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UNITED STATES GENERAL ACCOUNTING OFFICE
REGIONAL OFFICE
7014 FEDERAL BUILDING 1961 STOUT STREET
DENVER, COLORADO 80202

MAR 8 1971

Mr. James M. Ingles
Regional Director, Region 7
U. S. Bureau of Reclamation
Building 20, Denver Federal Center
Denver, Colorado 80225

Dear Mr. Ingles

The General Accounting Office has made a review of the operation of the Missouri River Basin Integrated Projects as conducted by the Bureau of Reclamation and the Corps of Engineers. Our review included an examination of administrative practices and procedures, an evaluation of internal controls, and such tests of the financial transactions as we considered necessary.

The overall results of our review relating to the consolidated operation and financial position of the integrated projects will be covered in a separate report to the Congress. At Region 7 of the Bureau of Reclamation we generally found the administrative procedures and controls to be adequate. However, we noted the following matters which were discussed with you and members of your staff during our exit conference. We would appreciate your comments especially as they relate to any proposed or accomplished corrective action.

CLASSIFICATION OF REHABILITATION AND BETTERMENT COSTS AS DEFERRED MAINTENANCE

Rehabilitation and betterment work on the North Platte Project costing $6,558,915 originally recorded as irrigation plant in service was reclassified as deferred maintenance and transferred to account 220, Other Charges Funded, on June 30, 1966. This action was taken after review of internal audit reports which questioned capitalization of practically entire amounts as irrigation plant in service. Regional justification stated that because much of the work performed was deferred maintenance, replacement accounting (which would involve retirement procedures) was not contemplated. It further stated that the journal voucher should contain a statement that if it is later determined that any portion of the work is considered as addition to plant, with no corresponding retirement, the cost will be capitalized as irrigation plant and transferred to account 102.1.

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We were advised that the rehabilitation and betterment work primarily involved replacement of unlined earth water supply and distribution works with pipe or concrete lined facilities. In some instances the new facilities were placed in the same location as prior facilities, while in other instances they were relocated and old facilities abandoned, however, information showing the specific locations where existing and new locations were used had not been accumulated. We were advised by members of your staff that considerable work would be required to obtain this data and the cost would not justify such an undertaking since the water users are obligated to repay the costs regardless of whether they are classified as irrigation plant in service or deferred maintenance.

We believe that the proper accounting treatment for improvements and betterments depends upon whether it is of a major or minor nature and is not affected by the reimbursability or non-reimbursability of the work accomplished. Major expenditures should be capitalized and the cost of the item replaced should be eliminated from the asset account We agree that a costly detailed analysis of both rehabilitacion and betterment work for the purpose of making a precise reclassification of costs may not be warranted. We also agree that identification of costs which should be retired may no longer be practical at this late date. It is our opinion, however, that the cost of concrete pipe and canal linings (which both the internal audit report and members of your staff state are betterments) should be capitalized as irrigation plant.

We recommend that action be taken to determine or estimate the cost of such betterments and that accounting records be adjusted accordingly.

ACCOUNTING FOR PLANT RETIREMENTS

Our review disclosed a number of instances where all components of construction costs were not used for recording plant retirements as prescribed by Reclamation Instructions 464 1.10C.

Project	Item	Costs excluded from retirement
Missouri River Basin	Transformer-Ogallala Substation	$ 20,695
" " "	Transformer-Lovell Substation	42,976
" " "	Transformer-Sinclair Substation	20,510
" " "	Transformer-Lovell Substation	15,095
" " "	Boysen Camp	247,000a/
Riverton	Turbine runners-Pilot Butte Power Plant	b/

a/Approximate amount.
b/Amount not determined. New runners installed without retiring existing runners.

The above cases of improper accounting for plant retirements have resulted in the plant accounts being overstated by the costs excluded from the retirement transactions, and have also distorted the annual provision for depreciation computations.

During our exit conference the above errors were acknowledged and we were advised that corrective action had been or would be taken and that all retirement transactions would be reviewed for similar errors. We were further advised that a new computer operated system was being developed which would preclude the occurrence of future errors of this nature

COMPUTING AND ACCOUNTING FOR DEPRECIATION

The following deficiencies in computing and accounting for depreciation were noted during our review.

