

**Audit**



**Report**

OFFICE OF THE INSPECTOR GENERAL

**INSPECTOR GENERAL, DOD, OVERSIGHT OF THE  
ARMY AUDIT AGENCY AUDIT OF THE U.S. ARMY  
CORPS OF ENGINEERS, CIVIL WORKS PROGRAM,  
FY 1996 FINANCIAL STATEMENTS**

Report No. 97-125

April 10, 1997

**Department of Defense**

**Additional Copies**

To obtain additional copies of this audit report, contact the Secondary Reports Distribution Unit of the Analysis, Planning, and Technical Support Directorate at (703) 604-8937 (DSN 664-8937) or FAX (703) 604-8932.

**Suggestions for Future Audits**

To suggest ideas for or to request future audits, contact the Planning and Coordination Branch of the Analysis, Planning, and Technical Support Directorate at (703) 604-8939 (DSN 664-8939) or FAX (703) 604-8932. Ideas and requests can also be mailed to:

OAIG-AUD (ATTN: APTS Audit Suggestions)  
Inspector General, Department of Defense  
400 Army Navy Drive (Room 801)  
Arlington, VA 22202-2884

**Defense Hotline**

To report fraud, waste, or abuse, contact the Defense Hotline by calling (800) 424-9098; by sending e-mail to [Hotline@DODIG.OSD.MIL](mailto:Hotline@DODIG.OSD.MIL); or by writing the Defense Hotline, The Pentagon, Washington, DC 20301-1900. The identity of each writer and caller is fully protected.



**INSPECTOR GENERAL**  
**DEPARTMENT OF DEFENSE**  
**400 ARMY NAVY DRIVE**  
**ARLINGTON, VIRGINIA 22202-2884**



April 10, 1997

**MEMORANDUM FOR UNDER SECRETARY OF DEFENSE (COMPTROLLER)**  
**AND CHIEF FINANCIAL OFFICER**  
**DIRECTOR, DEFENSE FINANCE AND ACCOUNTING**  
**SERVICE**

**SUBJECT: Audit Report on Inspector General, DoD, Oversight of the Army Audit Agency Audit of the U.S. Army Corps of Engineers, Civil Works Program, FY 1996 Financial Statements (Report No. 97-125)**

We are providing this audit report for your information and use and for transmittal to the Director, Office of Management and Budget. It includes our endorsement of the Army Audit Agency (AAA) disclaimer of opinion on the U.S. Army Corps of Engineers, Civil Works Program, FY 1996 financial statements, along with the AAA report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works." An audit of the U.S. Army Corps of Engineers, Civil Works Program, financial statements is required by the Chief Financial Officers Act of 1990, as amended by the Federal Financial Management Act of 1994. Since this report contains no recommendations, comments are not required.

We appreciate the courtesies extended to the audit staff. Questions on the audit should be directed to Mr. Richard B. Bird, Audit Program Director, at (703) 604-9145 (DSN 664-9145; e-mail [rbird@DODIG.OSD.MIL](mailto:rbird@DODIG.OSD.MIL)), or Mr. John J. Vietor, Audit Project Manager, at (317) 542-3855 (DSN 699-3855; e-mail [jvietor@DODIG.OSD.MIL](mailto:jvietor@DODIG.OSD.MIL)). See Appendix D for the report distribution. The audit team members are listed inside the back cover.

Robert J. Lieberman  
Assistant Inspector General  
for Auditing

Office of the Inspector General, Department of Defense

Report No. 97-125  
(Project No. 6FI-2022.01)

April 10, 1997

**Inspector General, DoD, Oversight of the Army Audit  
Agency Audit of the U.S. Army Corps of Engineers, Civil  
Works Program, FY 1996 Financial Statements**

**Executive Summary**

**Introduction.** The Chief Financial Officers Act of 1990, as amended by the Federal Financial Management Act of 1994, requires an audit of the U.S. Army Corps of Engineers, Civil Works Program, financial statements. We delegated the audit of the FY 1996 U.S. Army Corps of Engineers, Civil Works Program, financial statements to the Army Audit Agency on May 17, 1996. This report provides our endorsement of the Army Audit Agency disclaimer of opinion on the U.S. Army Corps of Engineers, Civil Works Program, FY 1996, financial statements, along with the Army Audit Agency report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works."

**Audit Objective.** The audit objective was to determine the accuracy and completeness of the audit of the U.S. Army Corps of Engineers, Civil Works Program, FY 1996, financial statements conducted by the Army Audit Agency. See Appendix C for a discussion of the audit process.

**Audit Results.** The Army Audit Agency report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works," February 28, 1997, stated that the auditors were unable to express an opinion on the Statement of Operations and Changes in Net Position. We concur with the Army Audit Agency disclaimer of opinion; our endorsement of that disclaimer is Appendix A. The Army Audit Agency report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works," is Appendix B.

**Internal Control Structure and Compliance With Laws and Regulations.** The Army Audit Agency issued reports on the U.S. Army Corps of Engineers, Civil Works Program, management controls and compliance with laws and regulations. These reports are included in the Army Audit Agency report (Appendix B).

**Summary of Recommendations and Management Comments.** This report contains no recommendations that are subject to resolution in accordance with DoD Directive 7650.3. Accordingly, comments are not required.

# Table of Contents

---

<b>Executive Summary</b>	i
Appendix A. IG, DoD, Endorsement Memorandum	1
Appendix B. AAA Report, “FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works”	3
Appendix C. Audit Process	124
Appendix D. Report Distribution	125

# Appendix A. IG, DoD, Endorsement Memorandum



INSPECTOR GENERAL  
DEPARTMENT OF DEFENSE  
400 ARMY NAVY DRIVE  
ARLINGTON, VIRGINIA 22202-2884



March 1, 1997

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE (COMPTROLLER) AND  
CHIEF FINANCIAL OFFICER  
DIRECTOR, DEFENSE FINANCE AND ACCOUNTING SERVICE

SUBJECT: Endorsement of the Disclaimer of Opinion on the FY 1996 U.S. Army Corps of Engineers, Civil Works Program, Statement of Operations and Changes in Net Position (Project No. 6FI-2022)

The Chief Financial Officers Act of 1990, as amended by the Federal Financial Management Act of 1994, requires financial statement audits by the Inspectors General. On May 17, 1996, we delegated to the Army Audit Agency (AAA) the audit of the FY 1996 financial statements of the U.S. Army Corps of Engineers, Civil Works Program. The AAA audit for FY 1996 concentrated on the Statement of Operations and Changes in Net Position. Summarized below are the AAA opinion letter on that financial statement and the results of our review of the audit conducted by AAA. We endorse the disclaimer of opinion expressed by AAA (see the Enclosure) in its audit of that financial statement.

**Endorsement of the Disclaimer of Opinion.** The AAA disclaimer of opinion, dated February 28, 1997, stated that AAA was unable to express an opinion on the FY 1996 Statement of Operations and Changes in Net Position of the U.S. Army Corps of Engineers, Civil Works Program. We concur with the AAA disclaimer of opinion.

The primary reasons that auditors were unable to satisfy themselves as to the fairness of presentation of the Statement of Operations and Changes in Net Position were:

- o Accounting policies for self-insurance, plant increment, repairs and maintenance, and asset disposals seriously distorted revenues, expenses, and net position.
- o Material uncertainties existed as to the reasonableness of amounts reported for most revenues and expenses because the reporting process lacked audit trails, consistency, and full disclosure.
- o The absence of an integrated accounting system, including appropriate revenue and expense accounts, prevented the U.S. Army Corps of Engineers from asserting that data reported on the Statement of Operations and Changes in Net Position of the Civil Works Program were reliable.

The financial statements of the U.S. Army Corps of Engineers, Civil Works Program, were audited by the General Accounting Office in FYs 1991 and 1992 and by the AAA in FY 1993 as part of the Army's General Fund financial statements. Opinions were disclaimed in each of those years. Beginning in FY 1994, DoD required separate financial statements and a separate audit opinion for the U.S. Army Corps of Engineers, Civil Works Program. The AAA disclaimed an opinion on the FY 1994 U.S. Army Corps of Engineers, Civil Works Program, Statement of Operations and Changes in Net Position. The AAA did not attempt to render an

\*

\*The enclosure was omitted from Appendix A and included in Appendix B.

## Appendix A. IG, DoD, Endorsement Memorandum

2

opinion on the FY 1995 financial statements of the U.S. Army Corps of Engineers, Civil Works Program. Generally, the disclaimers of opinion were the result of inadequate accounting systems.

**Internal Controls and Compliance With Laws and Regulations.** AAA concluded that the internal control structure did not fully account for and effectively manage resources, ensure compliance with laws and regulations, and ensure that the financial statements contained no material misstatements. As a result, in the overall control environment for financial accountability, the risk of material misstatement was high. The U.S. Army Corps of Engineers acknowledged and properly reported most of these weaknesses in its FY 1996 annual statement of assurance on internal controls.

**Review of Army Audit Agency Work.** To fulfill our responsibilities for determining the accuracy and completeness of the independent audit conducted by the AAA, we:

- o reviewed the AAA approach and planning of the audit, and
- o monitored the progress of the audit at key points.

We also performed other procedures necessary to determine the fairness and accuracy of the audit approach and conclusions.

We conducted our review of the AAA audit of the FY 1996 Statement of Operations and Changes in Net Position of the U.S. Army Corps of Engineers, Civil Works Program, from May 17, 1996, through February 28, 1997, in accordance with generally accepted Government auditing standards. We found no indication that we could not rely on the AAA disclaimer of opinion on that financial statement and the related AAA evaluation of internal controls and compliance with laws and regulations.



Robert J. Lieberman  
Assistant Inspector General  
for Auditing

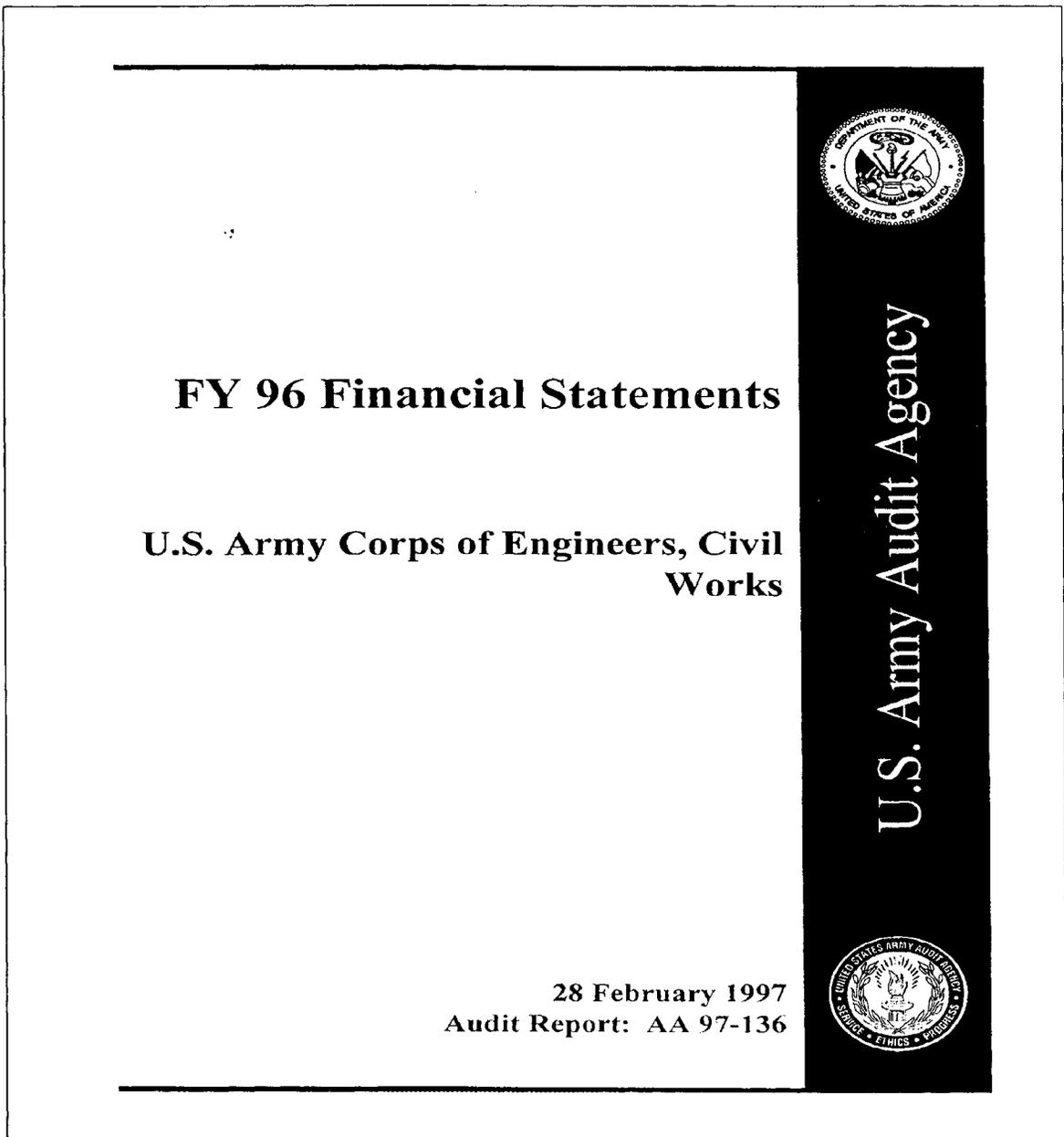
\*

Enclosure

\*The enclosure was omitted from Appendix A and included in Appendix B.

---

**Appendix B. AAA Report, “FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works”**



**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

---



DEPARTMENT OF THE ARMY  
OFFICE OF THE AUDITOR GENERAL  
3101 PARK CENTER DRIVE  
ALEXANDRIA, VA 22302-1596



28 February 1997

Secretary of the Army  
Commander, U.S. Army Corps of Engineers

This is our report on the audit of the Statement of Operations and Changes in Net Position for the fiscal year ending 30 September 1996 for the U.S. Army Corps of Engineers, Civil Works. The Commander, U.S. Army Corps of Engineers and the Deputy Auditor General for Financial Audits, U.S. Army Audit Agency signed an engagement letter in June 1996 defining the audit.

We couldn't express an opinion on the Statement of Operations and Changes in Net Position because of methods used to recognize and report the revenues and expenses, as well as fundamental weaknesses in the Corps' legacy financial accounting system. We were unable to apply other procedures to satisfy ourselves as to the fairness of the presentation of the statement.

On the positive side, the Corps continues to make significant progress with its initiatives to produce reliable financial information and to improve its financial management practices. Its new automated Corps of Engineers' Financial Management Information System (CEFMS) is in the fielding process. Our audit results showed that the system operates with a high degree of reliability and resolves many of the problems found under the previous system. In addition, the Corps' executive management fosters an environment for improvements with a commitment to open communications and working relationships. As a voluntary pilot project for performance measurement under the Government Performance and Results Act, the Corps demonstrates its intent to move forward and improve financial management practices.

Our results showed that the Corps took numerous actions and applied command emphasis to correct many of the problems that we reported in FY 93 and FY 94. For example, the Corps corrected its Construction-In-Process costs and accounting for Engineer and Design Costs. However, improvements were still needed in several areas. We summarize our audit results in the Auditor's Opinion. Details of our review are included in these sections:

*"Fifty Years of Excellence: 1946 - 1996"*

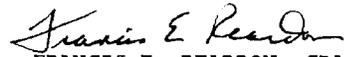
**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

---

- Significant matters.
- Report on management controls.
- Report on compliance with laws and regulations.
- Overview information.

This report also includes our recommendations and the Corps' responses to those recommendations. Annex C contains a copy of the Corps' verbatim replies. The command-reply process prescribed in Army Regulation 36-2 will establish the Army's official position on the findings, recommendations, potential monetary benefits, and command comments included in this report.

I appreciate the cooperation and courtesies extended to us during the audit.

  
FRANCIS E. REARDON, CPA  
The Auditor General

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

---

**CONTENTS**

	<b>Page</b>
<b>Background</b> . . . . .	5
<b>Auditor's Opinion</b> . . . . .	9
<b>Significant Matters</b> . . . . .	13
Finding A - Accounting Policies . . . . .	15
Finding B - Financial Reporting . . . . .	28
Finding C - Financial Management Systems . . . . .	36
<b>Report on Management Controls</b> . . . . .	43
Finding D - Management Controls . . . . .	47
Finding E - Followup Cycle . . . . .	57
<b>Report on Compliance with Laws and Regulations</b> . . . . .	65
<b>Overview Information</b> . . . . .	69
Finding F - Performance Measures . . . . .	71
<b>Objectives, Scope, and Methodology</b> . . . . .	79
<b>Annexes</b>	
A - Corps of Engineers FY 96 Financial Statements . . . . .	85
B - Audit Reports Issued and Activities Included in the Audit . . . . .	120
C - Verbatim Command Comments . . . . .	121
D - Others Receiving Copies of the Report . . . . .	135
E - Audit Staff . . . . .	136

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

---

**BACKGROUND**

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

---

### BACKGROUND

The U.S. Army Corps of Engineers is a complex organization with civil works and military missions. As the largest public engineering, design, and construction management agency, it employs a workforce of about 39,000 civilians and 600 military personnel. The Corps also contracts with commercial architectural, engineering, and construction firms for most design work and for all construction work.

Within the civil works program, the Corps develops, maintains, and manages many of the nation's water and related environmental resources. This mission includes designing, constructing, and operating projects for:

- Commercial navigation of rivers, harbors, and channels.
- Flood control.
- Hydroelectric power development.
- Restoration of fish and wildlife.
- Recreation areas.

Under its military program, the Corps manages and administers contracts for engineering services for the Army. When requested, the Corps provides these services to the Air Force, other DOD and government agencies, and foreign governments. The Corps also does research and development in engineer support (specialized equipment and procedures) of combat operations.

The Corps uses a decentralized management structure consisting of 64 major operations located worldwide: a headquarters, 13 divisions, 39 districts, 4 laboratories, and several field operating activities.

The Corps budgeted about \$10.3 billion for its FY 96 program--about \$4.2 billion for civil works and about \$6.1 billion for military programs. It operates a revolving fund for common services that apply to multiple projects.

**AUDITOR'S OPINION**

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"



DEPARTMENT OF THE ARMY  
OFFICE OF THE AUDITOR GENERAL  
3101 PARK CENTER DRIVE  
ALEXANDRIA, VA 22302-1596



Secretary of the Army  
Commander, U.S. Army Corps of Engineers

In accordance with the Chief Financial Officers Act of 1990, as amended by the Government Management Reform Act of 1994, the U.S. Army Corps of Engineers prepared the accompanying principal financial statements and engaged us to audit its Statement of Operations and Changes in Net Position for the fiscal year ended 30 September 1996. The statement is the responsibility of the Corps' management.

We couldn't express an opinion on the reliability of the Statement of Operations and Changes in Net Position primarily for the following reasons:

- Several accounting policies used by the Corps within its Revolving Fund for self-insurance, plant increment, repairs and maintenance, and asset disposals seriously distorted its revenues, expenses, and reported net position on the Statement of Operations. These policies also distorted the assets, liabilities, and equity reported on the Statement of Financial Position. Although this statement wasn't included in our audit, we reported the statement's impact because of the inherent linkage between these two statements.
- Material uncertainties continued to exist regarding the reasonableness of amounts reported for most of the Corps' revenues and expenses because the Corps' reporting process lacked audit trails, consistency, and full disclosure.
- Absence of an integrated accounting system prevented the Corps from asserting that data reported in the Statement of Operations and Changes in Net Position was reliable. The Corps' accounting system lacked the appropriate revenue and expense accounts.

We were unable to apply other auditing procedures to satisfy ourselves as to the fairness of the presentation of the Statement of Operations and Changes in Net Position for FY 96. Consequently, we couldn't express an opinion on the statement.

*"Fifty Years of Excellence: 1946 - 1996"*

Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

Therefore, we caution users that the information presented in the Statement of Operations and Changes in Net Position, as well as the other financial statements, may not be reliable.

We concluded that management controls weren't fully effective in accounting for and managing resources, ensuring material compliance with laws and regulations, and ensuring there were no material misstatements in the financial statements. As a result, the overall financial accountability control environment is such that the risk of material misstatement is high. The Corps acknowledged and properly reported most of these weaknesses in its FY 96 annual assurance statement on management controls.

We also evaluated, on a limited basis, the information presented in the Corps' Overview section. During our previous audits in FY 93 and FY 94, we reported that the Corps needed to improve its methods of measuring performance to effectively portray its civil works mission, resources, goals, and results. The Corps initiated some new actions during FY 96--still in progress at the time of our audit--to improve performance measures. However, for the FY 96 Overview section, the Corps used the same performance measures that it used in the previous fiscal years. Accordingly, the significance of the performance measures presented in the FY 96 Overview remains questionable.

