OFFICE OF INSPECTOR GENERAL

U.S. Department of Energy

MANAGEMENT LETTER

DOE-OIG-20-26

February 2020

AUDIT OF THE DEPARTMENT OF ENERGY'S CONSOLIDATED FINANCIAL STATEMENTS FOR FISCAL YEAR 2019

Department of Energy
Washington, DC 20585

February 5, 2020

MEMORANDUM FOR THE DEPUTY CHIEF FINANCIAL OFFICER

FROM: Sarah B. Nelson
Assistant Inspector General
for Technology, Financial, and Analytics
Office of Inspector General

SUBJECT: INFORMATION: Management Letter on the "Audit of the Department of Energy's Consolidated Financial Statements for Fiscal Year 2019"

Pursuant to requirements established by the *Government Management Reform Act of 1994*, the Office of Inspector General engaged the independent public accounting firm of KPMG LLP to perform the audit of the Department of Energy's Fiscal Year 2019 Consolidated Financial Statements. During the audit, KPMG LLP considered the Department's internal controls over financial reporting and tested for compliance with certain provisions of laws, regulations, contracts, and grant agreements that could have a direct and material effect on the consolidated financial statements.

During the course of the audit, KPMG LLP identified deficiencies in internal control that are included in the attached management letter. Specifically, the attached letter contains 13 new findings and a total of 20 recommendations that were issued during the Fiscal Year 2019 Audit of the Department of Energy's Consolidated Financial Statements. Management fully concurred with all but one recommendation included in the management letter and had taken or planned to take corrective actions. Management's responses are included with each finding. The audit did not identify any deficiencies in internal control over financial reporting that are considered material weaknesses.

I would like to thank all participating Department elements for their courtesy and cooperation during the review.

Attachment

cc: Chief of Staff
Under Secretary of Energy
Under Secretary for Science
Administrator, National Nuclear Security Administration

Audit Report: DOE-OIG-20-26

KPMG LLP
Suite 12000
1801 K Street, NW
Washington, DC 20006

December 13, 2019

Ms. Teri L. Donaldson
Inspector General
U.S. Department of Energy
1000 Independence Ave, S.W.
Washington, DC

Dear Ms. Donaldson:

In planning and performing our audit of the financial statements of the United States Department of Energy (the Department) as of and for the year September 30, 2019, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, and in accordance with Office of Management and Budget Bulletin No. 19-03, *Audit Requirements for Federal Financial Statements*, we considered the Department's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Department's internal control. Accordingly, we do not express an opinion on the effectiveness of the Department's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses and/or significant deficiencies and therefore, material weaknesses and/or significant deficiencies may exist that were not identified. In accordance with *Government Auditing Standards*, we issued our report dated November 18, 2019, on our consideration of the Department's internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. During our audit, we identified deficiencies in internal control that are included in Exhibit A. The Office of Inspector General will issue a separate management letter addressing information technology control deficiencies.

The Department's responses to the findings identified in our audit are included in Exhibit A. The Department's responses were not subjected to the auditing procedures applied in the audit of the consolidated financial statements and, accordingly, we express no opinion on the responses.

This purpose of this letter is solely to describe the deficiencies in internal control identified during our audit. Accordingly, this letter is not suitable for any other purpose.

Very truly yours,

KPMG LLP

MANAGEMENT LETTER

Index to Exhibits

OPEN FINDINGS – INTERNAL CONTROLS AND OTHER OPERATIONAL MATTERS *(with parenthetical references to findings and recommendations issued during the engagement)*

OPEN FINDINGS RELATED TO FISCAL YEAR 2019 NOTICES OF FINDINGSAND RECOMMENDATIONS

Exhibit A

OPEN FINDINGS – INTERNAL CONTROLS AND OTHER OPERATIONAL MATTERS
Property, Plant and Equipment

19-SNL-F-01 – Untimely Recording of Transfers from Construction Work in Process (CWIP) to Property, Plant and Equipment (PP&E)

The National Nuclear Security Administration's (NNSA) Field Chief Financial Officer, in conjunction with the Sandia Field Office, is responsible for ensuring that the PP&E process used by the Sandia National Laboratories (Sandia) contractor, National Technology and Engineering Solutions of Sandia (NTESS), is compliant with all applicable guidance and accounting standards. The recording of transfers of new assets in the general ledger from CWIP to PP&E is handled by the Financial Accounting Department based on information received from other departments. The other departments are expected to inform the Financial Accounting Department on a timely basis regarding the existence, and date placed in service, of new assets.

During our substantive test work over PP&E additions at Sandia, we identified 16 assets with a combined dollar value of $10.1 million that were placed in service prior to April 1, 2018. However, these assets were not transferred to PP&E until after October 1, 2018, more than 6 months after the date the assets were placed in service as stipulated by the Department of Energy's *Financial Management Handbook*. In addition, the fiscal year (FY) 2019 general ledger reflected additional depreciation expense for these assets that should have been recorded in FY 2018.

The weaknesses identified occurred because Sandia had not developed sufficiently designed controls to ensure timely communication between the other departments and the Financial Accounting Department. As a result, prior year PP&E was misclassified by $10.1 million. Further, CWIP was overstated by $10.1 million while general PP&E (Structures and Equipment) was understated by $10.1 million. In addition, related depreciation expense was understated by $788,000 and current year depreciation expense is overstated by $788,000.

