TESTIMONY OF
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Nutrition, and General Legislation

on the
Status of Financial Management
at the Department of Agriculture

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Thank you, Mr. Chairman and members of the Committee. I am pleased to be here to provide testimony about the Department of Agriculture’s financial management. With me today is James Ebbitt, Assistant Inspector General for Audit.

I will discuss today the issues that you requested I address, specifically: financial management in USDA, Government Performance and Results Act issues, and the adequacy of USDA agencies’ implementation of corrective actions in response to audit recommendations.

FINANCIAL MANAGEMENT

In order to be effective, management must have reliable financial information. The need for this information resounds throughout all activities, from the more obvious stewardship over assets, fiduciary responsibilities, and budgeting, to operational matters such as performance measurement. For the Department to fulfill its mission and otherwise serve the public, it **must know** how much money has been received, spent, and is needed. It **must know** where its assets are and when they need to be repaired or replaced. It **must know** the costs of its operations to make informed decisions and identify where efficiencies and economies need to be implemented.

Financial information in USDA is, on the whole, not reliable. Our annual financial statement audits, which we have performed since 1991, have disclosed only a limited correlation between the accounting numbers the Department reports and the resources or events those numbers are to represent. Our initial audit opinions on the Department were adverse -- meaning the Department did not conform with prescribed accounting principles. We have since issued disclaimers of opinions for the past 6 years. In other words, the books and records of the Department have been so
poorly maintained we have been unable to compile and analyze sufficient evidence to enable us to reach an opinion. What we are saying is that, due to the significance of the deficiencies in the Department’s accounting systems, the resulting limitations on the scope of our audits were so material that we could not possibly do enough work to determine the reliability of the amounts in the USDA financial statements, such as its $118 billion in assets. And, given the extent of internal control weaknesses, amounts presented on USDA’s statements are highly questionable. More critically, this also means that the managers of the programs and operations may be relying on this highly questionable information. Thus, their ability to do their jobs effectively and efficiently would be significantly impaired.

I will discuss the primary problems preventing USDA from getting an improved opinion on their financial statements.

**Department’s Accounting Systems**

The Department has six primary accounting systems used to account for program costs of over $60 billion. Key to this activity are the financial management systems maintained at the National Finance Center, or NFC. NFC’s, and one of the Department’s most critical systems is the Central Accounting System, or CAS. The problems with CAS have been well chronicled—it is poorly documented, provides for only summary, and not detailed, data and does not meet Governmentwide accounting requirements. An example of the impact of this systemic weakness on the Department’s financial statements is the Forest Service’s $195 million in accounts receivable. In the absence of a subsidiary ledger, individual cash collections or write-offs cannot be matched to the specific receivable. As a result, this material account becomes unauditable. CAS does not have an adequate audit trail and so-called reconciliations and adjustments are processed extensively and without justification.
Simply stated, CAS does not work and cannot be fixed. Only one clear course of action was apparent to enable the Department to emerge from the murky pool of bad data that seeps from CAS--jettison the system. The Department embarked on fulfilling this goal in 1993 through an initiative referred to as the Financial Information System Vision and Strategy, or FISVIS. The purpose of this significant undertaking was to replace CAS with a new system that came to be called the Foundation Financial Information System (FFIS). FFIS establishes a common coding structure, and integrates data from other financial, and mixed systems, while modernizing or replacing existing administrative, financial and mixed systems. The primary goal was to improve financial management in USDA by providing timely, accurate, and cost effective information to policy, management, and operating personnel. At the core of FFIS is a commercial off-the-shelf system, which is compliant with Government accounting and system requirements, to replace CAS. A critical decision at the outset of the implementation of FFIS has stymied implementation and significantly driven up costs. Specifically, the Department, in concert with the user agencies, opted to retain many of the legacy “feeder” systems and interface them with the new core package. The interfaced “feeder” system transactions require complex analytical processes (called mapping) to generate FFIS general ledger entries. Because the “feeder” systems are old and poorly documented, problems have been encountered when “mapping” these transactions to FFIS.

The task of converting data from CAS to FFIS is critical to the success of FFIS. Our reviews identified problem areas related to the conversion of personal property data, data clean-up, and write-off of unreconciled amounts.
**Fund Balance with Treasury**

Another longstanding accounting problem at NFC, the Department’s “Fund Balance with Treasury,” has finally been rectified for CAS. NFC’s CAS account had not reconciled with Treasury records since at least 1992, when we first reported on it. NFC’s annual “fix” of this problem was to plug its accounts to reconcile with Treasury. The unreconciled differences as of September 30, 1999, was $5 billion (the absolute value). This problem was of paramount importance for several reasons—the amount of money involved and the inherent vulnerability of cash to theft or misappropriation. To resolve this problem, the Department brought in a “Big 5” CPA firm to reconcile the cash at NFC. The contractor, at considerable expense, was able to reconcile all but $236 million; it projected the cash impact to be an increase of $7.9 million. (Complete reconciliation could not be achieved due to an absence of records to support dated activity. Significantly, however, FFIS is now out of balance due to many of the control weaknesses that befell CAS. The Department is working aggressively now to identify and eliminate the variances.

