CR-B-99-01

AUDIT REPORT

THE U.S. DEPARTMENT OF ENERGY'S WORKING CAPITAL FUND

OCTOBER 1998

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

DEPARTMENT OF ENERGY
Washington, DC 20585

October 1, 1998

MEMORANDUM FOR THE DIRECTOR, BUSINESS MANAGEMENT STAFF

FROM: William S. Maharay
Acting Manager, Capital Regional Audit Office,
Office of Inspector General

SUBJECT: INFORMATION: Audit Report on the Department's Working Capital Fund

BACKGROUND

The Department established the Working Capital Fund (Fund) in January 1996 as a financial management tool for charging the costs of common services provided at Headquarters to Departmental program offices. The objectives in establishing the Fund were to increase efficiency of the Department's operations, improve management of administrative services through the use of flexible and business-like finance methods, and provide an accurate full cost budget for programs and activities.

RESULTS OF AUDIT

Although the Fund is making progress in meeting its objectives, additional management attention could result in further cost reductions to the Department. The operation of the Fund promoted economies and efficiencies in the use of administrative services by the Department and met the expectations established by the Congress. Despite these achievements, we identified three areas that require additional management attention to facilitate further cost reductions in the Department's operations.

First, HR incurred a disproportionate share of the Fund's costs. HR did not focus enough attention on minimizing its own use of mail, telephone, and LAN services provided through the Fund. As a result of unnecessary subsidies to business lines, HR created false economies and efficiencies for the other Departmental programs and forfeited the opportunity for savings to the Department as a whole. HR resource managers should implement a process to optimize their use of Fund services and periodically perform comparative analysis of use to that of other organizations.

Second, the operation of the Department's supply business has posed persistent financial and management problems. The Board had not developed procedures to assess whether Fund business lines are competitive with outside vendors, correct inefficient operations, and shut down those unable to compete. The Fund Board risked permitting inefficient, noncompetitive business lines to continue. We recommend that HR develop procedures to periodically assess business lines for efficiency and cost effectiveness in providing their goods and services. In addition, procedures need to be developed to address how and when to discontinue business lines that cannot compete with outside sources.

Third, the Fund's financial management system (FMS) did not efficiently provide timely and accurate information. During the latter part of Fiscal Year 1996 when system implementation steps were initiated, Fund management did not fully coordinate their efforts with the business line managers and the CFO in designing and implementing an integrated financial management system. In Fiscal Year 1997, the Department spent about $202,000 on modifications to the billing system without effectively addressing the performance problems. Fund Management and the business lines in conjunction with the CFO should take steps to improve the performance of the FMS.

MANAGEMENT REACTION

Management concurred with the findings and recommendations and agreed to take corrective actions. The Office of Human Resources and Administration planned to: (1) review their use of Fund services during the first half of Fiscal Year 1999, (2) develop procedures both for cost effectiveness comparisons and for deciding whether and how to discontinue services, (3) develop procedures that require a case-by-case review by the Fund manager of any new system purchases, and (4) coordinate with the CFO and CIO on the BMIS initiative.

The U.S. Department Of Energy's Working Capital Fund

TABLE OF CONTENTS

Overview

INTRODUCTION AND OBJECTIVE

The Department established the Working Capital Fund (Fund) in January 1996 as a financial management tool for charging the costs of common services provided at Headquarters to Departmental program offices. Prior to establishing the Fund, the Office of Human Resources and Administration (HR) paid most of the costs of these services from the Departmental Administration account without attempting to allocate the costs back to the programs using the services. Since the Fund's implementation, Departmental program offices have made periodic advance payments to the Fund from their program direction accounts and are then charged for the services they consume. The Department's objectives in establishing the Fund were to increase efficiency of the Department's operations, improve management of administrative services through the use of flexible and business-like finance methods, and provide an accurate full cost budget for programs and activities. The costs of the services administered by the Fund are expected to total about $80 million in Fiscal Year 1998, which excludes Federal salaries and some other indirect charges incurred by HR.

