opportunities exist to improve managerial cost information and cost recovery
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Table 1: Bureauwide Program Activities Funded by the “Water and Related Resources” Appropriation 11
September 20, 2002

The Honorable Gale A. Norton
Secretary of the Interior

In previous work at the Department of the Interior's (Interior) Bureau of Reclamation (Bureau), we identified reimbursable project costs that were not being recovered by the Bureau.\(^1\) Based on this and other work we have performed at the Bureau, we reviewed the Bureau's managerial cost accounting and cost recovery practices. Our objectives were to determine whether the Bureau (1) identifies and distributes for management purposes all the costs it incurs in operating its projects and administering its programs, and (2) ensures that recoverable costs are identified and recovered from customers.

Results in Brief

Federal accounting standards seek to ensure that relevant and reliable information on the full costs of a government entity's activities is readily available to aid program managers and congressional officials in making decisions regarding the allocation of limited federal resources. In addition, the President's governmentwide management initiatives require the availability of quality cost information. However, the Bureau does not currently identify and distribute all the costs it incurs to its specific projects and activities. For example, the combined costs of Policy and Administration and Bureauwide programs, which were budgeted to be about $200 million (21 percent of the Bureau's budget) in fiscal year 2002, are not distributed to specific projects and activities. These costs are not distributed because the Bureau considers them nonreimbursable and the Bureau's cost accounting system is used primarily to capture costs related to reimbursable purposes such as irrigation, municipal and industrial (M&I) water supply, and power generation. While we recognize that the Bureau does not have the authority to recover certain costs, such as those funded through the Policy and Administration appropriation, all the costs should nevertheless be distributed to the relevant activities to provide information useful in managerial decision making. Because not all costs are distributed, information on the full cost of projects and activities is not readily available to the Congress, program managers, and others to

facilitate decision making and the allocation of the federal government’s resources. We recommend that the Bureau enhance its managerial cost accounting so as to provide information that facilitates managerial decision making and fulfills each of the five purposes of the Managerial Cost Accounting Standards. This would include distributing Policy and Administration and Bureauwide program costs to the appropriate projects and activities.

Even though its cost accounting system is designed primarily to facilitate cost recovery, the Bureau does not recover all costs that benefit specific Bureau projects. Reclamation law provides that the Bureau recover the costs of certain reimbursable activities, including irrigation, M&I water supply, and power generation. Federal policy requires that the full costs incurred by the federal government in providing services be recovered from the beneficiaries of those services, unless the recovery of such costs is legislatively precluded. However, the Bureau treats many costs as being precluded from recovery under the Fact Finders Act, even though these costs directly or indirectly provide benefits to the Bureau's projects. We disagree with the Bureau's treatment and do not believe the act precludes the Bureau from recovering the costs (direct and indirect) benefiting specific projects through water delivery contracts and rates charged to customers. We recommend that the Bureau review the Bureauwide programs and recover the costs of those that either directly or indirectly benefit projects, unless cost recovery is prohibited under current law.

Interior concurred with our recommendation regarding reviewing the Bureauwide programs and recovering the costs of those that benefit projects. Interior did not concur with our recommendation regarding distributing the Policy and Administration and Bureauwide program costs to projects and activities. Interior stated that the current cost accounting system provides the necessary information for program management and external reporting. Interior also stated that distributing costs to the projects and activities would not be cost effective. We disagree. Without distributing the Policy and Administration and Bureauwide program costs, which represented 21 percent of the Bureau's budget for fiscal year 2002, the Bureau has no basis to determine the full costs of its projects or activities or, in the case of Bureauwide program costs, for recovering the portion that benefit projects. System changes needed to accomplish this could be made in concert with the planned departmentwide implementation of a new cost accounting system. Interior’s written comments are reproduced in appendix II and are summarized and addressed in detail later in the body of this report.
Scope and Methodology

We conducted our audit work at the Bureau's Denver, Colorado office and at its Mid-Pacific region. We reviewed and analyzed relevant legislation, written policies and directives, accounting standards, and other documents pertaining to managerial cost accounting. We also interviewed knowledgeable personnel at each audit site to obtain information relevant to the objectives of this assignment.

The scope of our review included the Bureau's managerial cost accounting practices and the Bureau's treatment of different types of costs related to its administration and operation of its projects and the delivery of its programs. We conducted our review from November 2001 to July 2002 in accordance with generally accepted government auditing standards. Appendix I describes our objectives, scope, and methodology in detail. We provided the Department of the Interior and the Bureau of Reclamation with copies of a draft of this report for review and received written comments on the report.

Background

The Bureau constructs and operates multiple-purpose water resource projects in 17 western states. These projects provide water for irrigation, M&I use, power generation, recreation, and fish and wildlife protection, and also provide for flood control, water conservation, and land resource management. The Bureau's facilities include 348 reservoirs with a storage capacity of 245 million acre-feet of water, 58 hydroelectric power plants, and more than 300 recreation sites. These facilities:

- generate more than 40 billion kilowatt hours of energy each year, making the Bureau the nation’s second largest producer of hydroelectric power;

- deliver water to one out of every five western farmers for about 10 million acres of irrigated land that produces 60 percent of the nation’s vegetables and 25 percent of its fruit and nuts;

- deliver 10 trillion gallons of municipal, rural, and industrial water to over 31 million people in the West;

- provide water to support habitat for wildlife refuges, migratory waterfowl, fish, and threatened and endangered species;
• deliver water to Native American tribes through irrigation projects and potable water supplies;

• provide water-based recreation activities for about 90 million visitors a year; and

• provide flood control benefits and drought contingency planning and assistance to western states and tribes.

Construction, operation, and maintenance of these projects and Bureau programs are financed primarily with federal funds. The Bureau assigns a percentage of capital and operation and maintenance (O&M) costs to each project purpose based on the project’s expected uses and benefits. Costs associated with irrigation, M&I use, and power generation are generally required to be recovered through water delivery contracts and rates charged for water and power. In contrast, costs associated with flood control, fish and wildlife enhancement, and recreation are generally not recoverable under current law. To facilitate cost recovery and manage the projects and programs, the Bureau collects budget and cost information through its program and budget and financial accounting systems.

The need for cost information is not unique to the Bureau. Cost information is needed throughout government for management, resource allocation, and oversight purposes. The cost of government is a concern to the public as well as to the federal government itself. One of the ways to capture cost information is by applying managerial cost accounting techniques. By using managerial cost accounting information, agency executives and managers, the Congress, citizens, news media, and interest groups can better assess the costs of governmental activities.

The need for useful managerial cost information has been recognized for some time. The Congress and others have taken a number of actions to require cost accounting information and to encourage its use in administering federal projects and programs. Some of the specific requirements for managerial cost accounting are as follows.

