



U.S. Department of Agriculture



Office of Inspector General
Southwest Region

Audit Report

Natural Resources Conservation Service Survey of Controls Over Centers and Institutes

Report No. 10099-4-Te
December 2004



UNITED STATES DEPARTMENT OF AGRICULTURE

OFFICE OF INSPECTOR GENERAL

Washington D.C. 20250



DATE: December 22, 2004

REPLY TO

ATTN OF: 10099-4-Te

SUBJECT: Survey of Controls Over Centers and Institutes

TO: Bruce I. Knight
Chief
Natural Resources Conservation Service

ATTN: Acting Director
Operations Management and Oversight Division

We conducted a survey of the Natural Resources Conservation Service's (NRCS) management controls over its centers and institutes. This survey was performed at the NRCS National Office in Washington, D.C., and NRCS offices in Fort Worth, Texas.

Our objectives included determining whether NRCS' management controls effectively ensured that expenditures by the centers and institutes were in compliance with laws and regulations and evaluating the implementation of recommended controls cited in a prior Office of Inspector General (OIG) audit. We determined that management controls over budgeting, procurement, credit cards, and payments to vendors were in place at NRCS centers and institutes and found no evidence indicating expenditures were not properly authorized or made in compliance with regulations.

However, in preparing its annual statement of assurance reports (i.e., the Federal Managers' Financial Integrity Act (FMFIA) reports to the Department) for fiscal years (FY) 2002 and 2003, NRCS relied on general statements by agency officials that no material weaknesses had been identified. These statements did not acknowledge the suspension of some of the agency's internal controls or provide a rationale for the assurance. For these years, NRCS discontinued the controls it had implemented several years earlier when OIG audits reported an ongoing embezzlement, but it did not communicate to managers the effect of the discontinuance. Consequently, agency leadership based their judgments about controls on assurances from their staff that no control weaknesses rose to the level of materiality.

NRCS' questionable assurances in FYs 2002 and 2003 occurred because the agency's procedures did not specify how risk assessments would be conducted to allow control issues to be brought to management's attention. As a result, the Department had limited assurance as to the overall adequacy and effectiveness of management controls within the agency, as reported in its FMFIA reports for FYs 2002 and 2003.

Although NRCS contended that FMFIA guidance established in the Office of Management and Budget (OMB) Circular No. A-123 is general and does not require specific certification as part of the assurance statement, NRCS officials agreed with our recommendation that NRCS develop and implement a formal process for documenting its internal management controls used in the preparation of NRCS' annual statement of assurance in the FMFIA report.

BACKGROUND

NRCS provides grants and guidance to State and local agencies engaged in conserving the environment. Conservation projects range from preservation of wetlands to restoration of acreage damaged by flood, fire, or other natural disasters.

The reorganization of NRCS in 1994 led to the formation of the National Science and Technology Consortium. The National Science and Technology Consortium is a group of Federal, State, and local scientists who join their technical knowledge to stay on the forefront of conservation matters. The Consortium began with a network that included 10 centers and 7 institutes, each of which provided administrative and/or technical assistance to State office staff, field office staff, and local decision makers. Each center and institute receives administrative funding to carry out its mission.

Prior to 2000, the centers and institutes did not routinely inform NRCS headquarters officials of the nature of their administrative expenses. This changed after OIG found that an employee at one of the centers was able to embezzle funds because of the lack of controls and the disengagement of higher-level management. OIG issued its report in March 2000. In response to the embezzlement, NRCS instituted a reconciliation and reporting system designed to ensure that NRCS managers and officials were informed of the nature of all expenditures at the centers and institutes. The reconciliation and reporting system allowed NRCS to eliminate conditions that otherwise constituted a material control weakness.

NRCS Administrative and Information Technology Review staff performs annual risk assessments designed to determine if accounting and administrative controls are in place and functioning as intended. Results of the various risk assessments are reported to higher-level managers and eventually consolidated in an annual status report, in which officials evaluate their agency's internal control structure and the risks that the agency could face.¹

The Operations Management and Oversight Division, under the direction of the Deputy Chief of Strategic Planning and Accountability, is assigned responsibility for overseeing NRCS' FMFIA reporting process. The division's agency liaison prepares the assurance statements. By September 2003, NRCS had reduced its number of centers from 10 to 9. It is currently reorganizing the staffs at the seven institutes into three new centers.