The Fund organization consists of a Board, a Fund manager, business line managers, and customer program managers. The Board is made up of representatives from Departmental programs appointed by the Deputy Secretary. The Board and its components oversee development of pricing policy, administrative controls, and coordination of dispute resolution. The Office of Human Resources Business Management staff (HR-1) is responsible for the Fund's financial position. This includes overseeing billing, revenue, cost, and budget activities. The business line managers monitor and control the costs of services provided through the Fund's 10 business lines. The Office of Administrative Services (HR-2) oversees five business lines: Building Occupancy, Printing and Graphics, Copying, Mail Services, and Supplies. The Office of Information Management (HR-4) oversees three business lines: Telephones, Networking, and Desktop Support. The Office of Procurement and Assistance (HR-5) oversees the Contract Closeout Business Line. The Office of Personnel Policy, Programs and Assistance (HR-3) and the Office of Budget (CR-14) manages the newly added Payroll and Personnel business line. Customer program managers oversee purchases of administrative services offered by the business lines and, when possible, seek out opportunities to optimize resource use and keep administrative costs to a minimum.

To support its operation, the Fund operates a financial management system (FMS) that links the business lines to the Department's Headquarters accounting system. Each business line uses an information system, referred to as a feeder system, to collect and export monthly billing information to HR-1. HR-1 summarizes the data imported from the feeder systems using a billing information system. The billing system is used to create the customers' monthly billing reports and export data to the Department's Headquarters accounting system, which feeds the Department's core accounting system.

The House of Representatives Committee on Appropriations (Committee) supports the Department's use of the Fund in the annual budget request. The Committee's approval of the Fund for Fiscal Years 1997 and 1998 was contingent on the Department establishing administrative controls to ensure the following:

- Federal salaries or other expenses of Federal employees should not be charged to the Fund.
- Departmental representation on the Board establishing policies and procedures must be broad based and include smaller organizations.
- Pricing policies must be sound, defensible, and not include added factors for administrative costs.
- Advance payments from customers must be no more than necessary to cover outstanding commitments.
- A process must be established to dispose of excess advance payments.
- The Fund must not be managed in a manner that produces a profit.
- The Fund must not be used as a vehicle for maintaining unencumbered funds.
- The Fund must be audited each year by the Office of Inspector General.

The objective of the audit was to determine whether the Fund was operated in an economic and efficient manner. In addition, we followed up on management's progress on implementing recommendations from last year's audit of the Fund.

CONCLUSIONS AND OBSERVATIONS

Although the Fund was making progress in meeting its objectives, additional management attention could result in further cost reductions to the Department. The operation of the Fund promoted economies and efficiencies in the use of administrative services by the Department and met the expectations established by the Congress. In addition, Fund management implemented corrective actions for recommendations issued during last year's audit, continued to improve the operation of the Fund, and assisted another Government agency in developing its own working capital fund.

Cost Reductions

The operation of the Fund promoted economies and efficiencies in the use of administrative services by the Department. During Fiscal Years 1997 and 1998, actual costs incurred by the Fund have been lower than budgeted amounts. In Fiscal Year 1997, the total costs for the Fund totaled about $3 million less than the budgeted amount based on historical use. This trend continued into Fiscal Year 1998 when the budget estimate for the Fund was $85.2 million. Yet, as of the end of the second quarter, the Department was on track to spend only $79.2 million. Fund management reported that these savings were primarily the result of the participation by program managers in the day-to-day decision making in the consumption of the goods and services offered by the Fund. In our survey of program customers, the majority stated that they had taken a proactive approach to reduce overhead costs through reductions in use of office space, telephone lines, supplies, and mail stops. Also, business line managers continued to contribute to cost reductions. For instance, the Mail Services Business Line reduced the cost per mail stop from $10,000 to $9,500 after the first quarter of this year through a reduction in the support service contract.

Congressional Expectations

Fund management followed administrative controls that met the expectations established by the Congress. Specifically, we reviewed costs incurred by the Fund for the inclusion of Federal salaries or other expenses of Federal employees in the Fund and found none. We observed that the representation on the Board was broad based and included smaller organizations. We concluded last year that the pricing policies were sound and defensible and were unchanged this year. We tested the administrative controls without identifying any discrepancies or exceptions. Through review of the financial statements and pricing policies, we concluded that the Fund was not being managed in a manner that produced a profit.