• The Chief Financial Officers Act of 1990 includes among the functions of chief financial officers “the development and reporting of cost information” and “the systematic measurement of performance.”

the objectives of federal financial reporting are to provide useful information to assist internal and external users in assessing the budget integrity, operating performance, stewardship, and systems and control of the federal government. It also states that federal financial reporting should provide information that helps users to determine the (1) costs of specific programs and activities and the composition of, and changes in, those costs, (2) efforts and accomplishments associated with federal programs and their changes over time and in relation to costs, and (3) efficiency and effectiveness of the government’s management of its assets and liabilities.

- Statement of Federal Financial Accounting Standards (SFFAS) No. 4, *Managerial Cost Accounting Standards* states that the objective of the standard is to (1) provide program managers with relevant and reliable information relating costs to outputs and activities, (2) provide relevant and reliable cost information to assist the Congress and executives in making decisions about allocating federal resources, authorizing and modifying programs, and evaluating program performance, and (3) ensure consistency between costs reported in general purpose financial reports and costs reported to program managers. The stated purposes in the standard for managerial cost accounting are:
  
  - budgeting and cost control,
  - performance measurement,
  - cost reimbursement (and setting fees and prices),
  - program evaluations, and
  - making economic choice decisions.

- The Federal Financial Management Improvement Act of 1996 (FFMIA) requires agencies to implement and maintain financial management systems that comply with federal accounting standards, including SFFAS No. 4.

- The Joint Financial Management Improvement Program (JFMIP) issued a statement on January 31, 2002, stating that “A key element of financial planning and evaluation is clear measurement of the full costs of agencies’ activities during each fiscal year.”
The Bureau has taken steps in recent years to improve its cost accounting practices. It better defined the treatment of costs by issuing in 1999 the Standard Processes of Costing (SPOC) report that clarified and standardized direct and indirect cost treatment. In addition, it changed the basis it uses to distribute some indirect costs to better reflect actual usage. Also, at the direction of the Department of the Interior, the Bureau will be implementing Activity Based Costing (ABC), a cost accounting method that measures the cost of work efforts leading to a specific result. On January 16, 2002, Interior’s Deputy Secretary sent a memo to all Bureau and office heads directing them to implement an ABC cost model by fiscal year 2004 (October 1, 2003). The Bureau’s ABC initiative is discussed in more detail later in this report.

The Bureau Lacks Full Cost Information to Support Managerial Decisions

The Bureau does not distribute all the costs it incurs to its specific projects and activities. Thus, full cost information is not available for managerial decision making as envisioned in federal accounting standards and the President’s management improvement initiatives.

The Bureau’s distribution of costs is driven largely by the need to recover certain costs. Its cost accounting system focuses primarily on recovering costs in accordance with specific project provisions. It does not identify the full costs of the Bureau’s activities such as irrigation, M&I water supply, power generation, recreation, fish and wildlife protection, flood control, water conservation, and land resource management. Therefore, complete information on the cost of the Bureau’s activities is not readily available to support managerial decisions pertaining to each of the purposes of managerial cost information described in SFFAS No. 4, *Managerial Cost Accounting Standards.* The standard notes that when full cost information is made available, analysts and decision makers will have a comprehensive data source to develop the cost concepts that they need in their analyses. However, it recognizes that full cost is not necessary for all analyses and decisions.

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2 As stated previously, the purposes of managerial cost information in the standards are (1) budgeting and cost control, (2) performance measurement, (3) cost reimbursement (and setting fees and prices), (4) program evaluations, and (5) making economic choice decisions.
Two large categories of costs—Policy and Administration costs and Bureauwide program costs—are not distributed to project purposes. Policy and Administration costs are not distributed to project purposes because the Bureau’s focus is on cost recovery and legislation specifically designates these costs to be nonreimbursable as provided by 43 U.S.C. sec. 377.3 Bureauwide program costs are generally not distributed to project purposes for one of two reasons: either because legislation specifically designates these costs to be unrecoverable4 or the Bureau has otherwise decided not to seek reimbursement for them.5 These two undistributed cost categories totaled nearly $200 million or 21 percent of the Bureau’s total budget authority for fiscal year 2002. See appendix III for additional information pertaining to budgeted amounts for Policy and Administration and Bureauwide program costs for fiscal years 1997 through 2002. As discussed in the next section, we believe that certain of these undistributed costs may be recoverable.

Because such a large portion (21 percent) of the Bureau’s budget is not distributed, complete information regarding the total cost of each of the Bureau’s activities is not readily available. Bureau managers and external parties, such as congressional appropriators, do not have information on the total costs of the Bureau’s main activities at their disposal for decision making purposes. For example, it is not possible to analyze what the Bureau spends on irrigation, M&I water supply, power generation, recreation, fish and wildlife protection, flood control, water conservation, and land resource management either currently or over time.

The Bureau’s managerial cost accounting system contrasts sharply with that of another Department of the Interior organization—the Bureau of Land Management (BLM). BLM has already implemented an ABC model, which contributed to Interior’s previously mentioned decision to

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3 Commonly referred to as the Fact Finders Act.

4 Some Bureauwide program costs are recoverable. The Power Program Services costs are reimbursable and a few programs, such as the Land Resources Management Program, are partially reimbursed depending on the activities that are being funded. See table 1 for information regarding those programs that are partially reimbursed.

5 The cost accounting standard discusses the need for full cost information. It states that only with reliable full cost information can management ensure that user charges fully recover the costs and that in those cases where user charges are exempted or restricted by law, agencies would nevertheless need the full cost information to assess the extent to which costs are not recovered.
implement ABC departmentwide. BLM's model fully distributes costs and can readily identify, among other things, (1) the full costs of each of its activities, and (2) what it costs to pursue each of its strategic goals. BLM’s system provides detailed information that facilitates external reporting and can be used for internal purposes such as developing budgets and analyzing the unit costs of activities and outputs.

Interior plans to implement the ABC method departmentwide as part of its implementation of the President’s Management Agenda and the department’s vision for effective program management. As stated in the Deputy Secretary’s memo directing all Interior bureaus to adopt an ABC model, each of the President’s governmentwide management initiatives—competitive sourcing, improving financial performance, integrating budget and performance, increasing electronic government, and managing human capital—requires quality cost information. According to the Deputy Secretary’s memo, implementing ABC successfully across the Department of the Interior will:

“...provide the linkage of strategic planning, budgeting, costing and performance reporting. It will increase the value we provide to our customers through more efficient operations and enhance accountability to the Congress and the public (by tying costs to performance measures). This approach can provide the Department with an important tool for managers to monitor and evaluate program performance/results and more effectively allocate resources.”

The department’s directive to implement an ABC model presents an opportunity for the Bureau to provide more relevant and reliable cost information to better meet the needs of decision makers and fulfill each of the five purposes of the Managerial Cost Accounting Standard.

The Bureau Does Not Recover All Reimbursable Costs

While cost information is important for a variety of managerial purposes, as discussed above, it is particularly important to the Bureau in executing water delivery contracts and in setting rates to accomplish its cost recovery requirement. However, even though its cost accounting system has focused primarily on cost recovery, the Bureau is not recovering all reimbursable costs associated with operating its projects.

