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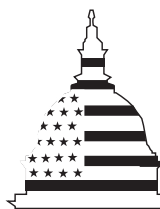
Report to the Chairman, Subcommittee  
on Water and Power, Committee on  
Resources, House of Representatives

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May 2000

**BUREAU OF  
RECLAMATION**

**Information on  
Operations and  
Maintenance Activities  
and Costs at  
Multipurpose Water  
Projects**



**G A O**

Accountability \* Integrity \* Reliability

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**United States General Accounting Office**  
Washington, D.C. 20548

**Accounting and Information  
Management Division**

B-283210

May 31, 2000

The Honorable John T. Doolittle  
Chairman, Subcommittee on Water and Power  
Committee on Resources  
House of Representatives

Dear Mr. Chairman:

This report responds to your request that we review the Bureau of Reclamation's operation and maintenance (O&M) of federal water projects. In response to our previous work regarding the Bureau's sources and uses of funds at the multipurpose water projects it operates and maintains, you asked us to review in more detail the Bureau's O&M activities. Specifically, you asked us to answer the following questions:

- How does the Bureau define O&M activities?
- What latitude does the Bureau have in deciding which O&M costs to charge to customers?
- How does the Bureau account for O&M costs?
- How does the Bureau define overhead?
- How does the Bureau calculate the O&M costs that it charges to customers?
- What concerns have been raised by customers about excessive O&M costs and to what extent do customers have an opportunity to review cost origins and recommend reductions?
- How do the Bureau's cost recovery practices compare to those of other entities?

To respond to your request, we conducted audit work at the Bureau's Washington, D.C. headquarters and Denver, Colorado office, and at its Mid-Pacific and Pacific Northwest regions. We also conducted audit work at the U.S. Army Corps of Engineers, State of California, and at the offices of representatives from water users' interest groups and customers from projects representing most of the Bureau's O&M costs in the Mid-Pacific and Pacific Northwest regions. We interviewed knowledgeable personnel at each audit site to obtain information relevant to the questions we were asked to answer.

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We also reviewed and analyzed relevant legislation and documents, including (1) reclamation law, (2) a 1998 Bureau report to Congress on O&M activities,<sup>1</sup> (3) a 1999 Bureau cost accounting report,<sup>2</sup> (4) federal guidance for determining and accounting for the full costs incurred by federal agencies in providing goods and services, (5) Corps documents pertaining to O&M activities and cost accounting, (6) State of California documents pertaining to O&M activities and cost accounting, and (7) customers' bills and contracts related to the Bureau's water-related activities. In addition, we obtained written responses from Bureau officials to document the Bureau's position on selected questions and observed a budget review meeting held by the Mid-Pacific Region for its customers.

The scope of our review included the Bureau's O&M activities and costs related to the Bureau's delivery of water for irrigation and municipal and industrial uses, but did not include reviewing the Bureau's efficiency in performing O&M activities or incurring the related costs. We conducted our review from June 1999 through March 2000 in accordance with generally accepted government auditing standards. We provided the Department of the Interior and the Bureau of Reclamation copies of a draft of this report for review and comment. They generally agreed with the thrust of our report's conclusions and recommendations. We have incorporated their views, including certain technical comments from the Bureau, into the report, as appropriate, and have reproduced the comment letter in appendix II. Appendix I describes our objectives, scope, and methodology in detail.

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## Background

The Bureau of Reclamation operates single and multiple-purpose water projects. Major project purposes include supplying water for irrigation and for municipal and industrial use; producing hydropower; and providing for flood control, recreation, and fish and wildlife protection. The facilities necessary to serve these purposes are diverse, as are the related operations and maintenance activities conducted by the Bureau.

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<sup>1</sup>*Annual Costs of Bureau of Reclamation Project Operation and Maintenance for Fiscal Years 1993-97*, Bureau of Reclamation, September 1998.

<sup>2</sup>*Standard Processes of Costing Business Practices*, Bureau of Reclamation, September 30, 1999.

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The Bureau's costs of operating and maintaining its projects are classified as either reimbursable or nonreimbursable. Reimbursable costs are recovered from customers; nonreimbursable costs are not and are instead borne by the federal government. Generally, costs associated with supplying water for agriculture and for municipal and industrial use and hydroelectric generation are reimbursable. Costs that are related to these reimbursable purposes, either directly or indirectly, are to be distributed or allocated to those purposes. Reimbursable costs are billed to, and recovered from, water supply and power customers. Costs related to power generation generally are recovered by the federal power marketing administrations (PMA) through power rates. Costs related to flood control, recreation, and fish and wildlife enhancement generally are nonreimbursable.

The Bureau's major funding appropriation for O&M activities is the Water and Related Resource appropriation, which is included in the Energy and Water Development Appropriation. The costs funded by this appropriation can be related to either reimbursable or nonreimbursable purposes. The Bureau also receives a Policy and Administration appropriation. Costs funded by this appropriation are nonreimbursable by law.

In September 1997 the Conference Committee for the 1998 Energy and Water Development Appropriations Bill asked the Bureau to prepare a report on the O&M costs of its projects for fiscal years 1993 through 1997. This included a request that the Bureau report total annual O&M costs and the amount and percentage of those costs attributable to overhead for each project. The Bureau's report in response to this request was issued in September 1998.

Because of the number and diverse nature of the questions you asked us to address, we are responding in a question and answer format. The answers to your specific questions follow.

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## How Does the Bureau Define O&M Activities?

The term operations and maintenance, or O&M, is commonly used by many different types of organizations in referring to the normal activities they undertake in conducting their endeavors. The Bureau defines operations as "activities related to the normal performance of the functions for which a facility or item of equipment is intended to be used." Examples of operations costs include the costs of operating facilities and equipment, utilities (electricity, water, sewage), fuel, janitorial services, window cleaning, rodent and pest control, upkeep of grounds, vehicle rentals, waste

management, and salaries and wages for personnel who perform these functions.

The Bureau defines maintenance as “the upkeep of constructed facilities and structures and capitalized equipment necessary to realize the originally anticipated useful life of a fixed asset.” The Bureau incurs maintenance costs for activities such as preventive maintenance, replacement of parts or components of equipment, periodic inspection and assessment of the condition of equipment, periodic adjustment, lubrication, and cleaning (nonjanitorial) of equipment, painting and resurfacing, special safety inspections, and other actions to ensure continuing service and to prevent breakdown. Examples of typical Bureau O&M activities are shown at table 1.

**Table 1: Examples of Bureau of Reclamation O&M Activities**

<b>Operations</b>	<b>Maintenance</b>
• Monitoring river flows	• Upgrading or replacing automated control systems
• Operating the gates and valves in a dam for water releases	• Painting and refinishing facilities, such as dam gates and office buildings
• Preparing annual operating plans	• Ordering and maintaining equipment and parts inventories
• Long-range forecasting of river conditions	• Inspecting facilities and equipment at regular intervals
• Reporting on the results of project operations	• Periodically tearing down, inspecting, and rebuilding pumps and other equipment
• Developing and updating standing operating procedures	• Lubricating equipment at prescribed intervals
• Land resources management activities	
• Environmental compliance activities	
• Administering the laws and contracts that apply to water projects	
• Responding to occasional emergencies	
• Keeping irrigation canals free of weeds	
• Health and safety code compliance activities	
• Handling and managing hazardous materials	
• Bureau review of O&M performed by customers of Bureau-owned facilities	

Source: *Annual Costs of Bureau of Reclamation Project Operation and Maintenance for Fiscal Years 1993-97*, Bureau of Reclamation, September 1998.