1. Depreciation factors

The depreciation factors established for the Boysen and Glendo units of the Missouri River Basin Project to implement the compound interest depreciation method were not properly developed All multipurpose land and land right costs were included in the base used to establish the composite lives and depreciation rate factors, whereas, only that portion of these costs allocated to the power production purpose should have been included.

After we brought this matter to the attention of your staff, action was taken to correct the Boysen unit rate factor. In addition an adjusting entry was processed to properly record an additional depreciation accrual of $190,739 which was required as a result of the rate factor adjustment. We were advised that corrective action was not initiated for the Glendo unit because the dollar amount of the error was not significant. Furthermore, they pointed out that new studies to establish service lives and rate factors are required as of June 30, 1970, and that the Glendo unit would be adjusted at that time.

We believe that the accomplished and planned corrective action has adequately resolved this matter.

2. Depreciation on movable equipment

Fiscal year 1968 and 1969 movable equipment depreciation accruals were not computed in accordance with Reclamation Instructions 489.1.5

This instruction states that movable equipment depreciation should be computed on the balances in the equipment accounts, less estimated salvage, using straight-line depreciation rates The region deviated from the above instruction by also excluding net accumulated reserves.

Agency officials advised us that this method was used because their equipment in some composite accounts was fully depreciated. It was their opinion that not up-dating movable equipment on the older projects had caused the depreciation problem. They also stated that the depreciation rates prescribed by the Reclamation Instructions were equitable and based on sound criteria.

Reclamation Instructions permit the computation of depreciation on an individual item basis when automatic data processing equipment is used. We believe that consideration should have been given towards obtaining permission from the Commissioner to use the individual item basis or to exclude fully depreciated items from the base

We recommend that the region advise the Commissioner on the movable equipment depreciation circumstances, and request permission to either compute depreciation on an individual item basis or deviate from the prescribed procedures by excluding fully depreciated items from the composite account balances.

3. Electric facilities acquired with contributed funds not subject to depreciation

The fiscal year 1963 through 1969 depreciation accruals were understated for one or more projects because contributions in aid of construction were excluded from the net plant subject to depreciation We were advised that this procedure was followed in order to show the net plant subject to depreciation in agreement with the unpaid investment subject to interest computations on the Power Systems Average Rate and Repayment Studies.

Region officials agreed that contributions in aid of construction should not be excluded from net plant subject to depreciation. They advised us that adjustments have been made for all projects except Kendrick, and that an adjustment for the Kendrick project was currently being made. They also advised us that a letter has been sent to the Commissioner concerning the treatment of contributions on the Power Systems Average Rate and Repayment Studies, and that no further action will be taken until official comments are received from the Commissioner's Office.

We believe that the accomplished and planned corrective action will adequately resolve the incorrect depreciatior accrual computations. The letter sent to the Commissioner's Office has also properly advised him of the problem concerning the presentation of contributions on the Power Systems Average Rate and Repayment Studies.

4. Provision for depreciation

Plant in service, other than movable property, was depreciated using the compound-interest method of depreciation This method includes the computation of interest on the reserve for depreciation. Movable property was depreciated using the straight-line method

When computing interest on the reserve for depreciation under the compound-interest method, the Bureau has not removed the reserve for depreciation for movable property before applying the interest factor.

We believe that the application of an interest factor to the reserve for depreciation for movable property violates the straight-line depreciation concept and inflates depreciation charges related to plant in service thus creating a reserve which will eventually exceed the value of the assets being depreciated.

We recommend that the reserve applicable to movable property be excluded from the computation of interest on the depreciation reserve.

As was pointed out during our exit conference we believe this problem could be eliminated if movable property were not included in plant in service but instead identified separately, similar to service facilities. We believe that movable property would be better identified in its own classification and we recommend that the possibility of excluding movable property from plant in service be explored.

We wish to acknowledge the cooperation given our representatives during the review. Your comments and advice as to the action taken or contemplated on the matters discussed above will be appreciated.

A copy of this letter is being sent to the Commissioner, Bureau of Reclamation.

Sincerely yours,

S D. McElyea
Regional Manager