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UNITED STATES GENERAL ACCOUNTING OFFICE

WASHINGTON, D.C. 20548

RESOURCES AND ECONOMIC DEVELOPMENT DIVISION

JUL 24 1975

Lieutenant General W. C. Gribble, Jr.
Chief of Engineers
Corps of Engineers
Department of the Army

Dear General Gribble:

We have completed a review of certain financial activities of the Southeastern Federal Power Program and the overall results of our review will be included in a separate report to the Congress.

During our review at the Corps' Ohio River Division (ORD) and the South Atlantic Division, we noted several problem areas which we believe should be brought to your attention for corrective action. These matters--which will not be included in our report to the Congress--show a need for improvements in management controls and closer adherence to established accounting procedures. Such improvements are important to maintaining the reliability of financial statements for the Southeastern Federal Power Program and to establishing appropriate electric power rates.

NEED FOR IMPROVING MANAGEMENT CONTROLS

Our review of financial records of Corps multiple-purpose projects showed instances where (1) incorrect cost allocation percentages were used to distribute project costs, (2) incorrect rates were used to compute interest and depreciation expenses, (3) accounting records and reports were not reconciled, and (4) reallocation of project costs was not made on a timely basis.

Incorrect cost allocation percentages

Percentages, based on cost allocation studies, are used to allocate the cost of joint use facilities that serve more than one purpose of a multiple-purpose project. Two sets of percentages are developed, one applicable to construction expenditures--which is also used for allocating depreciation costs--and one for operation and maintenance (O&M) costs.

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Following are instances where the Corps' accounting offices used incorrect percentages for allocating either depreciation costs or joint operation and maintenance costs.

--The Savannah District used O&M cost allocation percentages in allocating annual depreciation charges for joint use facilities on the Kerr, Philpott, Clark Hill, and Hartwell projects rather than using the construction allocation percentages, as prescribed by Corps regulations (ER 37-2-10). The O&M percentages were used for allocating depreciation costs on these projects for fiscal years 1971 through 1974. The effect of using the incorrect allocation percentages in fiscal year 1974 was to overstate depreciation costs applicable to power, as follows:

	Over or (under) statement
Kerr	$19,696
Philpott	2,841
Clark Hill	413
Hartwell	(404)
	$22,546

--ORD used 18.40 percent in allocating joint depreciation cost to power at the J. Percy Priest project in fiscal years 1972 and 1973. ORD used 6.10 percent for allocating joint construction costs and should have used this same percentage for joint depreciation costs. The Division had detected the fiscal year 1973 error but its proposed corrective action would not completely correct the error. No adjustment was made for the fiscal year 1972 error. As a result, joint recreation depreciation costs were understated by about $44,000 and total joint flood control and power depreciation costs were equally overstated.

--The Savannah District allocated joint accounts receivable on the Clark Hill and Kerr projects at June 30, 1974, using construction rather than O&M cost allocation percentages. As a result, Clark Hill power receivables were understated by $628 and Kerr power receivables were understated by $23,491.

Incorrect interest rates

Each project has a fixed rate which is used in computing interest during construction, interest expense, and depreciation costs. The rate used in computing interest expense on current fiscal year O&M costs, and an interest credit on income, applicable to power projects, however, can change each fiscal year. We noted that some accounting offices had not used the correct interest rate when making computations of interest expense or depreciation.

- --The Savannah District used the current year's rate of 5 5/8 percent, instead of the project rate of 2 1/2 percent, to compute an adjustment to interest expense for amounts previously repaid on the Federal investment in the Clark Hill project. Interest expense is determined based on a formula which includes accounts with debit and credit balances. The use of the higher incorrect interest rate significantly increased the credit elements in the interest computation. As a result, total project interest expense was understated by about $977,000 of which $955,000 was applicable to the power program. This same type of error was made in calculating interest expense for the Hartwell, Kerr, and Philpott projects. The Southeastern Power Administration noted the large reduction in interest costs reported by the Corps and questioned the Corps' district office as to the validity of the amount reported. As a result, the Corps discovered its error and submitted revised financial statements which increased net interest expense applicable to the power program by over $1.7 million.

- --Total interest expense at the Millers Ferry project was understated about $79,000 by the Mobile District because the district used a 2 1/2 percent project rate instead of the correct rate of 2 5/8 percent. About $48,000 of the understatement of interest expense was applicable to the power program.

- --At the Mobile District, annual depreciation costs on the Jones Bluff project for fiscal years 1972 through 1974 was computed using a rate of 2 1/2 percent instead of the approved rate of 2 5/8 percent. This error resulted in accumulated depreciation on non-power functions being overstated by about $10,620 at June 30, 1974.

Accounting records and reports not reconciled

The ORD finance and accounting office prepared two records of outstanding accounts payable at June 30, 1974. One record contained a listing of the unpaid vouchers by date and amount, and the other record was a summary listing of the unpaid accounts by appropriation, project, and cost account. The summary listing, prepared only at the end of each fiscal year, is used by accounting personnel to allocate outstanding accounts payable by projects.

Our review disclosed that there was a difference of about $1.1 million between the totals on the two listings. As a result of our inquiry, Corps officials determined that an error existed in the computer program used to prepare the summary listing. The error had existed for several years and had not been detected because the summary listing had not been reconciled to the other accounts payable listing.

The Corps prepared a corrected computer program and, as a result of its use, the June 30, 1974, accounts payable applicable to the power program, were reduced by about $126,000.