Our review of reclamation law did not surface any legally encompassing definition of the activities that comprise the operation and maintenance of Bureau facilities. Federal courts have confirmed the Secretary of the

Interior's broad discretion to define what can properly be assessed as O&M expense. This discretion is constrained by the provisions of appropriations acts and other authorities. Bureau contracts require that water supply customers pay for O&M expenses assigned to irrigation or municipal and industrial purposes. Some contracts generally define what O&M expenses are. For example, one contract for the supply of irrigation water provides that the

"costs which make up the construction and operation and maintenance obligations to be paid by the Contractor to the United States under this contract shall embrace all expenditures of whatsoever nature or kind in relation to the function for which the charge is made, including, but without limitation by reason of this enumeration, cost of surveys and investigations, labor, property, material and equipment, engineering, legal work, superintendence, administration, overhead, general expenses, inspections, special services, and damage claims of all kinds, whether or not involving the negligence of officers, agents, or employees of the United States. The Secretary's determination as to what costs are properly chargeable, the amount thereof, and the classification of those charges for repayment purposes shall be conclusive."

The Bureau defined the O&M activities associated with its projects in its 1998 report to Congress by describing its complex mission and by providing examples of the widely varied activities it conducts. The report stated that the Bureau is "responsible for the O&M of an extensive infrastructure of constructed facilities, including diversion and storage dams, pumping plants, powerplants, canals and laterals, pipelines, and drains." Further, it said that the Bureau is "also responsible for management of the federally owned lands on which these facilities are located and for the natural and cultural resources of those lands."

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## What Latitude Does the Bureau Have in Deciding Which O&M Costs to Charge to Customers?

The Bureau's ability to determine which O&M costs to charge to customers is governed by general provisions of reclamation law, project-specific legislation, and specific provisions of contracts the Bureau enters into with water users. Within these constraints, the Bureau<sup>3</sup> has broad discretion in defining which of the activities it undertakes constitute O&M that can be charged to customers. Federal accounting standards and guidance provided by the Office of Management and Budget (OMB) indicate that the full costs incurred by the federal government in providing services should

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<sup>3</sup>The authority to make this determination is delegated to the Bureau by the Secretary of the Interior.

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be recovered from beneficiaries of those services, unless such cost recovery is legislatively precluded.

We reviewed the Bureau's exercise of its discretion in determining which O&M costs to charge to customers in four areas. The areas we reviewed were Policy and Administration costs, costs funded with Area Manager funds, Associated O&M Program costs, and certain employee benefit costs. We found that, in accordance with specific legislation, the Bureau was not recovering the Policy and Administration costs. For the other three categories of costs, we found that the Bureau was not recovering them even though certain of these costs are recoverable and guidance contained in OMB Circular A-25 and federal accounting standards indicates that the costs should be recovered. Each of these areas is discussed in the following sections.

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### **Appropriations Act Prohibits Recovery of Policy and Administration Costs**

The Bureau classifies all costs funded from its Policy and Administration appropriation as nonreimbursable. As such, the costs are not recovered from customers. We reviewed the Bureau's authority for classifying costs funded by the Policy and Administration appropriation as nonreimbursable and found that the legal basis for excluding costs funded by the Policy and Administration appropriation from recovery is clear. The Bureau's fiscal year 2000 appropriations act, for example, specifically states that the Bureau's Policy and Administration Appropriation is to be nonreimbursable.

We reviewed a limited number of costs funded by the Bureau's Policy and Administration appropriation in 1998 and found that they were reasonably in accordance with the definitions of Policy and Administration costs that the Bureau provided to Congress in its budget request.



## Certain Other Costs the Bureau Does Not Recover Can and Should Be Recovered

The Bureau does not recover certain other costs indirectly related to water supply that are not specifically exempted from recovery by legislation. These indirect costs should be recovered from customers in accordance with OMB Circular A-25, which provides guidance for federal agencies to use in setting fees to recover the full costs of providing goods or services.<sup>4</sup> OMB Circular A-25 defines full costs as all direct and indirect costs of providing the goods or service. This definition is consistent with that contained in federal accounting standards.<sup>5</sup> The federal accounting standards define the full cost of an entity's output as "the sum of (1) the costs of resources consumed by the segment that directly or indirectly contribute to the output, and (2) the costs of identifiable supporting services provided by other responsibility segments within the reporting entity, and by other reporting entities." Applying the definitions of "full cost" used in OMB Circular A-25 and federal accounting standards indicates that the full cost of the water supplied by the Bureau includes all direct and indirect costs incurred in providing these services and that these costs should be recovered, except where precluded by law. The indirect costs that could be recovered are included within Area Manager funds, Associated O&M Programs,<sup>6</sup> and certain pension and postretirement health benefits costs for Bureau employees.

## Area Manager Funds

The Bureau's Budget Review Committee established Area Manager funds in fiscal year 1997 "to be distributed to area offices in recognition of their expanded role and participation in broader policy issues and budget and program formulation activities." In fiscal year 1998, Area Manager funds were used for activities in two regions—the Pacific Northwest Region and the Great Plains Region—where the amounts funded totaled \$883,000 and \$348,000 respectively.

<sup>4</sup>The purpose of OMB Circular A-25 is to implement a law commonly known as the User Fee Statute. However, its guidance may be used by agencies in setting fees authorized by other laws to the extent that it does not conflict with the requirements of those laws.

<sup>5</sup>Financial Accounting Standards Advisory Board Statement of Federal Financial Accounting Standards (SFFAS) No. 4, *Managerial Cost Accounting Concepts and Standards for the Federal Government*, June 1995.

<sup>6</sup>Beginning in the fiscal year 1998 budget, the Bureau discontinued the Associated O&M Programs terminology and included their constituent programs in its "Bureauwide" budget category.

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We found that Area Manager funds have been used to fund such activities as

- meeting periodically with irrigation district managers to discuss Bureau policy and initiatives;
- developing out-year programs and budgets and discussing these budgets with irrigation district managers; and
- responding to requests from irrigation districts seeking easements across Bureau-held lands.

Since these are indirect costs of supplying water, we asked the Bureau why they were being excluded from reimbursable O&M. The Bureau responded by citing the following language from the Fact Finders Act.<sup>7</sup>

“The cost and expense after June 30, 1945, of the Office of the Commissioner<sup>8</sup> in the District of Columbia and, except for such cost and expense as are incurred on behalf of specific projects, of general investigations and of nonproject offices outside the District of Columbia, shall be charged to the reclamation fund and shall not be charged as a part of the reimbursable construction or operation and maintenance costs.”

We reviewed the authority that the Bureau cited for classifying costs funded by Area Manager funds as nonreimbursable. While it exempts from recovery the cost of “general investigations”<sup>9</sup> and “nonproject offices,” in our opinion it does not exempt from recovery the types of costs we identified, such as discussing with irrigation district managers, budgets that benefit the irrigation purpose and projects. These costs should be allocated on a reasonable basis to irrigation projects for recovery from water customers, instead of being classified as nonreimbursable, in accordance with the full cost definitions included in OMB guidance and federal accounting standards.

## Associated O&M Programs

The Bureau’s O&M report identified a group of individual programs that are collectively called Associated O&M Programs. The report stated that the

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<sup>7</sup>Fact Finders Act of April 19, 1945 (59 Stat. 54) (43 U.S.C. §377).

<sup>8</sup>Commissioner of the Bureau of Reclamation.

<sup>9</sup>General investigations are studies and planning efforts designed to “acquire and analyze data and to formulate plans for improved management and development of water and related land resources.” Examples of activities undertaken as general investigations include water conservation studies and studies related to the construction of new facilities for water supply or delivery.

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Associated O&M Programs group involves a variety of services “in support of its overall project O&M program.” As such, these are indirect O&M costs incurred by the Bureau. The Bureau’s O&M report listed examples of activities that had been funded by Associated O&M Programs, including

- developing new and improved O&M practices and procedures,
- providing the Bureau’s water and power users with information on the latest technical and nontechnical advances in the O&M of water and power projects,
- disseminating information concerning the agency’s overall O&M policies and programs, and
- providing for consistency and follow-through on the effectiveness of O&M programs from an agencywide perspective.

We reviewed some individual programs within the Associated O&M Programs group and identified some with purposes related to water supply, including

- the Negotiation and Administration of Water Marketing Program, which involves the administration of repayment contracts and operational studies for water marketing purposes,
- the Operation and Maintenance Program Management Program, with purposes that include standardization of O&M practices, and
- the Examination of Existing Structures Program, which provides for the review of Bureau facilities with respect to public safety, emergency management, and efficient energy and water management practices.