RECOMMENDATIONS:

1. We recommend that the NNSA's Field Chief Financial Officer, in conjunction with the Sandia Field Office Manager, direct Sandia to:

   A. Redesign controls to ensure necessary information to record the transfer of assets placed in service from CWIP to PP&E is provided timely to the Financial Accounting Department; and

   B. Develop training to remind employees of the revised and existing policies and procedures related to the timeframe for providing necessary information to allow for the timely transfer of assets from CWIP to PP&E following an asset's placed-in-service date.

MANAGEMENT RESPONSE:

Management concurs with the recommendations. NNSA will direct Sandia to review controls and identify improvements that will assist departments in providing timely information to the Financial Accounting Department. NNSA will also direct Sandia to remind employees of existing policies and procedures related to the timeline for providing necessary information to allow for the timely transfer of assets from CWIP to PP&E following an asset's placed in service date.

Grants

BACKGROUND:

As part of the terms and conditions for financial assistance awards, including those issued at the Chicago Office and the National Energy Technology Laboratory (NETL), award recipients are required to submit quarterly and final Federal Financial Reports (SF-425). The SF-425 details all financial assistance award funds requested and spent to date. In addition, the SF-425 allows for review of the recipient's cash activity to verify the recipient is not drawing down funds in excess of the funds necessary to pay for imminent expenditures or to verify that the recipient is not requesting reimbursement in excess of actual costs incurred.

19-CH-G-01 – Inadequate Monitoring of Financial Assistance Awards

During our final statistical sample test work over grants and cooperative agreements at the Chicago Office, we reviewed five unique awards and identified one recipient that reported $103,101 in cash on hand on its June 30, 2019, SF-425. This amount exceeded the threshold which required investigation by the Chicago Office. The June SF-425 was dated July 29, 2019, and the cash balance had not been investigated as of October 17, 2019.

The weaknesses identified occurred because the Chicago Office did not have adequate resources to follow up on every award with reported cash above the threshold requiring investigation. This inadequacy could cause Program Costs to be overstated. Because financial assistance awards are costed as they are paid, not following up on positive recipient cash balances in a timely manner could result in costs being recorded when the recipient has not incurred cost, thereby affecting the Program Cost balances recorded in the Department's consolidated financial statements.

RECOMMENDATIONS:

2. We recommend that the Field Chief Financial Officer for the Office of Science, direct the Division Director to:

   A. Strengthen policies and procedures to ensure SF-425s with reported cash on hand are reviewed in a timely manner to ensure recipient compliance with the requirement that cash balances maintained at the recipient level are kept to the minimum amount necessary to meet immediate recipient disbursement needs or are not in excess of actual costs incurred; and

   B. Develop and implement a strategy to ensure adequate transition of the reviews of financial assistance awards to other personnel.

MANAGEMENT RESPONSE:

The Office of Science Consolidated Service Center concurs with the recommendations. The Consolidated Service Center Chief Financial Officer will direct the Data Integrity and Financial Division Director to update local SF-425 procedures to prioritize the review of all SF 425s on hand to determine if any excess cash exists prior to addressing delinquencies and implement an automated process to send out delinquency notices.

In addition, the Consolidated Service Center Chief Financial Officer will direct the Data Integrity and Financial Division Director to train additional personnel to perform the SF-425 review function and develop a means to automate report submittal and comparison of data to minimize the level of manual effort involved.

19-NETL-G-01 – Failure to Implement Post-Award Monitoring Policies and Procedures for a Financial Assistance Award

During our interim statistical sample test work over grants and cooperative agreements at NETL, we reviewed 11 unique awards and identified one recipient that did not submit the required SF-425s for the reporting periods ending March 31, 2019, and June 30, 2019, in a timely manner. The recipient's SF-425s became delinquent 30 days after the end of the reporting period, per the Federal Assistance Reporting Checklist.

The delinquency of the March 31, 2019, SF-425 generated an automated First Notice of Delinquent

Reports in the Federal Information Tracking System (FITS). This notice was emailed to the recipient in June 2019. A Final Notice of Delinquent Reports letter was also generated in FITS and sent to the recipient on July 10, 2019. This letter stated that "effective on the date of this letter, payment is hereby withheld, as prescribed in 10 CFR 600.162(a)(1) or 10 CFR 600.243(a)(1), as appropriate. This will result in a suspension of your Automated Standard Application for Payment (ASAP) account or disapproval of invoices submitted for payment, whichever is applicable." However, the recipient's ASAP account was not suspended. The recipient completed a drawdown of funds on July 10, 2019, and then again on August 9, 2019. After we inquired about the recipient's SF-425s, NETL put a hold on the funds on August 9, 2019, subsequent to the recipient's drawdown. As of August 12, 2019, the recipient had provided the outstanding March 31, 2019, and June 30, 2019, SF-425s, and the reinstatement of the fund availability is currently pending action by NETL.

The weaknesses identified occurred because NETL did not adequately follow established policies and procedures for monitoring required deliverables to ensure that they were submitted by the dates specified in the Federal Assistance Reporting Checklist. Further, NETL did not adequately follow established policies and procedures requiring payments for awards under the ASAP payment system to be automatically suspended when reports become delinquent. As a result, there is an increased risk of misstatement across financial statement balances related to grant activity, including advances and prepayments, grant related liabilities, undelivered orders, and program costs.