We didn't audit the Statement of Financial Position as of 30 September 1996 or the Statement of Cash Flows for the period ended 30 September 1996. Therefore, we don't express an opinion on these statements.

  
FRANCIS E. REARDON, CPA  
The Auditor General

28 February 1997

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

---

**SIGNIFICANT MATTERS**

### SIGNIFICANT MATTERS

The U.S. Army Corps of Engineers is a leader among the major Army commands in striving to meet the goals of the Chief Financial Officers Act. In FY 93, the Corps was the first to prepare and submit a separate set of financial statements. In FY 94, the Corps volunteered as a pilot project under the Government Performance and Results Act. Throughout FY 95, the Corps worked diligently to correct several material weaknesses on the U.S. Army Annual Assurance Statement.

While a consistent pattern of disclaimers on the financial statements would normally lead to the conclusion that progress isn't being made, the Corps has made substantial movement forward in achieving the goals set forth in the Chief Financial Officers Act. We found that the Corps addressed and corrected most of the material conditions found during our FY 93 and FY 94 audits. However, there aren't easy solutions for many of the problems and the Corps must continue to invest substantial effort to achieve the desired results.

In this year's audit of the Statement of Operations and Changes in Net Position, we again weren't able to express an opinion. In this section we will discuss our primary areas of concern. As the Corps progresses forward with the fielding of its new management information system, these are the areas where we believe the Corps needs to focus its attention. These areas include:

- Accounting policies.
- Financial reporting.
- Financial management systems.

\* \* \*

If command carries out the recommendations in this report, there could be monetary benefits (based on the estimates we could reasonably make at the time of the audit).

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

---

### **FINDING A: ACCOUNTING POLICIES**

**For the Commander,  
U.S. Army Corps of Engineers**

#### **SUMMARY**

Within its Revolving Fund, the U.S. Army Corps of Engineers maintained accounting policies that weren't in accordance with the Federal Financial Accounting Standards.

One of management's primary responsibilities is to keep the Revolving Fund solvent at all times. Therefore, the Corps imbedded financing mechanisms in the fund to protect the balance of the fund by either accumulating reserves or increasing solvency (cash flows) within the fund.

We agreed with the business practices used by the Corps to accumulate reserves to offset future expected costs. They appeared to be prudent management decisions to finance Revolving Fund operations. We didn't agree with the practices implemented solely to produce cash flow. However, in either case the Corps didn't account for the associated revenues and expenses in accordance with accounting standards. These policies misrecorded and misreported the current year's operating expenses, distorting the financial statements.

As a result of the accounting policies used, the financial reporting of the results of operations wasn't accurately portrayed on the financial statements. We recommended adjusting entries totaling about \$223.2 million.

Our detailed discussion on these conditions starts on page 17. Our recommendations start on page 25.

#### **BACKGROUND**

The Civil Functions Appropriations Act of 1954, Public Law 153, authorized the creation and operation of the Corps' Revolving Fund. The law allows certain transactions to be initially financed by the Revolving Fund to include:

- Purchase of common inventories for civil works such as bulk materials and supplies.

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

- Operation of common storehouses that service more than one civil works project or appropriation.
- Acquisition, operation, and maintenance of facilities that support more than one civil works project.
- Finance of common services of the district office or services performed for other governmental agencies.

The Revolving Fund operates entirely within its own resources rather than from annual appropriations, recouping its expenditures through the sale of its services (via its rates) to its customers. The rates charged include an amount to recover the Corps' operating expenses and overhead. The fund must operate at a break-even point, income equal to expenses within a tolerance level of plus or minus 5 percent.

### Accounting Concepts

The Corps accounted for its operations under the accrual method of accounting. Under this method, the entity records financial effects of transactions or other events in the periods in which they occur, rather than in the periods in which cash is received or paid.

With regard to the Statement of Operations, there are several accounting principles and defining concepts:

- **Realization and Recognition.** Under these principles, revenues are earned when the required performance is completed. For example, incoming cash receipts for future work would be unearned revenue until work is completed.
- **Matching Principle.** The expenses incurred to generate the products or services of a given period must be matched with the revenues. Because some costs may have been paid in the past or will be paid sometime in the future, the proper matching of expenses to the period may require accruals, deferrals, or allocations. For example, depreciation is a systematic allocation, or spreading, of the acquisition cost of an asset to the periods that benefitted.
- **Expenses.** Generally Accepted Accounting Principles (GAAP) defines expenses as expired costs, or items that were assets but are no longer assets because they have no future value. Expenses of the current period can be either cash or noncash. For example, payroll expenses generally are cash expenses since funds are paid out on a periodic basis. Depreciation is a noncash expense

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

---

since the asset acquisition occurred in a previous period. Noncash expenses generate positive cash flows.

- **Prepaid Expenses.** Defined as advance payments on ordinary expenses. These prepaids are classified as assets on the Statement of Financial Position (balance sheet) until the expense occurs. Some examples of prepaid expenses would be premiums or rents paid for more than one period upfront, for example, a one year lease.

### Financing Concepts

Financing concepts focus on generating resources (or credit) to pay for large expenditures over an extended time period. They recognize the time and value of money by charging interest, determining the opportunity costs, and calculating the return on investment. Those used by the Corps focused only on cash outlay requirements and recoupment of initial investment or acquisition cost.

There exists a clear distinction between accounting and financing principles. The accounting principles record and report the transactions and events that occurred. The financing principles address how to ensure that the fund remains viable and solvent.

### DISCUSSION

---

The Corps designed several accounting policies in support of its business practices to ensure that funds accumulated to pay for future expected costs. Within the rates charged to customers in the current period, a predetermined amount was set aside to cover the following:

- Insurance.
- Plant increment.
- Repairs and maintenance.

The Corps had two accounting policies to generate cash flow and one policy for capitalizing expenses that also conflicted with accounting standards. Specifically these policies were:

- Disposal of assets.

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

- Salvage value on assets.
- Deferred asset costs.

The Corps' accounting for insurance, plant increment, and repairs and maintenance wasn't proper. Specifically, we found that the expenses associated with the business practices relating to insurance and plant increment weren't expenses of the current period and hadn't occurred at the time recorded. In accounting for the repair and maintenance reserves, the Corps incorrectly transferred the current period operating income into a deferred income account.

The accounting for asset disposals and deferrals also wasn't proper. By recording as expenses the residual asset values during the disposal of the assets or not recognizing salvage value, the operating expenses increased inappropriately and distorted the results of operations. Further, recording other costs as deferred asset costs instead of current period expenses understated operating expenses and overstated the assets.

All six of these policies tended to recognize expenses inappropriately or distort net income within the financial statements, usually understating reported net income. Further, there was a significant impact on the Statement of Financial Position as well, due to the linkage between the accounts and accounting cycles. We calculated that about \$223.2 million in adjusting entries were required to correct the financial statement impacts of these accounting policies.

In this section, we discuss the conditions found, proper accounting principles, and the financial statement impacts of the Corps':

- Accounting policies for business practices.
- Accounting policies to increase cash flow.
- Accounting entries required to adjust statements.

### Accounting Policies for Business Practices

#### Insurance

The Corps operates as a self-insured entity, charging a monthly premium on its assets and accounting for this premium as an operating expense of the period (debit) and a future liability (credit). The policy of charging for insurance and expensing that amount in the current period violated accepted accounting standards for self-insured

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

operations. Also, the recording of the offset as a liability wasn't appropriate since, at the time of collection of the premium, the Corps hadn't incurred any future liability. The correct offset would be to the Corps' equity. Self-insured operations can be accounted for using either of two acceptable methods:

- Record losses when incurred on the Statement of Operations (Income Statement).
- Appropriate Retained Earnings and record losses as incurred on the Statement of Operations (Income Statement).

The Corps' policy deviated from the acceptable methods by expensing an amount equal to the premium collections. When a loss occurred, the Corps accounted for it solely on its Statement of Financial Position (Balance Sheet) by reducing its fund balance and liability accounts.

As a result, this accounting policy overstated expenses and understated net income by the recurring premium collections. In FY's 95 and 96 this amounted to about \$2.5 million and \$3.1 million respectively. Losses bypassed the income statement and weren't reported properly in the period incurred. The result was overstating net income by the amount of the actual loss (FY 95 was \$4.2 million, FY 96 was \$0.8 million). In addition, the liabilities were overstated and the Corps' equity was understated by the balance of the Insurance Reserve amount--\$46.1 million.

The Corps agreed to implement actions to correctly report the insurance premiums, losses, and reserves at the corporate or headquarters level for financial statement presentation. We agreed with the Corps that, during the life of the legacy system, corporate-level adjusting entries would be more efficient than having all districts and reporting activities adjust their individual records and business practices.

### **Plant Increment**

In reviewing the Corps' accounting policy for Plant Increment (defined as an estimated additional cost, due to inflation, for plant replacements), we found that the amounts were charged as operating expenses in the current period and credited to an equity account entitled "Provision for Plant Replacement." Subsequently, the balances within the districts were transferred to the headquarters' general ledger account--Funds With Treasury.

The Corps' policy for plant increment charged a future estimated cost not yet incurred as a current-period expense,

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

---

violating the matching principle. Under generally accepted accounting principles, the plant increment wouldn't be recorded directly to the operating expense accounts. The amount would accumulate within a reserve or fund account until the purchase of the new or replacement asset. Then the asset would be capitalized and depreciated. The expense would then come about indirectly through the depreciation of the asset. The plant increment amount is a "Sinking Fund" and as such should be carried only on the balance sheet as an asset and not charged off as an expense.

Analysis of the credit side of the journal transaction also supported the "Sinking Fund" concept. Generally, the normal credit offset to operating expenses would be either the creation of a liability (such as Accounts Payable) or the decrease of an existing asset account. Neither was the case in the Corps' accounting policy. Instead, there was a charge to expense and an increase to an equity account. This is an illogical combination of events. Expenses by their very nature are always a reduction to the equity interest of the entity.

As a result, this accounting policy overstated expenses and understated net income by the plant increment collections, for FY 96 this amounted to about \$30.4 million. In addition, the assets were understated by the balance of the increment amount not capitalized through asset acquisitions.

**Repairs and Maintenance**

To smooth out the spiked costs associated with periodic major repairs or maintenance on selected assets, for example a major engine overhaul on a barge, the Corps charged the customers within its rates a prorated amount to cover both current and future expected repairs and maintenance costs. The Corps removed the portion of the charges applicable to the future repairs from the current-period operations and transferred the income into a deferred income account. There was a corresponding offset entry in an asset reduction (contra-asset) account. Corps personnel believed that their method would match the income to the expenses.

This belief was a misinterpretation of the matching principle. Generally, to determine net income, costs incurred to produce revenues are matched as expenses of the period to which the revenues relate. The portion of the repairs and maintenance rate charge that wasn't used in the current period or that was set aside to cover the future estimated cost of the repairs represents income or profit. The Corps, under the realization and recognition principles, earned the revenues and incurred the expenses in the current period, the difference being income. The income (cash) should be set aside to fund the future expense, either formally or

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

---

informally, as a restriction to the cash asset account. Proper accounting would also require that the offset be in the Corps' equity and not as a contra-asset.

As a result of this policy, net income was understated about \$37.9 million on the Statement of Operations. Also, on the Statement of Financial Position, the assets were understated by the amount not recorded as well as the total reserve amount recorded in the contra-asset account by or about \$98.1 million.

Our recommended actions to correct the accounting policies related to business practices are in Recommendation A-1.

### **Accounting Policies to Increase Cash Flow**

#### **Disposal of Assets**

The Corps' accounting policy for disposing of assets (whether transfer, salvage, or surplus) focused on increasing cash flows rather than the proper financial reporting of transactions and events.

The policy directed that the asset's remaining net book value (original cost less accumulated depreciation) be expensed in the current-year's operations prior to disposition of the asset. For example, at one district, we reviewed 21 revolving fund asset retirements made in FY 96. We found five, or 24 percent, had remaining book value totaling about \$27,100 that the district charged to its expense accounts before retiring the assets.

By analyzing the accounts (Book Value of Plant Sold and Sale of Plant) for minimal book value and significant sales proceeds, we identified 14 district offices and 1 division office that appeared to be following the expensing policy. Because of the limited visibility of the financial system (summary level data and no access to underlying transactions), we weren't able to quantify the underlying book value amounts expensed. But the net sales proceeds that were received totaled about \$1.8 million.

As a noncash expense, depreciation (or expensing of capital assets) generates an incoming cash flow to the fund when the services are billed out to its customers. Under the Revolving Fund's break-even profit motive, Corps personnel viewed this as the only financing mechanism they had to recover the initial outlay of funds used in the acquisition of the assets.

Proper accounting principles dictate that the asset not be expensed before disposal and a gain or loss should be

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

---

recognized as the difference between the proceeds, if any, and the remaining net book value. The writeoff of the net book value overstated current period operating expenses and didn't accurately reflect the nonoperating gains and losses on the Statement of Operations. However, compounding this issue was the Corps' policy for accounting for nonoperating gains and losses.

In reviewing this second policy on accounting for nonoperating gains and losses, we found that the nonoperating gains and losses were charged directly to the proprietary interest (net worth or equity) section on the Statement of Financial Position.

The nonoperating gains and losses moved through the Corps' general ledger accounts and accumulated solely within the equity section of the Statement of Financial Position under Investment of the U.S. Government. This account crosswalked from the Corps' general ledger to the Standard General Ledger equity account entitled Capital Investments.

We reviewed Office of Management Budget Bulletin 94-01 and the Treasury Financial Manual because nonoperating income and losses generally should be reported on the income statement.

The Treasury Financial Manual showed that the Corps' use of the Capital Investments equity account wasn't appropriate. The Standard General Ledger contains specific accounts for nonoperating income (gains) and losses. The gains are accounted for in the 7100 series of accounts, and the losses are accounted for in the 7200 series of accounts.

In addition, Office of Management and Budget Bulletin 94-01 showed that the nonoperating income and losses should be properly reported on the income statement. The income would be reported on Line 6, Other Revenues and Financing Sources. The losses would be reported on Line 14, Other Expenses. We determined the appropriate accounting by tracking the financial statement line items back to the Standard General Ledger using the Office of Management and Budget approved crosswalk.

In essence, the Corps' policy for gains and losses charged these balances directly to the Revolving Fund balance or equity. Given the Corps' policy to expense remaining book value prior to asset disposal, the current accounting policies allow for gains to flow directly into the Statement of Financial Position (balance sheet) accounts bypassing the Statement of Operations (income statement) and understating net income. Since neither the gains or losses were reflected on the income statement, the net income was incorrect.

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

### Salvage Value on Assets

The Corps didn't recognize any salvage value on any depreciable assets (buildings, structures, equipment) within the Revolving Fund.

Because salvage value represents a reduction to the amount used for depreciation, the Corps believed that any amount formally recognized would ultimately reduce the fund's balance. Within the context of a financing mechanism, the recognition of salvage value would reduce the depreciable basis of the asset and the corresponding depreciation expense and would result in less incoming cash flow. Also, recovery of the initial purchase amount would be dependent upon the sale or disposal of the asset. Corps personnel stated their concern that the recovery might never occur for permanent structures that the Corps occupies, maintains, or transfers to other governmental agencies without reimbursement.

Under generally accepted accounting principles, the recognition of salvage value on capital assets is an integral part of depreciation (allocation of expense) to the periods benefitted while it preserves some valuation for the asset residual.

We understood the Corps' rationale for its salvage value policy. However, the primary function of the accounting system is to accurately record the transactions and events for the entity. The Corps' concerns regarding the recovery of the initial acquisition costs are, or should be, part of the rationale and methodology used in establishing the plant increment rate.

To depreciate large assets, such as buildings, without acknowledging that residual value exists, isn't realistic. Over time the valuation of the asset amounts becomes misrepresented while the annual depreciation overstates operating expenses and understates net income. To illustrate, in FY 95 the Revolving Fund property, plant, and equipment (net of land costs) had an acquisition value or depreciable basis of about \$1.3 billion. The annual depreciation expense recorded was about \$62.8 million, or 5 percent. Assuming a composite salvage value of 20 percent, the depreciable basis would become \$1 billion and the corresponding annual depreciation would drop to about \$50.2 million. The difference of about \$12.6 million in annual expense is due to the recognition of salvage value.

We also found, in contrast to the fund's break-even profit motive, a consistent pattern of gains on asset disposals. We attributed this pattern to both the expensing of the net book value as previously discussed and the lack of salvage value recognition.

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

We expressed our concerns to the Corps that this pattern could indicate excessive charges to customers since under the existing system the gains went directly to the Corps' benefit. There was no mechanism in place to calculate either the gains or losses into the Revolving Fund's rates. Therefore, the current system exempted the customers from receiving the benefits of the gains or the decrements from the losses, whenever recognized.

### Deferred Asset Costs

The Corps' policy on accounting for assets placed in mothball status was to charge the costs incurred to the deferred asset account. These amounts accumulated on the Statement of Financial Position until the asset was placed back into service. The costs were then allocated to either the previous, present, or future users based on management decision.

As defined by the Financial Accounting Standards Board's Concepts Statements (Number 6), the mothballing costs are more appropriately expenses of the current period and not deferred assets. The assumption for making a deferral would require that there be some future economic benefit derived in some future period. While the mothballed asset may provide some future benefits, the costs associated for storage or warehousing won't and shouldn't become part of the cost of the asset.

In addition, the Corps' deferred asset account also incorrectly contained deferred income. This was accounted for in a manner similar to the repair and maintenance reserves previously discussed. In other words, earned income was transferred and held within the deferred account until additional expenses materialized to be offset against the income. For FY 96, we found adjustments totaling about \$6.8 million.

The financial statement's impacts of this policy are similar to the impacts associated with the policies previously discussed. In this instance, the policy understated net income on the Statement of Operations while also overstating assets on the Statement of Financial Position because a normal operating expense or income became a deferred asset.

Our recommended actions to correct the accounting policies related to generating cash flow are in Recommendations A-2 through A-7.

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

**Accounting Entries Required to Adjust Statements**

The accounting policies previously discussed have a significant impact on the Corps' financial statements. To correctly report the results of operations and financial position requires adjusting entries totaling about \$223.2 million. Specifically:

Policy	Adjustment Amount	Increase Account	Decrease Account	Remarks
Insurance	\$3.1 million	Asset (2)	Expense (1)	Annual premiums collected
Insurance	\$0.8 million	Expense (1)	Equity (2)	Report actual losses
Insurance	\$46.1 million	Equity (2)	Liability (2)	Restate reserve
Increment	\$30.4 million	Asset (2)	Expense (1)	Annual amount collected
Repairs & Maintenance	\$98.1 million	Equity (2)	Contra-Asset (2)	Restate repairs and maintenance reserves
Repairs & Maintenance	\$37.9 million	Revenues (1)	Contra-Asset (2)	Recognize income earned
Asset Disposals	Not Quantified	Gains or Losses (1)	Expense (1)	Lacked transaction visibility
Salvage Value	Not Quantified	Asset (2)	Expense (1)	To be analyzed and determined
Deferred Assets	\$6.8 million	Revenues (1)	Asset (2)	Recognize income earned
Total	\$223.2 million			

- (1) On Statement of Operations and Changes in Net Position
- (2) On Statement of Financial Position

**RECOMMENDATIONS AND COMMAND COMMENTS**

This section contains specific recommendations and a summary of command comments for each recommendation. Verbatim command comments are in Annex C.

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of  
Engineers, Civil Works"**

---

The Corps agreed to implement corrective measures on its accounting policy for insurance premiums with a proposed implementation date of 30 September 1996. However, due to technical difficulties in posting and balancing the FY 96 Trial Balance, the Corps didn't meet the proposed implementation date.

**A-1 Recommendation:** Correct the accounting policies (insurance, plant increment, repairs, and maintenance reserves) associated with the Corps' business practices to ensure that the:

- Policies are in accordance with Federal Accounting Standards and Generally Accepted Accounting Principles.
- Statement of Operations and Changes in Net Position correctly reflects the expenses, net income, gains, and losses of the current period.
- Statement of Financial Position shows the correct balances in the prepaid assets and fund balance reserve amounts.

**Command Comments:** The Corps agreed with the recommendation and stated that it recognized the current accounting wasn't in full compliance with accounting principles. The Corps planned to make adjusting and corrective closing entries beginning in FY 97, during yearend closeout.