Because some of these are indirect costs of supplying water, we asked the Bureau why they were being excluded from reimbursable O&M. The Bureau again responded that its authorization for excluding the costs was the Fact Finders Act. As discussed previously, while the Fact Finders Act exempts from recovery the cost of “general investigations” and “nonproject offices,” in our opinion it does not exempt from recovery costs such as those we identified that benefit a reimbursable project purpose.

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## Certain Pension and Health Benefits Costs

The Bureau's water rates do not recover the full cost to the federal government of providing Civil Service Retirement System (CSRS) pensions and postretirement health benefits for current Bureau employees engaged in work directly related to water supply.<sup>10</sup> The employee and the Bureau both contribute annually toward the costs of future CSRS pension benefits. Since the employee and Bureau contributions toward CSRS pensions are less than the full cost of providing the pension benefits, the federal government must, in effect, make up the funding shortfall. In addition, neither the Bureau nor the employee pays the federal government's portion of postretirement health benefits, which will eventually be paid by the general fund of the Department of the Treasury.

As is the case in other federal agencies, CSRS employees and the agency each pay a fixed percentage of the employee's salary—7.25 percent for employees and 8.51 percent for the agency—to offset future pension costs. However, the combined contribution does not cover the full cost of the employee's future pension benefits, which amounted to 24.2 percent of salary as of September 30, 1999. Thus, for fiscal year 1999 the funding shortfall was about 8.44 percent of every CSRS employee's salary. The annual funding shortfall associated with pension benefits will be eliminated over time as CSRS employees leave the government and are replaced with Federal Employees Retirement System (FERS) employees, provided that FERS pension benefits remain fully funded annually.

The full cost of the federal government's portion of postretirement health benefits (for both CSRS and FERS employees) is likewise not paid by federal agencies, including the Bureau, during the period of the beneficiaries' employment. The Office of Personnel Management estimates that over \$2,550 per employee would need to have been contributed in fiscal year 1999 to cover the cost of each employee's postretirement health benefits earned. However, no fund has been established to accumulate assets to pay for these future benefits, which will eventually be paid by the federal government. In contrast to the situation regarding CSRS pensions, the annual funding shortfall associated with postretirement health benefits will not be eliminated as CSRS employees are replaced by FERS

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<sup>10</sup>According to Office of Personnel Management officials, pensions for employees covered by the Federal Employees Retirement System (FERS) are fully funded each year and cumulatively, so there are no similar unrecovered costs related to Bureau employees covered by FERS.

employees, since it is an entirely separate benefit program not related to individual retirement systems.

We analyzed the unrecovered costs for fiscal year 1999 related to CSRS pensions and postretirement health benefits at the Bureau's Mid-Pacific Region Central Valley Project (CVP) and at its Pacific Northwest Region. The results of our analysis are shown in table 2.

**Table 2: Fiscal Year 1999 Unrecovered CSRS Pension and Postretirement Health Benefits Costs for Bureau Employees Involved in Water-Related Activities at CVP and the Pacific Northwest Region**

Dollars in thousands

	CVP	Pacific Northwest Region
CSRS pension benefits	\$305	\$ 77
Postretirement health benefits	404	120
<b>Totals<sup>a</sup></b>	<b>\$709</b>	<b>\$197</b>

<sup>a</sup>Our analysis covered pension and postretirement health benefits for current employees only; we did not analyze the costs associated with retirees.

We previously reported that CSRS and postretirement health benefits costs associated with electricity generated by the Corps and the Bureau and marketed by the PMAs were similarly not being recovered.<sup>11</sup> In 1998 the Corps and the Bureau began estimating these costs and providing the results to the PMAs. The PMAs have begun recovering, through electricity rates, the full cost of CSRS pension and postretirement health benefits for their employees and for employees of the Bureau and Corps who are involved in power-related activities. The Bureau did not, however, make similar calculations for CSRS and postretirement health benefits costs associated with water supply and has not included these costs in its annual O&M rates.

<sup>11</sup>See *Power Marketing Administrations: Cost Recovery, Financing, and Comparison to Nonfederal Utilities* (GAO/AIMD-96-145, September 19, 1996), *Federal Electricity Activities: The Federal Government's Net Cost and Potential for Future Losses* (GAO/AIMD-97-110, September 19, 1997), and *Power Marketing Administrations: Repayment of Power Costs Needs Closer Monitoring* (GAO/AIMD-98-164, June 30, 1998).

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As with certain costs included in Area Manager funds and Associated O&M Programs, the costs of pensions and postretirement health benefits for Bureau employees are O&M costs incurred by the Bureau in providing services to project customers and recovering them is not precluded by specific legislation. Guidance contained in OMB Circular A-25 and federal accounting standards indicates that these costs should be recovered.

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## How Does the Bureau Account for O&M Costs?

The Bureau expenses O&M costs on an annual basis. For cost accounting purposes, Department of the Interior (DOI) policy requires that the Bureau classify costs into direct and indirect categories and ensure that these classifications are consistently used.

In June 1999 the Bureau established a team to study cost accounting practices. The team's goal was to "develop and implement a common and consistent set of business practices for defining, charging, reporting, and explaining both direct and indirect costs" within the Bureau. The team identified a number of needs that the current system did not meet, including

- lack of a common Bureau definition for indirect cost,
- lack of consistency between offices in charging costs,
- need for standard business practices that recognize and accommodate valid and justifiable differences between offices,
- flexibility for unique operations that result from project-specific legislation and organizational differences, and
- need to provide managers with the knowledge and tools to understand and explain costs.

The resulting *Standard Processes of Costing (SPOC) Business Practices*, issued in September 1999, represents current Bureau policy. This report provides guidelines for charging regional indirect costs. It also provides cost-charging examples from the Bureau's Reclamation Service Center, regional offices, and area offices and describes how the costs should be displayed to customers and others.

The SPOC report defines direct costs as "all costs which can be specifically and readily identified with an output or which can be specifically and readily identified with two or more outputs through a reasonable and economically feasible allocation." An output is defined as "a product or service specifically relating to a project or program." The report defines indirect costs as "costs that are jointly or commonly used to produce two

or more outputs but are not specifically identifiable with any of the outputs in an economically feasible way or through a reasonable allocation.”

Bureau personnel are guided by examples of direct and indirect costs as provided in the DOI *Financial Management Manual* and the SPOC report. Table 3 shows examples of direct and indirect costs from the SPOC report.