The Bureau’s authority to determine which costs to charge customers is governed by general provisions of reclamation law, project and program specific legislation, and specific provisions of contracts the Bureau enters into with water users. The costs of activities related to power and water
supply are generally recoverable; however, the Bureau does not recover
certain of these costs.

OMB Circular A-25,\(^6\) which provides guidance for federal agencies to use in
setting fees to recover the full costs of providing goods or services,\(^7\) 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. 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 power and
water supplied by Bureau projects includes all direct and indirect costs
incurred in providing these services. All costs directly or indirectly
benefiting the Bureau’s projects should be recovered, except where
specifically precluded by law.

Some Bureauwide program costs are not being recovered, even though the
programs either directly or indirectly benefit the Bureau's projects and are
not expressly precluded from recovery by specific legislation. Bureauwide
programs are comprised of about 30 programs (the number can vary from
year to year) that undertake a variety of activities that support the Bureau's
projects, involve coordinating with others, or provide technical and
financial assistance to others. Programs include dam safety, land resource
management, technical assistance to states, and O&M program
administration. The programs are administered by the Commissioner's
Office and/or the regional offices and are intended to be "bureauwide" in
scope and benefit the overall Bureau mission.

\(^6\) OMB Circular A-25, User Charges, Revised, July 8, 1993.

\(^7\) 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.
Bureauwide programs are funded with two appropriations: “Policy and Administration” and “Water and Related Resources.” The language of the “Policy and Administration” appropriation provides that it is made nonreimbursable as provided by the Fact Finders Act. The “Water and Related Resources” appropriation contains no express prohibition on reimbursement. Because the “Policy and Administration” appropriation is legislatively precluded from recovery, we limited our analysis in table 1 to Bureauwide programs funded through the “Water and Related Resources” appropriation. Table 1 shows, for each Bureauwide program, (1) the amount appropriated for fiscal year 2002 from the “Water and Related Resources” appropriation, (2) whether the Bureau recovers the costs, (3) which programs have specific legislation exempting them from recovery, and (4) whether the program provides direct or indirect project benefits, or both.

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8 The Policy and Administration appropriation funds the Bureau’s centralized management functions in the Commissioner’s Office, Denver Office, and regional and area offices. The appropriation’s purpose is to fund management and the administrative activities that are not chargeable directly to a specific project or program. Examples of activities funded include overall policy setting and program management, finance and accounting, information resources, and human resources management.

9 The Water and Related Resources appropriation is the largest appropriation received by the Bureau. It funds, in addition to a portion of the Bureauwide programs, construction and rehabilitation of Bureau projects, operation and maintenance of projects and facilities, land management and development, and fish and wildlife management and development.
Table 1: Bureauwide Program Activities Funded by the “Water and Related Resources” Appropriation

<table>
<thead>
<tr>
<th>Bureauwide programs</th>
<th>FY 2002 appropriation</th>
<th>Current cost recovery treatment</th>
<th>Specific legislation exempting</th>
<th>Direct project benefits</th>
<th>Indirect project benefits</th>
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<tr>
<td>Bureauwide programs</td>
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<td>Dam Safety Programs:</td>
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<td>Initiate Safety of Dams Corrective Action</td>
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<td>Safety Evaluation of Existing Dams</td>
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<td>Safety of Dams Corrective Action Studies</td>
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<td>Departmental Irrigation Drainage</td>
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<td>Drought Emergency Assistance</td>
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<td>Efficiency Incentives</td>
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<td>Emergency Planning and Disaster Response</td>
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<td>Examination of Existing Structures</td>
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<td>Federal Building Seismic Safety</td>
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<td>General Planning Activities</td>
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<td>Land Resources Management</td>
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<td>Miscellaneous Flood Control Operations</td>
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<td>National Fish and Wildlife Foundation</td>
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<td>Native American Affairs</td>
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<td>Negotiation &amp; Administration of Water Marketing</td>
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<td>Operations &amp; Maintenance Program Administration</td>
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<td>Power Program Services</td>
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<td>Reclamation Recreation Management Act Title XXVII</td>
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<td>Recreation and Fish &amp; Wildlife Administration</td>
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<td>Science and Technology Programs:</td>
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<td>Advanced Water Treatment Desalination</td>
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<td>Applied Science &amp; Technology Development</td>
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### Bureauwide programs

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<th>FY 2002 appropriation</th>
<th>Current cost recovery treatment</th>
<th>Benefits</th>
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<td>Hydroelectric Infrastructure Protection/Enhancement</td>
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<td>Technology Advancement</td>
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<td>Watershed / River System Management</td>
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<td>Site Security</td>
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<td>Soil &amp; Moisture Conservation</td>
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<td>Technical Assistance to States</td>
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<td>Title XVI – Water Reclamation &amp; Reuse</td>
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<td>Water Management &amp; Conservation</td>
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<td>Wetlands Development</td>
<td>3,836</td>
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</table>

### Notes:

*“Water & Related Resources” funds only, many of these programs also have administration and policy-setting activities funded by the Policy & Administration appropriation.

*Specific Legislation Exempting: Specific legislation, other than the Fact Finders Act, that exempts the program from cost recovery.

*Direct Project Benefits: Benefits can be identified to a specific project.

*Indirect Project Benefits: Benefits multiple projects.

Shaded Programs: Programs with project benefits and no specific legislation exempting cost recovery.

Source: Developed by GAO based on Bureau written program descriptions and interviews with program managers. Bureau officials provided input to the table. We did not independently verify the Bureau’s legal citations for specific legislation exempting some programs from cost recovery and did not independently determine whether there were other legislative exemptions.

The shaded items in table 1 represent costs that (1) are not currently recovered (or are only partially recovered) and (2) directly or indirectly benefit specific projects. In our opinion, these costs should be reviewed to determine whether they may be recovered in accordance with current law. Examples of these costs include the following.

- Environmental and Interagency Coordination program, which involves participating in activities with other agencies and public groups on water-related issues. Work proposed for fiscal year 2002 included working with other agencies to develop methods to evaluate environmental, social, and economic impacts associated with existing and future water resource programs; providing information to public groups; and reviewing other agency environmental compliance
documents to determine the possible impact on current and future Bureau activities (indirect benefits).

- Environmental Program Administration program, which involves activities the Bureau undertakes to ensure compliance with environmental law, policy, and initiatives. Work proposed in fiscal year 2002 was related to assuring compliance with the Endangered Species Act, the National Historical Preservation Act, and the National Environmental Policy Act (indirect benefits).

- 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. Our review of the program found that these inspections are related directly to Bureau projects and facilities, some of which provide water for irrigation and M&I purposes (direct benefits).

- General Planning Activities program, which involves funds used to accomplish various water resource management initiatives and other activities. Work proposed for fiscal year 2002 included maintaining and developing hydrologic models; coordinating with other federal, state, and local agencies; coordinating on wastewater reuse activities; and responding to congressional and public inquiries regarding planning activities (indirect benefits).