¹ General Manual, Title 110, part 403.20(b)

OBJECTIVES

Our objectives were to (1) determine what management controls over budgeting, procurement, credit cards, and payments to vendors were in place at NRCS centers and institutes; (2) determine whether such management controls effectively ensured that expenditures by these centers and institutes were in compliance with laws and regulations; and (3) evaluate implementation of recommended controls cited in a prior OIG audit.

SCOPE AND METHODOLOGY

We judgmentally selected for review two of the existing nine centers, the National Information Technology Center (NITC) and the National Cartography and Geospatial Center (NCGC). These centers had the highest funding level for both FYs 2001 and 2002.

Figure 1: Funding Levels For The Centers

Type of Funding	FY 2001	FY 2002
NITC Funding	\$ 9,696,319	\$ 8,264,800
NCGC Funding	8,706,072	7,259,700
OTHER CENTERS' Funding	26,570,766	23,958,800
TOTAL Funding	\$44,973,157	\$39,483,300

At the request of NRCS national officials, our scope did not include a review of the institutes because the institutes were scheduled to close pending the agency's reorganization of these centers and institutes. We performed fieldwork between September 2003 and August 2004 at the NRCS National Office in Washington, D.C., and NCGC in Fort Worth, Texas.² However, we did not perform an onsite review of NITC located in Fort Collins, Colorado. We did, however, expand our coverage to include all reviews completed in FYs 2001 through 2003 for the centers and institutes to determine the extent of NRCS' oversight and assessment of internal controls. We also reviewed the internal controls over budgeting, procurement, payments to vendors, and credit cards for FYs 2001 and 2002.

To accomplish the survey objectives, we (1) reviewed laws, regulations, policies, and procedures applicable to NRCS operations to identify management controls and regulatory requirements; (2) interviewed NRCS national and center officials to obtain a description of the centers' and institutes' organizational structures, operating procedures, accounting systems, and the agency's internal controls over budgeting, procurement, payments to vendors, and credit cards; (3) reviewed the assigned duties to ensure that responsibilities for authorizing, certifying, processing, recording, reconciling, and reviewing transactions were separated among different individuals; (4) examined budgetary data, memorandums of understanding, strategic plans,

² We reviewed the fiscal and administrative records for the selected centers that were maintained at the National Business Management Center in Fort Worth, Texas.

performance plans, annual plans, annual performance reports, FMFIA reports, an operation and evaluation review report, payment and procurement internal control review report, and an administrative review report to determine the extent of NRCS' oversight activities for the centers and institutes; and (5) assessed the effectiveness of corrective actions in response to recommendations cited in a prior OIG audit. Further, we analyzed a judgmental sample of 21 (totaling about \$323,200) of 277 transactions for procurement and payments to vendors and 55 (totaling about \$99,000) of 1,126 transactions for credit card purchases to determine whether transactions were properly authorized, properly recorded, and timely reported in the budget execution system for FYs 2001 and 2002. The samples were selected based on anomalies (e.g., transaction amounts near the purchase limits, transactions for the same purchase amount, transactions for unusual items) identified in analyzing the universe of data.

This survey was performed in accordance with generally accepted Government auditing standards. Accordingly, the survey included such tests of program and accounting records as necessary to meet the survey objectives.

FINDING

In preparing its annual statement of assurance reports (i.e., FMFIA reports to the Department) for FYs 2002 and 2003, NRCS relied on internal reviews that did not adequately communicate control issues to agency managers and, consequently, did not provide support for the assurances given by the agency. For these years, NRCS discontinued the controls it had implemented several years earlier when OIG audits exposed an ongoing embezzlement, but it did not communicate to managers the effect of the discontinuance. Consequently, agency leadership based their judgments about controls on assurances from their management staff that no control weaknesses rose to the level of materiality. Without some explanation of their reasoning, NRCS officials had little basis for their FYs 2002 and 2003 FMFIA statements that none of their control weaknesses was material.

NRCS' questionable assurances in FYs 2002 and 2003 occurred because the agency's procedures did not specify how risk assessments and other reviews would be conducted to allow control issues to be brought to management's attention. NRCS believed that the number of reviews it performed during FYs 2002 and 2003 was sufficient to form a basis for its assurances those years. However, the preponderance of program reviews and the absence of financial reviews resulted in an incomplete assessment of the agency's control structure and an incomplete portrayal of that structure to agency officials. As a result, the Department had limited assurance as to the overall adequacy and effectiveness of management controls within the agency (and, in turn, the agency's stewardship of its resources) as reported in its FMFIA reports for FYs 2002 and 2003.