**Personal Property**

Our fiscal year 1999 financial statement audit identified another issue which would impact the Department’s opinion unless rectified. Specifically, because of significant weaknesses, we were unable to substantiate whether the financial statements were free from material misstatements for personal property valued at over $888 million. The problem stems from one of NFC’s “feeder” systems, called PROP. Although system weaknesses exist, the primary cause of the misstatements is attributable to lack of required actions, such as annual inventories, by accountable officials. In addition, system reports
have not been used by the agencies. For example, our review of properties valued at over $1 million identified, among other questionable items, a $97 million vehicle, and an $11 million microscope.

**Credit Reform**

Another longstanding, highly complex and very material encumbrance to the Department’s efforts to secure a clean opinion has been its implementation of the credit reform legislation. USDA has a portfolio of loans totaling over $70 billion that is subject to credit reform (it is the largest direct lender in the Federal Government). Affected programs include: the Rural Housing Service’s Single Family and Multifamily Housing programs; the Farm Services Agency’s Farmer Program Ownership and Operating Loan programs; the Rural Business Service’s Business and Industry loan program; and the Rural Utilities Service Electric and Telephone Loan programs. The Federal Credit Reform Act of 1990 rectified an inherent disparity in that accounting data, loans disbursed, loan payments received, loan write-offs, etc., were recorded on a cash basis. This distorted the costs of the programs and precluded meaningful comparative analyses. The law required that the cost of extending or guaranteeing credit be recognized in the period that it was incurred. This cost, called the subsidy cost, must now be accounted for as the present value of the disbursements over the life of the loan less the estimated payments to be made back to the Government. A significant amount of historical data needs to be analyzed to compute these estimates, such as interest rate fluctuations and loan default rates. The initial predictions, or estimates, are to be reestimated at the end of the year to reflect any changes in the assumptions made and future loan performance.

The Department’s loan accounting systems were not equipped to provide the extensive detail necessary to fulfill credit reform requirements. Further, due to systemic deficiencies, much of the data generated
by these systems was incorrect. Congress recognized the potential lack of historical data in the accounting for loans and therefore reduced requirements for all loans made prior to fiscal year 1992. Due to the long term duration of USDA’s loans (up to 50 years), however, the characteristics of these older loans (made before 1992) must be analyzed to predict future performance.

OMB has issued guidance for deriving cash flow inputs to subsidy models for budget formulation and reestimates of all credit programs. The guidance requires current and complete documentation and justification for the estimation methods and assumptions used in determining the cash flow figures in the subsidy model. In the absence of usable historical data, USDA agencies have relied almost exclusively on the judgment of program managers to estimate, for example, the likely performance of loans in the 11th year of a 33-year note. No statistically valid studies or analyses are on hand, however, to support these critical assumptions. Although the systems were changed in 1992 to begin to capture the needed data, too many unknowns continue to exist regarding prior year activity which undermine the support for the estimates used.

The Department has launched an aggressive corrective action plan to overcome the noncompliances with credit reform requirements that we first reported in 1994. Whereas initial actions by the individual agencies were inadequate at best, under the leadership of the Chief Financial Officer, a task force including representatives of OIG was formed to redirect the sideways movement. A series of cash flow models have been devised to capture and analyze the necessary elements to yield meaningful subsidy estimates and reestimates. Legislative requirements impacting cash flow have been identified with emphasis on those having a material effect, and calculation methodologies have been developed. GAO is also participating in this venture. Substantial work remains, however, in that some of the key models,
such as RHS’ for Single Family Housing and those for all of FSA’s programs, require a significant amount of further review and refinement. Further, field testing needs to be performed to verify the key assumptions used.

Real Property

Another longstanding and major encumbrance to a clean opinion is the Forest Service’s accounting for real property. As of the September 30, 1999, the Forest Service reported about $2.6 billion in real property assets. About 60 percent of this dollar value is attributable to what is referred to as “pooled assets” – primarily roads. The remainder represents individual assets such as buildings. The Forest Service to date has been unable to support the valuation of its pooled assets, which is estimated to be $1.5 billion. Reliable records are not available which document the cost of the roads or the timeframe they were put into service, a critical factor needed to estimate depreciation and the value of their remaining useful life. The Forest Service, in concert with OIG, has now developed a strategy whereby this data can be reasonably estimated. The most prevalent problem in this area remains the lack of adequate supporting documentation to verify capitalized costs and in-service dates. We are currently examining real property during our FY 2000 financial statement audit.