- Negotiation and Administration of Water Marketing Program, which involves the administration of repayment contracts that the Bureau holds with entities to which water is delivered. A representative of the Bureau's Commissioner's Office told us that only two regions fund these activities through this program and the long-term goal is to have these regions use other reimbursable funds for these activities which would result in charging these costs to water customers (direct benefits).

- Reclamation Law Administration Program, which involves Bureau inspections to ensure that entities contracting for water delivery are in compliance with the Reclamation Reform Act of 1982. Bureau activities are focused upon ensuring that water districts, individual contractors, and individual water users are in compliance with the act. The Bureau conducts inspections and audits to ensure this compliance. Program costs are consequently directly related to the provision of water to districts, contractors, and users (direct benefits).
The Bureau treats many Bureauwide program costs lacking specific legislative exemption as nonrecoverable under the Fact Finders Act. The Fact Finders Act provides:

“The cost and expense after June 30, 1945, of the Office of the Commissioner 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.”

The Fact Finders Act exempts from recovery the cost of “general investigations” and “nonproject offices” that are not incurred on behalf of a specific project. The Bureau treats many Bureauwide program costs as precluded from recovery under the Fact Finders Act even though some directly or indirectly benefit a specific project or projects. In our opinion, the Fact Finders Act does not preclude recovery of costs when they are incurred directly or indirectly on behalf of a specific project or projects. These include the shaded programs identified in table 1. In our opinion such costs should be distributed to projects and the appropriate amount recovered through water delivery contracts and rates charged to project beneficiaries, unless specifically exempted by legislation.

Program managers, the Congress, and others need relevant and reliable cost information to facilitate budgeting and cost control, performance measurement, cost reimbursement, program evaluation, and economic choice decisions. However, the Bureau’s emphasis on reimbursable costs and cost recovery has left a large portion of its budget—about 21 percent in fiscal year 2002—undistributed to the Bureau’s projects and activities.

Conclusions


11 Commissioner of the Bureau of Reclamation.

12 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.

13 We previously informed the Bureau of our opinion in this regard. See pages 7-9 of U.S. General Accounting Office, Bureau of Reclamation: Information on Operations and Maintenance Activities and Costs at Multipurpose Water Projects, GAO/AIMD-00-127 (Washington, D.C.: May 21, 2000).
Therefore, complete information on the costs of the Bureau’s activities is not available to aid managerial decision making. The current departmental cost accounting initiative presents an opportunity for the Bureau to reevaluate its decisions regarding cost distributions and to make readily available information to support not only cost recovery but also the full range of managerial needs.

In addition to providing more complete cost information for decision-making purposes, the Bureau also has the opportunity to improve its cost recovery efforts by beginning to recover the costs of all programs that directly or indirectly benefit projects, including those related to nonproject offices and investigations. Reclamation law provides that the Bureau recover the costs of certain reimbursable activities, including irrigation, M&I water supply, and power generation. Federal policy requires that the full costs incurred by the federal government in providing services be recovered from the beneficiaries of those services, unless the recovery of such costs is legislatively precluded. However, the Bureau does not recover all costs that benefit specific Bureau projects, even though its cost accounting is focused primarily on cost recovery.

### Recommendations

We recommend that the Secretary of the Interior direct the Commissioner, Bureau of Reclamation, to:

- Enhance the Bureau’s managerial cost accounting so as to provide more complete cost information that facilitates managerial decision making and fulfills each of the five purposes of the Managerial Cost Accounting Standards. This would include distributing Policy and Administration and Bureawide program costs to the appropriate projects and activities and could be accomplished in conjunction with the Department of the Interior’s current cost accounting initiative.

- Review the Bureawide programs and recover the costs of those that either directly or indirectly benefit projects, unless cost recovery is prohibited under current law. Where it is determined that cost recovery is prohibited, this would include documenting the specific legal basis and rationale for the determination.
Agency Comments and Our Evaluation

The Department of the Interior provided written comments on a draft of this report. The comments are reproduced in appendix II and summarized and addressed below. Interior concurred with our recommendation to recover the costs of Bureauwide programs that either directly or indirectly benefit projects, unless cost recovery is prohibited under current law. Interior stated that, as part of ongoing action on a previous report, it will review Bureauwide programs and issue, by March 31, 2004, directives for those programs that will address, among other things, whether the associated costs are recoverable.

We are encouraged by Interior’s comment and look forward to seeing the results of its review. However, we note that the referenced action on the previous findings has been slow. For example, in comments on a draft of the May 31, 2000, report, Interior stated that it would work with the Solicitor’s office to determine whether it could recover costs identified in the report. In July 2002, in the course of our work on the current review, we inquired about the status of the Solicitor’s review and were told that the Solicitor’s input had not yet been requested. We believe it is important to note that while the previous report related only to unrecovered indirect costs, our work during this review identified unrecovered costs related to activities that benefit projects both directly and indirectly, as shown in table 1. Since the Bureau devotes significant resources to the Bureauwide programs and we have now identified costs that directly benefit projects but are not recovered from project beneficiaries, we believe that taking timely action to implement this recommendation is important.

Interior did not concur with our recommendation to distribute Policy and Administration and Bureauwide program costs to projects and activities; however, its comments in doing so were contradictory. Interior did not concur with the recommendation, but stated that it would explore doing as we recommend as part of its implementation of a departmentwide ABC system in fiscal year 2004. We believe that implementing this recommendation is critical if, as stated in its comment letter, Interior plans to implement the recommendation to recover the costs of Bureauwide programs because these programs consist of activities that directly or indirectly benefit projects. In our opinion, distributing these costs would

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facilitate appropriate cost recovery. Interior’s major comments in nonconcurring with this recommendation are synopsized below, along with our responses.

Interior’s first major comment was that the current cost accounting system already meets all of the cost accounting standards’ objectives and purposes and, due to the latitude allowed under the standards, is in compliance with the standards. Interior further states that our finding that the Bureau lacks full cost information to support managerial decisions is misleading. The primary focus of our review was not to narrowly assess compliance with the standards but, rather, to determine whether the Bureau identifies and distributes for management purposes all the costs it incurs in operating its projects and administering its programs. This included determining the Bureau’s primary focus with respect to the purposes of managerial cost information as delineated in the standards—budgeting and cost control, performance measurement, cost reimbursement, program evaluations, and economic choice decisions. We found that the Bureau, because of its focus on cost reimbursement, does not distribute a large portion of its budget (21 percent for fiscal year 2002) and, thus, complete information on the costs of the Bureau’s activities is not available to aid decision making. It is not misleading for us to note that distributing these costs would provide more complete cost information that would be useful for resource allocation decisions, cost analysis and management, and program and performance measurement.