RECOMMENDATIONS:

3. We recommend that the Director, NETL, direct the NETL Chief Financial Officer to:

   A. Ensure that established policies and procedures for monitoring the timely receipt of reports are consistently followed in accordance with the terms of the award; and

   B. Ensure that adequate controls are established to ensure that payments are suspended when reports become delinquent, in accordance with established policies and procedures.

MANAGEMENT RESPONSE:

Management concurs with the recommendations. NETL has reinforced with assigned personnel NETL's established process of receiving reports in a timely manner. NETL has also implemented steps to ensure that a recipient's account is suspended once they are issued a final notice of delinquency. As of the date of this response, payment has been suspended on all awards that have received a final notice of delinquency. To ensure continued compliance, NETL management will actively monitor the process of receiving reports and suspending payment.

Pensions

BACKGROUND:

The Department is a Federal agency with the largest civilian contractor workforce in the Federal government. The Department enters into large contracts with civilian commercial entities to operate the laboratories and other Department facilities. Most of these contractors sponsor defined benefit pension and postretirement benefits other than pensions (PRB) plans. The Department approves these contractors' pension and PRB plans and is ultimately responsible for the allowable costs of funding the plans based on the contracts with the commercial entities that are operating the Department's facilities. As the Department is contractually obligated for reimbursing the allowable costs of the contractor contributions to the defined benefit pension and PRB plans, the Department's financial statements reflect the assets, liabilities, and related costs relating to these plans. The contractors invest in a variety of securities and financial instruments to fund these plans.

19-Y12-P-01 – Pension Asset Valuation Review

During our test work over pension assets at Consolidated Nuclear Security, LLC (CNS), the Y-12 National

Security Complex's operating contractor, we found that CNS did not maintain sufficient and appropriate documentation of the performance of existing control activities over the valuation of pension plan investments as a means to allow external parties to re-perform and test the control and come to the same conclusion as the control operator. Specifically, as part of the control activities addressing the independent challenges of the valuation of pension asset investments, CNS carries out reviews of relevant periodic and annual investment fund manager reports and memoranda, as well as maintains ongoing dialogue and correspondence with the plan's trustee and investment consultant. However, CNS was not able to present formalized documentation substantiating these control activities.

The weaknesses identified occurred because CNS lacked formalized documentation of their review of the pension investment valuation as required. As a result, the valuation of the Department's pension investments may be incorrectly valued in the consolidated financial statements and disclosures.

RECOMMENDATION:

4. We recommend that the NNSA's Field Chief Financial Officer, in conjunction with the Manager, Y- 12 National Security Field Office, direct CNS personnel to strengthen internal control policies and procedures to maintain sufficient and appropriate evidence of the control activities performed.

MANAGEMENT RESPONSE:

Management concurs with the recommendation. NNSA will direct CNS to strengthen current internal control policies and procedures to maintain sufficient and appropriate evidence of the control activities performed in pension asset valuation.

CNS's corrective action plan is to revise pension asset valuation policies and procedures to include additional documentation. The revised policy will set CNS's objectives and further document internal controls. Documentation is required for the effective design, implementation, and operating effectiveness of CNS's internal control of pension asset valuation. This documentation will assist in management's design of internal controls by establishing and communicating the who, what, when, where, and why of internal control to CNS personnel. The revised policy and procedures will also provide a means to retain organizational knowledge and mitigate the risk of having that knowledge limited to a few personnel, as well as a means to communicate that knowledge as needed to external parties, such as external auditors.

CNS compares the asset values determined by the trustee to the asset values determined by the Investment Consultants on a quarterly basis. CNS will use a spreadsheet to document the pension asset valuation review. CNS will identify any variance larger than two percent and report these to the CNS Benefits and Investment Committee.

19-LBNL-P-01 – Errors Identified in Census Data Attributes

During our test work over census data at Lawrence Berkeley National Laboratory (LBNL), we identified discrepancies in certain personnel attributes (birth date and hire date) for 2 of the 20 employees we reviewed. As a result, this information was incorrectly included in census data files transmitted to the plan's actuary. Birth date is an input used by the actuary to calculate age within the projected benefit obligation, and hire date is an input used by the actuary to calculate the service credit within the projected benefit obligation (PBO).

These weaknesses occurred because LBNL did not have effective policies and procedures in place to fully ensure the correct census data was transmitted to the plan's actuary. As a result, the controls in place at LBNL did not prevent or detect discrepancies between source documents and the system of record used to record attributes for employees in PeopleSoft. Without the correct internal controls in place and operating effectively, LBNL has not addressed the risk that the actuarial estimate of the projected benefit obligation could be misstated due to incorrect data inputs used.

RECOMMENDATION:

5. We recommend that the Site Manager, Bay Area Site Office direct LBNL to ensure that documented policies and procedures to identify any errors or discrepancies between source documents and the system of record are implemented prior to submission to the actuary.

MANAGEMENT RESPONSE:

Concur. The Bay Area Site Office Manager will direct LBNL to ensure that documented policies and procedures to identify any errors or discrepancies between source documents and the system of record are implemented prior to submission to the actuary.

