

U.S. DEPARTMENT OF ENERGY
OFFICE OF INSPECTOR GENERAL

REPORT ON MATTERS IDENTIFIED AT THE
ROCKY FLATS FIELD OFFICE
DURING THE AUDIT OF THE DEPARTMENT'S CONSOLIDATED
FISCAL YEAR 1996 FINANCIAL STATEMENTS

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

REPORT ON MATTERS IDENTIFIED AT THE
ROCKY FLATS FIELD OFFICE
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FISCAL YEAR 1996 FINANCIAL STATEMENTS

Audit Report Number: WR-FS-97-03

SUMMARY

The Government Management Reform Act of 1994 requires that the Department of Energy submit audited financial statements to the Office of Management and Budget annually, beginning with the statements as of September 30, 1996. A Departmentwide audit was conducted to determine whether there was reasonable assurance that the Department's consolidated Fiscal Year 1996 financial statements were free of material misstatements. We conducted a portion of the Departmentwide audit at the Rocky Flats Field Office and its integrating contractor, Kaiser-Hill Company, LLC.

The audit at Rocky Flats and Kaiser-Hill disclosed errors, as of September 30, 1996, in the balances maintained in three Department accounts: Completed Property, Plant and Equipment; Accumulated Depreciation; and Construction Work-in-Progress. In addition, we found that Rocky Flats was not periodically reconciling the accounts payable/accrued expenses general ledger accounts to the supporting documentation.

We recommended adjustments and reconciliations for these accounts. Management generally concurred with the findings and recommendations and agreed to take corrective action.

_____(SIGNED)_____
Office of Inspector General

PART I

APPROACH AND OVERVIEW

INTRODUCTION

The Government Management Reform Act of 1994 significantly expanded the provisions of the Chief Financial Officers Act of 1990 and required that audited financial statements covering all accounts and associated activities of the Department be submitted

to the Office of Management and Budget (OMB) annually. The first submission involves financial statements as of September 30, 1996. A Departmentwide audit of consolidated Fiscal Year 1996 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 Department facilities.

The objective of the Departmentwide audit was to determine whether the Department's Consolidated Statement of Financial Position as of September 30, 1996, and Statement of Operations and Changes in Net Position for Fiscal Year 1996 presented fairly, in all material respects, its financial position and results of operations in conformity with applicable accounting standards. Departmentwide issues are addressed in Audit Report No. IG-FS-97-01.

The purpose of this report is to inform management of Rocky Flats of matters that came to the attention of the Office of Inspector General during the audit at Rocky Flats and Kaiser-Hill. Rocky Flats is responsible for the account balances entered into the Department's core accounting system.

SCOPE AND METHODOLOGY

The audit was conducted from June through December 1996 at Rocky Flats and Kaiser-Hill in Golden, Colorado. Specifically, we examined internal controls, assessed compliance with laws and regulations, and selectively tested account balances reported to Departmental Headquarters as necessary to achieve the Departmentwide audit objective.

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 control environment of certain financial systems and evaluated the reliability of the data on a test basis.

Because audit work was limited, it would not necessarily disclose all of the internal control weaknesses that may exist. Furthermore, because of inherent limitations in any internal control structure, 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 December 27, 1996. Projection of any evaluation of the structure 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 Office of Inspector General, certain cycles were reviewed by an independent accounting firm or internal audit personnel. The independent accounting firm reviewed Environmental, Pension, and Other Post-Retirement Liabilities; Fixed Assets; and Disbursements. Kaiser-Hill's internal audit personnel reviewed the Payroll Cycle and made recommendations to their own management.

The Office of Inspector General considered all findings, generated as a result of these reviews, when preparing the audit report on the Department's Consolidated Fiscal Year 1996 Financial Statements (Audit Report No. IG-FS-97-01) and the management report referred to in that report. Furthermore, the Office of Inspector General is also addressing issues requiring local management attention in this report.

An exit conference was held with Rocky Flats management on February 3, 1997.

