

U.S. DEPARTMENT OF ENERGY
OFFICE OF INSPECTOR GENERAL

REPORT ON MATTERS IDENTIFIED AT THE
HANFORD SITE
DURING THE AUDIT OF THE DEPARTMENT OF ENERGY'S
CONSOLIDATED FISCAL YEAR 1999 FINANCIAL STATEMENTS

Report Number: WR-FS-00-01
Date of Issue: March 15, 2000

Western Regional Audit Office
Albuquerque, New Mexico 87185

REPORT ON MATTERS IDENTIFIED AT THE
HANFORD SITE
DURING THE AUDIT OF THE DEPARTMENT OF ENERGY'S
CONSOLIDATED FISCAL YEAR 1999 FINANCIAL STATEMENTS

TABLE OF CONTENTS

	<u>Page</u>
SUMMARY.....	1
PART I - APPROACH AND OVERVIEW.....	2
Introduction.....	2
Scope and Methodology.....	2
Observations.....	3
PART II - AUDIT RESULTS.....	4
Environmental Liabilities Understated for Closure of Single Shell Tank Farms.....	4

U.S. DEPARTMENT OF ENERGY
OFFICE OF INSPECTOR GENERAL
OFFICE OF AUDIT SERVICES
WESTERN REGIONAL AUDIT OFFICE

REPORT ON MATTERS IDENTIFIED AT THE
HANFORD SITE
DURING THE AUDIT OF THE DEPARTMENT OF ENERGY'S
CONSOLIDATED FISCAL YEAR 1999 FINANCIAL STATEMENTS

Audit Report Number: WR-FS-00-01

SUMMARY

The Government Management Reform Act of 1994 requires that the Department of Energy (DOE) annually submit audited financial statements to the Office of Management and Budget (OMB). A departmentwide audit was conducted to determine whether there was reasonable assurance that DOE's consolidated Fiscal Year (FY) 1999 financial statements were free of material misstatements. We conducted a portion of the departmentwide audit at the Richland Operations Office (Richland); Office of River Protection (ORP); CH2M Hill Hanford Group, Incorporated (CH2M Hill); Bechtel Hanford, Incorporated (Bechtel); and Fluor Hanford, Incorporated (Fluor) and its subcontractors.

The audit disclosed an error, as of September 30, 1999, in the Environmental Liabilities account. Richland's Environmental Liabilities account was understated because the cost estimates for closure of single shell tank farms had not been updated to reflect current engineering estimates.

We recommended that Richland adjust the Environmental Liabilities account and that management review other project cost estimates to determine if estimates were based on the best available data. Management concurred with the recommendations and implemented corrective actions.

Office of Inspector General

PART I

APPROACH AND OVERVIEW

INTRODUCTION

The Government Management Reform Act of 1994 requires that audited financial statements covering all accounts and associated activities of DOE be submitted annually to OMB. A departmentwide audit of the consolidated FY 1999 financial statements was conducted by examining internal controls, assessing compliance with laws and regulations, evaluating accounting transaction cycles, and testing selected account balances at various DOE facilities.

The objective of the departmentwide audit was to determine whether DOE's consolidated financial statements presented fairly, in all material respects, the financial position of DOE as of September 30, 1999 and 1998, and its consolidated net cost, changes in net position, budgetary resources, financing activities, and custodial activities for the fiscal years then ended in conformity with generally accepted accounting principles. Departmentwide issues are addressed in Audit Report No. DOE/IG-FS-00-01, issued February 17, 2000.

The purpose of this report is to inform Richland and ORP management of matters that came to the attention of the Office of Inspector General (OIG) during the audit at the Hanford Site. ORP is responsible for the Hanford Site's tank waste remediation system. Richland is responsible for the account balances entered into DOE's core accounting system.

SCOPE AND METHODOLOGY

The audit was conducted from July 1999 through January 2000 at the offices of Richland, ORP, CH2M Hill, Bechtel, and Fluor at the Hanford Site, Washington. Specifically, we examined internal controls, assessed compliance with applicable laws and regulations, and selectively tested account balances reported to DOE Headquarters to satisfy departmentwide audit objectives.

The audit was performed in accordance with generally accepted Government auditing standards for financial audits. Since we relied on computer-generated data, we evaluated the general and application control environment of certain financial systems and evaluated the reliability of the data on a test basis.

Because the audit was limited, it would not necessarily disclose all of the internal control weaknesses that may have existed. Furthermore, because of inherent limitations in any system of internal controls, errors or irregularities may nevertheless occur and not be detected. The issues addressed in this report represent our observations of activities through the end of fieldwork on January 31, 2000. Projection of any evaluation of the internal controls to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

In addition to the audit work conducted by the OIG, an independent public accounting firm reviewed certain audit cycles. The independent public accounting firm reviewed the Overview, including expanded EDP procedures, Disbursement, and Financing cycles at Richland. The OIG reviewed the Environmental Liabilities cycle at Richland, ORP, CH2M Hill, Bechtel, and Fluor.