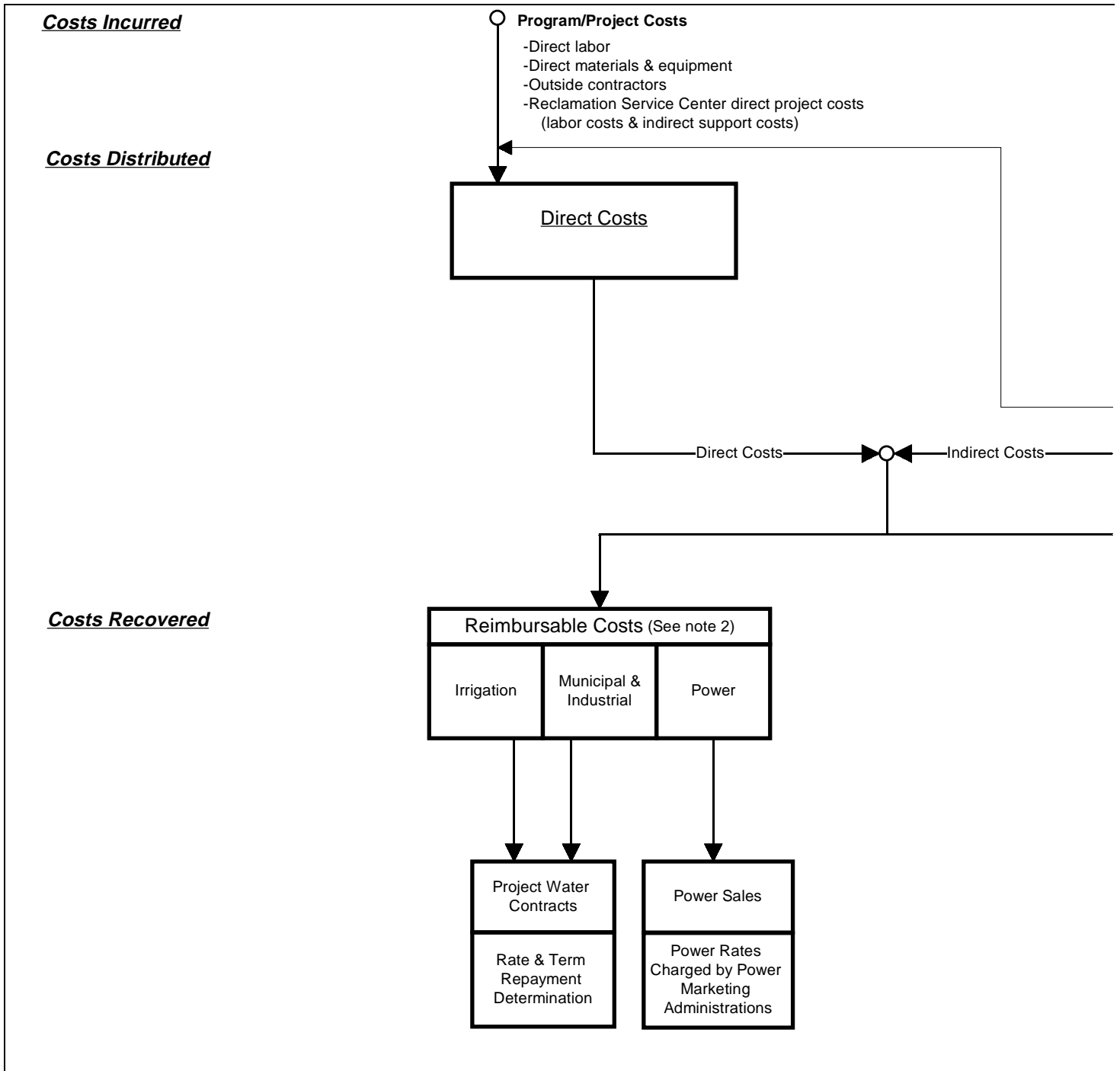
**Table 3: Examples of Bureau of Reclamation Direct and Indirect Costs**

<b>Direct costs</b>	<b>Indirect costs</b>
• Labor and equipment used on a specific program or task, such as maintenance on a water pump at a pumping station. The mechanic’s time, tools, and supplies are all direct costs of the pumping station.	• Labor and other costs not used on a specific program, such as services to the entire region provided by a staffing specialist in a regional office. The specialist’s time, training, travel, and supplies are indirect costs.
• Travel associated with a specific project.	• Space rental, postage, telephone expenses, and utilities (if not related to a specific program or task).
• Printing and data processing services associated with a specific program or project.	

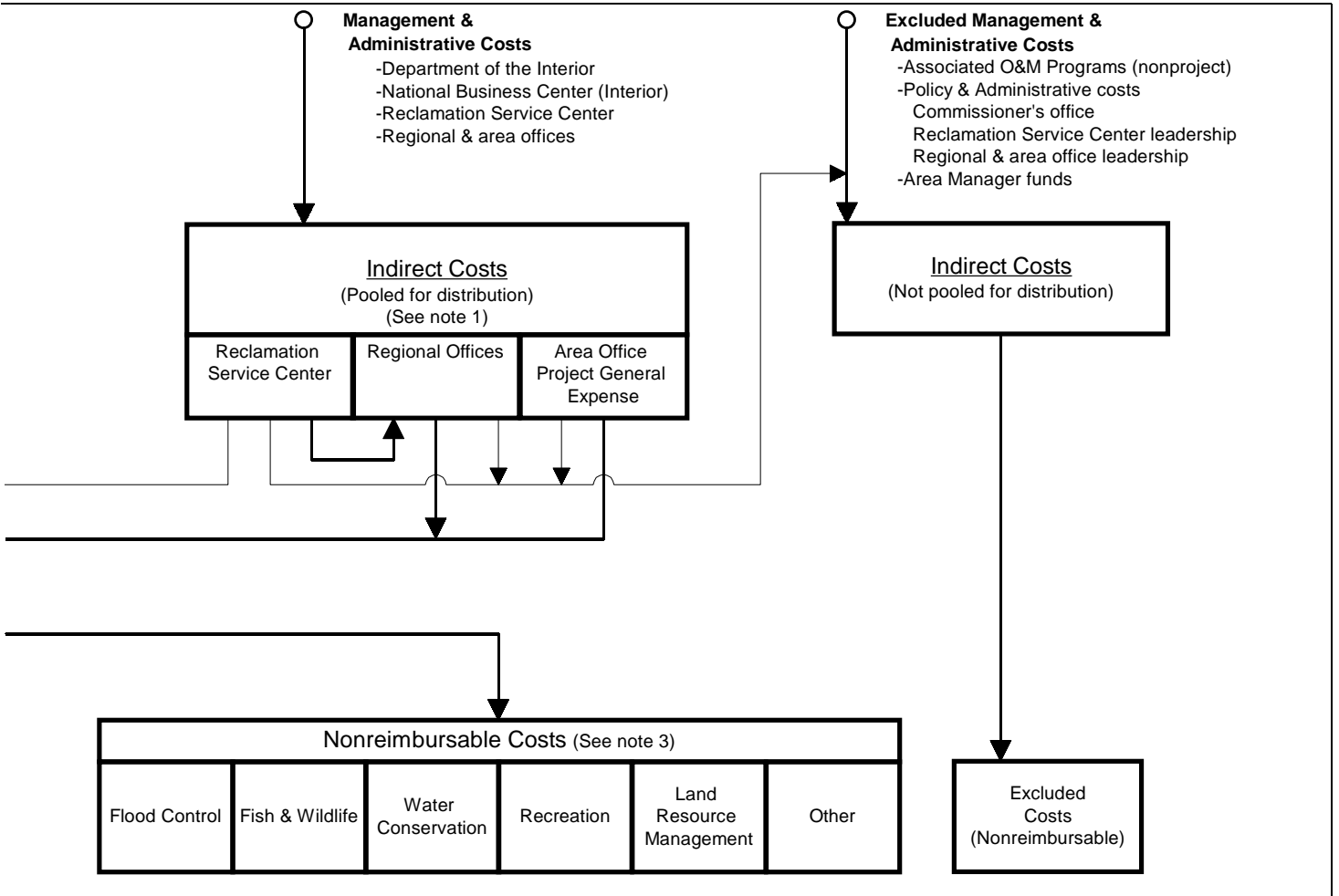
Source: Developed by GAO based on data from *Standard Processes of Costing (SPOC) Business Practices*, Bureau of Reclamation, September 30, 1999.

DOI policy also requires that the Bureau determine the cost of projects and services by reasonably distributing and allocating direct and indirect costs. Figure 1 shows how the Bureau distributes and allocates direct and indirect costs to the various reimbursable and nonreimbursable purposes served by water projects.

Figure 1: Bureau of Reclamation Cost Accounting—Allocation and Distribution







**Note 1 - Indirect Costs (Pooled)**

- 1-Reclamation Service Center
  - Centralized accounting
  - Wide-area network
  - Automated, centralized information systems
  - Services purchased under contract
- 2-Regional Offices
  - Financial management
  - Human resources
  - Acquisitions
  - Property management
  - Information resources
  - General management
- 3-Area Offices
  - Same categories as regional offices

**Note 2 - Reimbursable Costs:** Costs are recovered by receipts from customers and from miscellaneous revenues. Some reimbursable costs are not recovered because of legislative write-offs or other adjustments.

**Note 3 - Nonreimbursable Costs:** Costs are generally nonreimbursable but specific legislation may make some of these costs either fully or partially reimbursable.

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## How Does the Bureau Define Overhead?

