder systems and balancing edit errors – issues critical to this year's audit. Reconciliations of certain IC trial balances have been certified by the Department and testing of those procedures has begun.

However, more remains to be done to resolve reconciling differences associated with the Department's FBWT and various systems modules. Additionally, we believe that correction of the remaining unresolved balancing edit errors, as well as any new errors that may occur in the current month, represent a significant challenge. The remaining unresolved differences associated with the five IC trial balances are also significant and will most likely require substantial effort to correct. These issues, and other unresolved problems, could impact the Department's ability to meet this year's financial statement reporting deadlines.

SUGGESTED ACTION

We suggest that the Office of the Chief Financial Officer continue to realign resources and refocus efforts as necessary to effectively address ongoing unresolved issues.

MANAGEMENT REACTION

Management concurred with our assessment and suggested action. Management's comments regarding the status of various corrective actions have been incorporated into the table contained in Attachment B. The full text of management's comments is contained in Attachment C.

AUDITOR RESPONSE

Management's comments are responsive to our suggestion.

Attachments

cc: Deputy Secretary
Chief of Staff
Director, Office of Finance and Accounting

Attachment A**OBJECTIVE, SCOPE AND METHODOLOGY****OBJECTIVE**

To determine whether the Department's planned and completed corrective actions adequately address critical control weaknesses in the financial management and reporting process.

SCOPE

The review was performed from April 29, 2006, through June 15, 2006, at Department of Energy Headquarters and the Oak Ridge Financial Service Center. The review covered the Updated Mapping Report dated June 5, 2006, the Critical Issue Tracking Report provided to us on June 7, 2006, and the nine findings that are most critical to the completion of the FY 2006 Financial Statement Audit.

METHODOLOGY

To accomplish the review objective, we:

- Reviewed Exhibit A of the FY 2005 Management Letter, the Updated Mapping Report dated June 5, 2006, and the Critical Issue Tracking Report provided to us on June 7, 2006;
- Conducted interviews at Headquarters and the Oak Ridge Financial Service Center;
- Reviewed supporting documentation, guidance, correspondence, draft and final policies and procedures;
- Conducted tests at Headquarters and the Oak Ridge Financial Service Center, as appropriate, to determine if corrective actions had been implemented; and,
- Incorporated the results of tests performed by the independent public accounting firm as appropriate.

During this review, we focused our testing of corrective actions on the nine findings that we and the independent public accounting firm conducting the audit considered to be the most critical to the FY 2006 Audit of the Department's Consolidated Financial Statements. A complete status listing of the items we consider to be critical is contained in Attachment B. Ultimately, verification testing for all findings will be completed during the FY 2006 Financial Statement Audit.

This review was adjunct to and not an integral part of the FY 2006 Financial Statement Audit. The work completed during the course of this review was substantially less in scope than an examination whose objective is to express an opinion on the Department's financial statements. Accordingly, we do not express such an opinion. Had we performed such an examination, additional matters may have come to our attention and been reported to management. The possibility also exists that action to address financial management control weaknesses, although considered to be sufficient based on our preliminary review, may prove to not be completely effective once tested in an operational environment as part of the financial statement audit.

Other potential issues could adversely impact the upcoming audit. Specifically, because of the material weaknesses identified during the FY 2005 Financial Statement Audit, the independent public accounting firm was not able to perform the full suite of tests it would normally complete during the audit. Had it done so, it is possible that additional weaknesses may have been identified. As such, subsequent detailed testing performed during the FY 2006 Financial Statement Audit may uncover additional weaknesses that could jeopardize the successful completion of that effort.

Attachment B

STATUS OF CORRECTIVE ACTIONS¹

Description of Finding ²	FM PMO Planned Completion	FM PMO Reported Status	Status of OIG Testing	OIG's Comments	FM PMO Comments
Recording of Obligations -- Finding 1		Being Operationalized	Tests are underway	The Oak Ridge budget feeder system reconciliation is being tested. Tests of others expected to begin in July 2006.	April reconciliations complete with immaterial differences. May reconciliations are underway.
Budget Execution and Control -- Finding 2	June 06	In process	Tests are underway	Testing of STARS reports and reconciliations of IC trial balances began in May 2006. Tests will be performed as IC trial balances are provided for audit.	April reconciliations for 23 of the 28 contractors are complete and available for review. Differences of \$730M are being worked for the remaining 5 contractors.
Insufficient Supporting Documentation -- Obligations and Undelivered Orders -- Finding 5		Being Operationalized	Test of Headquarters obligations complete -- tests of field obligations and undelivered orders are underway.	We revised our testing approach because of systems issues related to specific transaction details. Initial results indicate some transactions were not timely, and minor differences between Schedule A and the Statement of Budgetary Resources.	While reports comprising the scope of the audit recommendations have been provided to the auditors, we will continue to support them as they perform their testing in this critical audit area.

¹ Status is presented for the nine findings we consider critical to the FY 2006 Financial Statement Audit.