BACKGROUND

Our prior audit report (Report on Matters Identified at the Rocky Flats Field Office During the Audit of the Department's Consolidated Statement of Financial Position as of September 30, 1995, Report No. WR-FS-96-03, March 22, 1996), disclosed weaknesses in the property accountability system that made it impractical to rely on the system. For example, Rocky Flats could not assure that property was correctly recorded in the accounts until Kaiser-Hill completed a wall-to-wall inventory in Fiscal Year 1996. Also, Rocky Flats had not completed its review of surplus facilities to determine the amount of the write-down. These and other errors at Rocky Flats, when combined with weaknesses at the Idaho National Engineering Laboratory, were one reason that the Office of Inspector General disclaimed an opinion on the Consolidated Statement of Financial Position of the Department as of September 30, 1995, in Audit Report No. IG-FS-96-01 (February 29, 1996).

Kaiser-Hill became the integrating contractor at the Rocky Flats Site on July 1, 1995. A 1994 audit had shown that the prior contractor at the Rocky Flats Site could not accurately determine how much property was at the Site. The contract with Kaiser-Hill, as amended, gave Kaiser-Hill two years from the effective date of the contract to complete a property inventory.

OBSERVATIONS

The weaknesses described in the preceding paragraph had been substantially reduced by September 30, 1996. During Fiscal Year 1996, the personal property inventory was completed at the Rocky Flats Site and Kaiser-Hill accepted the Rocky Flats personal property allocable to its contract. (Kaiser-Hill had not accepted, as of September 30, 1996, the Rocky Flats Site real property inventory, which had a net book value of about \$51 million, excluding land.) In May and August 1996, surplus assets with net book values of \$198 million and \$134 million, respectively, were written off. Accordingly, we concluded that Rocky Flats had made significant progress toward rectifying the weaknesses that had existed at September 30, 1995.

However, we observed errors in account balances and certain weaknesses at Rocky Flats and Kaiser-Hill during the course of our current review. The Completed Property, Plant and Equipment account and the Accumulated Depreciation account had errors

because they did not include all property physically inventoried. The personal property physical inventory disclosed that over 2,000 items were not in the accounting records. As a result, the Completed Property, Plant and Equipment account and the Accumulated Depreciation account were understated as of September 30, 1996. According to Rocky Flats, preliminary estimates indicated that the amount to be capitalized for the over 2,000 items was about \$12.6 million.

In addition, there were errors in the net book value of property, plant and equipment because Rocky Flats had not established the 2312 contra account to Construction Work-in-Progress for legacy waste projects. By not crediting the costs of legacy waste projects to the 2312 account, net property, plant and equipment was in error by at least \$15.1 million.

We also observed a control weakness. Specifically, Rocky Flats was not periodically reconciling the accounts payable/accrued expenses general ledger accounts to the supporting documentation.

Management generally concurred with the findings and recommendations and agreed to take corrective action.

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

PART II

AUDIT RESULTS

1. Completeness of Capital Asset Accounts

The Department's Accounting Handbook requires field elements to maintain accurate and up-to-date accounting records in order to provide the proper accountability for the Department's investment in property. However, the Completed Property, Plant and Equipment account and the Accumulated Depreciation account did not include all property physically inventoried and therefore were inaccurate. The personal property physical inventory completed during 1996 disclosed over 2,000 items that were not in the accounting records. As a result, the Completed Property, Plant and Equipment account and the Accumulated Depreciation account were understated, as of September 30, 1996. According to Rocky Flats management, preliminary estimates indicated that only about 700 of the 2,000 plus items of personal property exceeded the \$5,000 capitalization criteria, with an estimated total value of \$12.6 million.

Recommendations

We recommend that the Chief Financial Officer, Rocky Flats:

Direct Kaiser-Hill to adjust, as of September 30, 1996, the capital asset subsidiary ledgers for unrecorded assets and

reconcile the subsidiary ledgers to the property management database; and,

Reconcile, as of September 30, 1996, the Completed Property, Plant and Equipment and Accumulated Depreciation general ledger accounts to the subsidiary ledgers.