Corrective Actions Needed

Now, let me address what the Department needs to do to strengthen its financial management and obtain an upgraded audit opinion. First, FFIS must be fully functional and not beset by significant weaknesses. As of October 1, 1999, the Food Safety and Inspection Service and the remainder of the Forest Service were implemented (two of the nine Forest Service regions came on line the prior year, along with the Risk Management Agency). The plans call for the Animal and Plant Health Inspection
Service, Rural Development, the Natural Resources Conservation Service, and the Farm Service Agency to be implemented on October 1, 2000. Thus, after a slow start, the implementation is aggressively unfolding. Regarding resolution of the problems we identified in FFIS, the Department provided a very positive response to our report which describes, in part, analyses to be undertaken to eliminate the problem-causing feeder systems. The direction is therefore clear; the uncertainty stems from the speed and effectiveness with which these significant issues can be overcome.

In terms of personal property, we believe if our recommendations are implemented this problem area can be overcome. A broad based commitment by the Department’s accountable officials is needed however, and years have elapsed since this commitment has been manifested. Credit reform remains a huge obstacle to an improved audit opinion because of the breadth and complexity of the issue. Although some of the cash flow models are progressing to the point that data verification procedures can be performed, most have not. While the Department’s plans call for the problems to be resolved this fiscal year, much remains to be accomplished. The intensive commitment by all affected agencies is needed to assure the impact on the financial statements will be eliminated as soon as possible.

Forest Service officials assert that the accountability over real property has been achieved. As noted, our current audit is independently evaluating that assertion.
GOVERNMENT PERFORMANCE AND RESULTS ACT

The next area I would like to address is issues arising from the implementation of the Government Performance and Results Act, or GPRA. As you know, GPRA seeks to improve the effectiveness, efficiency, and accountability of Federal programs by requiring Federal agencies to set goals for program performance and to report annual performance compared with goals. Our audit of the Forest Service’s FY 1999 Annual Performance Report found, however, that it was based on flawed data and assumptions to the extent that the report did not provide reliable information about actual performance or the agency’s progress in meeting its goals and objectives. The Forest Service report did not accurately reflect agency performance or progress towards meeting goals and objectives. The quality of the underlying data was suspect. Errors and omissions occurred because performance reporting was not incorporated into the business processes of the FS and because field-level employees did not understand the need or value of accurate performance reporting. Reported data was garnered through a patchwork of information systems that lacked basic internal controls to include programmatic reviews, documentation of reported results, and clear written guidance.

At each of the four national forests we visited, we found instances where reported performance data contained material errors and omissions. A few examples follow:

- Under the Goal “Ensure Sustainable Ecosystems,” we found that one Ranger District had reported two miles of stream enhancement. When we asked to view the stream, Forest Service staff acknowledged that two miles of road had been repaired but reported as a stream.
• At one Ranger District, for the performance measurement, Noxious Weed Treatment, 5 acres were reported as treated, which met the target. However, we found that 18 acres had actually been treated; the reduced amount was reported to preclude an increased target in subsequent years.

• At one Forest, we found that the same portion of a road was annually reported as decommissioned. The forest would erect a barrier to preclude its use, passers-by would remove the barrier, and then agency personnel would re-erect it.

We recommended that FS develop and implement a comprehensive strategy to ensure the collection and reporting of accurate, complete, and meaningful performance data. As a part of that strategy, the agency should put in place a set of effective internal controls, to include comprehensive management reviews, program level reviews, and controls to test the reasonableness of reported performance data. We are currently conducting a review of the Rural Development mission area’s implementation of GPRA.

ADEQUACY OF CORRECTIVE ACTIONS

We conducted a review last year of the Department’s final action process, the legislative requirement that agreed upon audit recommendations be implemented within one year. Our review disclosed that USDA agencies had not exhibited the commitment necessary to promptly and effectively institute corrective actions that arise from audits. The Secretary’s Management Report to Congress was replete with examples of recalcitrance in terms of the agencies’ unwillingness to revise
their processes as they had agreed to after the issued audits were resolved. As a result, the audit process in USDA was potentially undermined. The failure to implement audit recommendations in a timely manner permitted the continuation of ineffective and inefficient Government operations. At the time of our review, the Secretary’s Management Report for the six-month period ending September 30, 1998, included 187 audits without final action within one year of the management decision date with over $989 million in funds to be put to better use identified by OIG. Since the conditions identified in these audits had perpetuated from in excess of one year to over 10 years, the monetary impact of these findings had compounded significantly.