During the fiscal year 1998 appropriations process, the Conference Committee on the Energy and Water Development Appropriations Bill asked the Bureau to report the “overhead rate” associated with its projects for fiscal years 1993 through 1997. The resulting report stated that the Bureau does not normally use the term overhead, nor is the term defined in the Federal Financial System. Consequently, the Bureau developed a definition of overhead specifically for use in the report to Congress. The Bureau defined “overhead rate” to be the indirect costs it identified as constituting overhead divided by total annual O&M costs.

The Bureau definition of overhead included some, but not all, indirect costs. Policy and Administration, Associated O&M Programs, and certain area office<sup>12</sup> indirect costs were excluded. The Bureau then calculated and reported the overhead rate applicable to specific projects and to the agency as a whole based on the portion of indirect costs that met its definition of overhead. The Bureau reported an agencywide overhead rate—overhead costs as a percentage of total O&M costs—ranging from 6 to 8 percent during fiscal years 1993 through 1997.

The report stated that the excluded area office indirect costs related to a variety of administrative services and support functions, such as clerical and secretarial staffs. The Bureau did not consider these costs to be overhead because each area office’s administrative and support costs related closely to projects. Consequently, the costs were not considered to be overhead, nor were they classified as direct costs. The costs were shown separately in a category called “Project General Expense.”

The Bureau’s report stated that even if these area office indirect costs were included in the definition of overhead, the Bureau’s agencywide percentage of overhead costs to total O&M costs would not have exceeded 15 percent in any of the 5 fiscal years under consideration.<sup>13</sup>

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<sup>12</sup>Each area office represents a designated geographic area within its respective regional office’s boundaries. Area office responsibilities include O&M for dams, pumping stations, canals, and other Bureau facilities.

<sup>13</sup>We confirmed the Bureau’s statement. The range was from 12.2 to 14.9 percent during this period.

The Bureau's report disclosed that Policy and Administration and Associated O&M Program costs were excluded because they are not reimbursable by project customers.<sup>14</sup> The resulting calculation of overhead—using only reimbursable costs—is meaningful to project customers, who are primarily concerned with costs they have to pay for.

We agree that this definition of overhead is meaningful to project customers. However, a definition that includes all indirect costs provides important additional information to the Congress and others. Table 4 provides a calculation of Bureauwide overhead that includes the indirect costs—Policy and Administration, Associated O&M Programs, and certain area office costs—that were not part of the Bureau report's customer-oriented definition.

**Table 4: Recalculation of Bureauwide Overhead if All Indirect Costs Are Included, Fiscal Years 1993 Through 1998**

Dollars in millions

Fiscal year	Bureauwide overhead		Percentage of overhead to total O&M	
	Per report	All costs included	Per report	All costs included
1993	\$31	\$149	8%	30%
1994	27	151	7	32
1995	22	135	6	28
1996	24	143	6	29
1997	25	152	6	28
1998	Not reported	150	Not reported	27

Source: Developed by GAO based on data from *Annual Costs of Bureau of Reclamation Project Operation and Maintenance for Fiscal Years 1993-97*, Bureau of Reclamation, September 1998, and from additional cost data provided by the Bureau of Reclamation.

<sup>14</sup>As discussed previously, the Associated O&M Program costs that are related to reimbursable project purposes and not legislatively precluded from recovery should be recovered because they are indirect O&M costs and OMB guidance and federal accounting standards indicate that they should be recovered.

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## How Does the Bureau Calculate the O&M Costs That It Charges to Customers?

The Bureau's contracts with customers for supplying water are of two types: repayment contracts and water service contracts. The Bureau calculates O&M costs charged to customers in accordance with the provisions of these different types of contracts. For repayment contracts, the customer's O&M costs are generally based on the percentage of the reservoir's water supply to which the customer is entitled. For water service contracts, costs are based on the amount of water delivered multiplied by the rate applicable to the particular customer.

The following discussion describes, in general, how the Bureau calculates the O&M charge for each type of contract. The examples are derived from repayment contracts as used by the Bureau's Pacific Northwest Region and water service contracts as used by the Mid-Pacific Region's Central Valley Project. Both examples assume that there is no Bureau charge for any O&M related to the conveyance of water, since this function has largely been taken over by the customers in both regions. The calculations shown are generalizations—specific contractual terms can result in a difference in how O&M charges are calculated for individual contracts. Moreover, while our examples cover only O&M costs, customers are also responsible for repaying certain capital costs of the facilities from which they receive their water.

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### Repayment Contracts

Repayment contracts are the most common legal instrument that the Bureau uses to obtain reimbursement from its customers for O&M costs incurred by Bureau projects. Generally, the O&M costs charged to the customer are allocated based upon the share of the reservoir water supply the customer is entitled to by contract; in some cases, certain other O&M charges may be based on benefits received in proportion to all project benefits. The customer must pay O&M costs in advance, based on the Bureau's internal budget estimates for the upcoming year. The customer's bill is subsequently adjusted for the difference between actual costs incurred and advance payments that have been made based on estimates.

For example, for a repayment contract entitling Customer A to 10 percent of the water stored in a particular dam's reservoir, the O&M charge is calculated as follows:

- The Bureau estimates that for fiscal year 1999, the reimbursable O&M costs for the dam, including both direct and certain indirect costs, will total \$100,000. Customer A's share of the Bureau's estimated fiscal year

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1999 O&M is 10 percent of \$100,000, or \$10,000. Customer A must pay this “up front,” i.e., before the Bureau performs the work.

- The Bureau’s actual O&M costs for the dam turn out to be \$90,000. Customer A’s share of actual costs is 10 percent of \$90,000, or \$9,000.
- Customer A’s bill for fiscal year 2000 estimated O&M costs will be credited for the \$1,000 overpaid in fiscal year 1999.

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## Water Service Contracts

The Bureau’s most common use of water service contracts is at its Central Valley Project in California. Under water service contracts, contractors pay a combined capital and O&M charge for each acre-foot<sup>15</sup> of water delivered. The contracts typically entitle the customer to a specified quantity of water annually. The O&M costs paid are based upon a rate the Bureau establishes for each individual customer. The rate is composed of separate charges for each of the services the Bureau provides to the customer. Water storage, marketing,<sup>16</sup> pumping, drainage, and conveyance are the primary services involved.

The Bureau establishes a charge for each of these services by estimating the annual total O&M costs expected to be incurred by that service—for example, for water storage. Total annual estimated water storage O&M costs are then divided by the total quantity of water expected to be delivered during the year. The result is a unit charge for water storage that is applied to each acre-foot of water sold to each customer.

The Bureau’s Central Valley Project has two types of water service contracts—cost-of-service and fixed-rate. For cost-of-service contracts, the O&M cost the customer pays annually is the rate the Bureau calculates based on budgeted costs and water delivery projections. For fixed-rate water service contracts, the O&M cost is based on the rate established by contract. For both types of contracts, if actual costs exceed the contract payments, the Bureau establishes an “O&M deficit” that is carried over to future years for payment. If actual costs are less than contract payments, excess payments are applied to interest, O&M deficits, and capital

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<sup>15</sup>An acre-foot of water is the volume necessary to cover 1 acre to a depth of 1 foot. It is approximately 326,000 gallons of water.

<sup>16</sup>Water marketing costs are for those administrative activities associated with the sale of project water, including contracting, contract administration, water accounting, and water ratesetting functions. Certain environmental mitigation costs are also included in the water marketing component of rates.

repayment (an amount assessed to cover project construction costs) in accordance with Central Valley Project ratesetting policies.

Under both cost-of-service and fixed-rate water service contracts, customers pay O&M in advance. The advance payments are based on the Bureau's O&M budget estimate and the amount of water expected to be delivered. The customer's bill is adjusted for the difference between actual costs incurred and payments that have been made based on estimates. The following examples show how the customer's costs are calculated for both cost-of-service and fixed-rate water service contracts.