The FMFIA of 1982³ requires the head of each Federal agency to conduct an annual evaluation of its management controls and financial management systems and to report the results to the President and Congress. OMB Circular No. A-123⁴ provides the guidelines for assessing management controls. The Circular provides that if a Federal manager determines that there is insufficient

³ Public Law 97-255, FMFIA of 1982, dated September 8, 1982

⁴ OMB Circular No. A-123, Management Accountability and Control, revised June 21, 1995

information available upon which to base an assessment of management controls, appropriate reviews should be conducted to provide such a basis.

NRCS strengthened its management control structure in 2000, after it experienced embezzlement the year before. During FY 1999, OIG disclosed a number of material weaknesses in NRCS' computerized accounting system that allowed an employee at a technology support center to access the system and change the payee's name and address at a number of points subsequent to payment certification by a certifying officer. The material weaknesses were reported in the FY 1999 FMFIA, and the OIG report (Audit Report No. 10601-1-Te) was issued on March 31, 2000. To address the recommendations in the OIG report, NRCS introduced a reconciliation process at the support centers that would detect any further misuse of the accounting system, and a reporting process that would provide higher-level managers with the results of the reconciliations. In addition, NRCS implemented onsite review procedures that required NRCS' Administrative and Information Technology Review staff to conduct systematic, detailed reviews of the financial management, human resources management, information technology, and management services operation of NRCS offices.

In FY 2001, the FMFIA report stated that NRCS had completed all corrective actions on the material weaknesses described in the FYs 1999 and 2000 FMFIA reports. The assurances that year were based partly on the controls implemented in 2000 and partly on the risk assessments performed by the Payment and Procurement Internal Control Review Team to assure managers that all controls were in place and functioning as designed. These assessments are required by OMB⁵ and Departmental guidance,⁶ which states that each agency should schedule and perform a sufficient number of control evaluations in order to make a determination for the annual assurance statement.

NRCS guidance⁷ appoints the Deputy Chief for Management to coordinate the reporting of management control activities, maintain the system for preparing the NRCS Chief's annual report, and advise the NRCS Chief periodically whether management controls are operating properly.

In FYs 2002 and 2003, NRCS discontinued the reconciliation process it established in 2000 because the new system it was implementing, the Foundation Financial Information System, did not produce accurate reconciliation reports. Although the centers continued to perform informal reconciliations, NRCS could not substantiate that reports of these activities were sent forward to allow managers to monitor the centers.

Also during FYs 2002 and 2003, the Financial Management Division (FMD) discontinued its risk assessments, which were agreed to as part of NRCS' corrective action to the earlier OIG report and the vehicle by which higher-level managers will normally be alerted to any adverse changes in the control environment. Consequently, the NRCS managers echoed staff assurances that appropriate controls were in place, even though the control environment had lapsed into a less reliable

⁵ OMB Circular No. A-123, Management Accountability and Control, revised June 21, 1995

⁶ Departmental Manual 1110-002, U.S. Department of Agriculture's Management Control Manual, dated November 29, 2002

⁷ General Manual, Title 130, part 404.5(c)

condition. Under such circumstances, NRCS managers are obligated to explain the basis of their assurances. OMB and Departmental guidance note that the FMFIA statement can only be (1) a statement of assurance, (2) a statement of no assurance, (3) a qualified statement, or (4) a statement with exceptions noted. The agency head must describe the analytical basis for the type of assurance being provided, and the extent to which agency activities were assessed. NRCS' FYs 2002 and 2003 statements showed no such analysis. NRCS used the verbatim wording from the sample assurance statement provided by the Department's Office of the Chief Financial Officer.

