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

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APR 12 1971

Mr. Harold E. Aldrich
Regional Director, Region 6
Bureau of Reclamation
P.O. Box 2553
Billings, Montana 59103

Dear Mr. Aldrich:

The General Accounting Office has made a review of the operations of the Missouri River Basin (MRB) Project and the integrated projects through June 30, 1969. The review was performed in Region 6 and Region 7 of the Bureau of Reclamation, Department of the Interior, and the Omaha District, Corps of Engineers, Department of the Army.

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 6 of the Bureau of Reclamation we generally found the administrative procedures and controls to be adequate. However, during our review various matters which require correction or resolution were identified.

The following have been discussed with you and your staff. These items are being reported to you since corrective action had already been taken or was contemplated on many of the items and we would appreciate your comments especially as they relate to accomplished or proposed corrective action.

ALLOCATION OF CONSTRUCTION COSTS AND OPERATION AND MAINTENANCE EXPENSE

1. Preparation of the Statement of Project Cost and Repayment; the Power System Average Rate and Repayment Study; and the computations of interest on investment, provision for depreciation, and interest during construction all take place shortly after the close of the fiscal year. However, inconsistent rates were used for allocating

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multipurpose plant to the purposes served by the project. For example, the rates used for allocating multipurpose plant to power for the Yellowtail Unit during fiscal year 1969 were as follows:

Description	Percentage
Statement of Project Cost and Repayment - June 30, 1968	34.47
Average Rate and Repayment Study - June 30, 1968	34.57
Interest on commercial power - FY 1969	34.57
Provision for depreciation - FY 1969	62.3
Interest during construction - FY 1969	62.16

Also, Reclamation Instructions 116.5.9 states that annual operation and maintenance (O&M), replacement, and investment costs shall be allocated concurrently. We found that the ultimate development rates for allocating multipurpose O&M to purposes served did in some cases equal the current-use rates but these rates were not those actually used to allocate multipurpose plant costs for the same purpose. For example, the Allocation of Cost of Operation and Maintenance of Multipurpose Facilities and Other Joint Works, CY 1969-1972, dated February 24, 1969, stated that the ultimate development rate and the current-use rate for allocating multipurpose O&M to power for the Yellowtail Unit was 42 percent; yet, this rate equaled none of those used above for allocating plant costs.

We were unable to determine which, if any, of the above allocation rates used were official. We believe that all unit rates for allocating multipurpose plant and O&M for functions developed as ultimately planned should be properly established, reviewed, and communicated to all interested parties for consistent application in the accounting records and reports.

During our exit conference members of your staff commented that this resulted from a lack of communication of official allocation rates, but advised that steps would be taken to correct this matter. We recommend, in addition, that the applicable finance offices make a review to determine what effect the use of inconsistent allocation rates has had on the accounting records and that appropriate adjustments be made when the effect is determined to be material.

2. The Allocation of Cost of Operation and Maintenance of Multipurpose Facilities and Other Joint Works, CY 1969-1972, dated February 24, 1969, indicated in some cases, that O&M allocated to "Other Irrigation" on ultimate development should be charged fully to flood control in the current-use allocation.

We believe that the charging of all "Other Irrigation" O&M to flood control may not give proper distribution to these costs if other purposes currently benefit from the use of water ultimately planned for "Other Irrigation." We believe such costs should be distributed to all active purposes of the unit or project.

We recommend that the current distributions of O&M ultimately allocated to "Other Irrigation" be re-examined to consider distribution of such costs to all other purposes currently benefiting from the use of water ultimately planned for "Other Irrigation."

INTEREST ON INVESTMENT

Under provisions of the Reclamation Act of 1939 interest expense shall be charged on that part of the construction costs allocated to municipal water supply or other miscellaneous purposes, if the Secretary determines an interest rate to be proper. However, as of June 30, 1969, no interest expense had been charged on any of the applicable MRB Project units.