**A-2 Recommendation:** Discontinue the policy of expensing the remaining book value of assets prior to asset disposal. In accordance with accounting principles, recognize nonoperating gains or losses on the assets as the difference between the net book value and proceeds received, if any.

**Command Comments:** The Corps agreed and stated that it is incorporating this recommendation in change 88 to its Engineer Regulation 37-2-10, which should be completed by 30 September 1997.

**A-3 Recommendation:** Record and report nonoperating income and losses on the Statement of Operations and Changes in Net Position.

**Command Comments:** The Corps agreed and said it will comply with Office of Management and Budget

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

---

Bulletin 97-01 during the preparation of the FY 97 financial statements.

- A-4 Recommendation:** Implement procedures to ensure that gains and losses are incorporated into the rate structure and passed on to the Revolving Fund customers.

**Command Comments:** The Corps agreed to incorporate the recommended practice into the operating budget process for all Revolving Fund plant accounts.

- A-5 Recommendation:** Implement a policy to recognize salvage value on depreciable assets. Consider using either a composite standard rate or various rates by major class of assets by reviewing historical records to determine the net realizable value received as a percentage of acquisition cost or by allocating amounts based on estimated salvage value.

**Command Comments:** The Corps concurred stating that it will require salvage value calculation in the depreciation formula for all structures in Engineer Regulation 37-2-10.

- A-6 Recommendation:** Discontinue the policy of recording deferred asset charges for equipment in mothball status. Record these costs as current period expenses.

**Command Comments:** The Corps agreed and said that revised procedures will be incorporated in change 88 to Engineer Regulation 37-2-10 by 30 September 1997.

- A-7 Recommendation:** Determine the cumulative impact on the financial statements of the policies not in conformance with generally accepted accounting principles. Record and report prior period adjustments to correct balances.

**Command Comments:** The Corps agreed and stated that it would make the appropriate adjustments in the FY 97 financial statements.

Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

**FINDING B: FINANCIAL REPORTING**

For the Commander,  
U.S. Army Corps of Engineers

**SUMMARY**

The Corps' financial reporting process needed significant improvement. In reviewing the FY 95 and FY 96 documentation for the compilation and presentation of the statements, we found that it lacked:

- Adequate audit trails.
- Consistency.
- Sufficient disclosure.

As in FYs 93 and 94, the Corps elected to expend minimal resources in FY 95 on producing financial statements resulting from its old financial management system. The old system couldn't produce adequate financial data because it lacked key accounts and wasn't designed to account for revenues and expenses (see Finding C of this report).

We agreed with the Corps that expending additional resources to modify the legacy accounting system wouldn't be prudent. However, the fielding of the new management information system dictates that sufficient effort be placed in the process starting in FY 96 to ensure that balances brought forward are accurate, reliable, and auditable. The Corps agreed with our assessment and initiated several actions in the FY 96 yearend closeout. These efforts established a starting point; however, the actions couldn't correct the primary underlying condition--the inadequacy of the legacy financial management system.

As a result, the FY 95 and FY 96 financial statements didn't accurately portray the results of operations or the financial position of the Corps. In addition, this also affected the opening balances established for FY 97 at the close of FY 96.

Our detailed discussion on these conditions starts on page 29. Our recommendations start on page 34.

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

---

### **BACKGROUND**

---

The Corps of Engineers operates using a decentralized management structure. For the most part, each of the districts, divisions, labs, and reporting activities manage and account for their own funds and costs. There are exceptions for certain centralized operations, such as payroll or vehicle leasing, or for small districts or operations that are supported by a larger one.

The financial reporting process consists of an upward reporting system. The reporting entities periodically submit their account balances to the Corps' Finance Center. Also submitted are details on special interest items and standard forms used for budgetary and financial reporting. Using the available information, the Finance Center compiles and prepares the Corps' consolidated financial statements. None of the Corps' entities below the headquarters level produced financial statements.

### **DISCUSSION**

---

In this section we discuss:

- Financial reporting problems.
- Upward reporting.
- Corrective actions for FY 96.
- Upcoming requirements for FY 97 and beyond.

#### **Financial Reporting Problems**

As noted previously in our FY 93 and FY 94 audits, the financial reporting process used to compile and prepare the consolidated financial statements wasn't adequate. During FY 95 and FY 96, the condition worsened due to several causes:

- The Corps made a conscientious decision not to expend significant resources modifying its outdated financial system while fielding its new financial management system.
- The reporting function migrated organizationally and then physically to the Finance Center. According to

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

Corps personnel, some of the documentation was lost during the transitions.

We noted that the Corps didn't:

- Have adequate audit trails and documentation.
- Display consistency in its presentation of the financial statements.
- Report sufficient information within its footnote disclosures.

### **Audit Trails and Documentation**

There was no record of the adjusting, closing, or eliminating entries being made to produce the FY 95 consolidated financial statements.

The adjusting, closing, and eliminating journal entries are integral to the preparation of the financial statements. They provide the rationale and link between the financial statements and the trial balances. Adjusting and closing entries formally close out the reporting period and establish zero balances within the accounts for the upcoming period. Eliminating entries remove transactions that otherwise would result in the double-counting of revenues, expenses, assets, or liabilities.

Without an audit trail of these transactions, we weren't able to track from the financial statements to the trial balances. For example, in attempting to reconcile the assets, liabilities, and net position, we reviewed 27 appropriations, with assets totaling \$40.6 billion, and found the following absolute differences:

- Assets, \$962.1 million.
- Liabilities, \$659.4 million.
- Net Position, \$1.4 billion.

Only 5 of the 27 appropriations, representing \$49.7 million of assets (the Corps' smaller appropriations), had no differences between the financial statements and the trial balances.

### **Consistency in Presentation**

There wasn't a consistent methodology for compiling and presenting the financial statement information.

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

There were extreme variances on the financial statement line items between fiscal years. No one from within the Corps was able to provide an explanation for these variances. For example on the FY 95 Statement of Operations, the line item Revenues from Sales to the Public showed \$14.2 million. This line item in FY 94 reported \$258.6 million for a variance of about \$244.4 million. Further, in FY 93 the line reported \$13.1 million while in FY 92 it was \$387.6 million, a variance of \$374.5 million.

We traced most of the variance to the General Construction and Rivers and Harbors appropriations within the appropriation reimbursements. We provided this information to the Corps but it had no explanation for the dramatic revenue spikes occurring in these fiscal years. Apparently the Corps reported amounts between the two line items (Sales to the Public or Sales to the Government) on alternating fiscal years without any supporting documentation.

We recognized that the legacy financial system couldn't produce reliable information. However, without a methodology or consistent rationale to present the financial statements, the financial information it did produce was more questionable and of less value. Consistency is an underlying accounting principle established to ensure comparability. Even questionable information, if compiled and presented consistently, can provide limited meaningful information through the use of variance or other analyses.

### **Sufficient Disclosure**

The footnotes to the financial statements lacked sufficient disclosure.

Office of Management and Budget Bulletin 94-01 provides detailed guidance on the preparation and presentation of the financial statements, to include adequate footnote disclosures. In reviewing the Corps' disclosures, we found:

- Amounts reported within the footnotes didn't match the amounts reported in the financial statements. For example, Fund Balance With Treasury showed \$1.923 billion on the financial statement but only \$1.889 billion as the total on Note 2, or a difference of about \$34 million.
- Amounts reported within the footnotes weren't adequately labeled. For example, under Note 14 (Property, Plant, and Equipment), the category of Other showed about \$12 billion of assets. There was no description or explanation as to the composition of this amount.

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

- Narrative explanations didn't exist or weren't adequate to provide sufficient information regarding the disclosures. Of the total 13 Notes reported, 7 had no narrative explanations and the remarks on the remaining 6 didn't provide the information required by the bulletin. Further, the Corps didn't address the Note requirements for Other Disclosures and Contingencies.

We attributed these conditions to the inability of the legacy financial system to provide sufficient data, the limited visibility of the upward reporting system, and the Corps' decision not to employ significant resources to correct these deficiencies.

Full disclosure requires that sufficient information be presented both on the face of the financial statements and within the notes to the financial statements. These notes provide the detailed explanations and justifications to evaluate management actions and initiatives.

Our recommended actions to further correct these conditions are in Recommendation B-1.

### Upward Reporting

The existing upward reporting process provided limited benefits to the Corps. Its primary function was to supply the data necessary for the Finance Center to prepare Corps-wide consolidated financial statements. As such, the process didn't provide:

- The Finance Center with visibility of the supporting transactions within the account balances.
- The districts, divisions, or other reporting activities with the management information that would be derived from formal financial statements.

The process required reporting activities (districts, divisions, labs) to extract and forward amounts from the trial balances. It also required numerous standard forms and manual reports to reconcile and report information not readily visible within the account balances.

The reporting activities received no benefit from the existing process because they couldn't use the consolidated financial statements at their level. Management information that could be useful at the lower levels lost its visibility in the consolidation of the data.

An alternative approach that would meet the needs of all reporting levels would be to prepare formal financial statements at each reporting activity. The consolidated

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

---

financial statements could then be prepared by rolling up the division-level statements along with any other reporting activities outside the division structure.

Our recommended actions to improve the reporting process are in Recommendation B-2.

### **Corrective Actions for FY 96**

The Corps agreed with our assessment that additional effort would be required starting in FY 96 to ensure that the financial statements properly reported transactions and events consistently. The Corps took immediate corrective actions, to include:

- Increasing the number of personnel assigned to the preparation of the financial statements.
- Requesting assistance from our agency to formally document the rationale and audit trail used.

These actions couldn't correct the primary underlying condition (the inadequacy of the old financial system), and the resulting compilation required that:

- Personnel manually enter data into automated spreadsheets to calculate and summarize the financial statements.
- Budgetary accounts be used to derive revenues and expenses for activities operating under the old financial system.

However on the positive side, the efforts yielded some substantial benefits. The Corps was able to adequately:

- Compile a test set of financial statements (excluding the narrative footnote disclosures) solely from the information contained within the Corps of Engineers' Financial Management System (CEFMS).
- Document and produce an audit trail for the rationale and methodology used to ensure consistency in future periods.

### **Upcoming Requirements for FY 97 and Beyond**

The reporting requirements for preparing and presenting financial statements will change dramatically in FY 98. Prudent planning dictates that proper planning begin in FY 97 to meet these new requirements. New accounting standards and concepts developed by the Federal Accounting

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

---

Standards Advisory Board (FASAB) require implementation during FY 98. For example, the Advisory Board's Statement of Accounting Standards, Number 6, scheduled for implementation in September 1997 has new requirements to account for:

- Heritage and multi-use heritage assets.
- Stewardship land.
- Deferred maintenance.
- Cleanup costs associated with hazardous waste removal, containment, or disposal.

The standards segregate these new accounting requirements onto its new financial statement entitled the Statement of Net Cost. In addition, the Advisory Board, under its Standard Number 7, created these additional financial statements:

- Statement of custodial activity.
- Statement of changes in net position.
- Statement of budgetary resources.
- Statement of financing.

Implementation of these statement requirements begins after 30 September 1997 (FY 98).

Financial reporting for governmental entities continues to evolve as the standards and practices are defined. The Corps needs to take an active role within its resource management operations to ensure that upcoming requirements are anticipated and can be met.

Our recommended actions on these future requirements are included in Recommendation B-3.

### **RECOMMENDATIONS AND COMMAND COMMENTS**

This section contains specific recommendations and a summary of command comments for each recommendation. Verbatim command comments are in Annex C.

The Corps implemented actions to correct deficiencies on its financial statement compilation and presentation. We agreed with the actions taken; therefore, we aren't making any additional recommendations at this time on compilation and presentation for the FY 96 effort.

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

---

**B-1 Recommendation:** Continue to develop and implement formal accounting procedures to document and produce an audit trail for adjustments (to include eliminating entries), transactions, methodology, and rationale used during the compilation process.

**Command Comments:** The Corps agreed and said that its Finance Center will consolidate the data and maintain an audit trail for any adjustments required to produce the consolidated financial statements.

**B-2 Recommendation:** Implement the alternative reporting process of preparing formal financial statements at each reporting activity.

**Command Comments:** The Corps agreed and stated that one of its long range objectives is to have each activity produce the full set of required financial statements.

**B-3 Recommendation:** Develop policies and procedures to ensure that the new reporting requirements are adequately addressed in the financial management system.

**Command Comments:** The Corps agreed and stated that it will work closely with Army Audit Agency during the FY 97 financial statement audit to ensure that the new requirements are appropriately included in the financial management system.

Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

---

**FINDING C: FINANCIAL MANAGEMENT SYSTEMS**

For the Commander,  
U.S. Army Corps of Engineers

**SUMMARY**

---

Material uncertainties continued to exist regarding the reasonableness of reported amounts on the financial statements. This occurred because the Corps' legacy financial system (Corps of Engineers Management Information System (COEMIS)) has fundamental weaknesses that prevent the Corps from reporting reliable financial information. Specifically:

- The system lacks revenue and expense accounts.
- The system isn't based on the U.S. Government's Standard General Ledger, and the existing crosswalk isn't accurate.
- The system isn't integrated with other Corps' systems.
- Auditable transactions to support computed balances don't exist.

We've reported these inadequacies since FY 93 in our audit reports. The Corps is aware of these problems and is in the process of fielding a new financial management system--the Corps of Engineers Financial Management System (CEFMS).

On the positive side, our audit results showed that the new financial system appeared to be operating with a high degree of reliability. It resolved standard general ledger and integration deficiencies found in the legacy system and enhanced management controls.

Our detailed discussion on these conditions starts on page 37.

**BACKGROUND**

---

The Corps recognized that its current financial system had many inadequacies and had begun development of a replacement system called the Corps of Engineers Financial Management System. During FY 96, the Corps had the new system at its Headquarters, Huntsville Division, the Waterways Experiment

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

---

Station, the Construction Engineering Research Lab, and throughout the Southwestern and South Atlantic Divisions. The Corps plans to complete deployment to all districts, divisions, and activities in FY 98.

We have worked with the Corps since FY 95 to help ensure that the new financial management system produces timely and reliable financial information. To date, it appears that the new system will operate effectively; it is an integrated system that crosswalks to the U.S. Government's standard general ledgers.

### **DISCUSSION**

---

The Corps' financial statements contained several key line items that weren't produced from or supported by its general ledger system because the Corps' old system (COEMIS):

- Isn't based on the U.S. Government's standard general ledger, and the existing crosswalk isn't accurate.
- Isn't integrated with other Corps automated systems.
- Lacks revenue and expense accounts.

Our previous audit reports in FY 93 and FY 94 extensively documented the inadequacies of the Corps' legacy financial management system (COEMIS). Those conditions, summarized in the preceding paragraph, continued to exist throughout FY 96.

In contrast, FY 96 marked the first year that the new financial management system (CEFMS) was fully operational for an entire year at the district level and subjected to an audit. The results showed that the new system:

- Resolved the Standard General Ledger deficiencies.
- Resolved, or is scheduled to resolve, system integration deficiencies.
- Enhanced management controls.

In this section we discuss these three areas, comparing and contrasting the two financial systems.

#### **Standard General Ledger**

The old system (COEMIS) wasn't based on the U.S. Government's Standard General Ledger. It required a crosswalk

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

between its ledger accounts and the standard ledger accounts. The crosswalk wasn't accurate because the old system lacked key accounts, to include revenue and expense accounts.

To compensate for these deficiencies, the Corps compiled its financial statements using budgetary accounting information, external sources, and manual calculations. For example, the Corps used accrued expenditures to determine revenues from sales to the public, Treasury reports to derive appropriated capital used, and manual calculations to determine operating expenses.

Conversely, the Corps built the new system (CEFMS) using the approved Standard General Ledger. It contains both the budgetary and propriety accounts to properly record and report the transactions and events within the financial management system. During our audit, we performed account balance reconciliations and found the system to be operating effectively.

### **System Integration**

The Corps' legacy system also wasn't integrated with other automated systems to simultaneously update general and subsidiary ledger accounts. Integrated systems are required by Office of Management and Budget Circular A-127.

With integrated systems, only one keyed entry needs to be made. For instance, the new system (CEFMS) is integrated with the Real Estate Management Information System (REMIS). When a transaction involving real estate is entered into either system, both systems update automatically. A second entry doesn't need to be made.

Integrated systems are an important feature in any financial management system because they reduce errors and save valuable time. The Corps developed and continues to develop the Financial Management System (CEFMS) to ensure integration with other automated systems used by the Corps.

### **Management Controls**

The Corps' new financial management system also significantly improved the Corps' management controls over its financial data. Before financial statements can be relied upon, effective controls must be in place and operating to ensure that financial data can't be manipulated or altered before it is reported.

The Corps has several key management controls built into its new system. For example:

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

---

- An access control matrix provides selective permissions to users based on management approvals.
- The system requires signature cards and passwords to allow personnel access into the system and its electronic signature capabilities.
- The system performs the financial accounting in the background based on established correlation tables.

Management controls are integral to producing reliable financial statements. The Corps' new system incorporates many controls that weren't present in the old system. This in itself will help provide reasonable assurance that the Corps produces reliable financial statements.

### **RECOMMENDATIONS**

---

Due to the Corps' ongoing implementation of its Financial Management System (CEFMS) to correct the deficiencies we've reported since FY 93, we aren't making any recommendations at this time.

**REPORT ON MANAGEMENT CONTROLS**

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

### REPORT ON MANAGEMENT CONTROLS

We concluded that management controls weren't adequate to support the reliable preparation and presentation of the financial statements.

We discuss the material weaknesses related to accounting policies, financial reporting, and financial management systems in Findings A, B, and C within the Significant Matters section of this report. In the subsequent portion of this section in Findings D and E we discuss the remaining reportable conditions related to various aspects of the Corps' management controls.

We consider the problems related to reporting results of operations and accounting systems to be material weaknesses. The Corps correctly reported these material weaknesses as a previously identified but uncorrected weakness in its FY 96 Annual Assurance Statement for compliance with the Federal Managers' Financial Integrity Act.

In planning and performing our audit of the Statement of Operations and Changes in Net Position, we evaluated selected aspects of the Corps' internal control structure. We assessed whether the internal control structure met basic management control objectives and what audit procedures were necessary to express an opinion on the financial statement. Specifically, we evaluated management controls designed to ensure that:

- Transactions are properly recorded to maintain accountability for assets and to permit the preparation of reliable financial statements.
- Funds, property, and other assets are safeguarded against loss, unauthorized use, or misappropriation.
- Accounting policies and procedures are established to provide adequate guidance and standards for recording transactions in accordance with Federal Accounting Standards and Generally Accepted Accounting Principles.
- Transactions are in accordance with applicable laws and regulations.

In our review, we obtained an understanding of the significant internal control structure policies and procedures. We assessed the level of control risk relevant to significant cycles, classes of transactions, and account balances. We tested key controls to determine whether the controls were effective and working as designed (see the Objectives, Scope, and Methodology section of this report for the cycles and processes identified).

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

We reviewed the Corps' management controls over selected aspects of the budgetary cycle for both the Revolving Fund and civil works operations. These controls which help ensure that the fund remains solvent and sufficient appropriations are available for project construction, and for operations and maintenance, included:

- Use of realistic operating budgets to set overhead distribution rates within the Revolving Fund.
- Use of resource allocation plans to ensure that project appropriations and requirements are adequately identified within the budget process.
- Periodic review and assessment of planned and actual budgetary results based on approved budgets.

We found that the four Corps districts included in our review implemented sufficient management controls to ensure that the budget cycles of both the Revolving Fund and the civil works operations operated effectively at the time of our audit.

We also reviewed selected management controls related to the Corps' employee payroll cycle. Controls within the payroll cycle are important because payroll represents a significant portion of the Corps' operating expenses and the payroll processing transitioned to the Defense Finance and Accounting Service in FY 96.

At the four districts we visited, we found that adequate controls were in place and operating. Specifically:

- There was a proper segregation of duties between the timekeepers and the customer service representatives.
- All timesheets required supervisory review and approval.
- Each employee certified the hours worked and the leave taken, if any, on the timesheets.

However, we identified several problems involving the management control structure and its operation. We consider these problems to be reportable conditions as defined by the standards established by the American Institute of Certified Public Accountants and Office of Management and Budget Bulletin 94-01, Audit Requirements for Federal Financial Statements.

Reportable conditions involve significant deficiencies in the design or operation of the entity's management control structure. A reportable condition sometimes results in a material weakness (a condition for which management controls

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

---

don't reduce, to a relatively low level, the risk that errors or irregularities may occur and may not be detected within a timely period).

Findings A through E of this report discuss in detail the material weaknesses and reportable conditions found within the revenues/receipts and the expenses/disbursements cycles.