Fiscal Year 1997 Audit

Fund management concurred with and implemented corrective actions to resolve prior year audit recommendations. During the Fund's first full year, we conducted an audit and issued the report, "Audit of the Internal Control Structure of the Department of Energy's Working Capital Fund," No. CR-B-98-01, dated October 8, 1997. We addressed four conditions that required management's attention. In response to these conditions, Fund management developed formal policies and procedures and began conducting quarterly financial reviews of the business lines. Our recommendation that the Board consider a simpler allocation process for billing contract audit services was resolved by the Committee. In its Fiscal Year 1998 report, the Committee recommended that the Contract Audit Business Line be removed from the Fund. The Committee reported that costs incurred for contract audits were direct costs and, as such, should not be included in the Fund. More recently, the Fund manager addressed our recommendation to identify and provide information to the Board on all direct and indirect costs associated with the operation and administration of the Fund. During May 1998, the Fund manager issued a paper on inclusion of Federal salaries and other indirect costs in the Fund and the impact on the viability of each business line if these costs were included in the pricing structure for Fiscal Year 2000.

Continued Improvements In Fund Operations

Fund management continued its efforts to improve the operation of the Fund during Fiscal Year 1998. The Fund emphasized using newly created reports from the Headquarters accounting system to assist business line managers and customers in decision making. The Office of Chief Financial Officer (CFO) began preparing financial statements, which are expected to improve financial management of business lines. Also, the CFO, Office of Financial Policy, issued new guidance on the handling of advance payments including how to treat one-year appropriations.

Program customers responded favorably to questions pertaining to the Fund's performance in meeting its objectives. We asked 24 program resource managers to respond to questions pertaining to the Fund's performance, their efforts to satisfy the Fund's objectives, and ways to improve the operation of the Fund. Sixteen managers responded to the survey and the majority responded that they:

- were satisfied with the Fund's operation,
- believed the Fund had met its objective of initiating cost savings by allowing managers to oversee the day-to-day use of goods and services,

- would accept reductions in services if necessary to benefit the Department as a whole,
- advanced payments to the Fund in a timely manner,
- thought the level of detail provided by the monthly bill was adequate,
- were not willing to use their money to pay for new financial management systems,
- had not purchased or developed internal financial management systems to assist in managing their use of the Fund's goods and services,
- did not use a significant amount of human resources to manage their use of the Fund's goods and services, and
- did not want additional business lines added to the Fund.

In addition, Fund management was in the process of assisting the Central Intelligence Agency (CIA) in developing its own working capital fund. CIA representatives learned through a Government contractor organization that the Department's Fund could be used as a benchmark. On several occasions, CIA representatives attended Fund Board meetings and met with key officials to examine Fund operation both from the customer and business line perspective. One CIA official stated that they were impressed with the relationship between Fund management and its customers as well as the flexibility of its operation.

Additional Attention Required

Despite these achievements, we identified three areas that require additional management attention to facilitate further cost reductions in the Department's operations. Specifically:

- HR incurred a disproportionate share of the Fund's costs. As a result of subsidies and inefficiencies, HR forfeited the opportunity for savings to the Department.

- The operation of the Department's supply business has posed persistent financial and management problems, including estimated financial losses of over $1 million. Without procedures to assess performance, the Fund risked permitting inefficient, unprofitable, and noncompetitive business lines to continue operating indefinitely.

- The Fund's FMS did not efficiently provide timely and accurate information. As a result of an uncoordinated approach to system development, the Department spent about $202,000 during Fiscal Year 1997 without effectively addressing the system's performance problems.

/S/
Office of Inspector General

Use Of Fund Resources

Reasonableness Of Fund Costs

As a customer organization, HR incurred a disproportionate share of the Fund's costs. During Fiscal Year 1997, HR accounted for 17.9 percent (1,213) of the Department's 6,788 Federal and contractor staff working in the Capital area, but expended 23.5 percent of the $79.8 million Fund. Analysis of use in the business lines providing mail, telephone, and network services underscores the disparity in expenditures. For example, in Fiscal Year 1997:

- HR funded 36 mail stops at a cost of $378,000 excluding the cost of space and other Federal subsidies. The average number of mail stops for the Department's other customer organizations was only three. We also observed that many HR-sponsored mail stops shared the same floor of the same building.

- HR's use of telephone services was also disproportionately higher than that of other customer organizations. HR funded over 2,600 telephone lines while employing about 1,213 Federal and contractor employees. Other customer organizations were able to work with a smaller ratio of telephone lines to employees.

- A similar condition existed in HR's use of network services. HR funded over 1,400 local area network (LAN) connections while employing 1,213 Federal and contractor workers.