19-LBNL-P-02 – Internal Controls and Documentation over Lawrence Berkeley National Laboratory Census Data

LBNL relies on the University of California Office of the President (UCOP) to calculate both Covered Gross Compensation and Years of Service, two key census data attributes used to calculate the PBO for LBNL participants in the University of California Retirement Plan (UCRP). In our test work over census data at LBNL, we noted that LBNL did not have a control in place to validate source data for Covered Gross Compensation amounts for two active participants within the UCRP. Additionally, LBNL was not able to timely explain or provide timely documentation to support the process for the calculation and transmittal of the Years of Service census data attribute to UCOP.

While the University of California manages the day-to-day operations of the UCRP, including the LBNL data, LBNL is responsible for providing complete and accurate data attributes to UCOP personnel, understanding all key inputs to the UCRP for use in the actuary's estimate, and recording a complete and accurate liability for LBNL's portion of the UCRP in the Department's financial statements. These weaknesses occurred because LBNL has relied on the UCOP to accurately transmit key relevant census data attributes (such as covered gross compensation and years of service) to the actuary. Without sufficient internal controls in place and operating effectively, LBNL has not addressed the risk that the actuarial estimate of the projected benefit obligation could be misstated due to incorrect data inputs used.

RECOMMENDATIONS:

6. We recommend that the Site Manager, Bay Area Site Office, direct LBNL to:

   A. Implement sufficient internal controls to prevent or detect and correct potential errors in the attributes; and

   B. Document the process for transmitting census data for LBNL participants to the UCOP that are used in the actuarial estimate of the projected benefit obligation.

MANAGEMENT RESPONSE:

Concur. The Bay Area Site Office Manager will direct LBNL to implement sufficient internal controls to prevent or detect and correct potential errors in the attributes. Further, direction will be given to document the process for transmitting census data for LBNL participants to the UCOP that are used in the actuarial estimate of the projected benefit obligation.

19-LANL-P-01- Inaccurate Pension Census Data

During our census data test work at Los Alamos National Laboratory (LANL), we noted that the census data provided by LANL's third party census data custodian, Aon Hewitt, did not properly reflect the 2016 death of a plan beneficiary. LANL received proof of death in 2016 and provided that information to Aon Hewitt, who subsequently completed a lump sum death benefit payout to the deceased's beneficiaries. However, Aon Hewitt did not reflect the employee as deceased in the census data but instead as a term vested employee. When active employees die, they are reclassified as term vested employees by Aon until the death is confirmed with the Social Security Death Index (SSDI), at which time the employee will be reflected as deceased within the census data. Aon Hewitt did not reflect the employee as deceased until March 2018, after the date they transmitted the population to the actuary for valuation. As a result, the employee remained in the census data population for which the actuarial pension liability was determined through the actuarial valuation date of October 1, 2018.

These weaknesses occurred because LANL does not have sufficiently designed controls in place or operating effectively to ensure accurate and timely update of census data information provided to the third-party actuary. Without proper controls in place that are operating effectively, LANL has not addressed the risk that census data records can be misclassified or inappropriately included/excluded in respective populations for which valuations are performed. From our sample over census data, we determined that one employee record was inappropriately included in the pension actuarial liability valuation as of October 1, 2018, which causes the estimated pension liability to be overstated by $450,000.

RECOMMENDATION:

7. We recommend that the NNSA's Field Chief Financial Officer, in conjunction with the Manager, Los Alamos Field Office, direct LANL to redesign/implement controls to ensure census data information is updated timely and accurately provided to the actuary.

MANAGEMENT RESPONSE:

Concur. LANL has implemented controls to ensure that census data information provided by Aon Hewitt is updated timely and accurately. LANL has instructed Aon Hewitt to implement a process that includes regularly scheduled comparisons of the SSDI against the non-active population. The process requires the SSDI to be run immediately prior to the collection and transfer of census data to the actuary for use in the plan's evaluation. This process improvement has been tested and is effective. The participant is now correctly categorized. Aon Hewitt is also researching coding alternatives to Terminated Vested for use on deceased participants whose death is not yet reflected on the SSDI.

Financial Reporting

19-HQ-FR-01 – Documentation of Non-GAAP Practices and Their Impact on Recording Accounting Transactions

During our test work over financial reporting, we noted that the Department has not documented its analysis of the effect of accounting policies or practices that do not align with applicable accounting standards; nor, has the Department documented its determination of the impact of these policies or practices on the recording of Department accounting transactions or balances, whether material or immaterial. Specifically, the audit team identified non-generally accepted accounting principles (GAAP) accounting practices in the Department's accounting for which analyses to determine immaterial amounts have not been provided. Examples in which analyses have not been provided include accrued liabilities related to procurement accrual thresholds used at contractor sites and the use of a single discount rate to determine pension obligations.

Any accounting policies/practices that are not in accordance with GAAP, regardless of materiality, are considered non-GAAP accounting policies/practices. In addition, the Department's financial statements must comply in all material respects with GAAP. The Department records certain accounting transactions and balances outside of GAAP requirements due to a need for operational efficiency and because they are not deemed material to the Department's financial statements individually or in the aggregate. However, the Department does not prepare a formal assessment, analysis, or evaluation of these transactions.