**FINDING D: MANAGEMENT CONTROLS**

**For the Commander,  
U.S. Army Corps of Engineers**

**SUMMARY**

The Corps needed to strengthen its management controls in several areas. We found in the following areas that controls were in place, but not operating or not operating effectively:

- Capitalization versus expense of assets.
- Asset retirements.
- Insurance premium collections.
- Accounts receivables.
- Yearend cutoff.
- Sponsor's contributions on reimbursable projects.

These controls weren't working because personnel didn't comply with existing policies and procedures. For example:

- District-level managers misinterpreted some of the headquarter's accounting guidance and policies.
- Some finance and accounting personnel didn't know how to correctly account for the transactions.

In addition, the legacy financial system hampered the Corps' control efforts by requiring labor-intensive procedures. As in the past, the Corps correctly reported the system deficiencies of its legacy financial system as a material weakness in its FY 96 Annual Assurance Statement. We agreed with the Corps in its assessment. We believe the remaining issues to be reportable conditions but not material weaknesses.

As a result, the financial reporting of the results of operations wasn't accurately portrayed on the financial statements. More importantly, the Corps needs to strengthen its verification and compliance mechanisms to help ensure effective operations. Current mechanisms didn't identify problems.

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

---

Our detailed discussion on these conditions starts on page 48. Our recommendations start on page 54.

### **BACKGROUND**

---

For financial reporting purposes, the Corps' management control objectives are to ensure that:

- Transactions properly record and maintain accountability for assets and permit the preparation of accurate and reliable financial statements.
- Funds, property, and other assets are safe from loss, unauthorized use, or misappropriation.
- Transactions are in accordance with applicable laws and regulations.

Numerous factors, both individually and collectively, comprise the overall control environment. For example:

- Management's perceptions and integrity concerning the importance of controls will reflect in the entity's overall attitude.
- Policies designed to establish some measure of control must be strictly enforced.
- Procedures implemented should adhere to fundamental control techniques such as segregating key duties, providing for tests and reconciliations, and limiting access.

A comprehensive management control structure consisting of checks and balances ensures that the control objectives will be met. In order to be efficient, it must be cost-effective.

### **DISCUSSION**

---

During our audit we found several controls that were in place but not operating or not operating effectively. In this section we discuss the management controls that needed improvement:

- Capitalization versus expense of assets.
- Asset retirements.

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

---

- Insurance premium collections.
- Accounts receivables.
- Yearend cutoff.
- Sponsors' contributions on reimbursable projects.

**Capitalization Versus Expense of Assets**

The headquarters distributed guidance for asset acquisitions requiring capitalization in a memorandum dated 29 January 1996. It established policy and contained detailed criteria. For example:

- A recognition threshold was established at \$25,000. Items above that amount with a useful life of 2 or more years were assets to be recorded (capitalized) on the accounting records and depreciated accordingly.
- All real property (land and buildings), regardless of value, was to be capitalized.
- Group purchases, where individual items exceeded a purchase price of \$300 and the total acquisition exceeded the threshold, were also to be capitalized.

Although the policy was in place, it wasn't operating effectively. Districts purchased assets exceeding the \$25,000 threshold and charged the costs to current period operating expenses. For example:

- The Huntington District charged two computer equipment purchases, costing about \$420,000, and 46 purchases of integrated furniture systems, costing about \$875,000, to current year expenses rather than to the appropriate asset accounts.
- The Vicksburg District expensed a \$131,000 telecommunication system and a \$117,000 computer-design and drafting system.
- The Alaska District expensed about \$130,000 of group purchases related to office furniture and automation equipment.

Districts didn't comply with the new guidance because they believed that the guidance was ambiguous and conflicted with previous guidance received. As a result, the districts' actions overstated current year expenses and understated reported assets and net income.

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

The headquarters, or an office serving as its representative, needs to perform analytical reviews on the expense accounts to identify, research, and correct these type of transactions.

Our recommended actions to correct this condition are in Recommendation D-1.

### Asset Retirements

Districts didn't follow existing policies and procedures for retiring assets from service. The retirement process:

- Moves inactive assets to a holding account called Retirement-In-Progress.
- Cancels the charging of plant increment, insurance, and depreciation on assets within the retirement account.
- Accounts for any additional costs until the asset disposal is complete, then accounts for any gain or loss.

The controls were in place, but not operating or not operating effectively. For example:

- At the Vicksburg District, assets that were no longer owned (disposed of through sales or otherwise) were still within the accounts-generating plant increment, insurance, and depreciation expenses because the district discontinued the use of Engineer Form 3013. The routing of this form through the process ensures that the appropriate personnel receive notification of the asset disposal.
- At the Alaska District, inactive assets were also still within the accounts generating plant increment, insurance, and depreciation expenses because of a turnover within its accounting personnel. The new employees didn't know how to properly record the transactions.

As a result, the operating expenses were overstated, net income understated, and gains and losses incorrectly deferred and reported in the wrong accounting periods.

The Corps needs to implement verification and compliance mechanisms to "close the loop." For example:

- Analytical reviews of the accounting records would identify abnormal balances or conditions that warrant further study.

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

- Periodic site inspections would reveal control breakdowns with documentation, processes, or training.

Our recommended actions to strengthen and improve the controls over asset retirements are in Recommendation D-2.

### Insurance Premium Collections

The Corps operates as a self-insured entity by maintaining an insurance reserve account to absorb losses and damages to Revolving Fund capitalized property and warehouse stock. Customers pay insurance premiums for using the insured asset to the Corps' activity that owns the asset. This reserve enables the Corps to insure against losses and damages without assessing the full cost of an insurance loss to the current customers at the time of the loss.

The premium collections are kept in the insurance reserve account. When a division or district suffers a loss of property or equipment, these losses are charged against the insurance reserve account. The reserve account absorbs the impact of the loss.

Corps management allowed a significant balance to accumulate in the insurance reserve account. This occurred primarily because:

- Corps management didn't use historical data to determine the balance needed in the insurance reserve account.
- Corps management didn't adjust the annual premiums to reflect actual losses.

The Corps continued to collect annual insurance premiums despite the fact that annual insurance losses didn't support maintaining the large insurance reserve balance.

We reviewed the activity in the insurance reserve account for the last 4 years (FY 93, FY 94, FY 95, and FY 96). Our review revealed that the Corps collected between \$2.1 million and \$3.4 million a year in insurance premiums and had an insurance reserve balance of \$46.1 million as of 30 September 1996.

For the period between FY 93 through FY 95, insurance losses exceeded premium collections by an average of \$1.94 million. At this rate, it would take approximately 23 years to deplete the insurance reserve fund.

However, these losses weren't representative of normal operating losses. The balance of \$46.1 million within the insurance reserve account as of 30 September 1996

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

accumulated through the systematic application of a set or standard rate. The history of the insurance reserve account indicated that the Corps routinely collected more in insurance premiums than it paid in insurance losses. For example, in FY 96 the Corps collected about \$3.1 million in insurance premiums and had only about \$0.8 million in actual insurance losses.

The large balance in the reserve account aggregated at the expense of the Corps' customers. By analyzing historical loss rates and adjusting its premiums, the Corps can reduce its costs and pass these savings on to its customers.

Our recommended actions to reduce the balance in the insurance reserve account to a level representative of historical losses and to produce procedures to maintain that balance are in Recommendation D-3.

### Accounts Receivables

Districts didn't follow existing policies and procedures for pursuing the collection of delinquent accounts receivable. These policies required accounting personnel to do the following:

- Reconcile accounts receivable on a monthly basis.
- Send demand letters to customers for delinquent receivables each 30 days of delinquency for receivables greater than \$100. Demand letters can stop after 90 days.
- Obtain approval from district counsel to write off the receivables less than \$5,000 as uncollectible.

Although these policies and procedures were in place, they were not operating effectively. For example:

- At the Fort Worth District, about \$2.86 million (53 percent) of the Revolving Fund's \$5.4 million and about \$770,000 (21 percent) of the Civil Fund's \$3.7 million of accounts receivable were more than 180 days old.
- At the Alaska District, about \$184,000 of Revolving Fund receivables and about \$147,000 of Civil Fund receivables were more than 180 days old.

Delinquent accounts receivable balances also included invalid receivables that were already paid.

Districts didn't consider these receivables to be uncollectible because they were due from other Corps

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

districts or other government agencies. Therefore, districts didn't establish an allowance for doubtful accounts or aggressively pursue collections.

As a result, users of the Corps' financial statements have little assurance that the amounts reported for accounts receivable are accurate.

Our recommended actions to reduce the level of delinquent accounts receivable and improve the certainty of accounts receivable balances are in Recommendation D-4.

### Yearend Cutoff

Districts didn't always record expenses in the proper accounting period. For example:

- The Alaska District incorrectly recorded \$20,437 of \$28,853 in sampled disbursements as FY 96 expenses when they were really FY 95 expenses.
- The Vicksburg District incorrectly recorded \$34,000 of \$535,000 of sampled disbursements as FY 96 expenses when they were really FY 95 expenses.

We noted that these transactions were within the Corps' Revolving Fund, a no-year fund. As such, no Anti-Deficiency Act violations occurred.

According to accounting personnel at the districts, these expenses were not recorded as FY 95 expenses because:

- Activities didn't receive vendor's invoices in time.
- Activities were late in submitting the documentation.
- Accounting personnel primarily focused on accruing higher dollar expenses.

As a result, districts overstated FY 96 expenses and understated FY 95 expenses. Generally Accepted Accounting Principles require matching of expenses and revenues in the period incurred.

Our recommended actions to record expenses in the proper period are in Recommendation D-5.

### Sponsors' Contributions on Reimbursable Projects

The Corps didn't effectively manage sponsors' contributions for reimbursable projects.

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

---

Our review of reimbursable and contributed funded projects at the Huntington District revealed that the financial management of the non-Federal funds was different. Although there were guidelines for the management of the contributed funds, such as establishing an escrow account, we found inadequate guidelines for financial management of reimbursable funds.

As an example, the Corps encourages the use of an interest-bearing escrow account whenever cost-shared projects are constructed over a period of years. This allows the sponsors to earn interest on their funds when obligations are delayed. No such guidance exists for reimbursable projects.

As a result, during the period from FY 93 to FY 96, the Huntington District held between \$1.956 and \$2.482 million of sponsor's unobligated funds without placing them in an interest-bearing escrow account for the benefit of the sponsor.

The proper management of non-government funds is a good business practice and also enhances customer relations. We believe that this is a good opportunity for Corps' headquarters to explore the possibility of enhancing the financial management of reimbursable funds. This could include establishing guidelines for escrow accounts, reimbursing the customers for unobligated funds, or adjusting yearly amounts needed in order for the customers to maximize their funds.

Our recommended actions to establish guidelines or regulations to enhance business practices for the financial management of reimbursable funds are in Recommendation D-6.

### **RECOMMENDATIONS AND COMMAND COMMENTS**

This section contains specific recommendations and a summary of command comments for each recommendation. Verbatim command comments are in Annex C.

**D-1 Recommendation:** Ensure compliance with asset capitalization policy by implementing compliance mechanisms. At a minimum, direct that local Internal Review offices:

- Perform periodic analytical reviews on the expense accounts based on the established criteria for asset capitalization.

Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

- Identify and research those expenses that meet the asset capitalization criteria.
- Correct the accounting records as necessary.
- Hold individuals accountable for their actions.

**Command Comments:** The Corps partially concurred stating that it planned to reemphasize the capitalization policy in FY 97 and include compliance with the policy as part of its FY 97 audit program. In addition, all districts would be directed to do a 100 percent compliance review.

**Agency Evaluation of Command Comments:** The Corps didn't provide sufficient information concerning its partial concurrence. The proposed actions are in compliance with the recommendation. We didn't see any reason for only a partial concurrence.

- D-2 **Recommendation:** Strengthen controls over the asset retirement process using the organizational structure to ensure compliance. Direct that echelons above perform periodic analytical reviews and site visits.

**Command Comments:** The Corps agreed with the recommendation and stated that it would change its management control checklist to include a test question on asset retirement to enforce compliance. The checklist will be updated by 31 March 1997.

- D-3 **Recommendation:** Use historical insurance loss data to determine the correct level for the insurance reserve account. Reduce rates to allow the insurance reserve balance to decrease to this level. Adjust insurance premiums to reflect actual losses so that a consistent level can be maintained.

**Command Comments:** The Corps agreed stating that it had already initiated an action plan recommending the discontinuing of insurance premium charges until the reserve balance lowers to \$25 million.

- D-4 **Recommendation:** Ensure that districts perform monthly reconciliations of accounts receivable and aggressively pursue delinquent accounts receivable as prescribed in Engineer Regulation 37-2-10. This should specifically

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

---

include a revalidation of each account over 180 days old.

**Command Comments:** The Corps agreed and said it will reissue command guidance by 31 March 1997.

D-5 **Recommendation:** Develop yearend closeout procedures that will ensure all expenses are recorded in the proper accounting period.

**Command Comments:** The Corps agreed and stated that its Finance Center will continue to refine the published yearend closeout procedures.

D-6 **Recommendation:** Establish guidelines or regulations to enhance business practices for the financial management of reimbursable funds. Such guidelines could include:

- Establishing interest bearing escrow accounts for long-term reimbursable projects, as done on contributed-funded projects.
- Refunding excess amounts to the customer if project features are delayed.
- Reviewing and adjusting, if necessary, estimated schedule of sponsors' costs for reimbursable projects for future fiscal years.
- Reviewing agreements and determining whether the sponsors' funds are properly managed by the district.

**Command Comments:** The Corps agreed with the recommendations and plans to incorporate the guidance in its change 89 to Engineer Regulation 37-2-10, which is scheduled for completion by 30 September 1997.

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of  
Engineers, Civil Works"**

---

**FINDING E: FOLLOWUP CYCLE**

**For the Commander,  
U.S. Army Corps of Engineers**

The Corps continued to make progress in correcting two of the material weaknesses found in previous financial statement audits. Specifically, the Corps gave particular attention to management and control in the areas of:

- Real property.
- Labor cost transfers.

For FY 96, the Corps reported Real Property as a corrected material weakness in its Annual Assurance Statement. Our audit results agreed with this assessment. Further, we noted that the Corps made significant improvements in reducing and justifying Labor Cost Transfers. While our review covered only four districts, and the results can't be projected to the entire Corps, these four sites appeared to have adequate controls over the transfers.

However, the Corps needed to strengthen management controls for fund balance reconciliation. For example, the Corps should:

- Implement transactions that will capture revenues and expenses as they are incurred, not just at yearend.
- Research and resolve discrepancies between the Balance Fund With Treasury and the Corps' records.

Our detailed discussion on these conditions starts on page 58. Our recommendation starts on page 60.

**BACKGROUND**

**Real Property**

During our audit of the FY 93 and FY 95 Corps' financial statements, we identified that real property wasn't properly recorded. We found that the Corps didn't use subsidiary ledgers or other records to support the value of real property assets reported. This was because procedures weren't in place to ensure that acquisitions, disposals, and improvements were recorded in both accounting and real property records. In addition, some real property records

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

---

were incomplete and in some cases records did not exist for Civil Works real property.

In order to correct these problems the Corps established a workgroup to monitor progress and address problems in completing inventories and reconciliations. Also, it issued guidance for capitalizing real property assets, reconciling general and subsidiary ledgers, and issuing suspense dates for completion of all inventories and reconciliations. By the end of FY 95 the Corps' actions had corrected these conditions. We included this issue in our FY 96 effort to ensure that these conditions remained corrected.

### **Labor Cost Transfers**

Our audits on labor cost transfers during FY 93 and FY 95 showed that Corps personnel continued to change deficit balances by transferring costs to other projects or overhead accounts. In addition, many transfers were made without supporting justification.

We recommended that the Corps strengthen internal controls to ensure that all labor cost transfers were valid and properly authorized because improper transfers can mischarge customers, possibly violate Anti-Deficiency Act, and damage the integrity of the Corps' cost accounting system. The Corps implemented stricter measures to justify transfers and to hold personnel accountable.

### **Fund Balance Reconciliations**

The issue of Fund Balance with Treasury surfaced during our FY 93 audit. We found that the accounts in the Corps of Engineers Management Information System didn't match the Treasury's reported balance. Rather than tracking down the causes and discrepancies, the Corps used the amounts reported by the Treasury on the financial statements. The Treasury requires the Corps to submit a detailed list of all transactions affecting these accounts and to compare this list with actual disbursements and receipts, in other words, perform a reconciliation. The Anti-Deficiency Act, USC 1517, applies when obligations exceed appropriations. It also applies to the Revolving Fund when disbursements exceed cash (Funds with Treasury).

### **DISCUSSION**

---

In this section we discuss:

- Real property.
- Labor cost transfers.
- Fund balance reconciliations.

### Real Property

For the most part, the districts that we audited had adequate controls in place to provide assurance that real property was properly recorded. These controls require the districts to inventory their real property at least once every 3 years and to reconcile the results with the financial management records. Alaska District had real property records that weren't in agreement with the general accounting ledger. However, during the audit the Real Estate Division of the Alaska District took appropriate action to make the adjustments to its real property records.

The audited districts followed the established procedures to conduct a physical inventory of all of their real property once every 3 years. Except for Fort Worth, the audited districts had clear and concise records of each project's real property, including reconciled costs and the year the project's real property was put into service. Fort Worth district personnel didn't clearly document the results of their real property inventories; however, based on the records we reviewed, it was evident that they conducted detailed inventories. Using their documentation, it was difficult to determine exactly when and what the final results were. Since this was an isolated incident, and not systemic to the Corps, the recommendations to correct this issue of real property are in the district's site report.

### Labor Cost Transfers

The audited districts appeared to have adequate controls over labor cost transfers; however, during our review, we found that some districts still had minor problems. For example:

- One district had conflicting guidance regarding who could process labor cost transfers.
- At another, controls weren't always working effectively to prevent or minimize errors occurring in proper labor cost transfer requests.

Our review wasn't sufficient to conclude that the Corps as a whole was following procedures, but results were acceptable at the four districts that we audited. Continued management emphasis will ensure that all labor cost transfers are in

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

---

accordance with Corps policy. Since the minor problems were isolated incidents and not systemic to the Corps, the recommendation to correct these incidents are in the districts' site reports.

### Fund Balance Reconciliation

The Corps needs to improve its fund balance reconciliation procedures. While reconciliations appeared adequate for the Revolving Fund, within the Civil Works appropriations, we found that large absolute differences continued to exist. This occurred because reconciliations weren't performed until yearend for FY 96 and no research was done.

#### Revolving Fund

The Fund Balance with Treasury reconciliation for Revolving Funds appeared to be adequate. There were differences between the Treasury report and the Corps' Finance Center's report, but these were largely due to timing problems. The Revolving Funds eventually reconciled to a zero balance after each fiscal quarter. Reasonable justifications were given to support these timing errors. Fort Worth's Resource Management personnel blamed some of the errors on their learning curve with the new financial management system.

#### Civil Works

The Fund Balance with Treasury reconciliation for Civil Works Appropriations, totaling \$1.6 billion, wasn't adequate. The overall picture showed that the Corps ended FY 96 with a net out-of-balance amount of \$10.8 million. However, the absolute values range from a positive \$21.5 million to a negative \$10.2 million. The reconciliation showed that 5 of the 19 appropriations had negative balances, totaling about \$11 million.

Our recommended actions to correct the Fund Balance with Treasury are in Recommendation E-1.

### RECOMMENDATION AND COMMAND COMMENTS

This section contains a specific recommendation and a summary of command comments for the recommendation. Verbatim command comments are in Annex C.

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of  
Engineers, Civil Works"**

---

**E-1 Recommendation:** Strengthen management controls over fund balance with Treasury by:

- Implementing transactions that will capture revenue and expenses as they are incurred, not just at yearend.
- Establish analytical reconciliation procedures over the financial data produced by the financial management system to validate the integrity of the crosswalk.
- Develop procedures at the district level to research and resolve discrepancies between the district's fund with Treasury Balance and the district's records.
- Consider writing off absolute unreconcilable differences in order to balance the accounts.

**Command Comments:** The Corps agreed and said that it planned to revise the general ledger correlation tables within its financial management system to capture revenues when earned by 30 September 1998. This coincides with the full deployment of the new system. The Corps would also develop additional reconciliation edits into its upward reporting system by 1 March 1997, advise districts to establish local procedures for resolving reconciliation discrepancies, and take appropriate action to write off unreconciling balances that remain after the new system is fully deployed.