#### Water Service Contract Cost-of-Service O&M Cost Calculation

A cost-of-service water service contract entitles Customer B to a maximum of 15,000 acre-feet of water per year. The Bureau estimates that it will be able to deliver 15,000 acre-feet to Customer B in fiscal year 1999. The O&M charge is calculated as follows:

- The services Customer B uses are water storage and water marketing. Customer B does not use, and is not charged for, other services that can comprise the Bureau's water service contract rate (e.g., water conveyance, pumping, and drainage).
- The Bureau estimates that it needs to charge \$4.61 per acre-foot for water storage in order to cover all of the O&M costs that are related to water storage. The Bureau also estimates that it needs to charge \$4.63 per acre-foot to cover all of the O&M costs that are related to water marketing costs. Consequently, the rate Customer B is charged for O&M costs is \$9.24 per acre-foot.
- Customer B pays a total of \$138,600 in estimated O&M costs in advance of water delivery (\$9.24 per acre-foot multiplied by the 15,000 acre-feet estimated amount of water delivery).
- After actual costs become known, Customer B's total fiscal year 1999 payments are applied to the customer's allocated costs. Excess payments generate capital and/or deficit repayment, while a shortage generates a deficit.

#### Water Service Contract Fixed-Rate O&M Cost Calculation

For a fixed-rate water service contract under which Customer C is to pay \$3 per acre-foot for water delivered, the O&M charge is calculated as follows:

- Customer C's estimated water delivery is 2,000 acre-feet in fiscal year 2000.
- Customer C prepays \$6,000 (\$3 per acre-foot multiplied by 2,000 acre-feet).

- Customer C is delivered 1,500 acre-feet in fiscal year 2000. The contract with Customer C, however, requires Customer C to pay for 2,000 acre-feet, whether or not it actually was delivered. The total cost based on actual deliveries is \$4,500. Therefore, Customer C has made payments of \$1,500 in excess of cost.
- Customer C is credited for \$1,500 against its allocated capital costs.
- If the contract's fixed rate is inadequate to cover the Bureau's actual O&M costs, Customer C incurs an O&M deficit that is carried over to future years for payment. A contract might have an accumulated deficit at the end of the contract term.

## What Concerns Have Been Raised by Customers About Excessive O&M Costs and to What Extent Do Customers Have an Opportunity to Review Cost Origins and Recommend Reductions?

We met with representatives from 31 organizations who were Bureau customers, or represented the interests of Bureau customers, in the Bureau's Mid-Pacific and Pacific Northwest regions. A list of the customers we contacted can be found in appendix I.

The customers we contacted were generally concerned about the level of the Bureau's costs and their ability to influence costs. Some customers thought the Bureau's overhead costs were excessive. Others were more concerned with total O&M costs.

The Bureau's 1998 SPOC report recognized that concerns had been raised by customers in the recent past in regard to their perception that the Bureau's O&M costs were excessive. Some customers stated that the Bureau's O&M report, which showed relatively low overhead costs, was not convincing to them and did not alleviate their concerns about Bureau costs. The customers commented that the report's results were largely dependent upon how indirect costs were defined and that they were concerned that their water rates contained costs that should have been nonreimbursable and therefore excluded. Finally, some customers commented that the Bureau report concerned itself primarily with indirect costs and did not adequately address the issue of why water rates have continued to increase.

A directive from the Bureau's Commissioner dated September 24, 1998, required Bureau regions to involve customers in the budget process. We confirmed that in the Mid-Pacific and Pacific Northwest regions, customers have been given increased opportunities by the Bureau to review budget data. Both regions had held meetings to present budget estimates and to obtain customer comments. The customers told us that the Bureau's recent

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initiative to “get them involved” in the budget process was a “good start.” Detailed customer comments included the following:

- Mid-Pacific Region customers we interviewed stated that they were generally encouraged by this year’s efforts by the Bureau to get them involved in the budget process. However, they said they need a great deal more detail to be able to make substantive determinations as to the appropriateness of O&M activities and charges. For example, they stated that they would like enough detail to be able to identify Policy and Administration costs in order to ensure that they were not being charged for costs that are by law nonreimbursable.
- Some Mid-Pacific Region customers expressed concern that there was no mechanism for them to determine whether the Bureau had acted upon any of their comments. They stated that they would like to obtain feedback with regard to the extent to which their suggestions were implemented. Bureau regional officials responded that timely feedback was difficult because of OMB restrictions placed upon the release of data before the budget is enacted, but that they would work with customers on providing this information.
- Pacific Northwest Region customers generally were encouraged by the Bureau’s efforts to involve them in the budget review process. However, some customers commented that they did not have enough detail to identify indirect costs.
- Some Pacific Northwest Region customers complained that the final bill that they received from the region was not sufficiently detailed—that it was just a one-line bill for O&M costs for the year. Regional officials stated that they were studying the possibility of providing more detail in the bills.
- Some Mid-Pacific Region customers stated that the water marketing costs that were included in rates were excessive. They stated that they did not know what these costs were for and that increases were troubling because there appeared to be “no end in sight.” Bureau Mid-Pacific Region officials stated that details on water marketing costs and other information about rates were communicated to customers attending customer group meetings, such as those held by the Central Valley Project Water Association, and in responses to questions posed directly to ratemaking staff. Customers were optimistic that the budget review meetings and the new cost accounting policies adopted by the Bureau in its SPOC report would provide increased opportunities to review these costs.



- Some Pacific Northwest Region customers said that the Bureau's basis for classifying costs as O&M, rather than capitalizing them, was unclear.<sup>17</sup> However, most customers contacted in both regions were not concerned about the Bureau's capitalization policy and generally understood the basis for the decisions the Bureau made. They stated that these decisions were governed by the specific terms within the individual contracts and by published guidance the Bureau uses that lists specific items and establishes criteria to determine whether the cost should be capitalized.
- Two Mid-Pacific Region customer groups that we contacted had taken over the responsibility for O&M on some of the Bureau's water conveyance facilities. One of the groups stated that its O&M costs were lower than the Bureau's had been because it was using fewer employees to do the same work. The Bureau responded that the comparison was invalid because the customer group overstated the number and costs of employees that the Bureau had used. An official from a group that represents many customers of the Central Valley Project—the largest project in the Mid-Pacific Region—told us that it would be difficult to substantiate any such claims that facilities taken over by customer groups are operated more efficiently than they had been by the Bureau.

## How Do the Bureau's Cost Recovery Practices Compare to Those of Other Entities?

As previously discussed, the Bureau manages large multiple-purpose water projects and is required to recover reimbursable costs it incurs from water service and other customers. The U.S. Army Corps of Engineers and the State of California's State Water Project offer meaningful comparisons to the Bureau. The Corps is a federal entity that manages multiple-purpose water projects with cost recovery requirements. California's Department of Water Resources manages the State Water Project, which is the largest multiple-purpose water project managed by a nonfederal entity in the United States.

Both Corps projects and the California State Water Project have reimbursable and nonreimbursable project purposes that are similar to those of the Bureau. These include reimbursable purposes, such as water service and electrical power production, and nonreimbursable purposes, such as recreation, fish and wildlife protection, and flood control.

<sup>17</sup>Classifying costs as O&M and expensing them in the year incurred puts greater upward pressure on current rates than capitalizing the costs and recovering them over a period of years.

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Laws applicable to the Bureau of Reclamation and Bureau interpretations of those laws lead to some differences in the types and amounts of costs the Bureau classifies as reimbursable when compared to other entities. Some differences are described below.

- The Bureau excludes costs funded by its Policy and Administration appropriation from recovery, in accordance with the specific provisions in the appropriations laws that are applicable to the Bureau. The California State Water Project does not have a similar legislatively mandated exclusion.
- The Corps excludes costs funded by its General Expense appropriation from recovery. However, unlike the Bureau, the costs funded by this appropriation are limited to the agency's headquarters and division levels. We did not review the Corps' legal authority for excluding these costs from recovery.
- The Bureau classifies some categories of indirect costs as nonreimbursable because they are of "Bureauwide" benefit rather than benefiting any specific project. These include the Associated O&M Programs costs and costs paid for by Area Manager funds.<sup>18</sup> According to Corps and State of California officials, neither the Corps nor the California State Water Project excludes similar categories of indirect costs from recovery.
- Neither the Bureau nor the Corps recovers the full cost of employee pensions and postretirement health benefits.<sup>19</sup> State of California officials advised that the full pension and health benefits costs associated with the State Water Project are recovered from customers.