The audit team provided more in-depth descriptions of these non-GAAP accounting practices to management. In addition, through multiple meetings management has not demonstrated an understanding of or articulated their understanding of the significance or risk of not performing and documenting analyses around non-GAAP accounting practices. While certain provisions of the accounting standards allow for materiality considerations, the Department does not have the ability to evidence proper monitoring of the impact of these practices and therefore, cannot evaluate the materiality of these practices individually or in the aggregate because the Department does not document the impact of the individual practices.

These weaknesses occurred due to the Department's interpretation of the Statement of Federal Financial Accounting Standards (SFFAS) being limited to items that are material and the Department striving for operational efficiency. As a result, the Department believed it was acceptable to have certain policies and practices that are not in accordance with GAAP. The Department believed that transactions recorded, and balances reported using their non-GAAP policies/practices are immaterial individually and in the aggregate. Because the Department believed that there is low risk that these accounting transactions and account balances will ever become material to the Department, it did not document an analysis of the effect of the non-GAAP practices on the financial statements. Without adequate documentation, the Department is unable to substantiate the immateriality of its non-GAAP policies/practices nor can management substantiate the aggregation risk of the non-GAAP policies/practices in place. In addition, without proper documentation management does not have the ability to demonstrate these analyses year-over-year.

RECOMMENDATION:

8. We recommend that the Director, Office of Finance and Accounting, document, in accordance with OMB Circular A-123 and the Green Book, the ongoing monitoring controls over non-GAAP policies and practices Department-wide that assess the impact of non-GAAP policies/practices on the financial statements in the current period and expected future period(s), as a part of their evaluation and assessment of internal controls over financial reporting.

MANAGEMENT RESPONSE:

Non-concur. The Office of the Chief Financial Officer (OCFO) does not agree that additional monitoring practices are needed for immaterial non-GAAP practices. OCFO will not establish accounting guidance for non-GAAP non-material practices. OCFO has a robust internal control review process which evaluates OCFO practices to document and validate the practice and the guidance associated with the practice. OCFO will not issue guidance for nonmaterial infrequent non-GAAP practices. OCFO focuses on high value work based on risks.

The OCFO is responsible for Department-wide policies, however we are not necessarily aware of specific local practices which may validly vary from specific guidance based on local judgements of materiality or other basis. Through the Management Representation Letter process, in prior fiscal years and the current fiscal year, field accounting offices asserted that they did not have any accounting practices that were material and non-GAAP. The representation for FY 2019 was: "The FIELD ELEMENT has disclosed to you all accounting policies and practices we have adopted that, if applied to significant items or transactions, would not be in accordance with U.S. GAAP. We have evaluated the impact of the application of each such policy and practice, both individually and in the aggregate, on the Department's current period consolidated financial statements and our assessment of internal control over financial reporting, and the expected impact of each such policy and practice on future periods' financial reporting.

We believe the effect of these policies and practices on the consolidated financial statements and our assessment of internal control over financial reporting is not material. Furthermore, we do not believe the impact of the application of these policies and practices will be material to the consolidated financial statements in future periods.

KPMG's review of potential non-GAAP practices resulted in identification of only Contractor Accrued Liabilities and Pension Liabilities Single Discount Rate that are accepted immaterial Department practices which are non-GAAP. The Department reviewed these practices when they were implemented many years ago and determined the practices to be acceptable.

Contractor Accrued Liabilities - Contractors are permitted to choose their own accrual threshold based on their expert professional judgement. In the Department's *Financial Management Handbook*, Chapter 11, 1., (5), "Accounts shall be maintained on an accrual basis.... A balance should be maintained between the effort required to measure accrued costs precisely and the added value of such precision." Based on the last part of this guidance, some of the contractor sites have adopted immaterial thresholds that they use for cost accruals. This is an accepted business practice to balance the effort to accrue costs. The contractors need to focus on items above those thresholds to align the accrual efforts with those items of greatest risk.

Pension Liabilities Single Discount Rate - The total pension benefit obligation for the Department from an individual plan discount rate to the aggregate discount rate would not materially change the amount (other than a few hundred million due to rounding when adding each individual contractor benefit obligation). The aggregate discount rate approach is determined from all 51 contractor pension plans by applying the Citigroup yield curve to the stream of collective benefit payments for the 51 plans. Each year the discount rate changes based on the yield curve in effect on the last day of the fiscal year.

The Department selects the discount rate used for all 51 contractor pension plans by applying the Citigroup yield curve to the stream of collective benefit payments for the 51 plans. Each year the discount rate changes based on the yield curve in effect on the last day of the fiscal year.

GAAP requires that the discount rate be determined separately for each plan. However, when the Department began reporting the liabilities of contractor pension and postretirement benefit plans on its financial statements, it decided with the agreement of its auditor that using one discount rate determined using the collective benefit payments would produce results that would not be materially different from those produced by using separate discount rates for each of the plans sponsored by the Department's contractors. Due to all of the plans having a similar maturity this practice is acceptable to the Department.

Lastly, the OCFO disagrees with the statement, "In addition, through multiple meetings management has not demonstrated an understanding of or articulated their understanding of the significance or risk of not performing and documenting analyses around non-GAAP accounting practices." The OCFO understands very well through these meetings what the auditors was communicating; in fact, the OCFO had pointed out several areas that the auditors had to revise either for clarity or accuracy during these meetings. Based on management judgment and past analyses or reviews, we do not believe in performing low value work that does not add value to the overall process where strong and robust internal controls are in place.