After bringing this to the attention of Finance officials, interest expense of $93,494 for the Helena Valley Unit (which includes the Canyon Ferry Unit for M&I water) and $60,416 for the Oahe Unit-James Section was charged into the accounts during FY 1970, including the retroactive adjustments through FY 1969. Subsequently, in FY 1971, interest expense of $453,219 for the Rapid Valley Unit was charged to interest expense.

Since the other units are either exempt or interest being deferred--Dickinson was said to be exempt because an interest component had not been included in the M&I rates approved by the Secretary and Yellowtail interest expense was being deferred under provisions of the Water Supply Act of 1958 until the water supply is actually used--we are making no further recommendations at this time.

INTEREST DURING CONSTRUCTION

1. Computations of IDC in the Missouri-Souris Projects Office contained errors as discussed below:

a. In computing IDC for FY 1964, the amount recorded on line 13c of the Report on Budget Status was inadvertently used instead of current year disbursements for the Transmission Division. As a result, the amount used as current year disbursement was understated by $2,210,747. Therefore, IDC for FY 1964 was understated by $22,301 computed as follows:

$\$2,210,747 \div 2 = \$1,105,374$

$\$1,105,374 \times 80.7\% \times 2.5\% = \$22,301$

b. In FY 1965 and subsequent years IDC has been incorrectly computed due to:

1. The carry forward affect of a. above,

2. Use of 81.3 percent to compute commercial power rather than 80.7 percent as set forth in the Report on Financial Position, December 1963, and

3. Nonrecognition of the 83-17 percentage basis for computing IDC at the 2.5 and 3 percent rates as provided by the Regional Office letter dated June 9, 1966. All of the IDC was computed at 2.5 percent.

We recommend that appropriate adjustments be made to correct IDC for fiscal year 1964 to date.

2. In accordance with the Acting Regional Director's letter of June 9, 1966, to the Project Manager-Bismark and Huron, IDC for FY 1966 and subsequent years for the Transmission Division was computed at 2.5 percent on 83 percent of the annual disbursements and at 3 percent on the 17 percent balance associated with the Bureau. But, no mention was made of the rate to be used on the Bureau's production plant.

Subsequently IDC has been computed at 2.5 percent for the Yellowtail Unit production plant. We believe that the use of 2.5 percent for IDC for the Bureau production plant is inconsistent with the application of 3 percent for IDC for the Bureau's share of Transmission Division. We recommend that the Bureau adjust the IDC for the Yellowtail Unit production plant since FY 1966 to reflect 3 percent for IDC and to be consistent with the June 9, 1966, letter cited above.

During our exit conference we were advised that Yellowtail was the only project affected and corrective action would be taken to reflect IDC at 3 percent on production plant.

PROVISION FOR DEPRECIATION

1. 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 which results in 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.

We believe that 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.

2. Depreciation charges consist of an annuity portion and a computation of interest on the reserve. In computing depreciation for Canyon Ferry Transmission Division the Regional Office used 3 percent rate factors in the annuity portion but interest on the reserve was computed using 2.5 percent and 3 percent rates after allocation of the reserve on the 83-17 percent basis (Public Law 89-108).

Proper computations require that both the annuity portion and the interest on the reserve be computed on the same basis. Thus, Transmission Division plant costs being depreciated should be allocated on the 83-17 percent basis with the annuity portion also computed using the 2.5 and 3 percent rate factors.

We further point out that the Canyon Ferry production plant is part of the Bureau's 3 percent investment and not subject to the 83-17 percentage allocation. However, in FY 1969 interest on the production plant reserve was computed by using the proper 3 percent rate but the rate was applied to only 83 percent of the reserve, instead of 100 percent.

We recommend that these be corrected in the future.

3. In computing the provision for depreciation for the Yellowtail Unit in FY 1968 and 1969, a rate factor of 0.00465358 was used. Reclamation Instructions provided that a rate factor of 0.00225556 was to be used.

After we brought this to the attention of Finance officials action was taken to correct depreciation for FY 1968 and 1969 and an adjustment of $283,404 was recorded. However, in both the original computation and the adjustment for FY 1969 only 83 percent of the reserve for depreciation was subjected to interest, instead of 100 percent.