The Chief of Systems and Procedures, ORD, told us that the computer programs that were used each year, such as the accounts payable summary listing, were not properly documented with such essential items as flowcharts, applications, and summaries of input and output data. Absence of such documentation may contribute to the failure to detect program errors, such as those in the accounts payable summary. The Chief, Finance and Accounting Center, ORD, told us that this type of error would not occur again because a new computer system (COEMIS) was being installed and all programs under that system would be fully documented.

Also, the amount of contractor's earnings withheld on a contract for work at the Cordell Hull Project was recorded at about $83,275 more than had actually been withheld. The Examination Branch in the accounting office computed and maintained a listing of the amount of the contractor's earnings withheld and refunded, and the Finance Section recorded the amounts withheld in the accounting records. According to a Corps official, the error resulted because the Finance Section improperly recorded some refunds as an increase in contractor withholding. Although we were told by a Corps official that the Corps periodically reconciles and verifies the accuracy of its records, we noted that part of the error dated back to 1972.

Reallocation of project cost not done on a timely basis

The final cost allocation report on the Walter F. George project was adopted by the Chief of Engineers on May 9, 1973, as a basis for distributing costs among the authorized project purposes. Retroactive adjustments to the accounting records were required because the project began operation in 1963 and costs recorded from that date were based on tentative allocations. The Mobile District did not receive the approved cost allocation report in time to adjust the accounting records at June 30, 1973, but did reallocate the costs for the fiscal year 1974 statements.

Although the district adjusted the accounting records in June 1974, the adjustments were estimated amounts and were not based on a detailed reallocation of project cost. District officials said that they had not had the time to make the reallocation and do the other accounting work required at the end of the fiscal year. They told us that the reallocation would be made during fiscal year 1975.

We agree that the close of the fiscal year was probably not the appropriate time to complete the reallocation of the Walter F. George project costs due to the year-end closing of accounts and preparation of financial statements. However, the district was aware in July 1973 that a firm allocation had been adopted, and reallocation of project costs should have been undertaken sometime during fiscal year 1974.

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The error in contractor earnings withheld at ORD was corrected in December 1974. Corps accounting officials told us that they would correct the items discussed above.

ACCOUNTING PROCEDURES WERE NOT FOLLOWED OR WERE APPLIED INCONSISTENTLY

We noted several instances where Corps accounting procedures were not being followed or were being inconsistently applied by the Corps accounting offices.

Transfers to plant-in-service

Our review of interest computations for periods when transfers are made from work in progress to plant-in-service accounts disclosed that the Mobile and Nashville Districts were not following the procedure required by the Corps accounting manual (ER 37-2-10, Chapter 8-7). The manual provides that interest will be computed monthly and charged to construction cost (interest during construction) from the start of construction until the date of transfer to plant-in-service. As of the first of the following month, interest as a charge to construction ceases and interest expense charged to operations commences on the costs transferred to plant-in-service.

Interest during construction applicable to the power program was understated by about $60,000 for the J. Percy Priest project, primarily because cost applicable to the power program were included by the Nashville District in flood control and recreation costs when those costs were transferred to plant-in-service. The flood control and recreation costs were transferred to plant-in-service before power costs were transferred. A similarly incorrect procedure was used by the Mobile District for the Millers Ferry project, but we did not compute the amount of the understatement of interest expense involved.

Basis for costs transferred

Corps regulations (ER 37-2-10, Chapter 8-7) provide that costs transferred to plant-in-service will be the total estimated cost of the specific facilities plus the portion of the total estimated joint use facilities cost allocated to that purpose. Later, when all project purposes are in service, plant-in-service accounts are to be adjusted to agree with actual costs.

Our review of transfers of cost from work in progress to plant-in-service accounts on the Cordell Hull, J. Percy Priest, and Millers Ferry projects showed that a different basis was being used to record the initial transfer of completed functions to plant-in-service.

On the Cordell Hull project, ORD used estimated direct construction costs but actual engineering and design, and supervision and administration costs incurred at the time of transfer. The Mobile and Nashville Districts, however, used only estimated costs on the Millers Ferry and J. Percy Priest projects, respectively, when transferring costs to plant-in-service. The use of actual costs incurred at the time of transfer understated the plant-in-service accounts. For example, the actual engineering and design costs accumulated to August 1973, date of the transfer of the cost of the first power unit at Cordell Hull to plant-in-service, totaled about $4,976,000 whereas the estimated cost on which the transfer should have been based was $5,106,000.

CONCLUSIONS

We believe that the matters discussed above show the need for closer adherence to Corps' accounting instructions and for additional supervisory review of the work performed by personnel involved with accounting and other records applicable to multi-purpose water resources projects.

RECOMMENDATIONS TO THE CHIEF OF ENGINEERS

We recommend that the applicable Corps Division and District Offices be required to correct the accounting and other matters discussed in this report and to provide additional supervisory review of the work performed by personnel involved with accounting and other related records on multi-purpose water resources projects.

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We would appreciate receiving your comments on the matters discussed in this report and being advised of the corrective actions that will be taken. We wish to express appreciation for the cooperation extended to our staff during our review.

Copies of this report are being sent to the Corps' Division Engineers of the Ohio River Division and South Atlantic Division and to the Chief, U.S. Army Audit Agency.

Sincerely yours,

Harold Pichney

Harold Pichney
Assistant Director