AUDITOR RESPONSE:

We thank the OCFO for its response. We do not disagree with management's determination regarding the use of non-GAAP policies or practices for immaterial items. However, a practice determined acceptable "many years ago" may no longer be acceptable in the current year or future years. In addition, a non-GAAP practice acceptable at various reporting levels (i.e., field sites and contractor sites), but not consolidated for evaluation at the consolidated reporting level may not be appropriate. Without a documented evaluation of that policy or practice by management, the effect of the non-GAAP practice on the consolidated financial statements is unknown. We continue to assert that the Department needs to improve its documentation of monitoring practices related to non-GAAP accounting policies and practices as it relates to the current year financial statements and the impact it may have on future years. Without this documentation in place, it is not possible to ascertain at what level monitoring takes place and if an appropriate level of materiality is applied to the consolidated financial statements in relation to the two areas cited above individually and when aggregated. While management asserts in the response that materiality is considered, materiality thresholds or levels of precision used for evaluation have not been specified in instructions to the Department's sites or its contractors nor in their responses in representations to the Department for consolidation purposes.

Environmental Liabilities

19-HQ-EL-01 – Inappropriate Review Permissions

The Integrated Planning, Accounting, and Budgeting System (IPABS) is configured to restrict approving change requests as outlined in prior Standard Operating Policy and Procedure revisions. A miscommunication with the IPABS Support team led to granting a site liaison the ability to approve change requests (including those with Associate Principal Deputy Assistant Secretary for Site Operations, EM-3, (APDAS-level) review). During our test work over the Environmental Management (EM) program liability, we noted that five APDAS-level change requests did not undergo APDAS-level approval because the site liaison who was granted APDAS-level approval rights in IPABS logged the change requests as approved.

These weaknesses occurred because EM's internal controls over the process granting authority to review/approve change requests in IPABS failed to ensure that change requests were properly approved by stipulated authority levels within EM. The EM environmental liability at June 30, 2019, was $383 billion. Of that $383 billion, $256 billion represents baseline estimates stored in IPABS and subjected to the change request process. The total dollar amount of the change requests that did not undergo APDAS-level review is $472.7 million (absolute value).

After the error was identified, all five change requests underwent APDAS review. The APDAS determined the change requests to be reasonable and approved them. Therefore, the error had a zero-dollar impact on the liability. EM also corrected the IPABS settings so that site liaisons did not have APDAS-level review permissions after identifying the error.

RECOMMENDATION:

9. We recommend that EM's Director for Budget and Planning develop and implement policies and procedures to review permissions granted to IPABS users in order to evaluate that the permissions granted are in accordance with EM's Standard Operating Policy and Procedure 74.

MANAGEMENT RESPONSE:

EM concurs with the recommendation to develop and implement policies and procedures to review permissions granted to IPABS users in order to evaluate that the permissions granted are in accordance with EM's Standard Operating Policy and Procedure 74. EM has implemented a monthly procedure to review authority levels granted in IPABS and approve/disapprove of any changes in authority. The authority levels are reviewed by the EM-5.112 Headquarters IPABS administrators, as well as the IPABS Support Team. In addition to the monthly authority level review, the IPABS Support Team is implementing a permissions template for user management requests that will specifically outline the intended results of a request. This template file will include requestor, specific permission requests, and approver information and can then be tracked in EM's ticket catalog (which will be moving to DAYS). These steps will further enhance the existing policy and procedures and map the EM business request to the IT application security implementation.

19-HQ-EL-02 – Insufficient Review of Surplus Plutonium Liability

In estimating the surplus plutonium liability for FY 2019, NNSA assumed that the estimated transportation costs associated with shipping the plutonium from the Savannah River Site to Waste Isolation Pilot Plant (WIPP) for permanent disposal would be included in EM's WIPP environmental liability. Accordingly, NNSA did not include the costs of transportation when estimating the surplus plutonium liability because it is part of WIPP Operations. However, while EM's WIPP liability does include transportation costs for waste approved to be disposed of at WIPP, transportation costs for the 34 metric tons was not included as the waste has not yet received regulatory approval for disposal at WIPP. Therefore, the estimate was not complete as transportation costs for the 34 metric tons was not included in the Department's surplus plutonium liability.

These weaknesses occurred because NNSA's assumptions associated with costs that were expected to be covered by the EM's liability were not clearly communicated to EM. The exclusion of transportation costs to WIPP resulted in an understatement of $70 million in the surplus plutonium liability as of September 30, 2019, prior to an entry to correct the misstatement.

RECOMMENDATION:

10. We recommend that the Director, Office of Finance and Accounting strengthen communication between the OCFO, EM, the NNSA, and the WIPP regarding the assumptions used for the environmental liability associated with the 34 metric tons of surplus plutonium.

MANAGEMENT RESPONSE:

The OCFO concurs. For the permanent disposal of the surplus plutonium, EM assumed responsibility for the transportation costs of the surplus plutonium from the Savannah River Site to WIPP. These transportation costs were excluded from NNSA's surplus plutonium liability since it is a part of the WIPP operations. During the OCFO's review of the surplus plutonium liability, EM and WIPP were asked to review NNSA's surplus plutonium environmental liability. WIPP responded that there was no double counting or missed costs. WIPP stated the baseline included transportation and disposal costs for all transuranic waste currently known or projected to be produced (including 34 metric tons of surplus plutonium). However, WIPP did not inform NNSA or OCFO that it removed the 34 metric tons transportation costs from its environmental liability, because the waste has not received regulatory approval.