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

---

**REPORT ON COMPLIANCE WITH LAWS AND REGULATIONS**

**REPORT ON COMPLIANCE WITH LAWS AND REGULATIONS**

We tested the Corps' compliance with the provisions of the laws and regulations listed in the Objectives, Scope, and Methodology section of this report. The audit identified instances of material noncompliance with selected laws and regulations. An instance of material noncompliance is reportable if it could result in a material misstatement to the financial statements, or if the sensitivity of the matter would cause others to perceive it as significant.

Most of the noncompliance problems we found were directly or indirectly tied to the management control weaknesses we identified. As such, those instances of noncompliance are discussed as part of each functional area in the Significant Matters and the Report on Management Controls sections of this report.

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

---

**OVERVIEW INFORMATION**

**OVERVIEW INFORMATION**

The Corps' overview information is incorporated into the Army's financial statement overview. We reviewed the Missions, Operations and Performance Measures--Civil Works Program (Annex A). We didn't find any inconsistencies between the missions and operations sections and the information presented in the financial statements. We did, however, find some weaknesses in the adequacy of the performance measures identified.

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

---

### **FINDING F: PERFORMANCE MEASURES**

**For the Commander,  
U.S. Army Corps of Engineers**

#### **SUMMARY**

---

For FY 96, the presentation of the Overview Information in the Corps' financial statements didn't reflect the Corps' progress in developing and reporting performance measures to portray its mission, resources, goals, and results. The degree of progress wasn't reflected because:

- The Corps was still in the process of preparing its Strategic Plan.
- Preliminary performance measures developed and initiated in FY 94 weren't implemented.

As a result, these conditions forced the Corps to use the same performance measures in FY 96 that it used in the previous fiscal years. However, to its credit, the Corps was in the final draft stages of its strategic plan and had performance measures to support the plan. According to Corps personnel, the first set of outcome-focused performance measures were part of the FY 98 budget preparation discussions sent to the Office of Management and Budget. These actions were still ongoing at the end of our audit.

Our detailed discussion on these conditions starts on page 73. Our recommendation is on page 75.

#### **BACKGROUND**

---

Since 1990, the Federal Government has placed increased emphasis on measuring the performance of its agencies. Two important acts passed show that emphasis.

##### **Chief Financial Officers Act**

In 1990, Congress passed the Chief Financial Officers Act. It requires annual financial statements be prepared for selected government agencies. One of the purposes of the act was to provide for complete, reliable, timely, and consistent financial information to decision makers. In

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

implementing the guidance, the Office of Management and Budget required audited activities to include performance measures as a part of the overview to the financial statements. In essence, the guidance stated that useful performance measures are a key element in ensuring the usefulness of the financial statements.

### **Government Performance and Results Act**

In 1993, Congress passed the Government Performance and Results Act with an intent to hold management responsible for policy making and spending decisions. The Results Act emphasized the importance of measuring performance against established strategic plans and objective performance goals. It requires agencies to:

- Develop strategic plans before FY 98.
- Prepare annual plans setting performance goals beginning in FY 99.
- Start annual reporting of actual performance compared with performance goals by the year 2000.

Under the Results Act, the Office of Management and Budget established pilot programs to test and demonstrate (i) annual performance plans and reports, and (ii) managerial accountability. The Corps of Engineers' Civil Works Operation and Maintenance Program became one of the pilot projects.

### **Previous Audit Results**

In our FY 93 audit, we reported that the Corps hadn't developed performance measures that effectively portrayed its civil works mission, resources, goals, and results. The performance measures we reviewed didn't have the three integrated components of good performance measures--inputs, outputs, and outcomes.

In our FY 94 audit, we reported that although the Corps made some progress in developing better performance measures, that progress wasn't reflected in the overview to the financial statements. We stressed that the Corps must develop a strategic plan that should contain:

- A comprehensive mission statement covering the major functions and operations of the agency.
- General goals and objectives, including outcome-related goals and objectives, for the major functions and operations.

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

---

- A description of how the goals and objectives are to be achieved, including a description of the operational processes and resources required to meet those goals and objectives.

### **DISCUSSION**

---

In this section we discuss:

- Current status.
- Previous efforts.
- Planned and ongoing actions.

#### **Current Status**

For FY 96, the Corps' financial statements showed little, if any, progress in presenting and reporting performance measures.

In its Overview to the FY 96 Financial Statements, the Corps intended to report the same or similar performance measures that were in its previous financial statement presentations. As shown during our previous audits, these measures aren't outcome-related. They measure activities or processes, not program outcomes.

In reporting and presenting performance measures at the financial statement level, it would appear that the Corps had made no substantive progress within the last 3 years. However, this wasn't the case. The Corps continued to demonstrate a commitment to meeting or exceeding established implementation dates. At the close of our audit, the Corps was finalizing a draft strategic plan and determining the performance measures to implement to meet the goals and objectives of that plan.

#### **Previous Efforts**

The Corps' preliminary efforts didn't materialize into useable and meaningful performance measures for the Corps. In FY 94, the Corps identified 84 potential candidate measures to use in assessing performance. These measures weren't implemented because:

- Many of the measures were found to be activity and process oriented when subjected to critical review.

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

- The performance information couldn't be easily or readily extracted from the Corps' legacy financial system.

In FY 95, the Corps built upon this initial effort and used the lessons learned to embark on its current phased approach. Under Phase I of this concept, the Corps:

- Established a four-tier system to ensure that the needs of all organizational levels (executive leadership, national program level, district, project level) are addressed.
- Developed a mission statement for the Civil Works Program linked to the nine results-oriented programs identified: Navigation, Hydropower, Regulatory, Environment, Flood and Coastal Damage Reduction, Recreation, Emergency Management, Water Supply, and Support for Others.
- Identified five key performance areas to reflect the multidimensional nature of performance measurement, products, and customers.

This approach focuses on program outcomes rather than the organizational hierarchy along which the Corps is aligned. Further, the performance measures under development intend to provide a linkage within the budgetary process. The new measures should tie projected budgetary performance for the budget years with the performance achieved during the prior years. However, Corps personnel acknowledged that within this link there is an inherent problem. A significant time delay exists in the budget development process. For example in December 1996, the Corps will be compiling performance information for FY 96 while at the same time making final adjustments to the FY 98 President's budget submission. The actual performance data available to influence the budgetary program performance goals will lag by at least 2 fiscal years.

Another positive aspect of the tier approach is that it embodies the principles of Total Quality Management by empowering the different user levels to participate in the performance measure development. We believe that the Corps could further enforce these principles by including performance measure development activities as a critical element or priority work item within the formal personnel standards and appraisal system.

Our recommended actions to improve the development process is at Recommendation F-1.

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

---

### Planned and Ongoing Actions

The Corps' planned and ongoing actions demonstrated its commitment to developing an effective program within or before established implementation dates. For example:

- The current milestone schedule showed the Corps anticipated finalizing its strategic plan and preparing its initial FY 99 annual performance plan early in 1997, well ahead of the FY 98 and FY 99 requirement dates.
- The Corps intended to staff its strategic plan with several outside agencies for their views and suggestions.

### RECOMMENDATION AND COMMAND COMMENTS

This section contains a specific recommendation and a summary of command comments for the recommendation. Verbatim command comments are in Annex C.

**F-1 Recommendation:** Reinforce the commitment of personnel assigned to support the performance measure initiatives by including these efforts as a critical element or priority work item in the personnel performance standards and appraisal system.

**Command Comments:** The Corps partially concurred and said that while it agreed with increasing the commitment of personnel involved, initiating the action was premature at this time due to the sequential nature of its current plan.

**Agency Evaluation of Command Comments:** Whether an increased commitment would be premature is debatable. The intent of the recommendation was to strengthen and foster personnel efforts into a concerted action during the planning and development stages to ensure a successful outcome. We didn't articulate a predefined timeframe for initiating this recommendation. However, given the existing milestones and the amount of coordination and consensus that must be accomplished, the Corps should consider implementing actions simultaneously rather than sequentially.

**OBJECTIVES, SCOPE, AND METHODOLOGY**

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

### OBJECTIVES, SCOPE, AND METHODOLOGY

The Corps' management is responsible for:

- Preparing the annual financial statements in conformity with applicable accounting principles.
- Establishing and maintaining management controls and systems to provide reasonable assurance that the control objectives of the Federal Managers' Financial Integrity Act are met.
- Complying with applicable laws and regulations.

Our responsibility was to perform tests to obtain reasonable assurance about whether the Statement of Operations and Changes in Net Position was reliable and whether relevant management controls were in place and operating effectively. We were also responsible for testing compliance with provisions of selected laws and regulations and for performing limited procedures with respect to certain other information appearing in the financial statement.

We tested compliance with selected provisions of the following laws and regulations:

- Chief Financial Officers Act of 1990 (Public Law 101-576) and Office of Management and Budget implementing regulations (OMB Bulletins 93-02 and 93-06).
- Federal Managers' Financial Integrity Act of 1982 (31 U.S.C. sections 3512 (b) and (c)).
- Prompt Payment Act (31 U.S.C. sections 3901 through 3906) and Office of Management and Budget implementing regulations (OMB Circular A-125).
- Anti-Deficiency Act (31 U.S.C. sections 1341, 1342, and 1511 through 1519).
- Office of Management and Budget financial management system implementing regulation (OMB Circular A-127).
- Office of Management and Budget Bulletin Number 94-01, Form and Content of Agency Financial Statements.
- DOD Internal Audit Policy Memorandum Number 93-03, Management and Legal Representation Letters for Audits of Financial Statements.
- Department of Defense appropriation acts.

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of  
Engineers, Civil Works"**

---

- Department of Army appropriation acts.
- U.S. Army Corps of Engineers appropriation acts.

We also considered compliance with the process required by the Federal Managers' Financial Integrity Act for evaluating and reporting on management controls and accounting systems. We didn't evaluate all management controls relevant to operating objectives as broadly defined by the act and implementing guidance, such as those controls related to preparing statistical reports and ensuring efficient operations. Instead, we limited our work to accounting and other controls necessary to achieve the objectives outlined in our opinion on management controls.

Losses, noncompliance, or misstatements may occur and not be detected because of the inherent limitations in any system of management controls. We caution that projecting our evaluation to future periods is subject to the risk that controls may become inadequate due to changes in conditions or the degree of compliance with controls may deteriorate.

Except for the limitations described, we performed our work in accordance with:

- Generally accepted auditing standards.
- Government auditing standards issued by the Comptroller General of the United States.
- Office of Management and Budget Bulletin 93-06, Audit Requirements for Federal Financial Statements.

In carrying out our responsibilities, we:

- Examined, on a test basis, evidence supporting the amounts and disclosures in the Statement of Operations and Changes in Net Position.
- Assessed the accounting standards and policies used.
- Evaluated the overall presentation of the Statement of Operations and Changes in Net Position.

We also evaluated and tested relevant management controls for the following processes:

- Payroll.
- Receipts and disbursements.
- Revenues and expenses.
- Nonoperating income and losses.

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

---

- Accounting systems.
- Programming and budgeting.
- Cost management.
- Real property accountability.
- Performance measures.
- Financial reporting.

**ANNEXES**

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

---

**ANNEX A**

**CORPS OF ENGINEERS FY 96 FINANCIAL STATEMENTS**

***U.S. ARMY CORPS OF ENGINEERS  
CIVIL WORKS***

*Table of Contents*

Overview .....	1
Principal Statements .....	15
Footnotes to the Principal Statements .....	

*End 2*

ANNEX A

***U. S. ARMY CORPS OF  
ENGINEERS***

***CIVIL WORKS***

***OVERVIEW***

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

ANNEX A

### U. S. ARMY CORPS OF ENGINEERS MISSION AND PROGRAM PERFORMANCE

#### CIVIL WORKS MISSION STATEMENT

The mission of the Civil Works Program of the Army Corps of Engineers is to promote prosperity and democracy and to strengthen national security through the development, management, protection, and enhancement of the Nation's water and related land resources for flood damage reduction, commercial navigation, environmental restoration, and allied purposes. This program is accomplished by applying the Corps planning, engineering, scientific, and management skills, in cooperation with non-Federal sponsors, Federal, state, and local agencies, and other interested stakeholders, to achieve productive, efficient, responsible solutions to water resources problems. The program provides for responsible stewardship of its water resources infrastructure including the associated natural resources and provides emergency services to the Nation for disaster relief. The Civil Works Program also provides planning, engineering, environmental, recreation, research and real estate services to other Federal agencies and non-Federal customers, provides support to the Army in both peacetime pursuits and during national emergencies, and stands ready to adapt to evolving national needs and priorities. The Corps, moreover, plays a major role in the protection of waters of the United States, including wetlands, by regulating the discharge of dredge and fill material into the Nation's waters.

#### STRATEGIC GOALS AND OBJECTIVES

To accomplish the Civil Works Program, the following five strategic goals and supporting objectives have been proposed:

- > **Serve the Nation with high quality engineering, scientific, planning and technical expertise.**
  - Provide efficient, cost effective, innovative, and environmentally sustainable solutions to water resource infrastructure problems
  - Maintain and enhance the technical expertise of the Corps
  - Increase support to other Federal agencies through the Support for Others Program.
  - Provide engineering, environmental, real estate, and other technical services to the Department of Defense and the Nation.
  - Provide rapid and effective emergency response and recovery for disasters

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

### ANNEX A

#### > Lead in the development, management, protection, and restoration of the nation's water resources.

- Advance the development of productive, environmentally sustainable solutions to water resources problems.
- Expand the Corps' role in the restoration and protection of the environment.
- Promote stewardship of Corps projects, lands, and waters.
- Protect the Nation's waters by maintaining a fair, flexible, and effective regulatory program.

#### > Improve the performance of the U. S. Army Corp of Engineers Civil Works Programs.

- Develop and implement meaningful approaches to measure and improve performance.
- Completely rethink and validate our current approaches to project formulation to ensure that we move projects from conception to implementation in a more expeditious, cost effective manner.
- Ensure the Corps is organized properly for current missions.
- Improve partnerships with stakeholders.

#### > Create a 'we team' in the U. S. Army Corps of Engineers and take care of the team.

- Recognize that from Corps Districts to the Office of the Assistant Secretary of the Army for Civil Works, it is one U. S. Army Corps of Engineers Civil Works Team.
- Provide timely and accurate information to all team members, even when it is bad news.
- Think corporately, understand and respond to the fiscal challenges facing the Corps and the Federal Government.

#### > Communicate effectively, at all levels, the important national role of the U. S. Army Corps of Engineers Civil Works Programs.

- Increase awareness of the contributions of the Civil Works Mission in promoting national security, prosperity, and democracy
- Improve communications with all Civil Works stakeholders
- Articulate more clearly the capabilities and limitations of Civil Works Programs

Meeting these goals and objectives will enhance the Nation's prosperity through capital investments in new economic and environmental infrastructure and operation and maintenance of its existing infrastructure. It will also provide a trained workforce which can promote democracy and respond to natural and national emergencies, thereby enhancing security

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

### ANNEX A

#### FUNDING

The Civil Works Program receives Federal funding through the annual Energy and Water Development Appropriations Act. Program funding also comes from non-Federal project sponsors who share in project costs according to formulas established by project authorization acts. A third source of funding comes from through the Support for Others Program, which is conducted under reimbursable agreements with Federal agencies. The charts on the following pages show the amount of FY 1996 funding by source and business program.

#### BUSINESS PROGRAMS

The Civil Works Program will accomplish these strategic goals by providing important services in eight business programs: flood and coastal storm damage reduction, navigation, environment, hydropower, recreation, regulatory, emergency preparedness and disaster response, and support for others. Program performance goals are being established for each of the eight programs to demonstrate progress in achieving the strategic goals. Program performance measures being used in Fiscal Year 1996 to measure performance in achieving program goals are described below. Other measures, which will be used in Fiscal 1997 and beyond, are being developed.

#### Flood and Coastal Storm Damage Reduction

**Description.** There are two general approaches to reducing flood damages. The first approach consists of constructing large scale engineering projects which operate to prevent flood waters from inundating property. The second approach consists of modifying property susceptible to flood damage to minimize the risk of flood damage. Frequently, a combination of approaches is used in Corps projects to prevent flood damages. Most of the Corps' flood and coastal storm damage reduction projects are constructed as joint ventures between the Federal government and non-Federal sponsors. New projects, once built, are owned, operated and maintained by the non-Federal sponsor. The Corps, however, has older projects, mostly reservoirs, which it operates and maintains. The Nation has invested \$26 billion in flood damage reduction projects and has prevented \$292 billion in flood damages for a return of eleven dollars in flood damage reduction for every dollar invested.

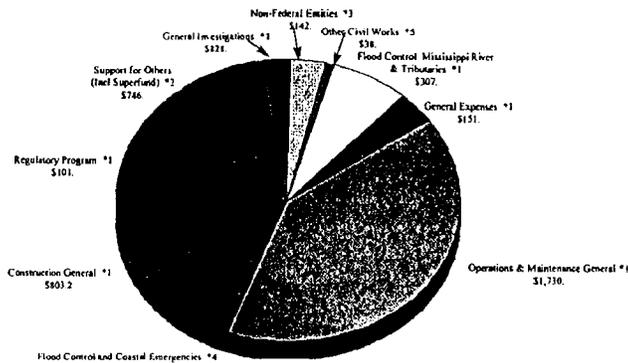
**Strategy.** Two program strategies have been established to respond to the strategic goals. They are as follows:

1. New investments will be undertaken which meet criteria for Federal participation and have been benefits in excess of costs.
2. Existing Federal infrastructure will be operated and managed to maximize the value of the services provided within available funds.

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

**ANNEX A**

**Corps of Engineers  
FY 96 Civil Works and Support For Others Program Funding  
(Millions)**

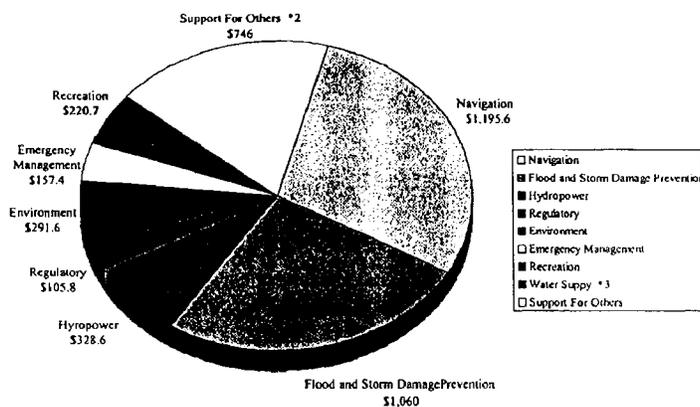


- \*1. Energy and Water Development Appropriations Act. Includes trust fund contributions.
- \*2. Reimbursable work for other agencies. (FY 95 data shown; FY 96 data will be available Feb 97. FY 96 value will be about the same as FY 95.
- \*3. Non Federal Contributed Funds (Cash contribution required by law for budgeted work and work anticipated to be done on a reimbursable basis).
- \*4. Includes supplemental appropriation for disaster activities.
- \*5. Other reports on Coastal Wetland Restoration Trust Fund work.

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

**ANNEX A**

**FY 96 Funding By Business Program<sup>1</sup>**



- \*1. Total funding reflected in this chart will differ from the previous chart due to rounding.
- \*2. Reimbursable work for other agencies. (FY95 data shown; FY96 data will be available in Feb 97. FY96 value will be about the same as FY95.)
- \*3. Water Supply for FY96 was \$2.0M or less than 0.06% of total program funding.

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

---

**ANNEX A**

**Performance Measures and Annual Performance Targets.**

**Performance Measure Number 1:** Actual performance of Corps facilities in providing flood damage reduction where flooding would have otherwise been experienced.

**Performance Target Number 1:** Maintain Corps facilities to provide the design level of flood damage reduction.

**Performance Achieved:**

	FY 93	FY 94	FY 95	FY 96
Flood Damages Prevented	\$32.1B	\$17.0B	\$26.8B	NA

**Navigation**

**Description:** The navigation program includes improvement and maintenance of harbors handling all of the Nation's seaborne commerce. The Corps combines direct appropriations with funds appropriated from the Harbor Maintenance Trust Fund to maintain navigability in 114 major deep draft harbors and over 400 smaller harbors. The Corps also has built an intracoastal and inland network of 12,000 miles of commercial navigation channels and over 200 locks and dams. Major improvements to inland waterway facilities are financed in part by the Inland Waterway Trust Fund. More than 600 million tons of commerce are moved every year on these waterways. Maintaining the navigation system, ports and inland waterways, involves removing more than 300 million cubic yards of dredged material each year.

**Strategy.** Two program strategies have been established to respond to the strategic goals. They are as follows:

1. New investments will be undertaken which meet criteria for Federal participation and have benefits in excess of costs.
2. Existing navigation infrastructure will be operated and managed to maximize the value of the services provided within available funds.