In addition, although stating that its system meets the cost accounting standards’ objectives and purposes, Interior also stated that it plans to continue enhancing the system to “more fully satisfy each of the five purposes” of the standards. Such enhancements were precisely what we had in mind in recommending that the Bureau distribute Policy and Administration and Bureauwide program costs so that more complete information on the costs of the Bureau’s activities would be available to decision makers both within and outside the Bureau. We believe that implementing our recommendation would aid the Bureau as it seeks to “more fully satisfy” the standards’ purposes by providing the Congress, executives, and managers with better and more complete information and analysis on resource utilization and the costs of activities and outputs.

Moreover, we believe that the nonconcurrence with our recommendation to distribute Policy and Administration and Bureauwide program costs contradicts the intent of Interior’s departmentwide effort to implement the President’s Management Agenda. The Deputy Secretary’s January 16, 2002,
memo cited in our report emphasizes the importance of cost information in implementing the President’s Management Agenda and specifically identifies ABC as Interior’s vehicle for understanding and managing costs. The Deputy Secretary’s memo states that “ABC is a cost accounting method that measures the cost of work efforts leading to a specific result.”

To implement its cost accounting initiative, Interior has created an interagency work group. In discussing how to integrate budgeting and performance and improve cost reporting, the work group wrote that ABC is a management tool that attempts to ensure that an organization’s expenditures, including direct and overhead costs, are allocated to products or services in order to identify the cost to the organization of delivering those products or services. The work group further wrote “ABC will facilitate understanding the full cost (direct and indirect) of performance by understanding what drives the cost of work processes… This approach helps assess the efficiency of performance, in dollar terms. It requires detailed accounting for all expenditures and permits aggregating the information at different levels to suit various decision making purposes.” The Bureau will not be able to assess the efficiency of its performance in delivering products and services in such a manner without distributing the costs of its Policy and Administration and Bureauwide program activities.

The second major comment by Interior was that the Bureau’s cost accounting system provides the necessary information for program management and full cost information for external reporting. We disagree. The full costs of the Bureau’s projects, programs, and activities are not reported. As we state in the report, the cost accounting system focuses primarily on cost recovery. It does not identify the full costs of the major activities undertaken by the Bureau in accomplishing the primary purposes of its water projects, such as irrigation, M&I water supply, power generation, recreation, fish and wildlife protection, flood control, water conservation, and land resource management.

As a result, the full costs of, for example, operating the Central Valley Project, the Examination of Existing Structures Program, or the various activities associated with operating and maintaining a facility are not known. In addition, the Bureau does not report the full costs of Bureauwide programs in either its annual report or budget documents. To report the full cost of Bureauwide programs, the Bureau would need to include the costs funded through the Policy and Administration appropriation because many of these programs use Policy and
Administration funds to pay the employees who administer the Bureauwide programs.

The Bureau does report total costs, in aggregate, by Government Performance and Results Acts (GPRA) responsibility segment. However, it does not distribute all of the Policy and Administration costs to its responsibility segments. For example, for fiscal year 2000, the Bureau made Policy and Administration one of its GPRA responsibility segments instead of distributing those costs to the other responsibility segments that Policy and Administration supports. The other responsibility segments were: (1) Water and Energy Management and Development, (2) Land Management and Development, (3) Fish and Wildlife Management and Development, (4) Facilities Operations, and (5) Facilities Maintenance and Rehabilitation. Since the Bureau did not distribute the Policy and Administration costs, it did not report the full costs of the other responsibility segments because the Policy and Administration appropriation funds activities that support the administration of the other segments.

For fiscal year 2001, the Bureau changed the GPRA responsibility segments to the Commissioner's Office and its five regional offices. The Policy and Administration costs were distributed to each of these six offices, with the Commissioner's Office accounting for over 60 percent of the Policy and Administration costs. However, since it made the Commissioner's Office a responsibility segment and did not distribute its costs to the five regional offices, the Bureau did not report the full cost of the regional offices because the Commissioner's Office supports the regional offices.

The third major comment by Interior was that distributing Policy and Administration and Bureauwide program costs would not improve decision making because these costs are not recoverable, are not controllable by project and program managers, and should not be aggregated with program and activity costs because these costs are not appropriated and budgeted to project-level activities. We disagree. The purposes for which managerial cost accounting information is used are different than those for financial and budgetary accounting information and public policy decisions regarding cost recovery that are made through the legislative process. While managerial cost accounting should be integrated with financial and budgetary accounting, it is different in that cost accounting information is developed and tailored to facilitate decision making by program managers, executives, and external stakeholders such as Members of Congress. These decisions often relate to one or more of the purposes delineated in
the cost accounting standards, one of which addresses cost recovery. To meet these needs, managerial cost accounting may employ data produced by the financial and budgetary accounting process as well as nonfinancial or programmatic data, such as units of output.

We understand Interior’s point that Policy and Administration and some Bureawide programs have been legislatively excluded from cost recovery. However this does not mean that these costs should be excluded from distribution and analysis for the purpose of managerial decision making. The Congress, executives, managers, and others need cost information in determining how effectively and efficiently resources are being used, irrespective of whether the costs are recovered. Both the Bureau’s customers and the public have an interest in assuring that resources are used effectively and efficiently and that the costs can be linked to results and outcomes.

We disagree that because costs are not controllable by a manager that costs should not be distributed to the activities managed by that manager. The cost accounting standard addresses this concern and states that:

“For performance measurement or other purposes, some entities may want to make a distinction between controllable and uncontrollable costs with respect to an individual responsibility segment or a cost center. The full cost information need not interfere with this distinction.”

The standard further addresses this issue by stating that:

“Ultimately, most costs are controllable at a certain level of activity by the entity. If some of them are not controllable at a lower level of the organization, they may very well be controllable at a higher level. Each segment should concern itself with the costs that are assigned to it on a cause-and-effect basis. These costs are often incurred because of a segment’s demand and use of services from other segments or entities. Although the service-receiving segment has no control over the efficiency in producing the service, it can influence the costs by changing the demand for the service. For an entity’s top management, full cost reporting provides it with an overview of how the entity’s various costs, including the general and administrative costs, are incurred and assigned to the entity’s segments. The full cost reporting also makes the entity’s top management aware of the costs of services that it receives from other entities. The management can closely review those costs and determine whether actions are needed to control them.”

We also disagree that aggregating Policy and Administration and Bureawide program costs with program and activity costs would make it difficult to evaluate the costs relevant to decision making. As costs are distributed to projects and programs, different types of costs need not lose their identity. For example, the Policy and Administration costs distributed
to projects or programs would retain their identity so managers would know which costs are controllable and recoverable. Understanding the makeup of project and program costs would aid in cost analysis. Again, the cost standard addresses this by stating:

"...as a principle, full cost should include the costs of all resources applied to a program, activity, and its outputs, regardless of funding sources."