In Fiscal Year 1997, HR was the largest user of Fund services across all business lines. On average, each HR employee (Federal and contractor) used about $15,400 of the Fund's goods and services. The average use of Fund goods and services per non-HR employee was about $10,900. HR's above average use continued into Fiscal Year 1998, and future budget projections suggest it will continue into Fiscal Year 1999.

HR management officials provided several explanations for the above average usage rates. For example, HR pays for the space used by Departmental services such as the health centers, libraries, and similar services. Also, HR bears the cost for all unassigned telephone and LAN connections located throughout the Headquarters complex and the supply costs incurred by contractors working for HR. Moreover, the officials explained that reductions in its administrative staff while maintaining its full range of service operations resulted in the disproportionately high number of mail stops. Finally, HR management stated that in some cases reducing HR usage would have meant transferring costs to other customers rather than reducing overall Departmental spending. While these explanations could justify some above average usage, officials agreed that more effort is needed to identify and reduce inefficiencies in the use of Fund services.

Review And Analysis Of Fund Costs Expected To Meet The Fund's Objectives

One of the goals of the Fund is to increase the efficiency of the Department's operations by having the cost of administrative services reflected in day-to-day decision making by program managers. To keep administrative costs to a minimum, customer organizations must be proactive in seeking out opportunities to optimize resource use and by comparing their performance with other users.

Review Approach Not Implemented

HR did not focus enough attention on minimizing its own use of mail, telephone, and LAN services provided through the Fund. For example, HR did not have a method for determining who was using its assigned telephone lines. In addition, HR had not completed a comprehensive inventory of desktop computers, which would have been helpful in identifying unused network connections. Although we were provided some valid reasons for HR's higher use of certain services, management had not conducted formal exercises to optimize use of mail, telephone, and network services or compared their use with other organizations.

Potential Savings Through Review Action

As a result of unnecessary subsidies to business lines, HR created false economies and efficiencies for the other Departmental programs and forfeited the opportunity for savings to the Department as a whole. In cases where Fund billing represented the distribution of fixed costs to the Department, higher than average use of services by HR resulted in lower costs for the other program customers. Although we recognize the existence of significant fixed costs and accept HR's reasons for higher use in some areas, the conditions cited above indicate opportunities for increased efficiencies. Had HR consumed goods and services provided through the Fund at a similar rate per person as other customer organizations, unit prices remaining constant, the potential savings for Fiscal Year 1997 would have been about $5 million.

RECOMMENDATION

HR resource managers should implement a process to optimize their use of Fund services and periodically perform comparative analysis of use to that of other organizations.

MANAGEMENT REACTION

Management concurred with the need to review the use of Fund services by their offices. Management has begun implementing corrective actions that resulted in a significant reduction in mail stops. Management plans to perform a review of their use of Fund services during the first half of Fiscal Year 1999. This review will focus on such "infrastructure" items as space, telephone and LAN lines, and mail stops. Management believed that reducing their use of these services will likely increase the proportion of fixed costs paid by other Departmental customers. Accordingly, while management agreed that a review process was warranted, the highest priority should continue to be placed on improving the efficiency of overall Departmental use of administrative resources, rather than cost shifting between HR and other customers.

AUDITOR COMMENTS

Management's comments and proposed actions are responsive to our recommendation. We agree that the highest priority should be placed on improving the efficiency of overall Departmental use of administrative resources. However, we believe that reductions in unnecessary usage by individual customers, including HR, are a key component in achieving increased efficiency for the Department as a whole. In the long term, reductions in usage will provide opportunities for overall cost reduction rather than mere cost shifting.

Assessing The Validity Of Fund Business Lines

Supply Business Line Not Clearly Competitive

The operation of the Department's supply store has not increased the economy and efficiency of the Department's administrative operations. Since the Fund's inception, customers indicated that the Department's supply store was not competitive with outside sources. To test this assertion, we conducted a price comparison of items offered by the Department's supply store to identical items offered by an outside vendor. We selected 26 out of 902 items and compared the prices to the prices offered by an outside vendor. Twenty of the 26 items selected (**77** percent) were more expensive at the Department's supply store than at the outside vendor, though convenience, ordering costs, and delivery times were not fully reflected in vendor price quotes. While a price comparison performed by the Supply Business Line concluded that their prices were competitive, HR management agreed that many items could be bought from outside sources at lower prices.