**Performance Measures and Annual Performance Targets**

**Performance Measure Number 1:** Actual performance of Corps facilities in providing low cost transportation of commerce. This measure looks at the volume of commerce and the cost to operate the fuel taxed waterways component of the navigation system.

**Performance Target Number 1:** Maintain Corps facilities to provide low cost transportation of bulk commodities to world markets.

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

**ANNEX A**

**Performance Achieved:**

	FY 93	FY 94	FY 95	FY 96
Ton Miles*	257B	265.0B	276.5B	**
Cost per Ton Mile*	\$0.0016	\$0.0018	\$0.0018	**

\* Ton mile data is reported on a calendar year basis; costs are on a fiscal year basis.

\*\* FY 96 data will be available October 1997.

**Performance Measure Number 2:** Percent of time navigation infrastructure (waterways, harbors, channels, and structures) were available as scheduled.

**Performance Target Number 2:** Maintain Corps facilities to be available 97% of the time they are scheduled to be available.

**Performance Achieved:**

	FY 93	FY 94	FY 95	FY 96
Actual Availability	96%	98%	99%	98%

**Performance Measure Number 3:** Minimize costs of dredging while assuring safe and reliable harbor and channel availability.

**Performance Target Number 3:** The volume of material dredged are largely dependent upon acts of nature and factors beyond the control of man; so no performance target is established. Cost of material dredged is influenced by depth of material to be dredged and placement of dredged material.

**Performance Achieved:**

	FY 93	FY 94	FY 95	FY 96(est)
Cubic Yards Removed*	245M	264M	217M	244M
Cost Per Cubic Yard	\$1.99	\$1.61	\$1.88	\$1.72

\*Volume of material dredged reflects maintenance dredging; it does not include dredging done for new construction projects.

**Environment**

**Description:** The environment program is similar to the preceding two programs in having a new investment component and an operation and maintenance component for existing projects. Capital investment is directed into environmental restoration and mitigation features at existing and new projects. The Corps has authority to incorporate ecosystem restoration in plans for new projects, as a modification of existing projects, and in determining placement of dredged material from authorized navigation projects. It also has some authority to restore ecosystems where a Corps project contributed to degradation of the environment. At existing Corps operated projects, the Corps uses the Environmental Review Guide for Operations to locate and plan

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

### ANNEX A

corrective action for environmental compliance deficiencies. District elements, regulatory agencies and private contractors offer support to facility managers who identify environmental compliance strengths and weaknesses in their own operations.

**Strategy:** Three program strategies have been established to respond to the strategic goals. They are as follows:

1. Investments in Corps mitigation and restoration projects or features make positive contributions to the Nation's environment resource base.
2. Investments in Corps mitigation and restoration projects and the operation of Corps facilities should assist in the recovery of Federally listed threatened and endangered species.
3. Assure that the operation of all Civil Works facilities and management of associated lands (including out granted areas) comply with environmental requirements contained in relevant Federal, state and local laws and regulations.

**Performance Measures:** Program performance measures for this program are under development

### Regulatory

**Description:** The Corps operates a comprehensive regulatory program which, through extensive public interest review, protects navigation and regulates the deposit of dredged and fill materials into the Nation's waters.

**Strategies:** The following program strategies have been established to respond to the strategic goals.

1. Administer the Regulatory Program in a manner that renders fair and reasonable decisions for applicants.
2. Administer the Regulatory Program in a manner that provides for efficient decision making.

**Performance Measures and Annual Targets.**

**Performance Measure Number 1:** Percent of decisions completed within 60 days on requests to do work in U. S. waters. Number of all actions (individual permits, general permits, letters of permission, and denials) completed in 60 days divided by the total number of requests.

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

**ANNEX A**

**Performance Target Number 1.** Target is to complete 85% of all actions in 60 days.

**Performance Achieved:**

	FY 94	FY 95	FY 96
Number of Permit Actions	58,391	73,515	71,870
% Completed within 60 days	91%	93%	94%

**Program Performance Measure Number 2:** Percent of decisions completed within 120 days on requests to do work in the U.S. waters if the proposal needs a standard permit; that is, the project is a larger one requiring more extensive review.

**Performance Target Number 2:** Target is to complete 70% of Individual Permits in 120 days.

**Performance Achieved:**

	FY 94	FY 95	FY 96
Number of Permit Actions	4,157	4,603	4,247
% Completed within 120 days	74%	78%	80%

**Performance Measure Number 3:** Percent of pending permit applications over two years old.

**Performance Target Number 3.** Target is to have no more than 0.8% of pending individual permit applications over two years old.

**Performance Achieved:**

	FY 94	FY 95	FY 96
Number of individual permits pending over two years at end of FY	NA	39	22
% of individual permits pending over two years at end of FY	NA	0.8%	0.4%

**Hydropower**

**Description:** The Corps operates 75 hydroelectric power generating units at many of its multipurpose reservoirs. The generation of electricity from these units is done from a renewable energy source and results in a significant supply of electricity to the nation. The electricity is made available to Federal power marketing agencies which market the power.

**Strategy:** One program strategy has been established to respond to the strategic goals. It is to maintain hydroelectric power production with a high degree generating unit availability at competitive cost.

**Performance Measures and Annual Targets.** Two program performance measures have been developed.

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

**ANNEX A**

**Performance Measure Number 1:** Actual performance of hydroelectric generating units at multi-purpose reservoir projects in providing power at competitive cost.

**Performance Target Number 1:** Historical performance has been recorded without an explicit performance target.

**Performance Achieved:**

	<u>FY 93</u>	<u>FY 94</u>	<u>FY 95</u>	<u>FY 96</u>
Kilowatt Hours Generated	73.7B	68.2B	77.4B	NA
Cost Per Kilowatt Hour	\$0.0022	\$0.0025	\$0.0024	NA

**Performance Measure Number 2:** Maintain a high degree of hydroelectric generating unit availability at multiple purpose projects.

**Performance Target Number 2:** Maintain generating unit availability at 93% of scheduled availability.

**Performance Achieved:**

	<u>FY 93</u>	<u>FY 94</u>	<u>FY 95</u>	<u>FY 96</u>
Performance Target	93%	93%	93%	90%
Actual Availability	89.6%	88.9%	87.9%	88.4%

**Recreation**

**Description:** There are 4,331 recreation areas at multipurpose reservoirs built by the Corps of Engineers. Of these 2400 are operated and maintained by the Corps and the others are operated and maintained by non-Federal entities. These areas provide for camping, swimming, boating, picnicing and related activities. The operation and maintenance of the recreation areas must be compatible with and not in conflict with the underlying primary purposes for which the reservoirs were authorized; i.e., flood protection and/or navigation.

**Strategy:** The following program strategies have been established to respond to the strategic goals. They are as follows:

1. Provide outdoor recreation opportunities in an effective and efficient manner at Corps operated water resource projects.
2. Provide continued outdoor recreation opportunities to meet the needs of present and future generations

**Program Performance Measures and Annual Targets.**

**Performance Measure Number 1:** Cost of visitor day in providing outdoor recreation services

**Performance Target Number 1:** The cost per visitor day is determined in part by number of recreation visitors. The visitor day parameter is influenced by economic conditions

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

**ANNEX A**

that are not under the management influence of the Corps of Engineers. The cost of providing recreation opportunities is a variable that can be managed by Corps managers. Historically, a management performance target has not been specified because of the inability to significantly influence the visitor day component of the measure. Actual statistical performance has instead been reported.

**Performance Achieved:**

	<u>FY 93</u>	<u>FY 94</u>	<u>FY 95</u>	<u>FY 96</u>
Visitor Days	199M	205M	205M	*
Cost Per Visitor Day	\$0.82	\$0.84	\$0.83	*

\*FY 96 data will be available in January 1997.

**Emergency Management**

**Description:** The Civil Works Program includes a disaster response and recovery program. The program is pursued under the Corps own authority under Public Law (P.L.) 84-99 and under the Federal Response Plan in coordination with the Federal Emergency Management Agency (FEMA) and others. Response activities are supplemental to state and local efforts. The Corps disaster response and recovery program is not limited to water resource related disasters. Disaster preparedness and response capabilities encompass a broad range of natural disasters and national emergencies because of the engineering skills and management capabilities that are maintained at a readiness state through peacetime Corps Civil Works Program support. The emergency preparedness planning and disaster response capability makes a significant and direct contribution to national security objectives.

**Strategy.** Two program strategies have been established to respond to the strategic goals. They are as follows:

1. Attain and maintain a high consistent state of preparedness
2. Provide for a rapid, effective, efficient all-hazards response

**Performance Measures and Annual Targets.** Performance measures for this program are being developed.

**Support for Others**

**Description.** The Corps Support for Others Program provides technical and specialized contract management assistance to other Federal agencies, state and local governments and, in limited instances, to private entities on a reimbursable basis. The Corps' considerable and far ranging environmental expertise is drawn upon by the Environmental Protection Agency and the Department of Energy to assist them in the Superfund and cleanup at nuclear production facilities.

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

---

**ANNEX A**

respectively. Corps support of other agency infrastructure programs includes designing and building space launch facilities for the National Aeronautics and Space Administration, and managing embassy construction and security efforts around the world for the State Department and the United States Information Agency.

**Strategy:** Ensure customer satisfaction.

**Performance Measure and Annual Target:** Performance measures are being developed for this program.

ANNEX A

***U. S. ARMY CORPS OF  
ENGINEERS***

***CIVIL WORKS***

***FINANCIAL STATEMENTS***

15

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

**ANNEX A**

Department of Defense  
Corps of Engineers  
STATEMENT OF FINANCIAL POSITION  
AS OF SEPTEMBER 30, 1996  
(Thousands)

**CONSOLIDATED STATEMENT**

	1996	1995
<b>ASSETS</b>		
<b>1. Entity Assets:</b>		
<b>a. Transactions with Federal (Intragovernmental) Entities:</b>		
(1). Fund Balance With Treasury (Note 2)	\$1,610,934	\$1,889,623
(2). Investments, Net (Note 4)	\$278,095	\$240,822
(3). Accounts Receivable, Net (Note 5)	\$355,816	\$341,996
(4). Interest Receivable	\$1,537	\$1,492
(5). Advances and Prepayments	\$0	\$0
(6). Other Federal (Intragovernmental) (Note 6)	(\$12,555)	\$2,939
<b>b. Transactions with Non-Federal (Governmental) Entities:</b>		
(1). Investments (Note 4)	\$0	\$0
(2). Accounts Receivable, Net (Note 5)	\$20,901	\$627,849
(3). Credit Program Receivables/ Related Foreclosed Property, Net (Note 7)	\$0	\$0
(4). Interest Receivable, Net	\$0	\$0
(5). Advances and Prepayments	\$2,821	\$2,332
(6). Other Non-Federal (Governmental) (Note 6)	(\$43,873)	(\$102,064)
<b>c. Cash and Other Monetary Assets (Note 3)</b>	\$0	\$0
<b>d. Inventory, Net (Note 8)</b>	\$0	\$0
<b>e. Work in Process (Note 9)</b>	\$0	\$0
<b>f. Operating Materials/Supplies, Net (Note 10)</b>	\$9,185	\$13,162
<b>g. Stockpile Materials, Net (Note 11)</b>	\$0	\$0
<b>h. Seized Property (Note 12)</b>	\$0	\$0
<b>i. Forfeited Property, Net (Note 13)</b>	\$0	\$0
<b>j. Goods Held Under Price Support and Stabilization Programs, Net (Note 14) (Note 13)</b>	\$0	\$0
<b>k. Property, Plant and Equipment, Net (Note 15)</b>	\$38,657,876	\$38,959,002
<b>l. Other Entity Asset</b>	\$219,559	\$28,046
<b>m. Total Entity Assets</b>	\$41,100,798	\$42,005,299
* DA Goal for WIP is 3 days (AR 37-106, paragraph 1-6)		
<b>2. Non-Entity Assets:</b>		
<b>a. Transactions with Federal (Intragovernmental) Entities:</b>		
(1). Fund Balance With Treasury (Note 2)	\$54,311	\$33,934
(2). Accounts Receivable, Net (Note 5)	\$1,842	\$1,644
(3). Interest Receivable	\$0	\$0
(4). Other (Note 8)	\$0	\$0
<b>b. Transactions With Non-Federal (Governmental) Entities:</b>		
(1). Accounts Receivable, Net (Note 5)	\$550,331	\$18,205
(2). Interest Receivable, Net	\$0	\$0
(3). Other (Note 6)	\$0	\$0
<b>c. Cash and Other Monetary Assets (Note 3)</b>	\$0	\$0
<b>d. Other Non-Entity Assets</b>	\$0	\$0
<b>e. Total Non-Entity Assets</b>	\$806,484	\$53,783
<b>3. Total Assets</b>	<b>\$41,707,282</b>	<b>\$42,059,082</b>

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

**ANNEX A**

Department of Defense  
Corps of Engineers  
STATEMENT OF FINANCIAL POSITION  
AS OF SEPTEMBER 30, 1996  
(Thousands)

**CONSOLIDATED STATEMENT**

	1996	1995
<b>LIABILITIES</b>		
<b>4. Liabilities Covered by Budgetary Resources:</b>		
a. Transactions with Federal (Intragovernmental) Entities:		
(1). Accounts Payable	\$167,978	\$144,414
(2). Interest Payable	\$0	\$0
(3). Debt (Note 15)	\$0	\$0
(4). Other Federal (Intragovernmental) Liabilities (Note 17)	\$26,458	\$209,802
b. Transactions with Non-Federal (Governmental) Entities:		
(1). Accounts Payable	\$423,836	\$413,413
(2). Accrued Payroll and Benefits		
(a) Salaries and Wages	\$80,889	\$0
(b) Annual Accrued Leave	\$168,868	\$0
(c) Severance Pay and Separation Allowance	\$0	\$0
(3). Interest Payable	\$0	\$0
(4). Liabilities for Loan Guarantees (Note 7)	\$0	\$0
(5). Lease Liabilities (Note 18)	\$0	\$0
(6). Pensions and Other Actuarial Liabilities (Note 19)	\$0	\$0
(7). Other Non-Federal (Governmental) Liabilities (Note 17)	\$131,669	\$1,044,875
<b>c. Total Liabilities Covered by Budgetary Resources:</b>	<b>\$998,698</b>	<b>\$1,812,504</b>
<b>5. Liabilities not Covered by Budgetary Resources:</b>		
a. Transactions with Federal (Intragovernmental) Entities:		
(1). Accounts Payable	\$0	\$0
(2). Debt (Note 15)	\$0	\$0
(3). Other Federal (Intragovernmental) Liabilities (Note 17)	\$1,841	\$0
b. Transactions with Non-Federal (Governmental) Entities:		
(1). Accounts Payable	\$0	\$0
(2). Debt (Note 18)	\$0	\$0
(3). Lease Liabilities (Note 18)	\$0	\$5
(4). Pensions and Other Actuarial Liabilities (Note 19)	\$0	\$0
(5). Other Non-Federal (Governmental) Liabilities (Note 17)	\$549,434	\$18,448
<b>c. Total Liabilities not Covered by Budgetary Resources</b>	<b>\$551,075</b>	<b>\$16,453</b>
<b>6. Total Liabilities</b>	<b>\$1,550,771</b>	<b>\$1,828,957</b>
<b>NET POSITION (Note 20)</b>		
<b>7. Balances:</b>		
a. Unexpended Appropriations	\$2,242,062	\$1,787,752
b. Invested Capital	\$38,402,480	\$38,458,454
c. Cumulative Results of Operations	\$63,044	\$2,372
d. Other	\$0	\$0
e. Future Funding Requirements	(\$551,075)	(\$16,453)
<b>f. Total Net Position</b>	<b>\$40,156,511</b>	<b>\$40,230,125</b>
<b>8. Total Liabilities and Net Position</b>	<b>\$41,707,282</b>	<b>\$42,059,082</b>

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

**ANNEX A**

Department of Defense Corps of Engineers STATEMENT OF OPERATIONS AND CHANGES IN NET POSITION FOR THE PERIOD ENDED SEPTEMBER 30, 1996 (In Thousands)			<b>CONSOLIDATED STATEMENT</b>	
	<b>1996</b>	<b>1995</b>		
<b>REVENUES AND FINANCING SOURCES</b>				
1. Appropriated Capital Used	3,708,850	4,543,717		
2. Revenues from Sales of Goods and Services				
a. To the Public		14,235		
b. Intragovernmental	3,301,497	2,780,707		
3. Interest and Penalties, Non-Federal	14			
4. Interest, Federal	15,519	13,250		
5. Taxes (Note 21)				
6. Other Revenues and Financing Sources (Note 22)	262,072	117,305		
7. Less: Taxes and Receipts Transferred to the Treasury or Other Agencies	<u>(191,786)</u>	<u>(98,363)</u>		
8. Total Revenues and Financing Sources	<u>7,098,166</u>	<u>7,370,851</u>		
<b>EXPENSES</b>				
9. Program or Operating Expenses (Note 23)	5,945,585	6,655,452		
10. Cost of Goods Sold (Note 24)				
a. To the Public		14,235		
b. Intragovernmental	812,971	517,408		
11. Depreciation and Amortization	349,603	180,865		
12. Bad Debts and Writeoffs	70	27		
13. Interest				
a. Federal Financing Bank/Treasury Borrowing				
b. Federal Securities				
c. Other				
14. Other Expenses (Note 25)				
15. Total Expenses	<u>7,108,229</u>	<u>7,367,985</u>		
16. Excess (Shortage) of Revenues and Financing Sources Over Total Expenses Before Extraordinary Items	<u>(12,063)</u>	<u>2,866</u>		
17. Plus (Minus) Extraordinary Items (Note 26)				
18. Excess (Shortage) of Revenues and Financing Sources Over Total Expenses	<u>(12,063)</u>	<u>2,866</u>		
19. Net Position, Beginning Balance, as Previously Stated	40,230,122	47,018,058		
20. Adjustments (Note 27)				
21. Net Position, Beginning Balance, as Restated	40,230,122	47,018,058		
22. Excess (Shortage) of Revenues and Financing Sources Over Total Expenses	<u>(12,063)</u>	<u>2,866</u>		
23. Plus (Minus) Non Operating Changes Note 28)	<u>(61,550)</u>	<u>(6,790,800)</u>		
24. Net Position, Ending Balance	<u>40,158,509</u>	<u>40,230,122</u>		

Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

ANNEX A

INDIRECT METHOD		
Department of Defense		
Corps of Engineers		
STATEMENT OF CASH FLOWS		
FOR THE PERIOD ENDED SEPTEMBER 30, 1996		
(Thousands)		
	1996	1995
<b>CASH FLOW FROM OPERATING ACTIVITIES:</b>		
Cash Provided by:		
1. Excess (Shortage) of Revenues and Financing Sources Over Total Expenses	(\$12,064)	\$2,868
Adjustments affecting Cash Flow:		
2. Appropriated Capital Used	(\$46,868)	(\$46,973)
3. Decrease (Increase) in Accounts Receivable	\$27,502	\$21,497
4. Decrease (Increase) in Other Assets	\$8,842	\$13,558
5. Increase (Decrease) in Accounts Payable	\$7,295	(\$15,608)
6. Increase (Decrease) in Other Liabilities	(\$23,986)	\$13,609
7. Depreciation and Amortization	\$65,310	\$62,783
8. Other Unfunded Expenses	\$0	\$0
9. Other Adjustments	\$74,154	\$78,777
10. Total Adjustments	\$112,249	\$127,533
11. Net Cash Provided (Used) by Operating Activities	\$100,185	\$130,401
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
12. Sale of Property, Plant and Equipment	\$1,148	\$1,212
13. Purchase of Property, Plant and Equipment	(\$54,464)	(\$82,857)
14. Sale of Securities	\$0	\$0
15. Purchase of Securities	\$0	\$0
16. Collection of Loans Receivable	\$0	\$0
17. Creation of Loans Receivable	\$0	\$0
18. Other Investing Cash Provided (Used)	\$0	\$0
19. Net Cash Provided (Used) by Investing Activities	(\$53,316)	(\$81,645)
<b>CASH PROVIDED (USED) BY FINANCING ACTIVITIES</b>		
20. Appropriations (Current Warrants)	\$0	\$0
21. Add:		
a. Restorations	\$0	\$0
b. Transfers of Cash From Others	\$0	\$0
22. Deduct:		
a. Withdrawals	\$0	\$0
b. Transfers of Cash To Others	\$0	\$0
23. Net Appropriations	\$0	\$0
24. Borrowing from the Public	\$0	\$0
25. Repayments on Loans to the Public	\$0	\$0
26. Borrowing from the Treasury and the Federal Financing Bank	\$0	\$0
27. Repayments on Loans from the Treasury and the Federal Financing Bank	\$0	\$0
28. Other Borrowings and Repayments	\$0	\$0
29. Net Cash Provided (Used) by Financing Activities	\$0	\$0
30. Net Cash Provided (Used) by Operating, Investing and Financing Activities	\$46,869	\$48,756
31. Fund Balances with Treasury, Cash, and Foreign Currency, Beginning	\$543,748	\$494,900
32. Fund Balances with Treasury, Cash, and Foreign Currency, Ending	\$590,615	\$543,748

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of  
Engineers, Civil Works"**

---

**ANNEX A**

Supplemental Disclosure Schedule of Cash Flow Information:

33. Total Interest Paid

Supplemental Schedule of Financing and Investing Activity:

33. Total Interest Paid		\$0
34. Property and Equipment Acquired Under Capital Lease Obligations	\$0	\$0
35. Property Acquired Under Long-term Financing Arrangements	\$0	\$0
36. Other Exchanges of Noncash Assets or Liabilities	\$0	\$0

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

---

### ANNEX A

#### Note 1. Significant Accounting Policies

- A. The U.S. Army Corps of Engineers has an estimated one (1) billion of continuing contracts for which no orders have been placed. This represents future contract authority.
- B. The Corps of Engineers Funds with Treasury balances have been adjusted to agree with Treasury's balances in accordance with Treasury's policy.
- C. The Corps of Engineers Management Information System (COEMIS) has not been programmed to capture data under GL 5700 (Appropriations expensed) or 6100 (Program Operating Expenses) on the Statement of Operations. Therefore, Appropriations Expensed and Program Operating Expenses have been adjusted on all statements.
- D. Footnote 23, Operating Expenses by Object Classification, has also been produced through the use of estimates/percentages depicted by object class taken from the U.S. Budget Report of Obligations (SF225). COEMIS general ledgers do not provide the level of detail required for this footnote.
- E. Footnote 29, Intrafund Eliminations: Our accounting system does not capture the detail information requested in order to comply with this footnote.