Interior’s fourth major comment was that implementing our recommendation would require changes to the Bureau’s accounting system that would not be cost effective. We are not aware of any formal Bureau analysis that has determined what system changes would be required nor the cost effectiveness of any changes. However, any changes would be to a detailed cost accounting system the Bureau already has in place and that already accounts for most of its direct and indirect costs. In addition, we are recommending that any changes be done in conjunction with the implementation of the department’s cost accounting initiative. The department’s interagency work group has recognized that some system modifications will be necessary for each of Interior’s bureaus. It formed a subgroup to identify contractors that the department’s bureaus may already be working with or are considering working with in implementing ABC with the intent of maintaining consistency and trying to pool resources across the department.

Moreover, system costs did not stop the BLM from distributing all of its costs and making changes to its cost accounting system as it implemented ABC. BLM’s implementation of ABC is in part what prompted Interior to implement ABC department wide. Although BLM and the Bureau have different missions and outputs, ABC is not a mission-dependent cost accounting system and it is being used in both the private and public sector by a wide range of businesses and federal agencies. BLM’s implementation of ABC resulted in its identifying activities and producing unit cost information for 131 outputs and tying these amounts back to its Statement of Net Costs (full costs).

We will send copies of this report to appropriate House and Senate Committees; interested members of the Congress; The Honorable Mitchell E. Daniels, Jr., Director, Office of Management and Budget; and other interested parties. This report will also be available free of charge on GAO’s home page at http://www.gao.gov. We will also make copies available to others upon request.
Please call me at (202) 512-9508, or Rob Martin, Assistant Director, at (202) 512-6131 if you or your staff have any questions. Major contributors to this report are listed in appendix IV.

Sincerely yours,

Linda M. Calbom
Director
Financial Management and Assurance
In previous work at the Department of the Interior’s Bureau of Reclamation, we identified certain reimbursable project costs that were not being recovered by the Bureau. Based on this and other work we have performed at the Bureau, we decided to examine the managerial cost accounting practices it uses in carrying out its financial management and cost recovery responsibilities. Our objectives were to determine whether the Bureau (1) identifies and distributes for management purposes all the costs it incurs in operating its projects and administering its programs, and (2) ensures that recoverable costs are identified and recovered from customers.

The scope of our review included the Bureau's managerial cost accounting practices and the Bureau's treatment of different types of costs related to its administration and operation of its projects and the delivery of its programs. We conducted our audit work at the Bureau's Denver, Colorado office and at its Mid-Pacific region. For comparative purposes, we also obtained and analyzed information on the managerial cost accounting practices, and use of Activity Based Cost accounting information, of the Department of the Interior's Bureau of Land Management.

The following sections provide details of our methodologies and any additional restrictions on the scope of our work.

Determining Whether the Bureau Allocates All Costs to Projects and Programs

We reviewed relevant legislation, accounting standards, and documents, including financial management laws such as the Chief Financial Officers Act of 1990 and the Federal Financial Management Improvement Act of 1996; reclamation law; Federal Financial Accounting Standards; a 1998 Bureau report to the Congress on operations and maintenance activities and overhead; a 1999 Bureau cost accounting report; and Department of the Interior and Bureau of Reclamation policies, accounting manuals, and other cost accounting guidance. We also reviewed the Bureau's Strategic Plan and annual reports to determine how managerial cost information is used or could be used. We requested and examined the types of cost accounting reports produced by the Bureau's financial accounting system.


Appendix I
Objectives, Scope, and Methodology

To determine how the Bureau distributes both direct and indirect costs, we reviewed Interior and Bureau policy and procedures for distributing costs and discussed these policies and procedures with Bureau officials. In addition, we interviewed knowledgeable personnel to enhance our understanding and consulted with Bureau Denver office officials to develop flowcharts that documented how the Bureau’s costs are distributed to project purposes.

Determining Whether the Bureau Identifies All Reimbursable Costs and Recovers Those Costs From Customers

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. We also reviewed prior GAO reports pertaining to the Bureau’s cost recovery practices.

We determined the Bureau’s basis for including or excluding costs from recovery. We did not independently verify the Bureau’s legal citations for specific legislation exempting some programs from cost recovery. We also reviewed the Fact Finders Act to determine the limitations it places on the Bureau’s ability to recover costs.

We identified the budget amounts associated with Policy and Administration and with each of the Bureauwide programs. We reviewed and analyzed Bureauwide programs for funding levels, cost recovery policies and practices, and the legislative basis for these policies and practices. We interviewed Bureau officials responsible for many of these programs, obtained information on the activities performed in these programs, and reviewed and analyzed the written descriptions of these programs. We provided a summary of our analysis to Bureau officials for their review and comment.

We conducted our review from November 2001 through July 2002 in accordance with generally accepted government auditing standards. We provided the Department of the Interior and the Bureau of Reclamation with copies of a draft of this report for review and comment. Written comments were received and have been reproduced in appendix II.
Appendix II

Comments From the Department of the Interior

United States Department of the Interior
OFFICE OF THE SECRETARY
Washington, D.C. 20240

Ms. Linda M. Calbom
Director, Financial Management and Assurance
General Accounting Office
441 G Street N.W.
Washington, D.C. 20548

Dear Ms. Calbom:

Enclosed is the Department of the Interior’s response to the General Accounting Office (GAO) draft report “Bureau of Reclamation: Opportunities Exist to Improve Managerial Cost Information and Cost Recovery” (GAO-02-973). We appreciate the opportunity to provide comments.

In response to Recommendation 1, the Bureau of Reclamation does not concur with the recommendation to distribute Policy and Administration (P&A) and Reclamation-wide program costs to the projects and activities. However, as the Department moves forward with the implementation of the Activity-Based Costing initiative in fiscal year 2004 Reclamation will explore reporting of P&A and Reclamation-wide program costs.

Reclamation will continue to enhance and improve its cost accounting to provide relevant and reliable information for decision-making and to more fully satisfy each of the five purposes of the Managerial Cost Accounting Standards. The Managerial Cost Accounting Standards provide, “Managerial costing should use a basis of accounting, recognition, and measurement appropriate for the intended purpose.” (emphasis added) Reclamation believes its current cost accounting meets its intended purpose as well as the objectives and purposes of the Managerial Cost Accounting Standards. Reclamation’s cost accounting system provides the information necessary for program management as well as provide the full cost of its programs and activities to external constituents. Distributing P&A and Reclamation-wide program costs would not improve the decision-making usefulness of the information since these costs are not appropriated or budgeted to project-level activities.

In response to Recommendation 2, Reclamation will continue to implement its planned actions to resolve a recommendation issued in a previous GAO audit report “Bureau of Reclamation, Information on Operations and Maintenance Activities and Costs at Multipurpose Water Projects” (GAO/AIMD-00-127), issued May 31, 2000. More specifically, Reclamation plans to review those Reclamation-wide programs that directly or indirectly benefit projects and issue
Reclamation Manual Directives and Standards for those programs. The updated directives and standards will address the basis for funding these programs, including cost recovery, if applicable.