The agency liaison stated that he obtained input from the U.S. Government Accountability Office, OIG, and the FMD to compile the annual assurance statements in FYs 2002 and 2003. However, we found that there were no U.S. Government Accountability Office or OIG audits of internal accounting and administrative controls performed during FYs 2002 and 2003.⁸ Additionally, the documentation that the agency liaison obtained from FMD consisted of only negative e-mail responses to attest that there were no material weaknesses. The Deputy Chief for Management's staff was directed to concentrate their efforts on the implementation of the 2002 Farm Bill instead of performing the required risk assessments in FYs 2002 and 2003. In addition, FMD staff relied on Foundation Financial Information System controls to provide reasonable assurance that expenditures were properly recorded and accounted for to permit the preparation of reliable financial and statistical reports to maintain accountability over assets, despite the fact that the system had not been able to produce accurate reconciliation reports.

The Deputy Chief of Strategic Planning and Accountability explained that her staff performed some program reviews in FYs 2002 and 2003. However, the reviews were not intended to include an assessment of the agency's internal accounting and administrative controls. The Deputy Chief stated that the agency leadership has primary responsibility for monitoring and assessing controls, and could use other sources as a supplement to their judgment in reporting on management controls. The Deputy Chief informed OIG that agency leadership had determined its process for compiling information to develop the annual assurance statement for FMFIA reporting was sufficient but acknowledged that documentation could be strengthened.

In FY 2004, NRCS reinstated the controls it had established in 2000. On August 3, 2004, the agency liaison notified OIG that in response to our ongoing survey, NRCS is instituting a more formal process for the completion of the assurance statement in 2004. The NRCS official further stated that an assurance statement has been drafted and will be modified based on the results of our review.

⁸ In 2002, OIG conducted a security review of NRCS' Information Technology Resources and a performance review of NRCS' National Production Services. Neither of these reviews included a financial review. (See OIG Audit Reports Nos. 10099-1-Te and 10099-2-Te, issued in February 2002 and July 2002, respectively.)

RECOMMENDATION

We recommend NRCS develop and implement a formal process for documenting its internal management controls for preparation of NRCS' annual statement of assurance in the FMFIA report, including assurance statements for FMFIA prepared by FMD.

NRCS RESPONSE

NRCS concurs with this recommendation. NRCS has already begun to develop a more formal FMFIA process for documenting its internal management controls, including assurance statements for FMFIA prepared by the FMD. A pilot of this procedure was used in the preparation of the 2004 FMFIA report. With some modification, NRCS will incorporate the pilot into formal agency policy and complete the FMFIA report for 2005 by September 30, 2005.

OIG POSITION

We accept the NRCS' management decision for this recommendation. For acceptance of final action, NRCS needs to provide the Office of the Chief Financial Officer, Director, Planning and Accountability Division, documentation of the written procedures that have been developed and incorporated into agency policy for a formal FMFIA process for documenting its internal management controls.

Please follow Departmental and your internal agency procedures in forwarding final action correspondence to the Office of the Chief Financial Officer, Director, Planning and Accountability Division. Final action on the management decisions should be completed within 1 year of the date of the management decisions to preclude being listed in the Department's annual Performance and Accountability Report.

We appreciate the courtesies and cooperation extended to our staff during this review.

/s/ R. W. Young
ROBERT W. YOUNG
Assistant Inspector General
for Audit

Attachment

EXHIBIT A – NRCS RESPONSE TO DRAFT REPORT

United States Department of Agriculture



Natural Resources Conservation Service
P.O. Box 2890
Washington, D.C. 20013

SUBJECT: OIG – 10099- 4-Te

DEC 14 2004

TO: Robert W. Young
Assistant Inspector General for Audit
Office of Inspector General

The Natural Resources Conservation Service (NRCS) provided OIG comments on the above audit on November 5, 2004. The NRCS response below is based on the following revised recommendation:

We recommend the NRCS develop and implement a formal process for documenting its internal management controls for preparation of NRCS' annual statement of assurance in the FMFIA report, including assurance statements for FMFIA prepared by FMD.

NRCS Response: NRCS has already begun to develop a more formal FMFIA process for documenting its internal management controls, including assurance statements for FMFIA prepared by the Financial Management Division and for FISMA prepared by the Information Management Division. A pilot of this procedure was used in the preparation of the 2004 FMFIA report. With some modification, NRCS will incorporate the pilot into formal agency policy and complete the FMFIA report for 2005 by September 30, 2005.

If you have additional questions, please contact me at (202) 720-3750.

A handwritten signature in black ink, appearing to read "S. Probst", written over a horizontal line.

STEVEN A. PROBST
Acting Management Control Officer