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

**ANNEX A**

**NOTE 2. Fund Balances with Treasury**

**CONSOLIDATED**

**A. Business Operations Fund (USD(C)) and All Other Funds and Accounts**

	<u>Entity Assets</u>				
	<u>Trust Funds</u>	<u>Revolving Funds</u>	<u>Appropriated Funds</u>	<u>Other Type Funds</u>	<u>Total</u>
Unobligated Balance Available:					
Available	\$70,286	\$283,904	\$328,952	\$14,857	\$697,999
Restricted					
Reserve for anticipated Resources					
Obligated (but not expensed)	82,509	308,711	520,198	3,517	912,935
Unfunded Contract Authority					
Unused Borrowing Authority					
Treasury Balance	<u>\$152,795</u>	<u>\$590,815</u>	<u>\$849,150</u>	<u>\$18,375</u>	<u>\$1,610,934</u>

**B. Defense Business Operations Fund Activities Below USD(C) Level**

	<u>Funds Collected</u>	<u>Entity Assets</u>	<u>Funds Disbursed</u>
Beginning Balance			
Transfers of Cash to Others			
Transfers of Cash from Others			
Funds Collected			
Funds Disbursed			
Ending Balance			

**C. All Funds and Accounts**

	<u>Funds Collected</u>	<u>Non-Entity Assets</u>	<u>Funds Disbursed</u>
Beginning Balance	(\$1,721)		\$35,656
Funds Collected	47,918		
Funds Disbursed	44,399		(16,858)
Ending Balance	\$1,798		\$2,513

**D. Other Information:**

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

**ANNEX A**

**NOTE 4. Investments, Net**

**CONSOLIDATED**

	(1) Cost	(2) Market Value	(3) Amortization Method	(4) Amortized Premium/ Discount	(5) Investments Net
<b>A. Intragovernmental Securities:</b>					
1. Marketable					
2. Non-Marketable: Par Value					
3. Non-Marketable: Market-Based	\$278,995	\$285,407		\$6,412	\$278,995
Subtotal	\$278,995	\$285,407		\$6,412	\$278,995
<b>B. Governmental Securities:</b>					
1.					
2.					
3.					
Subtotal					
<b>Total</b>	<b>\$278,995</b>	<b>\$285,407</b>		<b>\$6,412</b>	<b>\$278,995</b>

C. Other information: The above investments represent the invested portion of the Inland Waterways Trust Fund. This portion of the IWWTF is managed and accounted for by the Department of the Treasury.

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of  
Engineers, Civil Works"**

**ANNEX A**

NOTE 5, Accounts Receivable, Net

CONSOLIDATED

	(1) Gross Amount Due	(2) Allowance For Estimated Uncollectibles	(3) Allowance Method Used	(4) Net Amount Due
<b>A. Entity Receivables:</b>				
Intragovernmental	\$355,616			\$355,616
Governmental	\$20,901			\$20,901
<b>B. Non-Entry Receivables:</b>				
Intragovernmental	\$1,842			\$1,842
Governmental	\$550,331			\$550,331
<b>C. Other Information:</b>				

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

**ANNEX A**

**NOTE 6. Other Federal (Intragovernmental) and Non-Federal (Governmental) Assets:**

**CONSOLIDATED**

<b>A. Other Entity Assets</b>	
1. Federal (Intragovernmental)	
(a)	(\$12,555)
(b)	
(c)	
Total	(\$12,555)
2. Non-Federal (Governmental)	
(a)	(\$43,873)
(b)	
(c)	
Total	(\$43,873)
<b>B. Other Information.</b>	
<b>C. Other Non-entity Assets</b>	
1. Federal (Intragovernmental)	
(a)	
(b)	
(c)	
Total	
2. Non-Federal (Governmental)	
(a)	
(b)	
(c)	
Total	
<b>D. Other Information.</b>	

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

**ANNEX A**

**NOTE 10. Operating Materials and Supplies (OM&S), Net**

**CONSOLIDATED**

	(1) OM&S Amount	(2) Allowance For Losses	(3) OM&S, Net	(4) Valuation Method
A. OM&S Categories:				
1. Held for Use	\$9,185	\$0	\$9,185	c
2. Held in Reserve for Future Use	0	0	0	
3. Excess, Obsolete & Unserviceable	0	0	0	
<b>Total</b>	<b>\$9,185</b>	<b>\$0</b>	<b>\$9,185</b>	

B. Restrictions on operating materials and supplies:  
Amount applies to Revolving Fund.

C. Other Information:  
The Revolving Fund maintains a warehouse activity to receive, store and issue common inventory items required by multiple civil works activities and activities of the Revolving Fund. Issues are based on average unit cost.

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

**ANNEX A**

**NOTE 15. Property, Plant and Equipment, Net:**

**CONSOLIDATED**

	(1) Depreciation Method	(2) Service Life	(3) Acquisition Value	(4) Accumulated Depreciation	(5) Net Book Value
<b>Classes of Fixed Assets:</b>					
A. Land	N/A	N/A	\$7,247,421	\$0	\$7,247,421
B. Structures, Facilities, & Leasehold Improvements	IN	>20	28,502,393	3,234,762	25,267,631
C. Military Equipment					
D. ADP Software	SL	1-5	21,726	159	21,568
E. Equipment	SL	1-5	1,130,601	387,885	742,717
F. Assets Under Capital Lease					
G. Other	N/A	N/A	515,288	4	515,284
H. Natural Resources					
I. Construction-in-Progress	N/A	N/A	4,863,057	0	4,863,057
Total			<u>\$42,280,487</u>	<u>\$3,622,809</u>	<u>\$38,657,678</u>

**\*Keys:**

<b>Depreciation Methods</b>	<b>Range of Service Life</b>
SL - Straight Line	1-5 - 1 to 5 Years
DD - Double-Declining Balance	8-10 - 8 to 10 Years
SY - Sum of the Years' Digits	11-20 - 11 to 20 Years
IN - Interest (sinking fund)	>20 - Over 20 Years
PR - Production (activity or use method)	
OT - Other (describe)	

Other Information: Depreciation is not currently categorized in the accounting records as to amounts for equipment versus that of structures, facilities, etc. All depreciation is shown against structures, facilities & leasehold improvements. Currently our general ledgers do not separate land and equipment from structures, facilities and leasehold improvements in COEMIS. Footnotes submitted by Districts are used to calculate structures and facilities. The depreciation on equipment is computed in CEFMS

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

**ANNEX A**

Note 17. Other Liabilities

**CONSOLIDATED**

**A. Other Liabilities Covered by Budgetary Resources:**

	<u>Non-Current Liability</u>	<u>Current Liability</u>	<u>Total</u>
1. Intragovernmental			
a.	\$24,431	\$2,027	\$26,458
b.			0
c.			0
<b>Total</b>	<u>\$24,431</u>	<u>\$2,027</u>	<u>\$26,458</u>

	<u>Non-Current Liability</u>	<u>Current Liability</u>	<u>Total</u>
2. Governmental			
a.		\$85,532	\$85,532
b.	46,137		46,137
c.			
<b>Total</b>	<u>\$46,137</u>	<u>\$85,532</u>	<u>\$131,669</u>

**B. Other Information:**

**C. Other Liabilities Not Covered by Budgetary Resources:**

	<u>Non-Current Liability</u>	<u>Current Liability</u>	<u>Total</u>
1. Intragovernmental			
a.		\$1,641	\$1,641
b.			
c.			
<b>Total</b>		<u>\$1,641</u>	<u>\$1,641</u>

	<u>Non-Current Liability</u>	<u>Current Liability</u>	<u>Total</u>
2. Governmental			
a.		\$549,434	\$549,434
b.			
c.			
<b>Total</b>		<u>\$549,434</u>	<u>\$549,434</u>

**D. Other Information:**

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

ANNEX A

**NOTE 20. Net Position**

CONSOLIDATED

	<u>Revolving Funds</u>	<u>Trust Funds</u>	<u>Appropriated Funds</u>	<u>Total</u>
A. Unexpended Appropriations:				
(1) Unobligated:				
a. Available .....	\$424,799	\$70,286	\$343,778	\$838,863
b. Unavailable .....				
(2) Undelivered Orders.....		335,392	1,067,805	1,403,197
B. Invested Capital.....	560,880	1,034,644	36,806,956	38,402,480
C. Cumulative Results of Operations.....	63,044			63,044
D. Other.....				
E. Future Funding Requirement.....		(966)	(550,109)	(551,075)
F. Total	<u>\$1,048,723</u>	<u>\$1,439,356</u>	<u>\$37,668,430</u>	<u>\$40,156,509</u>
G. Other Information				

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

---

**ANNEX A**

Note 22. Other Revenues and Financing Sources

CONSOLIDATED

A. Other Revenues and Financing Sources	1996	1995
1. Insurance Premiums/Trust Fund Revenues	\$39,246	\$14,259
2. Plant Increment	\$31,039	\$4,683
3. Unavailable Receipts (General Funds)	\$191,787	\$98,363
<b>Total</b>	<b>\$262,072</b>	<b>\$117,305</b>

**B. Other Information:**

The Corps of Engineers is self-insured and collects monthly premiums for insurance on Revolving Fund assets. Insurance premiums were not listed separately on previous financial statements.

Plant increment is charged on Revolving Fund Assets to ensure the availability of funds for the replacement of these assets.

The Trust Fund Revenues amounting to \$22,898,020.00 are accounted for by the Department of Treasury and can provide any additional information needed.

The General Fund receipts of \$191,786,802.00 are unavailable receipts returned to Treasury.

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

**ANNEX A**

<u>Note 23, Program or Operating Expenses</u>	CONSOLIDATED	
	1996	1995
<b>A. Operating Expenses by Object Classification:</b>		
1. Personal Services and Benefits.....	\$1,019,978	\$1,318,685
2. Travel and Transportation.....	\$57,246	\$93,666
3. Rental, Communication and Utilities.....	\$103,808	\$120,073
4. Printing and Reproduction.....	\$19,484	\$34,370
5. Contractual Services.....	\$4,528,298	\$4,734,985
6. Supplies and Materials.....	\$210,148	\$344,232
7. Equipment not Capitalized.....		
8. Grants, Subsidies and Contributions.....	\$5,800	\$5,262
9. Insurance Claims and Indemnities.....	\$1,045	\$4,179
10. Other (describe):		
(a)		
(b)		
(c)		
11 Total Expenses by Object Class	\$5,945,585	\$6,655,452
<b>B. Operating Expenses by Program:</b>		
Flood Control - Mississippi River and Tributaries.....	\$302,541	\$383,573
General Investigations - Studies/collection of basic information pertaining to rivers/harbors flood control, shore protection & related projects.....	\$184,809	\$207,982
Construction, General - Advance Engineering & Design in relation to Navigation, Beach erosion, flood control, rehabilitation & dam safety, aquatic plant control, etc.....	\$789,710	\$1,087,406
Operation/Maintenance - for expenses necessary for the preservation & care of existing rivers and harbors, flood control & related work.....	\$1,205,871	\$1,689,091
Operation & Maintenance, General, Flooding, Midwest Act of 1993.....	\$10,535	\$8,825
General Expenses - for expenses necessary		

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

**ANNEX A**

<u>Note 23. Program or Operating Expenses</u>	<u>CONSOLIDATED</u>	
	1996	1995
for general administration & related functions in the Office of the Chief of Engineers & Division Engineers & other specified activities.....	\$148,813	\$148,480
Flood Control & Coastal Emergencies - for expenses necessary for emergency flood control, hurricane & shore protection activities.....	\$54,748	\$64,392
Flood Control & Coastal Emergencies, Flooding, Midwest Act of 1993.....	\$6,654	\$15,120
Regulatory Program - for expenses necessary for administration of laws pertaining to the regulation of navigable waters including bridges and wetlands.....	\$99,722	\$99,300
Consolidated Working Fund.....	\$1,723	\$17,805
Acquisition & Construction of Radio Facilities for the International Communication Agency.....	\$0	\$2,730

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

**ANNEX A**

<u>Note 23. Program or Operating Expenses</u>	CONSOLIDATED	
	1996	1995
Revolving Fund - provides the acquisition, operation & maintenance of plant/equipment used in Civil Works functions; for temporary financing of services chargeable to Civil appropriations and for furnishing facilities & services for military functions of the Dept of the Army, other government agencies & private persons.....	\$2,529,480	\$2,254,901
Payments to States.....	\$5,600	\$5,262
Operation & Maintenance of Dams and other Improvements, Navigable Waters.....	\$4,929	\$12,069
Coastal Wetlands Restoration.....	\$13,213	\$10,476
Inland Waterways Trust Fund.....	\$28,987	\$25,027
Contributed Funds - Improvements of Rivers and Harbors.....	\$113,294	\$122,731
Harbor Maintenance Trust Fund.....	\$482,126	\$519,196
Other.....	\$1,730	\$1,085
(4) Unallocated Expense	\$0	\$0
Totals	<u>\$5,945,586</u>	<u>\$8,655,451</u>

Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

ANNEX A

Note 24. Cost of Goods Sold.

CONSOLIDATED

A.	Cost of Services Sold	
	1. Beginning Work-in-Process	\$0
	2. Plus: Operating Expenses	812,971
	3. Minus: Ending Work-in-Process	0
	4. Minus: Completed Work for Activity Retention	0
	Cost of Services Sold	<u>\$812,971</u>

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

**ANNEX A**

<u>Note 28. Non-Operating Changes - (Transfers and Donations)</u>	<u>1996</u>	<u>CONSOLIDATED</u> <u>1995</u>
<b>A. Increases:</b>		
1. Transfers-In:		
a.	\$3,643,145	(\$2,345,639)
b.	\$0	\$0
c.	\$0	\$0
2. Unexpended Appropriations	\$0	\$0
3. Donations Received	\$0	\$0
4. Other Increases	<u>\$441,962</u>	<u>\$567,163</u>
5. Total Increases	<u>\$4,085,107</u>	<u>(\$1,778,476)</u>
<b>B. Decreases:</b>		
1. Transfers-Out:		
a.	\$567,630	\$2
b.	\$0	\$0
c.	\$0	\$0
2. Donations	\$0	\$0
3. Other Decreases	<u>\$3,579,027</u>	<u>\$5,012,322</u>
4. Total Decreases	<u>\$4,146,657</u>	<u>\$5,012,324</u>
 C. Net Non Operating Changes(Transfers)	 (\$61,550)	 (\$6,790,800)
 D. Other Information:		

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of  
Engineers, Civil Works"**

---

**ANNEX B**

**AUDIT REPORTS ISSUED AND  
ACTIVITIES INCLUDED IN THE AUDIT**

<u>Report</u>	<u>Title</u>	<u>Date Issued</u>
AA 97-108	Corps of Engineers' FY 96 Financial Statements, Vicksburg District	3 February 1997
AA 97-110	FY 96 Financial Statements, Corps of Engineers, Huntington District	3 February 1997
AA 97-98	FY 96 Financial Statements, Corps of Engineers, Fort Worth District	31 January 1997
AA 97-109	FY 96 Financial Statements, Corps of Engineers, Alaska District	31 January 1997

**Activities Included In The Audit:**

Headquarters, U.S. Army Corps of Engineers, Washington, DC

U.S. Army Engineer Divisions

Southwestern  
Ohio River  
Lower Mississippi River Valley  
Pacific Ocean

U.S. Army Engineer Districts

Fort Worth  
Huntington  
Vicksburg  
Alaska

Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

ANNEX C

VERBATIM COMMAND COMMENTS



DEPARTMENT OF THE ARMY  
U.S. Army Corps of Engineers  
WASHINGTON, D.C. 20314-1000

REPLY TO  
ATTENTION OF:

*24 January 1997*

CEAO (36-5c)

MEMORANDUM FOR DEPUTY AUDITOR GENERAL, FINANCIAL AUDITS, ATTN:  
SAAG-FAC, MR. PATRICK FITZGERALD, PROGRAM  
DIRECTOR, CORPS OF ENGINEERS AND CIVIL WORKS  
AUDITS

SUBJECT: USACE Comments on Draft Report of USAAA Audit of FY 96  
Financial Statements, Civil Works, U.S. Army Corps of Engineers

1. This is the Command reply to the subject draft report. The Command comments in the report generally reflect our official command position. The completion dates for recommended corrective actions and Command comments are provided in the enclosure.
2. We greatly appreciate the CFO audit partnering you have done with us the past several years. That cooperation enabled this MACOM to further improve our accounting processes. CFO actual audit plans have been jointly discussed in advance so that our internal corrective actions and audits complement your external audit work. A joint FY 95 construction-in-progress and DD form 1354 work effort succeeded in correcting these reported material weaknesses.
3. The point of contact for this action is Mr. John B. Byrne who can be reached at 202-761-1987.

FOR THE COMMANDER:

Encl

*Otis Williams*  
OTIS WILLIAMS  
Colonel, Corps of Engineers  
Chief of Staff

Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

ANNEX C

COMMENTS ON DRAFT AUDIT REPORT OF  
FY 96 FINANCIAL STATEMENTS, CIVIL WORKS

FINDING A: ACCOUNTING POLICIES

**Finding:** Within its revolving fund, the U.S. Army Corps Engineers maintained accounting policies that weren't in accordance with the Federal Financial Accounting Standards.

One of management's primary responsibilities is to keep the revolving fund solvent at all times. Therefore, the Corps imbedded financing mechanisms in the fund to protect the balance of the fund by either accumulating reserves of increasing solvency (cash flows) with the fund.

We agree with the business practices used by the Corps to accumulate reserves to offset future expected costs. They appeared to be prudent management decisions to finance revolving fund operations. We didn't agree with the practices implemented solely to produce cash flow. However, in either case the Corps didn't account for the associated revenues and expenses in accordance with accounting standards. These policies misrecorded and misreported the current year's operating expenses, distorting the financial statements.

As a result of the accounting policies used, the financial reporting of the results of operations wasn't accurately portrayed on the financial statements. We recommend adjusting entries totaling about \$223.2 million.

**Additional Facts:** The Corps agreed to record a corporate level adjusting entry for casualty losses and eliminating the insurance premium charges at year-end. Technical difficulties in posting and balancing the "General Ledger Trial Balance" prevented this from occurring for FY 1996. It will be done beginning with the FY 1997 financial statements.

1. **Recommendation A-1:** Correct the remaining accounting policies (plant increment and repairs & maintenance reserves) associated with the Corps' business practices to ensure policies reflect GAAP, expenses and net income reported in the current period and financial statements show the correct balances in the prepaid assets and fund balances reserve amounts.