Again, thank you for the opportunity to review the draft report. Reclamation’s response to the report’s recommendations, general comments on the draft report, and technical/editorial comments are enclosed for your review and consideration.

Sincerely,

[Signature]

Bennett Raley
Assistant Secretary for Water and Science

Enclosures
Bureau of Reclamation

Draft General Accounting Office (GAO) Report
Response to Audit Recommendations

Bureau of Reclamation: Opportunities Exist to Improve Managerial Cost Information and Cost Recovery
GAO-02-973

Recommendation 1:

Enhance the Bureau’s managerial cost accounting so as to provide information that facilitates managerial decision-making and fulfills each of the five purposes of the Managerial Cost Accounting Standard. This would include distributing Policy and Administration and Bureaumwide Program costs to the appropriate projects and activities and could be accomplished in conjunction with the Department of the Interior’s current cost accounting initiative.

Response: Nonconcur. The Bureau of Reclamation does not concur with the recommendation to distribute Policy and Administration (P&A) and Reclamation-wide program costs to the projects and activities.

Reclamation will continue its efforts to enhance and improve cost accounting to provide relevant and reliable information that facilitates managerial decision-making, to more fully fulfill each of the five purposes of the Managerial Cost Accounting Standards, and to report these costs in accordance with the Department of the Interior’s cost accounting initiative.

Reclamation will explore the reporting of P&A and Reclamation-wide program costs in accordance with the Department’s Activity-Based Costing initiative, to be implemented in fiscal year 2004. The Managerial Cost Accounting Standards provide, “Managerial costing should use a basis of accounting, recognition, and measurement appropriate for the intended purpose.” (emphasis added) Reclamation believes its current cost accounting meets its intended purpose as well as the objectives and purposes of the Managerial Cost Accounting Standards. Reclamation’s cost accounting system provides its managers with relevant and reliable information necessary to manage their programs in an efficient and effective manner as well as provide cost information to external users such as the Congress, customers, and other Federal agencies. Reclamation reports the full costs of its programs and segments in its annual financial statements and annual budget reports. In Reclamation’s opinion, reporting full costs in this manner is in accordance with the Chief Financial Officers Act of 1990, Government Performance Results Act of 1993, and the Managerial Cost Accounting Standards. Moreover, the Managerial Cost Accounting Standards provide management with latitude and flexibility in the application of the standard as follows, “These standards are based on sound cost accounting concepts and allow sufficient flexibility for agencies to develop managerial cost accounting practices that
are suited to their specific operating environments.” In Reclamation’s opinion, GAO’s recommendation does not take this flexibility into consideration.

Given Reclamation’s operating environment and various legislative requirements, we do not agree that this recommendation would result in information that was more decision useful. The allocation of P&A and Reclamation-wide program costs to specific programs and activities in the accounting system would not improve program management or decision-making since these costs are not appropriated or budgeted to project-level activities. On the contrary, if P&A and Reclamation-wide program costs were aggregated with the costs of programs and activities, it would make it more difficult to evaluate the costs relevant for decision-making, e.g., costs which are controllable by program managers. Also, since a considerable amount of Reclamation’s operations involve multipurpose water projects, e.g., irrigation, power, flood control, etc., the allocation of P&A and Reclamation-wide program costs would require a significant change to our accounting processes. This would require significant resources to modify the accounting system and would not be cost effective.

Recommendation 2:

Review the Bureauwide Programs and recover the costs of those that either directly or indirectly benefit projects, unless cost recovery is prohibited under current law. Where it is determined that cost recovery is prohibited, this would include documenting the specific legal basis and rationale for the determination.

Response: Concur. As part of continued action on Recommendation 1 of a previous GAO audit report “Bureau of Reclamation, Information on Operations and Maintenance Activities and Costs at Multipurpose Water Projects” (GAO/AIMD-00-127), issued May 31, 2000, Reclamation has developed a plan to review those Reclamation-wide programs that either directly or indirectly benefit projects and develop applicable, individualized Reclamation Manual Directives and Standards for those programs. The development of the revised or new directives and standards will address the basis for funding of these programs, as well as applicable rationale for the determination of appropriate cost recovery or the determination that costs are nonreimbursable. Issuance of the revised or new directives and standards are currently scheduled for completion by March 31, 2004.
Appendix II
Comments From the Department of the Interior

Bureau of Reclamation
Draft General Accounting Office (GAO) Report
General Comments on Draft GAO Report

Bureau of Reclamation: Opportunities Exist to Improve Managerial Cost Information and Cost Recovery
GAO-02-973

Finding: The Bureau Lacks Full-Cost Information To Support Managerial Decisions:

The title of this finding and the condition that GAO portrays is misleading. GAO’s report implies that Reclamation is not meeting the Statement of Federal Financial Accounting Standards No. 4, Managerial Cost Accounting Standards, and does not have cost information to support managerial decisions because it is not distributing Policy and Administration (P&A) and Reclamation-wide program costs. Reclamation does not agree with this narrow perspective and interpretation of the Managerial Cost Accounting Standards. Overall, Reclamation is in substantial compliance with the Managerial Cost Accounting Standards and Reclamation is making progress, in conjunction with the Department of the Interior’s costs initiative, to further enhance its cost accounting. Currently, Reclamation’s cost accounting system provides relevant and reliable cost information necessary for (1) managing Reclamation programs, (2) reporting cost information to external users, (3) ensuring consistency between costs reported in the general purpose financial statements and costs reported to program managers, and (4) addressing the variety of complex cost accounting needs.

(1) Reclamation’s cost accounting system provides its managers with relevant and reliable information necessary for informed program management. To fulfill its mission as a water resources management agency, which includes the recovery of capital investment and operation and maintenance costs associated with its multipurpose water projects, Reclamation has developed a detailed and comprehensive accounting system. In addition to accounting for all direct costs, the accounting system allocates all indirect costs to programs and activities. Indirect costs are in excess of $100 million annually. As mentioned in the report, a Reclamation-wide team recently completed a comprehensive evaluation of its costing processes to ensure the consistent treatment of direct and indirect costs.

(2) Reclamation currently provides full-cost information to external users such as the Congress, customers, and other Federal agencies. Reclamation reports the full costs of its programs and segments in its annual financial statements and annual budget reports. Reclamation believes that reporting full costs at this level is in accordance with external reporting requirements such as the Government Performance Results Act of 1993 (GPRA) and the Chief Financial Officer’s Act of 1990.
To more accurately reflect its water resources management mission, Reclamation implemented a new programmatic budget structure in fiscal year 1998. Reclamation's budget structure is more responsive to the planning, cost accounting, and reporting requirements of GPRA. This budgetary reporting structure provides decision makers, both internal and external with information necessary to determine if Reclamation is achieving statutory objectives and to determine the effectiveness and efficiency of its programs.