OCFO included the transportation costs in the FY 2019 financial statements. OCFO will request a call in FY 2020 with EM, NNSA, and WIPP to confirm that the surplus plutonium assumptions regarding the 34 metric tons surplus plutonium transportation costs are consistent with EM, NNSA, and WIPP. The notes from the meeting will be sent to all attendees to reflect the assumptions.

19-ORP-EL-01 – Insufficient Review of Baseline Changes

During our test work over the EM program liability at the Office of River Protection (ORP), we noted that ORP's Environmental Management Office (ORP-EM) formulated an increase to PBS 14 to incorporate a more current contractor estimate into the environmental liability recorded as of June 30, 2019. The current contractor estimate was previously included as an adjustment at EM Headquarters in FY 2018. When calculating the FY 2019 adjustment to the liability for PBS 14, ORP-EM inadvertently made a calculation error when formulating the amount of the adjustment needed to the liability, resulting in an understatement of the liability by $111 million.

While EM Headquarters has established a threshold (+/- 10 percent) for a more rigorous review of changes to the environmental liability, Hanford has not established such a threshold. Therefore, all calculations are reviewed with the same level of rigor, regardless of percent of change in the liability. As such, ORP-EM's reviews do not require an additional level of review of changes that meet a threshold of the liability. Therefore, every change, regardless of materiality, is reviewed in a similar fashion. The review of the spreadsheet, which included the review of the Environmental Management Environmental Liability adjustment amount, as well as the formulas used to calculate the adjustment, did not identify an error in the spreadsheet's formula logic.

Due to the inadequate review process, the known misstatement to the ORP-EM Environmental Liability estimate is an understatement of $111 million as of June 30, 2019, prior to an adjustment to correct the error. However, without a thorough review threshold in the calculation of environmental liability changes, the potential exists for additional misstatements to go undetected.

RECOMMENDATION:

11. We recommend that the Manager, Richland Operations Office, and the Manager, Office of River Protection, ensure that Hanford establishes a reasonable review threshold regarding increases/decreases to the environmental liability that would require review by a manager one level above the Office of River Protection Environmental Management point of contact developing the calculations and documentation supporting the liability changes, incorporating a tiered review approach based on the magnitude of the changes.

MANAGEMENT RESPONSE:

Management concurs. ORP will establish a review threshold (+/- 10 percent), similar to EM Headquarters, for a more rigorous review of changes to the environmental liability. Any liability calculations that increase or decrease by 10 percent from the prior booking will receive an additional review by the appropriate level manager.

19-OR-EL-01 – Insufficient Review of the Long-Term Stewardship Contingency

During our test work over the EM program liability at the Oak Ridge Office of Environmental Management (OREM), we noted that OREM did not have adequate controls in place to ensure that the revised contingency, maintained in IPABS system, was submitted for EM Headquarters approval and appropriately included in the long-term stewardship environmental liability estimate. Additionally, adequate procedures to ensure that the correct contingency percentage was being applied to the long- term stewardship liability were not in existence. This resulted in the long-term stewardship estimate included in IPABS having an incorrect contingency percentage applied to the base estimate in IPABS, which resulted in an overstatement of approximately $30.2 million and the long-term stewardship adjustment (EM Environmental Liability adjustment in IPABS) did not have contingency applied, which resulted in an understatement of approximately $700,000.

These weaknesses occurred because OREM posted an adjustment to IPABS for the long-term stewardship estimate on June 17, 2019, as well as an update to the long-term stewardship uncertainty scores. However, the update to the uncertainty scores was not submitted to EM Headquarters for approval in IPABS. In addition, OREM failed to verify the updates to the uncertainty scores were included in the environmental liability and did not record contingency for the long-term stewardship adjustment. As a result, the OREM environmental liabilities LTS estimate was overstated by approximately $29.4 million as of September 30, 2019.

RECOMMENDATIONS:

12. We recommend that the OREM's Director, Office of Program Planning:

    A. Develop and provide training(s) to IPABS users that focus on submitting changes in long-term stewardship contingency; and

    B. Develop a Non-EM site review procedure to be used to ensure the accuracy of the contingency percentage being applied to the total long-term stewardship liability.

13. We also recommend that the Director, Office of Finance and Accounting coordinate with the Office of Environmental Management Headquarters to distribute guidance to Non-Environmental Management sites to review the accuracy of the contingency in IPABS, including identifying the appropriate percentages are being applied to the total long-term stewardship liability.

MANAGEMENT RESPONSE:

Management concurs with the recommendation. The Office of Program Planning will develop and provide training to the field sites on various aspects of IPABS, including submitting changes in long-term stewardship contingency. Also, the Office of Program Planning will develop and document a site review procedure to ensure the accuracy of the contingency percentage being applied to the total long-term stewardship liability. This procedure will be distributed to the non-EM sites by the Office of Finance and Accounting. As an additional control, OREM will incorporate a check in the Environmental Liabilities procedure to verify percentage of contingency calculated by IPABS that is the basis for the 'CLNUP-REL' spreadsheet is consistent with the percentage for the backup of the Uncertainty Scoring provided to the auditors. OREM will train individuals assisting in development of the Environmental Liability Estimate on this and any new processes or procedures released by EM HQ.