The OIG considered all findings generated as a result of the reviews when preparing the departmentwide report and the management report referred to in that report. The OIG is addressing issues requiring local management's attention in this report.

An exit conference was held with the Director of Richland's Financial Division on February 29, 2000.

OBSERVATIONS

Richland's Environmental Liabilities account was understated by \$172 million because ORP and CH2M Hill had not updated the cost estimate for closure of single shell tank farms to reflect current engineering estimates. We recommended that Richland adjust the Environmental Liabilities account and that Richland and ORP review other project cost estimates to determine if they use the best available data. Management concurred with the finding and recommendations and implemented corrective actions.

Part II of this report provides additional details concerning the audit results and management's comments.

PART II

AUDIT RESULTS

Environmental Liabilities Understated for Closure of Single Shell Tank Farms

Statement of Federal Financial Accounting Standards No. 6, *Accounting for Property, Plant, and Equipment*, states that cleanup cost estimates must be revised periodically to account for material changes due to inflation or deflation and changes in regulations, plans and/or technology. It also states that new cost estimates should be provided if there is evidence that material changes have occurred. However, the costs for closure of single shell tank farms had not been updated to reflect current engineering estimates. This occurred because ORP and CH2M Hill focused funding and management efforts on planning and cost estimating for near-term activities. The cost estimates for out-year activities, such as closing the single shell tank farms, therefore received little management review since preparation of the initial cost estimate. As a result, Richland's Environmental Liabilities account was understated by \$172 million.

Recommendations

We recommend that Richland and ORP:

1. Adjust the Environmental Liabilities account upward by \$172 million; and,
2. Review other project cost estimates to determine if they use the best available data.

Management's Response

Management concurred with the finding and recommendations and adjusted the Environmental Liabilities account by \$172 million. ORP stated that it had previously made a management decision not to update the estimate for single shell tank farm closure. Management reasoned that there were uncertainties surrounding the cost estimates because they were out-year estimates. Additionally, management considered the recommended adjustment to be immaterial to the financial statements and to the total estimated program cost of \$7.2 billion for waste retrieval and closure of single shell tank farms (retrieval program). Although management concurred with Recommendation 2, ORP stated that it believed that the recommendation was already fully implemented because projects are continually reviewed and cost estimates are refined as additional information becomes available.

Auditor Comments

Management action is responsive to Recommendation 1. We agree with management that \$172 million is not material to either the financial statements or the \$7.2 billion cost of the retrieval program. However, the \$172 million is material to the specific project in question. For closure of single shell tank farms, the \$172 million represents a 59.9 percent increase over the existing baseline estimate of \$287 million. It is at this level that the cost estimates are developed.

The \$7.2 billion cost for the retrieval program is simply a roll up of the cost estimates for many individual projects.

Management's concurrence to review other project cost estimates is responsive to Recommendation 2. The OIG agrees that ORP has been performing reviews of project cost estimates. However, information obtained during the audit indicated that management's efforts were focused on near-term activities. According to CH2M Hill's Single Shell Tank Program Manager, there has been little funding available to perform any type of detailed cost estimating needed to update out-year project cost estimates.

CUSTOMER RESPONSE FORM

The Office of Inspector General has a continuing interest in improving the usefulness of its products. We wish to make our reports as responsive as possible to our customers' requirements, and therefore ask that you consider sharing your thoughts with us. On the back of this form, you may suggest improvements to enhance the effectiveness of future reports. Please include answers to the following questions if they are applicable to you:

1. What additional background information about the selection, scheduling, scope, or procedures of the audit would have been helpful to the reader in understanding this report?
2. What additional information related to findings and recommendations could have been included in this report to assist management in implementing corrective actions?
3. What format, stylistic, or organizational changes might have made this report's overall message more clear to the reader?
4. What additional actions could the Office of Inspector General have taken on the issues discussed in this report which would have been helpful?

Please include your name and telephone number so that we may contact you should we have any questions about your comments.

Name _____ Date _____

Telephone _____ Organization _____

When you have completed this form, you may telefax it to the Office of Inspector General at (202) 586-0948, or you may mail it to:

Office of Inspector General (IG-1)
Department of Energy
Washington, D.C. 20585

ATTN.: Customer Relations

If you wish to discuss this report or your comments with a staff member of the Office of Inspector General, please contact Wilma Slaughter at (202) 586-1924.

The Office of Inspector General wants to make the distribution of its reports as customer friendly and cost effective as possible. Therefore, this report will be available electronically through the Internet at the following address:

U.S. Department of Energy Management and Administration Home Page
<http://www.ig.doe.gov>

Your comments would be appreciated and can be provided on the Customer Response Form attached to the report.