**USACE Response:** Concur. We recognize that our present accounting treatment is not in full compliance with GAAP in that the statements make it appear that expenses are overstated. We

ENCLOSURE

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

### ANNEX C

will adjust our statements beginning FY 1997 year end to separate the current year Results from Operation from cumulative values. We will also make the appropriate year-end closing entries to reflect all income and expenses in the reporting period as recommend.

2. Recommendation A-2: Discontinue the policy of expensing the remaining book value of assets prior to asset disposal. In accordance with accounting principles, recognize non-operating gains or losses on the assets as the difference between the net book value and proceeds received, if any.

USACE Response: Concur. We are incorporating this recommendation in change 88 to ER 37-2-10 which should be completed by 30 September 1997.

3. Recommendation A-3: Record and report non-operating income and losses on the Statement of Operations and Changes in Net Position.

USACE Response: Concur. The USACE CFO's financial statements for FY 1996 had already been completed prior to the release of this draft report. OMB has issued bulletin 97-01 revising the instructions for this statement. We will comply with OMB bulletin for the preparation of FY 1997 financial statements.

4. Recommendation A-4: Implement procedures to ensure that gains and losses are incorporated into the rate structure and passed on to the revolving fund customers.

USACE Response: Concur. We will incorporate the recommended practice into the district Operating Budget process for all Revolving Fund plant accounts. In most cases, the amount will be immaterial and will not impact rates.

5. Recommendation A-5: Implement a policy to recognize salvage value on depreciable assets. Consider using either a composite standard rate or various rates by major class of assets by reviewing historical records to determine the net realizable value received as a percentage of acquisition costs or by allocating amounts based on estimated salvage value.

USACE Response: Concur. If there is materiality here, it will be with respect to structures. We will require salvage value calculation in the depreciation formula for all structures in ER 37-2-10.

Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

---

ANNEX C

6. Recommendation A-6: Discontinue the policy of recording deferred asset charges for equipment in mothball status. Record these costs as current period expenses.

USACE Response: Concur. Revised procedures will be incorporated in ER 37-2-10, change 88 which should be completed by 30 September 1997.

7. Recommendation A-7: Determine the cumulative impact on the financial statements of the policies not in conformance with GAAP. Record and report prior years' adjustments required.

USACE Response: Concur. We will determine the cumulative impact of the policies not in conformance with Fed GAAP on the financial statements to the maximum extent possible. Appropriate prior year adjustments will be reflected in the FY 97 financial statements.

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

### ANNEX C

#### FINDING B: FINANCIAL REPORTING

Finding: The Corps' financial reporting process needed improvement. In reviewing the FY 95 and FY 96 documentation for the compilation and presentation of the statements, we found that it lacked:

- Adequate audit trails.
- Consistency
- Sufficient disclosure

As in fiscal years 1993 and 1994, the Corps elected to expend minimal resources in FY 95 on producing financial statements resulting from its old financial management system. The old system couldn't produce adequate financial data because it lacked key accounts and wasn't designed to account for revenues and expenses (see our Finding C entitled Financial Management Systems).

We agreed with the Corps that expending additional resources to modify the legacy accounting system wouldn't be prudent. However, the fielding of the new management information system dictates that sufficient effort be placed in the process starting in FY 96 to ensure that balances brought forward are accurate, reliable, and auditable.

As a result, the FY 95 financial statements didn't accurately portray the results of operations or the financial position of the Corps. In addition, this also affected the opening balances established for FY96 at the close of FY 95.

Additional Facts: None.

1. Recommendation B-1. Continue to develop and implement formal accounting procedures to document and produce an audit trail for adjustments, transactions, methodology, and rationale used during the compilation process.

USACE Response: Concur. The USACE Finance Center (UFC) will obtain/receive CFO statements generated from CEFMS data for each location that is deployed on CEFMS for the appropriate reporting period. The UFC will consolidate the CFO reports and maintain an audit trail for any adjustments required to produce the consolidated CFO statements.

Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

---

ANNEX C

2. Recommendation B-2: Implement the alternative reporting process of preparing formal financial statements at each reporting period.

USACE Response: Concur. We will implement a procedure/process where the complete range of financial statements is produced at each location deployed on CEFMS. One of our long range objectives for the UFC is for each activity/location to prepare the full set of required financial statements to ensure that each Commander/Director has a increased awareness of their organizations input to the total product, consolidated financial statements.

3. Recommendation B-3: Develop policies and procedures to ensure that the new reporting requirements are adequately addressed in the financial management system.

USACE Response: Concur. We will interact with USAAA during the FY 97 Southwestern Division (SWD) CFO effort to ensure that all reporting requirements are appropriately addressed in the financial management system, CEFMS. Following the development of CEFMS CFO statements related to the SWD effort, we will emphasize the coordination, incorporation, and publicizing all new CFO reporting requirements as received.

## Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

### ANNEX C

#### FINDING C: FINANCIAL MANAGEMENT SYSTEMS

Material uncertainties continue to exist regarding the reasonableness of reported amounts on the financial statements. This occurred because the Corps' legacy financial system (Corps of Engineers Management Information System (CEMIS)) has fundamental weaknesses that prevent the Corps from reporting reliable financial information. Specifically:

- The system lacks revenue and expense accounts.
- The system isn't based on the U.S. Government's Standard General Ledger, and the existing crosswalk isn't accurate.  
The system isn't integrated with other Corps' systems.
- Auditable transactions to support computer balances don't exit.

We've reported these inadequacies since FY 93 in our audit reports. The Corps is aware of these problems and is in the process of fielding a new financial management system - the Corps of Engineers Financial Management System (CEFMS).

On the positive side, our audit results showed that the new financial system appeared to be operating with a high degree of reliability. It resolved standard general ledger and integrated deficiencies found in the legacy system and enhanced controls.

**Recommendation:** Due to the Corps ongoing implementation of its Financial Management System (CEFMS) to correct the deficiencies we've reported since FY 93, we aren't making any recommendations at this time.

Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

ANNEX C

FINDING D: MANAGEMENT CONTROLS

The Corps needed to strengthen its management controls in several areas. We found in these areas that controls were in place, but not operating or not operating effectively:

- Capitalization versus expenses of assets.
- Asset retirement.
- Insurance premium collections.
- Accounts receivables.
- Year-end cutoff.
- Sponsor's contributions on reimbursable projects.

These controls weren't working because personnel didn't comply with existing policies and procedures. For example:

- District level managers misinterpreted some of the headquarter's accounting guidance and policies.
- Some finance and accounting personnel didn't know how to correctly account for the transactions.

In addition, the legacy financial system hampered the Corps' control efforts by requiring labor-intensive procedures. As in the past, the Corps correctly reported the system deficiencies of the legacy financial system as a material weakness in its FY 96 Annual Assurance Statement. We agreed with the Corps assessment. We believe the remaining issues to be reportable conditions but not material weaknesses.

As a result, the financial reporting of the results of operating wasn't accurately portrayed on the financial statements. More importantly, the Corps needs to strengthen its verification and compliance mechanisms to help ensure effective operations. Current mechanisms didn't identify problems.

Additional facts: None.

1. Recommendation D-1: Ensure compliance with asset capitalization policy by implementing compliance mechanism. At a minimum, direct the local Internal Review Offices:

Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

ANNEX C

- Perform periodic analytical reviews on the expense accounts based on the established criteria for asset capitalization.
- Identify and research those expenses that meet the asset capitalization criteria.
- Correct the accounting records as necessary.
- Hold individuals accountable for their actions.

USACE Response: Partially concur. Implementation of the FY 1996 capitalization policy will be reemphasized in FY 1997. Furthermore, compliance with this policy will be part of the cyclical CFO audit program during FY 1997. All districts will be directed to do a 100% compliance review of the implementation of the FY 1996 asset capitalization policy and we will update our asset capitalization audit review guide on the basis of the FY 1996 USAAA CFO audit. Thereafter, compliance testing for this issue will be done on a four year cycle.

2. Recommendation D-2: Strengthen controls over the asset retirement process using the organizational structure to ensure compliance. Direct that echelons above perform periodic analytical reviews and site visits.

USACE Response: Concur. We will change our "Management Control Checklist for Revolving Fund Operations" to include a test question on asset retirement to enforce compliance. CERM-F will direct all Major Subordinate Command Finance and Accounting Officers to perform site visits for activities responding "no" to the checklist question. This checklist will be updated by 31 March 1997.

3. Recommendation D-3: Use historical insurance loss data to determine the correct balance for the insurance reserve account. Reduce rates to allow the insurance reserve balance to decrease to this level. Adjust insurance premiums to reflect actual losses so that a consistent balance can be maintained.

USACE Response: Concur. We have already initiated an action plan recommending discontinuing insurance premium charge until the reserve balance lowers to \$25 million.

4. Recommendation D-4: Ensure that Districts perform monthly reconciliations of accounts receivable and aggressively pursue

Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

ANNEX C

delinquent accounts receivable as prescribed in ER 37-2-10. This should specifically include a revalidation of each account over 180 days old.

USACE Response: Concur. We will reissue command guidance by 31 March 1997 to ensure field commanders enforce these requirements.

5. Recommendation D-5: Develop year end close out procedures that will ensure all expenses are recorded in the proper accounting period.

USACE Response: Concur. UFC will continue to refine published year end closing procedures to ensure that all accounting transactions are recorded in the appropriate accounting period. In addition, we will continue to refine and monitor the CEFMS automated fiscal year end closing process to ensure that all pertinent transactions are recorded in the appropriate accounting period. We will use all available Resource Management/Finance and Accounting forums to stress the critically of ensuring that all accounting transactions are recorded in the period in which they occurred.

6. Recommendation D-6: Establish guidelines or regulations to enhance business practices for the financial management of reimbursable funds. Such guidelines could include:

- Establishing interest-bearing escrow accounts for long-term reimbursable projects, as done on contributed-funded projects;
- Refunding excess amounts to the customer if project features are delayed;
- Reviewing and adjusting, if necessary, estimated schedule of sponsor's costs for reimbursable projects for future fiscal years;
- Reviewing agreements and determining whether the sponsor's funds are properly managed by the districts.

USACE Response: Concur with the recommendations. The current regulation (ER 37-2-10) will be rewritten to incorporate the recommended guidance in change 89 which is scheduled for completion by 30 September 1997.

Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

ANNEX C

FINDING E: FOLLOW-UP CYCLE

The Corps continues to make progress in correcting two of the material weaknesses found in previous financial statement audits. Specifically, the Corps gave particular attention to management and control in the areas of:

- Real Property.
- Labor cost transfers.

For FY 96, the Corps reported Real Property as a corrected material weakness in its Annual Assurance Statement. Our audit results agreed with this assessment. Further, we noted that the Corps made significant improvements in reducing and justifying Labor Cost Transfers. While our review covered only four districts, and the results can't be projected to the entire Corps, these four sites appeared to have adequate controls over the transfers.

However, the Corps needed to strengthen management controls for Fund balance reconciliation. For example, the Corps should:

- Implement transactions that will capture revenue and expense as they are incurred, not just at year-end.
- Research and resolve discrepancies between the Balance Fund with Treasury and the Corps' records.

Additional Facts: None.

1. Recommendation E-1: Strengthen management controls over Fund balance with Treasury by:

- Implementing transactions that will capture revenue and expenses as they are incurred, not just at year-end.

USACE Response: Concur. CEFMS general ledger correlations currently record expenditures as they are incurred. CEFMS also records revenue for reimbursable orders as it is earned. CEFMS general ledger correlations for civil direct appropriations will be revised to capture revenue as it is earned. These revisions will be completed prior to 30 September 1998 to be effective 1 October 1998, start of fiscal year FY 99, the first full fiscal year that all USACE locations will be deployed on CEFMS.

-10-

Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

ANNEX C

- Establish analytical reconciliation procedures over the financial data produced by the financial management system to validate the integrity of the crosswalk.

USACE Response: Concur. The USACE Finance Center will develop additional reconciliation edits, incorporate in the upward reporting application, that must be passed before acceptance of the financial reports from the reporting activities (field locations). These reconciliations will compare the same financial data from different reports to ensure the credibility of financial data submitted. These reconciliation edits will be completed and placed in production by 1 March 1997. During the FY 97 SWD CFO audit the UFC will coordinate with USAAA and SWD to ensure integrity/credibility of the financial data.

- Develop procedures at the district level to research and resolve discrepancies between the districts Fund with Treasury Balance and the district records.

USACE Response: Concur. Standard procedures will be developed for implementation in the post CEFMS environment. Activities operating in the COEMIS environment will be advised of the need to establish local procedures to research and resolve discrepancies between the Treasury Balance and their records.

- Consider writing off absolute unreconcilable difference in order to balance the accounts.

USACE Response: Concur. Appropriate action will be taken to write off any unreconcilable differences that remain after CEFMS is fully deployed.

ANNEX C

FINDING F: PERFORMANCE MEASURES

For FY 96, the presentation of the Overview Information in the Corps' financial statements didn't reflect the Corps' progress in developing and reporting performance measures to portray its mission, resources, goals, and results. The degree of progress wasn't reflected because:

- The Corps was still in the process of preparing its Strategic Plan.
- Preliminary performance measures developed and initiated in FY 94 weren't implemented.

As a result, these conditions forced the Corps to use the same performance measures in FY 96 that it used in the previous fiscal years. However, to its credit, the Corps was in the final draft stages of its strategic plan and had performance measures to support the plan. According to Corps personnel, the first set of outcome-focused performance measures were part of the FY 98 budget preparation discussions sent to the Office of Management and Budget. These actions were still ongoing at the end of our audit.

Additional Facts: None.

1. Recommendation F-1: Reinforce the commitment of personnel to support the performance measure initiatives by including these efforts as a critical element or priority work item in the personnel performance standards and appraisal system.

HQUSACE Response: Partially Concur. We agree with USAAA's assessment that we have made good progress in developing outcome focused program performance measures. In fact, we have submitted a draft set of results oriented performance measures to OMB to begin a dialogue with them on developing the FY 99 Annual Performance Plan. We also agree with USAAA concerning increasing the commitment of personnel to support the performance measures initiative. Performance standards for development of performance measures are in the TAPES of the program manager for the comprehensive initiative. However, we do not agree that the time has arrived to introduce performance development requirements into the performance standards of the large number of team members involved. Such an increased commitment is premature. The timing of increasing the personnel commitment is sequentially sensitive to the completion of the consultation process on the Civil Works Strategic Plan. The increased commitment of personnel should take place after we have achieved internal and external consensus on our Civil Works strategic Plan. Consensus

Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"

---

ANNEX C

building involves working with OMB and Congress; and is an evolutionary and iterative process. Such consensus is necessary as a first order of business before the senior leadership increases their commitment of personnel to developing the performance measures. This sequencing will assure sound alignment between performance measures development and what evolves from the strategic plan. We are committed to the further development of results oriented performance measures; and to that end the increased commitment of personnel and resourcing of that development effort will naturally follow the maturing of the strategic plan.

**Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of Engineers, Civil Works"**

---

ANNEX D

**OTHERS RECEIVING COPIES OF THE REPORT**

Assistant Secretary of the Army (Civil Works)  
Assistant Secretary of the Army (Financial Management and  
Comptroller)  
Director of the Army Staff  
The Inspector General  
Chief of Public Affairs  
Deputy Chief of Staff for Personnel  
Deputy Chief of Staff for Logistics  
Assistant Chief of Staff for Installation Management  
Deputy Assistant Secretary of the Army for Budget  
Director, Program Analysis and Evaluation  
Commanders  
    U.S. Army Criminal Investigation Command  
    3d MP Group, USACIDC  
    6th MP Group, USACIDC  
Commandant, U.S. Army Logistics Management College  
Director, Center for Army Lessons Learned

Appendix B. AAA Report, "FY 96 Financial Statements: U.S. Army Corps of  
Engineers, Civil Works"

**ANNEX E**

**AUDIT STAFF**

Audit Control Point, Washington, DC

Patrick Fitzgerald, CPA, Program Director  
Martin Hagan, CPA, Auditor-In-Charge  
Rich Bachman, CPA  
Eric Watkinson  
Mark Morin  
Errol Murdock  
Sherry Masters  
Gordon Craig, CPA  
Krystal Nienaber  
Jay Parmar

District Sites

Huntington, West Virginia

Rich Bachman, CPA, Auditor-In-Charge  
Errol Murdock  
Debbie Knight  
Krystal Nienaber

Vicksburg, Mississippi

Hugh McNeil, Audit Manager  
Keith Jones, CPA, Auditor-In-Charge  
Jesse Allday  
Dave Gilbert  
Hershel Rodgers

Fort Worth, Texas

Jerry Smith, Audit Manager  
John Vollbracht, Auditor-In-Charge  
Karen Barber  
Fran Thomas  
John Arechiga  
Barry Flick

Anchorage, Alaska

Pat Daly, Audit Manager  
Felix Guzman, Auditor-In-Charge  
Mark Hohn  
Wayne Palmer  
Tom Bridges

St. Louis Administrative Center

Winifred Curran  
Dana Dold

---

## Appendix C. Audit Process

**Audit Work Performed.** To fulfill our responsibilities under the Chief Financial Officers Act of 1990, as amended by the Federal Financial Management Act of 1994, for determining the accuracy and completeness of the independent audit conducted by the AAA, we reviewed the AAA audit approach and planning, and monitored audit progress at key points.

**Reviewing AAA Audit Approach and Planning.** We used the President's Council on Integrity and Efficiency "Federal Financial Statement Audit Manual" as the criterion for reviewing the AAA audit approach. Specifically, we reviewed the following: the notification and engagement letters, opening conference documentation, strategy formulation, entity profile, general risk analysis, account risk analysis, audit programs, and cycle memorandums.

We reviewed additional documentation as deemed necessary to accomplish the audit objective. We also participated in an audit planning workshop conducted by AAA.

**Monitoring Audit Progress at Key Points.** Through the IG, DoD, Integrated Audit Process Team and the Executive Steering Committee, we provided a forum for a centrally managed exchange of guidance and information leading to a focused DoD-wide audit of the DoD consolidated financial statements, to include the supporting financial statements of major DoD Components. Audit initiatives for monitoring the progress of the audit at key points also involved reviewing and commenting on related draft reports issued by AAA, including the audit opinion report and the report on management controls.

In addition to the oversight procedures, we performed other procedures deemed necessary to determine the fairness and accuracy of the AAA audit approach and conclusions.

**Audit Period and Standards.** We performed this financial statement audit from May 17, 1996, through February 28, 1997. The audit was made in accordance with auditing standards issued by the Comptroller General of the United States, as implemented by the IG, DoD. We did not use computer-processed data or statistical sampling procedures to conduct this audit.

**Contacts During the Audit.** We visited or contacted individuals and organizations in the DoD audit community. Further details are available on request.

---

## **Appendix D. Report Distribution**

### **Office of the Secretary of Defense**

Under Secretary of Defense (Comptroller)  
Deputy Chief Financial Officer  
Deputy Comptroller (Program/Budget)  
Assistant Secretary of Defense (Public Affairs)  
Director, Defense Logistics Studies Information Exchange

### **Department of the Army**

Assistant Secretary of the Army (Financial Management and Comptroller)  
Auditor General, Department of the Army  
Commander, U.S. Army Corps of Engineers

### **Department of the Navy**

Assistant Secretary of the Navy (Financial Management and Comptroller)  
Auditor General, Department of the Navy

### **Department of the Air Force**

Assistant Secretary of the Air Force (Financial Management and Comptroller)  
Auditor General, Department of the Air Force

### **Other Defense Organizations**

Director, Defense Contract Audit Agency  
Director, Defense Finance and Accounting Service  
Director, Defense Finance and Accounting Service Indianapolis Center  
Director, Defense Intelligence Agency

## **Non-Defense Federal Organizations**

Inspector General, Department of Education  
Office of Management and Budget  
Technical Information Center, National Security and International Affairs Division,  
General Accounting Office

Chairman and ranking minority member of each of the following congressional committees and subcommittees:

Senate Committee on Appropriations  
Senate Subcommittee on Defense, Committee on Appropriations  
Senate Committee on Armed Services  
Senate Committee on Governmental Affairs  
House Committee on Appropriations  
House Subcommittee on National Security, Committee on Appropriations  
House Committee on Government Reform and Oversight  
House Subcommittee on Government Management, Information and Technology,  
Committee on Government Reform and Oversight  
House Subcommittee on National Security, International Affairs, and Criminal Justice,  
Committee on Government Reform and Oversight  
House Committee on National Security

## **Audit Team Members**

This report was prepared by the Finance and Accounting Directorate, Office of the Assistant Inspector General for Auditing, DoD.

F. Jay Lane  
Richard B. Bird  
John J. Vietor  
Craig W. Michaels  
Cheri D. Givan  
Susanne B. Allen