Nuclear Materials

19-NNSA-N-01 – Capitalizing and Overcapitalizing of Stockpile Life Extension Program (SLEP) Costs in the Incorrect Accounting Period

During our test work over nuclear materials inventories, we noted that NNSA identified two sites, LANL and Sandia, which were not following the cost capitalization guidance for SLEP costs set forth in the FY 2018 SLEP Interim Reporting Guidance provided to the sites. Specifically, NNSA identified that LANL and Sandia expensed certain SLEP production costs that should have been capitalized; Sandia did not include the SLEP related depreciation in the Department's Standard Accounting and Reporting System; and, Sandia capitalized some of the direct and allocable costs in error as part of the capitalization process in prior years, which had to be reversed and expensed in the current year.

These weaknesses occurred because LANL and Sandia did not understand the requirements of the FY 2018 SLEP Interim Reporting Guidance. Furthermore, NNSA's review of the SLEP cost data was not performed at a level of detail sufficient to identify the prior period errors because the NNSA Accounting Guide, which provides guidance for capitalizing SLEP costs, was not issued until September 18, 2019. As a result, LANL and Sandia had not properly capitalized costs over the past 15 years, resulting in an understatement of its nuclear materials inventory of approximately $179 million as of September 30, 2018.

RECOMMENDATIONS:

14. We recommend that NNSA's Field Chief Financial Officer, in conjunction with the Field Office Managers with SLEP responsibilities:

    A. Direct nuclear material field sites to follow or implement internal controls to validate that SLEP cost data reported to NNSA Albuquerque and recorded in ABC Financials is properly following the NNSA Accounting Guide with respect to cost capitalization; and

    B. Implement additional training for the field sites over these policies and the revised NNSA Accounting Guide, to validate that accounting personnel understand which costs should be capitalized or expensed.

MANAGEMENT RESPONSE:

Concur. NNSA previously self-identified and corrected the SLEP errors described in KPMG's FY 2019 finding. These SLEP errors were identified during NNSA training and discussions with field sites.

NNSA's Field Chief Financial Officer, in conjunction with the NNSA Field Site Office Manager's with SLEP responsibilities, will direct nuclear material field sites to: (1) follow or implement internal controls to validate that SLEP cost data reported to NNSA Albuquerque and recorded in ABC Financials is properly following the NNSA Accounting Guide with respect to cost capitalization; and (2) Implement additional training for the field sites over these policies, and the revised NNSA Accounting Guide, to validate that accounting personnel understand which costs should be capitalized or expensed.

STATUS OF PRIOR YEAR FINDINGS

Prior Year Findings Related to Internal Controls and Other Operational Matters *(with parenthetical references to findings)*

	Status at September 30, 2019
Pensions and Other Post-Retirement Benefits	
A. Pension Assets Valuation Review (18-PNNL-P-01)	Closed in FY 2019
B. Pension Assets Valuation Review (18-RL-P-01)	Closed in FY 2019
C. Pension Assets Valuation Review (18-SRNS-P-01)	Closed in FY 2019
Grants	
D. Inadequate Review of Federal Financial Reports (18-NETL-G-01)	Closed in FY 2019
Nuclear Materials	
E. Incorrectly Calculated Inter-Project Shipping Entity Rate (18-Y12-N-01)	Closed in FY 2019
Procurement and Financial Reporting	
F. Timely Performance of Account Reconciliations (17-ANL-D-01)	Closed in FY 2019
G. Review of Accruals for the Comprehensive Field Financial Review and Certification (18-EMCBC-D-01)	Closed in FY 2019
Procurement	
H. Untimely Adjustments to Accounts Payable (18-SRNS-D-01)	Closed in FY 2019
Active Facilities	
I. Misstatement in Active Facilities Non-Modeled Estimate (18-ORO-AF-01)	Closed in FY2019
Environmental Management	
J. Ineffective Review of the Input Data in Two Risk Sheets (18-SR-EL-01)	Closed in FY2019

ACRONYMS

APDAS	Associate Principal Deputy Assistant Secretary for Site Operations
BASO	Bay Area Site Office
CNS	Consolidated Nuclear Security
Department/DOE	Department of Energy
Environmental Management	Office of Environmental Management
FITS	Federal Information Tracking System
FY	Fiscal Year
GAAP	Generally Accepted Accounting Principles
IPABS	Integrated Planning, Accounting, and Budgeting System
LANL	Los Alamos National Laboratory
LBNL	Lawrence Berkeley National Laboratory
LTS	Long-Term Stewardship
NETL	National Energy Technology Laboratory
NNSA	National Nuclear Security Administration
OCFO	Office of the Chief Financial Officer
OFA	Office of Finance and Accounting
OREM	Oak Ridge Environmental Management
ORP-EM	ORP Environmental Management
PBS	Project Baseline Summary
PBO	Projected Benefit Obligation
PRB	Postretirement Benefits Other Than Pensions
Sandia	Sandia National Laboratories
SFFAS	Statement of Federal Financial Accounting Standards
SLEP	Stockpile Life Extension Program
SSDI	Social Security Death Index
STARS	Standard Accounting and Reporting System
UCOP	University of California Office of the President
UCRP	University of California Retirement Plan

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