Federal power marketing administrations offer another contrast. These organizations market power produced at the Bureau's multiple-purpose projects. The power marketing administrations are recovering the full employee pension costs that are related to the production of power at Bureau facilities.

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<sup>18</sup>As discussed previously, the Area Manager funds and Associated O&M Program costs that are related to reimbursable project purposes and not legislatively precluded from recovery should be recovered because they are indirect O&M costs and OMB guidance and federal accounting standards indicate that they should be recovered.

<sup>19</sup>As discussed previously, the employee pensions and postretirement health benefits costs that are related to reimbursable project purposes and not legislatively precluded from recovery should be recovered because they are indirect O&M costs and OMB guidance and federal accounting standards indicate that they should be recovered.

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## Conclusions

To recover the full cost of providing services, the Bureau needs to identify and include in its billing all O&M costs that are related to reimbursable project purposes. The Bureau cannot have assurance that it is recovering all reimbursable costs until it undertakes a review of all costs funded by Area Manager funds and Associated O&M Programs and identifies costs that are either directly or indirectly related to reimbursable project purposes.

Recovering these costs, and the full costs associated with employee pension and health benefits, would help ensure that the federal government's net costs related to the services provided by the Bureau are minimized.

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## Recommendations

To fully recover all appropriate costs, we recommend that the Secretary of the Interior direct the Commissioner, Bureau of Reclamation, to

- examine Area Manager funds and Associated O&M Programs to identify costs related to reimbursable project purposes and recover those costs from the benefiting customers, and
- calculate and begin recovering the full costs of employee postretirement health benefits and CSRS employee pension costs related to reimbursable project purposes.

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## Agency Comments and Our Evaluation

The Department of the Interior generally agreed with the basic thrust of the report's conclusions and recommendations—that the Bureau of Reclamation needs to identify and recover appropriate costs related to providing services to project beneficiaries. DOI's comment letter is reproduced in appendix II.

DOI stated that, due to the complexity of the cost recovery issue and its potential impacts, it has asked the Bureau of Reclamation to more fully review the report and its recommendations and provide a preliminary report on them to Bureau and DOI officials by June 9, 2000. Specifically, DOI stated that (1) the Commissioner of the Bureau of Reclamation and the Solicitor would review costs charged to Area Manager funds and Associated O&M Programs to determine whether more of these costs can be recovered from project beneficiaries, and (2) the Solicitor would review the Bureau's legal authority to recover the full costs of employee

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postretirement health benefits and CSRS pension costs that are related to reimbursable project purposes.

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As agreed with your office, unless you publicly announce its contents earlier, we plan no further distribution of this report until 30 days from its date. At that time, we will send copies to Representative Calvin M. Dooley, Ranking Minority Member, House Subcommittee on Water and Power, Committee on Resources; Representative Joe Barton, Chairman, and Representative Rick Boucher, Ranking Minority Member, House Subcommittee on Energy and Power, Committee on Commerce. We are also sending copies of this report to the Honorable Bruce Babbitt, Secretary of the Interior, the Honorable Eluid L. Martinez, Commissioner, Bureau of Reclamation, and other interested parties. Copies will also be made available to others on request.

If you or your staff have any questions concerning this report, please contact me at (202) 512-9508. Key contributors to this report were Dave Bogdon, Mark Connelly, Michelle Dimodica, Brian Eddington, Larry Feltz, Rob Martin, and Jack Warner.

Sincerely yours,



Linda M. Calbom  
Director  
Resources, Community, and Economic Development  
Accounting and Financial Management Issues

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# Objective, Scope, and Methodology

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The Chairman, Subcommittee on Water and Power, House Committee on Resources, asked us to review several issues relating to the Bureau of Reclamation's operation and maintenance (O&M) of federal water projects. The specific objectives of our review were to determine (1) how the Bureau defines O&M activities, (2) the Bureau's latitude in deciding which O&M costs to charge to customers, (3) how the Bureau accounts for O&M costs, (4) how the Bureau defines overhead, (5) how the Bureau calculates the O&M costs that it charges to customers, (6) what concerns have been raised by customers about excessive O&M costs and to what extent customers have an opportunity to review cost origins and recommend ways to reduce them, and (7) how the Bureau's cost recovery practices compare to those of other entities. We met with Bureau customers in order to obtain their views on relations with the Bureau and the extent to which the Bureau has been responsive to their concerns.

As agreed with the requester, our review was limited to the Bureau's delivery of water for irrigation and municipal and industrial use. We did not review the Bureau's activities related to hydroelectric power production or to any nonreimbursable functions at multipurpose Bureau facilities, such as recreation, flood control, or fish and wildlife protection. Our work was also limited to O&M activities and costs; we did not review the recovery and treatment of capital construction costs. In addition, we did not assess the Bureau's efficiency in performing its O&M activities or in incurring related costs.

We conducted audit work at the Bureau's Washington, D.C. headquarters and Denver, Colorado office, and at its Mid-Pacific and Pacific Northwest regions. We also conducted audit work at the U.S. Army Corps of Engineers, State of California, and at the offices of representatives from water users' interest groups and customers from projects representing most of the Bureau's water sales in the Mid-Pacific and Pacific Northwest regions. We interviewed knowledgeable personnel at each audit site to obtain information relevant to the questions we were asked to answer. We also reviewed and analyzed relevant legislation and documents. In addition, we obtained written or oral responses from Bureau officials to document the Bureau's position on selected questions and issues and observed a budget review meeting held by the Mid-Pacific Region for its customers. The following section details the methodology used in our analyses and any additional restrictions on the scope of our work.

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## Determining How the Bureau Defines O&M and Overhead and Accounts for O&M Costs

To determine how the Bureau defines O&M and overhead and how it accounts for O&M costs (objectives 1, 3, and 4), we reviewed and analyzed relevant legislation and documents, including reclamation law; a 1998 Bureau report to Congress on O&M activities and overhead;<sup>1</sup> a 1999 Bureau cost accounting report;<sup>2</sup> Department of the Interior and Bureau of Reclamation policies, accounting manuals, and other cost accounting guidance; and certain contracts with water supply customers. We also reviewed sample O&M bills the Bureau issued to various water customers and traced the charges in these bills back to Bureau accounting records. In addition, we consulted with Bureau Denver office officials to develop a flowchart that documents how the Bureau's costs are allocated and distributed.

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## Determining How the Bureau Calculates O&M Costs

To determine how the Bureau calculates O&M (and overhead) costs (objective 5), we reviewed DOI and Bureau policy and procedures for determining O&M costs and discussed these policies and procedures with Bureau officials. We also traced sample O&M bills issued to customers back into Bureau accounting records to test the Bureau's ability to break O&M bills down into their constituent elements of materials, labor, and indirect costs and discussed our findings with Bureau personnel.

We reviewed repayment and water service contracts and discussed contract provisions with Bureau regional officials. We used this information to develop generalized examples of how a customer's O&M bill would be calculated under both types of contracts.

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<sup>1</sup> *Annual Costs of Bureau of Reclamation Project Operation and Maintenance for Fiscal Years 1993-97*, Bureau of Reclamation, September 1998.

<sup>2</sup> *Standard Processes of Costing Business Practices*, Bureau of Reclamation, September 30, 1999.

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## Determining the Bureau's Latitude in Deciding Which O&M Costs to Charge Customers

To determine the extent of the Bureau's latitude to designate costs as O&M (objective 2), we reviewed and analyzed relevant legislation, DOI and Bureau accounting policies and procedures, and the Bureau's O&M report. We reviewed Bureau capitalization policies and analyzed Department of the Interior Office of Inspector General reports relating to the Bureau's past practices in accounting for O&M costs. We met with Bureau customers to obtain their views on the Bureau's practices regarding the designation of costs as O&M and certain Bureau contracts with water supply customers.

We reviewed the Bureau's authority to include and exclude O&M costs from recovery. This review included analyzing the legislation pertinent to the appropriations that funded the costs; questioning Bureau officials; reviewing the legislation cited by the Bureau as justifying its determination that the costs were nonreimbursable; and identifying costs associated with the Bureau's exclusions.