Description of Finding ²	FM PMO Planned Completion	FM PMO Reported Status	Status of OIG Testing	OIG's Comments	FM PMO Comments
Unrecorded Accounting Transactions – Finding 7		Completed	Tests of receipts and payments have been completed.	Tests of receipts and payments exceptions found no errors. Written procedures for posting manual entries have not been developed.	Renewed emphasis on roles and responsibilities and increased management review will ensure this finding does not repeat. The Department will review existing procedures and determine if modifications are required.
Fund Balance with Treasury Reconciliation – Finding 9	July 06	In process	Corrective actions not sufficiently complete to permit testing.	Test work will begin on the process once remaining differences are resolved for January through May 2006.	Staff remain focused on the completion of the reconciliations. <i>January through May 2006 reconciliations are available and were provided to the OIG.</i>
Integrated Contractor Trial Balance Reconciliations – Finding 12	June 06	Being Operationalized	Tests are underway	Westinghouse Savannah River Corporation test work completed and Lawrence Berkeley National Laboratory test work is underway. Once other reconciliations are received, testing will commence. Five contractors have material unresolved differences which are expected to be resolved in June.	[Comments are the same as Finding 2] April reconciliations for 23 of the 28 contractors are complete and available for review. Differences of \$730M are being worked for the remaining 5 contractors

Description of Finding ²	FM PMO Planned Completion	FM PMO Reported Status	Status of OIG Testing	OIG's Comments	FM PMO Comments
Oracle Modules Reconciliations - Finding 13	July 06	In process	Purchase Order and Accounts Receivable module testing in process. Accounts Payable module testing has not yet started.	Currently testing resolution of differences in Purchase Order and Accounts Receivable modules but unresolved differences remain in the Purchase Order module. Fixed Assets module tested with no exceptions. Accounts Payable module reconciliations not expected to be completed until July 2006.	Monthly reconciliations are performed for the FA, AR and PO modules. There are no unresolved differences for the FA and AR modules. Unresolved differences for the PO module currently amount to \$271M. The Department continues to focus efforts on AP module reconciliation.
Significant Balancing Edit Errors - Finding 14	June 06	Being Operationalized	Corrective actions not sufficiently complete to permit testing.	We will begin our analysis of the resolution of edit errors after the status report becomes available in June.	Resolution of Balancing Edit Errors is an ongoing operation and a top priority for the Department. The current focus is resolution of critical material edits errors which amount to \$7,720M.

Description of Finding ²	FM PMO Planned Completion	FM PMO Reported Status	Status of OIG Testing	OIG's Comments	FM PMO Comments
Analysis of Budgetary/Proprietary Relationships Finding 18		Completed	Corrective actions not sufficiently complete to permit testing.	Three of the five Discoverer reports have been completed. The remaining two reports are expected to be complete in June, at which time testing will begin.	Actions to respond to the FY05 Audit Finding are complete. Existing edits capture Budgetary/Proprietary variances. These variances are then resolved through the edit error resolution process (refer to Finding 14). Even though new reports and procedures are being developed, Treasury's requirements for the analysis of Budgetary/Proprietary variances are being met with the current edit process.

² References are to audit findings contained in the Financial Statement Management Letter Report, DOE/OAS-FS-06-04, issued on December 15, 2005.

Attachment C**Financial Management Project Management Office (FMPMO) response to the
OIG's final report on their *Review of Actions to Correct Financial Control and
Reporting Weakness*.**

The FM PMO appreciates the OIG's recognition of the significant progress made by the Department in resolving our financial management and audit challenges surrounding the material weakness described in your *Report on the Department of Energy's Fiscal Year 2005 Financial Statements*. We concur with your latest overall assessment of the Department's position and are equally concerned with the amount of work remaining to be accomplished. In addition, we concur with the suggested action and will continue to re-align resources and re-focus efforts, as necessary, to effectively address any unresolved issues.

With regard to the "Results" section of the report, the FM PMO offers the following clarifying remarks and most up to date information:

- 23 of the 28 integrated contractor trial balance reconciliations for April have been certified as complete, and all of these are available for audit review (the two Bechtell Jacobs contracts at OR are treated as one IC). Differences of \$729M are being worked for the remaining five.
- The Department is focused on resolution of the critical material edit errors greater than \$1M. As of June 6, 2006, the edit errors balance was \$7,720M representing an 88% reduction since May 5, 2006.
- Deliverables marked as slipped in the "Deliverable Tracking" section were actually deliberately revised to accommodate changing priorities. In the case of Funds Balance with Treasury, draft procedures are in use today and finalization of the procedure documentation has been deferred until the reconciliation backlog is complete.
- Regarding Finding 9 – Funds Balance with Treasury – we have a concern that the OIG and independent auditors have confused this issue with the Treasury Statement of Differences. Attached is an email from the EFASC Director to clarify what is being done on both counts.

In addition, we have added summary-level finding specific comments to the "Status of Corrective Action" table attached to the report.

Thank you for the opportunity to comment on this final report. We look forward to continuing to work with you and the independent auditors as efforts for the FY 2006 Financial Statement audit proceed.