We recommend that a review be made to determine the significance of the errors in the depreciation adjustment and, if material, an amended adjustment be made.

OTHER

1. Account 107.1, Construction Work in Progress - General Construction for the MRB, contains $124,164 of investigations costs for the Transmission Division. These costs have not changed in amount at least since June 30, 1960, and we were told that there is no plan to construct the facilities for which these costs were incurred.

We recommend that action be taken to remove these costs from account 107.1 and charge them to account 116.9 - Investigations of Abandoned Works.

2. Cost Authority No. 68 for the Lower Marias Unit authorized the installation of perforated pipe and the repair of concrete gutters on the spillway. The Cost Authority cited account 107.3 - Operation and Maintenance Construction.

However, the completion report cited account 821.3 - Maintenance of Dams and Waterways and the costs for Cost Authority No. 68 were expensed.

We were told that the installation of drains was an improvement and that the drains did not exist formerly.

We believe that these costs should be capital costs and recommend that the costs associated with drains installation be capitalized instead of expensed.

3. Account 117.1 Settlers Assistance Costs (Transitional Development Costs) for the Shoshone Project was $616,309. This sum had not changed at least since June 30, 1960. Other projects also have entries in account 117.

We believe that account 117 was not intended to be a permanent account for costs originally charged there. We believe settlers assistance costs and future years capacity provisions should be removed from account 117 and charged to nonreimbursable expense when it is determined that the project or project unit on which these costs were incurred will not be developed as planned. We believe that only those costs associated with planned future construction should be retained in account 117 and then only until the construction is complete. Once the construction is complete, we believe these costs should be capitalized in the plant-in-service accounts and their reimbursability should be established.

We recommend that a review be made of these costs and similar costs in other projects to determine their status and that action be taken to transfer these costs to plant-in-service or that authority be requested to charge them off as nonreimbursable.

4. A Bill for Collection for the costs of O&M allocated to the Angostura Irrigation District was issued and recorded in the fiscal year prior to the year in which these charges were due. In our opinion this action distorted the amount of accounts receivable and irrigation income in the year the bill was recorded.

We recommend that these bills be handled in such a manner as to record the receivable and the income in the year in which the bill is actually due.

5. Articles 5(a), 5(b), and 5(c) of repayment contract No. 14-06-600-1302 with the Western Heart River Irrigation District state in essence that each year after the development period the district will pay to the United States $0.57 for each acre irrigated. The contract states that if the $0.57 per acre is less than the district's share of the total cost of operation and maintenance for the supply works during any year, the difference will be added to the district's next payment.

The Allocation of Cost of Operation and Maintenance of Multipurpose Facilities and Other Joint Works, CY 1969-1972, dated February 24, 1969, stated that the district's allocation of joint O&M was 10.7 percent but that this was limited to $761.10 ($0.30 x 2537 irrigable acres).

In 1968 and 1969, the Bureau collected $1,446.09 annually, which is $0.57 for each of 2,537 acres; but in accordance with the O&M allocation statement above, only $761.10 applies to payment of the district's O&M even though the district's share of O&M exceeds the $761.10. The additional $0.27 per acre has been applied to repayment of the investment in the supply works.

The district's O&M in excess of $0.30 per acre was allocated to non-district water users and to nonreimbursable flood control and fish and wildlife.

We believe that the provisions of article 5 are not being properly applied. We do not believe that the contract guarantees $0.27 per acre for repayment of the supply works nor does it limit the O&M chargeable to the district to $761.10.

It appears that to properly apply the contract provisions in article 5, the Bureau should first apply all the revenues from the district to repay the district's share of O&M and then apply only the excess revenue to repayment of the investment in the supply works.

We recommend that the provisions of article 5 be reviewed to determine if these provisions are properly applied and that any necessary corrective action be taken.

We wish to acknowledge the cooperation given our representatives during the review. Your comments and advice as to the action taken 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