Management Comments

Management concurred with the finding and recommendations. According to Rocky Flats, Kaiser-Hill was working with its subcontractor, Dyncorp, to complete the reconciliation of the property database maintained by Dyncorp to the property accounting records maintained by Kaiser-Hill. Preliminary estimates indicated that of the 2,380 items missing from the accounting records, 729 were above the \$5,000 capitalization criteria for a total of \$12.6 million. The remaining 1,651 items were below the capitalization criteria and were estimated to be valued at \$3.6 million. The items in question were added to the property management system at the end of Fiscal Year 1996 as a result of the personal property inventory and did not represent a material amount to the Rocky Flats property accounts. As of the date of this report, Recommendations 1 and 2 have been fully implemented.

Auditor Comments

Management's actions are responsive to the finding and recommendations.

2. Valuation Contra Account 2312

In April 1996, the Department's Office of Departmental Accounting and Financial Systems Development provided guidance to the field Chief Financial Officers about a new contra account, Account 2312, Fixed Assets--Construction Work-in-Progress, Accumulated Legacy Costs Incurred. This account was to be used to value projects being constructed to treat, store, or dispose of the Department's legacy waste. As environmental processing facilities were being constructed and capitalized in Account 2311, Construction Work-in-Progress, the costs of any portion of the facilities that were attributable to legacy waste activities were to be credited to Account 2312.

However, Rocky Flats had not established the 2312 contra account for valuing its legacy waste projects. Rocky Flats had such projects. For example, the Construction Work-in-Progress account included costs for Project Authorizations 368400, 368410, 368420, and 368430. These projects were for facilities that would store or stabilize various residues. Therefore, as the construction costs for these projects were capitalized in Account 2311, offsetting credits should have been recorded in Account 2312. By not establishing Account 2312, Rocky Flats overstated the net book value of its property, plant and equipment by at least \$15.1 million.

Recommendation

We recommend that the Chief Financial Officer, Rocky Flats, establish the 2312 contra account and record the costs of legacy waste Construction Work-in-Progress projects, as of September 30, 1996, in the account.

Management Comments

Management concurred with the finding and recommendation. Rocky Flats management responded that although Headquarters originally created account 2312 in April 1996, implementing instructions on entries to be used were not provided to the field until July 1996. Entries have now been developed at Rocky Flats to establish the account and all associated entries. Rocky Flats management targeted April 30, 1997, as the date that this account would be fully utilized for all Construction Work-in-Progress projects associated with legacy waste.

Auditor Comments

Management's planned actions are responsive to the finding and recommendation.

3. Reconciliation of Accounts Payable/Accrued Expenses

Department Order 534.1, Accounting, requires Field Element Chief Financial Officers to establish and maintain the official accounting records, which must be supported with valid documents and periodically reconciled to detect and correct recording errors. However, Rocky Flats did not periodically reconcile the general ledger accounts used for accounts payable and accrued expenses to the supporting documentation. During the audit, we issued a recommendation to Rocky Flats that it periodically perform such reconciliations. When Rocky Flats made the reconciliation at yearend, some errors were found, principally involving a misclassification within accrued expense accounts 3212 and 3215. Unless periodic reconciliations are performed, Rocky Flats will have an increased risk that other errors will occur in the future and not be detected.

Recommendation

We recommend that the Chief Financial Officer, Rocky Flats, periodically reconcile the accounts payable/accrued expense general ledger accounts to the supporting detail.

Management Comments

Management concurred with the recommendation. The reconciliation was performed as part of the yearend procedures for 1996. Based on the reconciliation, there were no material errors discovered that distorted the account balance. Quarterly reviews are scheduled for Fiscal Year 1997.

Auditor Comments

Management's actions are responsive to the finding and

recommendation.

OTHER MATTERS

Conditions similar to those raised in the Valuation Contra Account 2312 finding and recommendation were identified at other locations included in the overall audit. These conditions, therefore, were addressed in the audit report on the Department's Consolidated Fiscal Year 1996 Financial Statements (Audit Report No. IG-FS-97-01).

During our review, we identified additional errors in the Completed Property, Plant and Equipment and Construction Work-in-Progress accounts. Specifically, in August 1996, we issued a finding to Rocky Flats that stated that the Construction Work-in-Progress account contained 21 projects, costing about \$22 million, that were completed and, therefore, should have been transferred to Completed Property, Plant and Equipment. Rocky Flats took prompt action and made the appropriate adjustments during our review.

Report No. WR-FS-97-03

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