In addition, the Fund's pricing policies do not recover full costs, indicating the Department's supply store is not increasing the efficiency of the Department's administrative operations. Pursuant to Congressional guidance, the pricing policy for the Department's supply store excludes Federal salaries and certain other indirect costs. These costs were estimated to be over $1 million for Fiscal Year 1999. Although outside vendors must recover the full cost of their operations and presumably generate a profit, they were still able to effectively compete with the prices for supplies offered by the Department's supply store. The inclusion of Federal salaries and other indirect costs to the current pricing policy would cause a significant increase in the price of items offered by the Department's supply store and make the store even less competitive with outside vendors. However, consideration would also have to be given to charging programs for the receiving and transportation costs for outside purchases.

The Fund has established a market environment that provides customer organizations expanded flexibility to make decisions that affect the cost of supporting their program mission. In the case of the Department's supply store, program managers have increasingly decided to purchase supplies from outside sources. Officials from several customer organizations told us that they used their Government purchase card to go to outside sources for lower prices and a larger selection of items.

Responsibility For Assessing Validity

One of the primary objectives of the Fund is to provide customer organizations the ability to make decisions that affect the economy and efficiency of supporting their program mission. Such flexibility can have adverse effects on high cost business lines. The Fund's Board is responsible for ensuring that Fund activities are operated in a business-like manner by assessing the validity of business lines and the validity of continuing services.

Need For Periodic Review Of Business Lines

The Board had not developed procedures to assess whether Fund business lines are competitive with outside vendors, correct inefficient operations, and shut down those unable to compete. The indicators that the operation of the supply business line was not competitive, or necessarily benefiting the Department, were present as early as the second quarter of Fiscal Year 1997. These indicators were in the form of customer complaints about price and selection, reduction in sales volume, and losses incurred. During the past year, efforts were made to stem the supply store's losses. A new manager took over the business line and made operational changes. For example, supply store personnel conducted the first physical inventory in several years. In addition, procedures were changed to include the 30 percent markup on supplies picked up by customers from the warehouse. Finally, Fund management closed several self-service stores that were operating at a loss. Program offices were asked to fund these stores, but funding was not available to continue operations. During April 1998, the Office of Administrative Services developed and presented corrective actions to stem losses in the Supply Business Line. The Board agreed with the proposed corrective actions and recommended that the Administrative Services Working Group meet to develop further options for consideration.

Continued Operation Of Inefficient And Uneconomical Business Lines

The Fund Board risked permitting inefficient, noncompetitive business lines to continue. The costs for the Department's supply store, for example, exceeded revenues by $760,000 in Fiscal Year 1997. By March in Fiscal Year 1998, the Department's supply store costs exceeded revenues by $409,000. This loss excluded the cost associated with Federal salaries. HR estimated the cost of Federal salaries associated with the Supply Business Line in the Fiscal Years' 1999 and 2000 budget requests to be about $372,000 and $383,000, respectively. In addition, the cost of space occupied by the business line was not included in these losses. HR estimated this cost to be about $725,000 for Fiscal Year 1999. In addition, the Desktop and Graphics Business Lines might not be competitive with outside sources if Federal salaries were included in their pricing structures.

RECOMMENDATION

We recommend that the Fund manager and the Board develop procedures to periodically assess business lines for efficiency and cost effectiveness in providing their goods and services. Management's assessment should include full cost comparisons to outside sources to ensure that the objectives of the Fund are being met. In addition, procedures need to be developed to address how and when to discontinue business lines that cannot compete with outside sources.

MANAGEMENT REACTION

Management concurred with the need to develop procedures both for cost effectiveness comparisons and for deciding whether and how to discontinue services. The Fund manager, in conjunction with the Working Capital Fund Board, will develop procedures during Fiscal Year 1999.

Management reported some new developments in the Supply Business Line since the completion of the audit field work. These actions included closing self-service stores and conducting a market price comparison. While this business line incurred losses of about $1 million through mid-year, Fund management anticipated that the line would break even in Fiscal Year 1998. Management recognized that a full analysis of profit and loss for this business line would need to be performed after completion of a physical inventory.

AUDITOR COMMENTS

Management's comments and proposed corrective actions are responsive to our recommendation.