A major reason that final action had not been achieved was that the agencies have not published regulations, instructions, etc., to formally modify their operations in response to the audit within the one-year time frame mandated. Although this process is involved, requires various in-house and intradepartmental clearances, and can be the subject of political considerations, all sense of immediacy in the face of critical disclosures had been lost; rather, corrective actions became ensnared in a bureaucratic web from which it has taken years to be extricated.

One such example is an audit we issued in 1988—12 years ago—on the Food and Nutrition Service’s Women, Infants and Children (WIC) program. The overall objective of the audit was to evaluate the effectiveness of FNS’ management of the WIC Program relating primarily to the retail purchase systems used by State agencies. Our audit disclosed extensive program abuse by vendors. We made compliance purchases at 107 large non-chain stores and were overcharged by 82 of those stores by nearly 29 percent. We found the cause of this material weakness to be inadequate vendor monitoring systems, which had not been designed to identify, and followup on,
high-risk vendors. This, in turn, was traceable to the lack of specific vendor monitoring requirements in the FNS regulations.

A total of 38 recommendations were made, with 20 recommendations still awaiting final action. Corrective action for these recommendations was almost exclusively contingent upon the issuance of new regulations for the WIC Program.

FNS concurred with the recommendations to develop regulations to strengthen vendor monitoring requirements and management decision was reached on September 23, 1988. The explanations afforded by the agency, however, were not adequate to provide justification for the 12 year delay in the issuance of regulations. FNS proposed new WIC Food Delivery System regulations in 1990; however, according to agency officials, because of strong opposition from the vendor community, as well as Congressional concern, these regulations were never finalized. In fact, the regulations were removed from FNS’ regulatory agenda in 1993 and a policy decision to move forward again with the rule was not made until 1997. Without revised WIC Program regulations, FNS cannot ensure that abuse by WIC vendors is precluded or detected in a timely manner. If vendor abuse could have been reduced, additional funds would have been historically available to more persons eligible for WIC Program benefits. WIC funding has totaled $30 billion since FY 1988.

Another example is our audit of the Forest Service’s Timber Sale Cruising Controls, issued in 1993. Cruising represented a critical agency function to estimate the volume of wood available for sale and was to replace (pursuant to a recommendation by the House Appropriations Committee) the prevailing method of scaling, which had been found to be highly vulnerable to timber theft. Our
review of the cruising process, as it was being implemented, disclosed significant control weaknesses which had to be remedied immediately, as cruising was to be adopted as the preferred volume estimation method. According to the Secretary’s March 31, 2000, report, 5 years after the report was released only 3 of the 15 recommendations have been acted upon. The reason given for the delay is “Issuance of the FS Cruising Handbook is delayed due to the administrative process involved in publication.”

Another major reason corrective action has been slowed is that modifying automated systems, apparently, does not happen overnight, or, in the case of our 1991 audit of the Forest Service’s Timber Management Antitrust Controls issued in over 3314 nights. Corrective action on this audit has been delayed, due to “conversion to the IBM computer system from the data General computer system and the development of the new Timber Information System…” The 1991 audit was a followup to a 1986 audit which had identified a significant vulnerability to collusive bidding in the FS timber sale process. Numerous instances were disclosed in which timber companies did not bid against each other (and secured the purchase with the minimum bid), submitted only token bids, or subsequently shared sales after not bidding. The integrity of the timber sale program was at issue and, potentially, significant amounts of revenue were being lost. We recommended, in part that a computerized bid-monitoring system be developed to identify irregular bidding patterns which then could be used to refer possible antitrust violators to the Department of Justice. After 14 years, the agency’s response to this critical issue has been to do…nothing. The relevance of the conversion from Data General equipment to IBM is not readily apparent; nonetheless, it was not initiated until
long after the initial audit was issued. Similarly, the Timber Information System, now cited as part of the reason the corrective action has not been taken, was presumably not even a distant thought in 1986.

In its written comments to OCFO regarding this audit, the agency took issue with our characterization regarding the lack of corrective action, stating it had “…not sat idly by…in fact, the Forest Service has made major investments in time and money to be responsive to the issues raised by OIG.” The FS further stated that it had spent over $200 million to implement the IBM computer system and another $11 million to implement the Timber Information System. The agency expects the system to be working “around March 2000,” at which time the recommendation can be addressed. The FS did not dispute the severity of the underlying problem, nor that no corrective action has ensued since OIG disclosed this critical issue in 1986.

This does not appear to be “responsive” to the recommendation as asserted by the agency.

Subsequent to the issuance of this report, we instigated aggressive actions to get these reports closed. We worked closely with the Department and the agencies through correspondence and numerous face-to-face meetings, and are pleased to report that 59 audits were closed in the most recent reporting period. The number that still remains open is unacceptably high, however, at 166.

Mr. Chairman, this concludes my statement. I would be happy to answer any questions you may have.