To define the full cost of the services provided by the Bureau, we reviewed (1) Office of Management and Budget (OMB) Circular A-25, which provides guidance for use in setting fees to recover the full costs of providing goods and services and (2) Statement of Federal Financial Accounting Standards (SFFAS) No. 4, *Managerial Cost Accounting Concepts and Standards for the Federal Government*. OMB Circular A-25 defines full cost as all direct and indirect costs of providing goods and services and is consistent with guidance for full cost reporting contained in SFFAS No. 4.

To determine whether the activities funded by the Policy and Administration appropriation are reasonably in accordance with Bureau definitions of Policy and Administration costs, we reviewed and discussed with Bureau representatives, supporting documentation for a limited number of charges judgmentally selected from Bureau-prepared lists of transactions recorded as Policy and Administration costs in September 1998. To determine the nature of costs charged to Associated O&M Programs, we reviewed Bureau-prepared lists of costs charged to Associated O&M Programs by Bureau headquarters and regional offices during November 1997 and September 1998. From those lists we chose a limited number of judgmentally selected individual transactions and discussed the nature of those costs with a Bureau official.



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## Identifying Specific Concerns That Have Been Raised by Customers and the Extent to Which Customers Have an Opportunity to Review Cost Origins and Recommend Ways to Reduce Them

To identify specific concerns that customers have raised about excessive O&M costs and the extent to which customers have an opportunity to review the origins of O&M costs and recommend ways to reduce them (objective 6), we spoke to Bureau Mid-Pacific and Pacific Northwest region customers and customer groups from 31 organizations (the groups are listed at the end of this appendix). We selected a sufficient number of customer representatives to ensure that we had contacted parties representing more than a majority of the water supplied by the Bureau in each region, including both irrigation water supply and municipal and industrial water supply customers. These customers and customer groups were selected judgmentally and do not represent a projectable random sample.

We obtained customers' views on the O&M bills they receive from the Bureau and asked about recent trends in the amounts of these bills. We also asked about the extent to which the Bureau involves them in the O&M budget process and the extent to which they feel the Bureau is responsive to customers' concerns.

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## Determining How the Bureau's Cost Recovery Practices Compare to Those of Other Entities

To determine how the Bureau's cost recovery practices compare to those of other entities (objective 7), we identified two entities—the U.S. Army Corps of Engineers and the California State Department of Water Resources—that, like the Bureau, operate extensive, multiple-purpose water development projects. We discussed the policies and procedures for defining and accounting for O&M practices with officials of the Corps at their Washington, D.C., headquarters and selected division, district, and area offices, and with officials of the California State Department of Water Resources at their Sacramento, California, headquarters. We compared those policies and procedures with those we found used by the Bureau of Reclamation.

We conducted our review from June 1999 through March 2000 in accordance with generally accepted government auditing standards. We obtained written agency comments on a draft of this report, which are reproduced in appendix II.

We contacted the following organizations during the course of our work.

Black Canyon Irrigation District, Idaho  
Boise Project Board of Control, Idaho/Oregon

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**Appendix I**  
**Objective, Scope, and Methodology**

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California Department of Water Resources  
Central Valley Project Water Association, California  
Chowchilla Water District, California  
Contra Costa Water District, California  
East Columbia Irrigation District, Washington  
Exeter Irrigation District, California  
Fresno Irrigation District, California  
Friant Water Users Authority, California  
Ivanhoe Irrigation District, California  
Kennewick Irrigation District, Washington  
Kittitas Reclamation District, Washington  
Lindmore Irrigation District, California  
Madera Irrigation District, California  
Nampa and Meridian Irrigation District, Idaho  
Payette River Water Users' Association, Idaho  
Quincy-Columbia Basin Irrigation District, Washington  
Roza Irrigation District, Washington  
San Luis and Delta-Mendota Water Authority, California  
Santa Clara Valley Water District, California  
Saucelito Irrigation District, California  
Shaffer-Wasco Irrigation District, California  
South Board of Control, Owyhee Project, Idaho/Oregon  
South Columbia Basin Irrigation District, Washington  
South East Colorado Water Conservancy District, Colorado  
South San Joaquin Municipal Utility District, California  
Sunnyside Irrigation District, Washington  
Tea Pot Dome Water District, California  
Terra Bella Irrigation District, California  
Westlands Water District, California  
Yakima-Tieton Irrigation District, Washington

# Comments From the Department of the Interior



## United States Department of the Interior

OFFICE OF THE SECRETARY  
Washington, D.C. 20240

APR 20 2000

Mr. Jeffrey C. Steinhoff  
Acting Assistant Comptroller General  
General Accounting Office  
Washington, D.C. 20548

Dear Mr. Steinhoff:

We appreciate the opportunity to review and comment on the General Accounting Office draft report entitled "Bureau of Reclamation: Information on Operations and Maintenance Activities and Costs at Multipurpose Water Projects" (GAO/AIMD-00-127).

In general, we agree that the Bureau of Reclamation needs to identify and recover appropriate costs related to providing services to project beneficiaries. Reclamation has historically recovered project costs in accordance with Reclamation law and specific project legislation, which in some instances, restricts the costs that should be borne by project beneficiaries. It should be further noted that Reclamation's ability to impose charges on water users may be limited by the terms and conditions of water service or operation and maintenance contracts, which govern the reimbursement of costs. Nevertheless, we agree that Reclamation does have discretion with respect to identifying appropriate costs for reimbursement and will take steps to ensure that any new or existing business practices to recover costs are applied consistently.

Due to the complexity of this issue and its potential impacts, I have asked Reclamation to more fully review the report and its recommendations and provide a preliminary report to the Commissioner for the Bureau of Reclamation and myself by June 9, 2000. Reclamation will work closely with other offices within the Department of the Interior to address any legal or other issues that arise during the review process.

Again, thank you for the opportunity to review the draft report. Our comments to the report's recommendations are enclosed for your review and consideration.

Sincerely,

Mary Doyle  
Acting Principal Deputy Assistant Secretary  
for Water and Science

Enclosure

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**Appendix II**  
**Comments From the Department of the**  
**Interior**

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Response to General Accounting Office Draft Report  
“Bureau of Reclamation: Information on Operations and Maintenance  
Activities and Costs at Multipurpose Water Projects”  
(GAO/AIMD-00-127)

Recommendation 1

To fully recover all appropriate costs, we recommend that the Secretary of the Interior direct the Commissioner, Bureau of Reclamation, to: Examine Area Manager Funds and Associated O&M Programs to identify costs related to reimbursable project purposes, and recover those costs from the benefitting customers.

Response

Reclamation agrees with the general thrust of the recommendation, and seeks to recover all appropriate costs of its projects from project beneficiaries. The Commissioner will review the costs charged to “Area Manager Funds” and “Associated O&M Programs”, and will work closely with the Solicitor to determine if under current statutes and contractual arrangements it can recover more of those costs from project beneficiaries. The Commissioner will also take steps to ensure that cost recovery policies are applied consistently across Reclamation.

Recommendation 2

To fully recover all appropriate costs, we recommend that the Secretary of the Interior direct the Commissioner, Bureau of Reclamation, to: Calculate and begin recovering the full costs of employee postretirement health benefits and CSRS employee pension costs related to reimbursable project purposes.

Response

Reclamation agrees that the Federal accounting standards require the recognition of the full costs of its programs. With respect to the legal authority to recover all such costs, specifically post-retirement costs, Reclamation must first confer with its Solicitor to obtain direction as to what constitutes full cost for cost recovery purposes. Additionally, Reclamation must determine whether project legislation and/or contracts permit such recovery. If the inclusion of these post-retirement costs in Reclamation rates is determined to be warranted, a phase-in period may be necessary since ability to pay studies will be necessary to ascertain the impact on the water community, and because many water districts set their budgets and related rates a few years in advance.

The Department is deferring its final decision on the recommendations pending the outcome of reviews by the Commissioner and the Solicitor.

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