The Fund's Financial Management System

Financial Management System Has Continual Performance Problems

The Fund's financial management system (FMS) did not efficiently provide timely and accurate information. Since the Fund's inception, there has been a continual problem with providing monthly billings to customers and updating the Headquarters accounting system in a timely manner. Fund management established an objective of having customer bills ready by the second calendar week of each month. Since the start of our audit in March 1998, the Fund has managed to meet this timeliness objective for 5 consecutive months. Prior to that, the customers received their monthly billings before the 15th in only 2 of the 17 previous months. These billings have been anywhere from several days to over a week past the goal. In addition, the Fund has continued to have delays in entering the aggregate month end information into the Headquarters accounting system. The CFO's policy is to post month-end transactions by the fifth working day. The Fund has not met this requirement during Fiscal Year 1998.

We also noted inaccurate information in the internal reports prepared by the billing system. Specifically, summary reports did not agree with the detail bills produced by the system. While reviewing the preparation of the May 1998 bill, we identified several discrepancies between the source documents prepared by feeder systems and the files used to update the billing system. These discrepancies, though not material, were carried forward to the monthly bill and exported to the Headquarters accounting system.

Financial System Should Provide Complete, Timely, And Accurate Information

Financial management systems should support the partnership between program and financial managers, ensure the integrity of the information, and measure performance. To achieve these objectives, systems should collect timely, accurate, complete, reliable, and consistent information.

Lack Of Coordination Within HR And With CFO

During the latter part of Fiscal Year 1996, when implementation steps were initiated, Fund management did not fully coordinate their efforts with the business line managers and the CFO in designing and implementing an integrated financial management system. Since its inception, Fund management relied on contractor support to modify the system's software to correct performance problems and enhance system output. During the second quarter of Fiscal Year 1998, Fund management concluded that the billing system had proven difficult to use even for limited billing functions. Fund management hired a financial management consultant to identify options for resolving the

FMS shortcomings, determine the functional requirements of the FMS, and recommend options for a commercial FMS to replace the existing system. While this effort was on-going, some business lines purchased or planned to purchase new feeder systems and the CFO was in the early stages of replacing the core accounting system.

During this time, the Fund manager, business line managers, and the CFO were not acting in unison to develop an integrated FMS. For example, business line managers were preparing to buy new feeder systems to integrate with the current billing system, yet the Fund manager was considering replacing that system. Meanwhile, the CFO was in the process of replacing the existing core accounting system with the Business Management Information System (BMIS). We believe that failure to coordinate these activities could add to problems integrating the systems making up the FMS and the Department's Headquarters and core accounting systems.

The Fund, business line, and CFO managers held several meetings beginning in May 1998. The objectives of these meetings were to discuss the findings reported by the financial management consultant and to agree on a plan to improve the current FMS, while maintaining compatibility with the BMIS. Based on the cost estimates for the installation of a commercial system provided by the financial management consultant, the Fund manager advised the Fund Board that, in conjunction with the CFO, the Fund staff should find ways to reengineer the FMS to eliminate steps and make better use of its and the Headquarters accounting system's existing capabilities. This decision was in line with the position taken by program customers in recent surveys conducted by HR and our office, in which most respondents agreed that they were unwilling to pay for a new FMS. We believe these meetings, although late, were a positive and welcome example of coordination between Fund management and the CFO.

Performance Problems Continue To Exist

In Fiscal Year 1997, the Department spent about $202,000 on modifications to the billing system without effectively addressing the performance problems. The Fund and its customers rely on the Headquarters accounting system reports to make informed decisions regarding their costs, revenues, and use of goods and services. Without timely and accurate information, customers could exceed their budgets, neglect to pay for services received, and forgo increasing the efficiency of the Department's administrative operations. In addition, the Fund risks spending additional money on new systems that are not compatible with each other or with the Department's accounting systems.

RECOMMENDATION

Fund Management and the business lines in conjunction with the CFO should (1) identify the functional requirements of the FMS; (2) consider integration with feeder, billing, and the Headquarters accounting system; (3) coordinate this effort with HR's development of an Information Technology Architecture; and (4) develop procedures that require a case-by-case review by the Fund manager of any new system purchases.

MANAGEMENT REACTION

Management concurred with the recommendation. Both Fund management and program customers agreed that the Department needs to be cautious about investing in new financial systems. The current billing system, while producing adequate results for Fiscal Years 1997 and 1998, is not adequate to meet future information requirements. Yet, management acknowledged the need to avoid making major investments in new systems unless both added value to customers and compatibility with related systems can be demonstrated.

The CFO is working on the Strategic Information Management process for BMIS to baseline the current environment, identify requirements, and develop a business case for investment in this major initiative. This effort is co-chaired by the Chief Information Officer and involves representatives from most of the Headquarters program offices and all major field offices. This initiative is in the early stages; however, every effort is being taken to involve all business processes to improve integration and eliminate current and future duplication. This process is specifically intended to coordinate the BMIS initiative and promote participation from everyone.

AUDITOR COMMENTS

Management's comments and proposed corrective actions are responsive to the recommendation.

Appendix 1

SCOPE

We conducted fieldwork from March through July 1998 at Department of Energy Headquarters offices in Washington, DC and Germantown, MD. Fieldwork consisted of meetings with officials in the Office of Human Resources and Administration and the Chief Financial Officer.

METHODOLOGY

We discussed the Fund's system of internal controls with officials responsible for managing Fund activities and separate business lines. We observed and tested the system of internal controls to evaluate the adequacy, accuracy, and efficiency of the components of that system: control environment, risk assessment, control activities, information and communications, and monitoring. Based on an analysis of costs and business line complexity, we performed detail testing of three business lines to ensure that the Fund was meeting the expectations established by the Congress. This testing included determining whether pricing policies were reasonable, Board representation was fair, advance payments were in excess of Fund needs, proper disposition of unobligated Funds was made, and Federal and Departmental Administration costs were appropriately excluded. In addition, we traced costs from source documents through the FMS to determine the adequacy and efficiency of the information systems. Finally, we tested whether the Fund was operated in an economic and efficient manner by conducting a survey of program office officials, reviewing performance measures at the business line and Fund management level, analyzing costs incurred by each business line since the Fund's inception to identify anomalies and trends, determining the adequacy of contractor support for operating the business lines, and comparing prices of goods offered in-house to prices offered by private vendors.

The audit was performed in accordance with generally accepted Government auditing standards for performance audits and included tests of internal controls and compliance with laws and regulations to the extent necessary to satisfy the audit objective. Our assessment of the significant internal controls consisted of reviews of pricing and financial related policies and general operating policies and procedures as well as tests of billing controls. Because our review was limited, it would not necessarily have disclosed all internal control deficiencies that may have existed at the time of our audit. Although computer-processed data was not significant to the findings, we included tests to trace data from the Fund's billing system to supporting documentation.

Officials from the Office of Human Resources and Administration waived an exit conference.

The objectives of the Fund can only be fully achieved through the establishment of a mechanism to capture the full costs of providing administrative goods and services and the periodic analysis of this information through operating efficiency metrics. Statement of Federal Financial Accounting Standards Number 4, "Managerial Cost Accounting Concepts and Standards for the Federal Government," encourages Federal entities to use full cost information in making economic decisions on whether to continue providing a product or service. As we reported last year, without a mechanism to identify the unreimbursed costs, the Board had no baseline to identify the most efficient practices, nor could it make informed decisions on whether services provided by the Fund were competitive with the private sector.

In response to a recommendation issued during the 1997 audit, Fund management addressed the impact on the existing business lines of including the full costs of goods and services in the pricing structure. Fund management estimated that the cost of Federal salaries and other indirect costs for Fiscal Year 1999 would be about $11 million. The report concluded that the Desktop, Supply, and Printing and Graphics Business Lines would be impacted the most by a full cost pricing structure because these business lines are supported by large Federal staffs and have pricing policies more closely linked to consumption.

Fund management suggested that full cost analyses of the business lines be performed periodically to ensure the cost effectiveness of these services. Although the Fund currently does not recover the cost of Federal employees from customers, without a mechanism to consistently capture and report the full costs of goods and services offered by the Fund, the business lines subject to outside competition are not operating in a true market atmosphere. HR subsidization gives these business lines an unfair advantage over outside competitors by artificially keeping their prices competitive. A true market atmosphere cannot exist unless program customers have information available to compare the full costs of goods and services offered by the Department to the fully loaded prices of those offered by outside vendors. We agree that periodic analyses of the full cost incurred by each business line should be performed to help achieve the Fund's objective of increasing the efficiency of the Department's operations as a whole.

IG Report No. CR-B-99-01

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, DC 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 alternative address:

Department of Energy Human Resources and Administration Home Page
http://www.hr.doe.gov/ig

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

This report can be obtained from the
U.S. Department of Energy
Office of Scientific and Technical Information
P.O. Box 62
Oak Ridge, Tennessee 37831