This structure is used to report the costs of Reclamation's "program activities" consistent with the GPRA definition which provides "... program activity means a specific activity or project as listed in the program and financing schedules of the annual budget of the United States Government." GAO's recommendation to distribute P&A would result in mixing costs from different appropriations provided for different purposes. Reclamation does not distribute P&A costs to projects because these costs are "non-project" costs by definition. Policy and Administration is an entirely different appropriation than Water and Related Resources. The Congress purposely provides P&A as a separate and distinct appropriation with the intent of NOT mixing those funds and costs with those of programs funded by different appropriations.

Under Reclamation's budget structure, all funding is allocated into several appropriation accounts. Funding in the Water and Related Resources appropriation account is fully funded within the following five program activities: "Water and Energy Management and Development"; "Land Management and Development" activity; "Fish and Wildlife Management and Development" activity "Facility Operation" activity; and the "Facility Maintenance and Rehabilitation" activity. The sixth major appropriation account, "Policy and Administration (P&A)," involves the development of Reclamation policy and the direction of daily operations and is fully funded within the P&A appropriation account.

(3) Reclamation uses information from its Federal Financial System for Federal Agencies' Centralized Trial-Balance System (FACTS) I, for proprietary financial data, and FACTS II, for budget execution data, reporting to ensure consistency between costs reported in the general purpose financial statements and costs reported to program managers. In accordance with the Office of Management and Budget requirements and Departmental guidance, Reclamation reports the full cost of its responsibility segments and major program activities in its annual financial statements. Reclamation's accounting system integrates financial, budget, and cost accounting processes for management purposes.

(4) As stated above, Reclamation's cost accounting system addresses a wide variety of complex and often competing cost accounting requirements while meeting the objectives and purposes of the Managerial Cost Accounting Standards as well as departmental and governmental initiatives. GAO's report fails to fully recognize Reclamation's ability to respond to a variety of cost reporting perspectives such as organizational, customer, projects, budgetary, and financial accounting views. Rather, GAO's report focuses on distributing P&A and Reclamation-wide program costs which provide only one of many cost perspectives. The Managerial Cost Accounting Standards (Standards) provide,
"Managerial costing should use a basis of accounting, recognition, and measurement appropriate for the intended purpose." (emphasis added) Reclamation believes its current cost accounting meets its intended purpose as well as the objectives and purposes of the Standards. Moreover, the Standards provide management with latitude and flexibility in the application of the standard. In Reclamation's opinion, GAO's recommendation does not take this flexibility into consideration. The Standards, Section 24, provides, "These standards are based on sound cost accounting concepts and allow sufficient flexibility for agencies to develop managerial cost accounting practices that are suited to their specific operating environments."

Furthermore, Reclamation's cost accounting fulfills each of the five purposes of the Standard. Following is a brief description of the use of cost information for the five purposes.

Budgeting and Cost Control - To ensure accurate cost recovery and reimbursement, costs are accounted for at a detailed level. For example, for its multipurpose water projects, costs are accumulated at the detailed job level, such as a project feature such as a spillway, to enable the accurate recovery of costs allocated to reimbursable project purposes, e.g., irrigation. Historical costs are used as the basis for formulating future budgets. And finally, project and program costs are monitored to ensure that they do not exceed available funding.

Performance Measurement - Cost information is currently used for performance measurement. For example, one of the GPRA performance measures is the unit cost of hydroelectric power generation relative to other power generation entities. Costs are compiled in accordance with Federal Energy Regulatory Commission accounts to facilitate comparison with other entities.

Determining Reimbursements and Setting Fees and Prices - Reclamation's cost accounting system provides the cost information required for cost recovery and reimbursement purposes. For example, as required by legislation, capital costs allocated to certain project purposes, principally irrigation, municipal and industrial water, and power generation, are recovered from project beneficiaries. Moreover, these beneficiaries are responsible for an allocated share of operation and maintenance costs. To ensure that these cost recovery requirements are met, Reclamation's cost accounting system accounts for all direct and indirect costs at a detailed level.

In addition, Reclamation's cost accounting system provides the cost information required for the working capital and revolving funds. And finally, accurate cost information is required for reimbursement from foreign countries for technical assistance.

Program Evaluations - Reclamation's cost accounting system provides cost information which is used for cost-benefit analyses and to assess alternatives. For example, the cost of uprating a power generation facility might be compared to the increased power generation and the period necessary to recover the uprating costs.
Economic Choice Decisions - Cost information provided by the cost accounting system is used to assess project alternatives. For example, such information is used to assess various construction or facility rehabilitation alternatives.

Reclamation agrees, in concept, that full costing of its programs and activities might be useful in some situations. There are, however, mitigating factors that need to be considered when determining whether full costing should be developed, and if so, what categories of costs should be included. For example, it must be determined whether the inclusion of certain categories of costs will improve the decision-usefulness of the information. A related factor in assessing whether a category of costs should be included, is whether it will be cost effective to include this category of costs. The increased decision-making benefit of the additional information should exceed the additional cost of assigning this category of costs to specific programs and activities.

While theoretically appealing, the allocation of P&A and Reclamation-wide program costs to specific programs and activities in the accounting system would not improve program management or decision-making since these costs are not appropriated or budgeted to project-level activities. On the contrary, if P&A and Reclamation-wide program costs were aggregated with the costs of programs and activities, it would make it more difficult to evaluate the costs relevant for decision-making, e.g., costs which are controllable by program managers. Also since a considerable amount of Reclamation's operations involve multipurpose water projects, e.g., irrigation, power, and flood control etc., the allocation of P&A and Reclamation-wide program costs would require a significant change to our accounting processes. This would require significant resources to modify the accounting system and would not be cost effective.

Based on the latitude provided in the Standards, as mentioned above, Reclamation believes that it is not required to allocate P&A and Reclamation-wide program costs to the project-level activities in its accounting system.
## Total Policy and Administration and Bureauwide Program Costs In Comparison to the Bureau’s Total Budget, 1997-2002

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<tr>
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<tr>
<td>Policy &amp; Administration</td>
<td>$46,000</td>
<td>$47,558</td>
<td>$47,000</td>
<td>$47,424</td>
<td>$50,114</td>
<td>$52,968</td>
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<td>Percent of total Bureau budget</td>
<td>5.8</td>
<td>5.3</td>
<td>5.9</td>
<td>6.0</td>
<td>6.1</td>
<td>5.6</td>
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<td>Bureauwide programs (Water &amp; Related Resources funding)</td>
<td>$92,932</td>
<td>$114,087</td>
<td>$120,579</td>
<td>$123,491</td>
<td>$146,161</td>
<td>$145,148</td>
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<tr>
<td>Percent of total Bureau budget</td>
<td>11.7</td>
<td>12.7</td>
<td>15.1</td>
<td>15.6</td>
<td>17.9</td>
<td>15.4</td>
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<td>Total Policy &amp; Admin. and Bureauwide programs</td>
<td>$138,932</td>
<td>$161,645</td>
<td>$167,579</td>
<td>$170,915</td>
<td>$196,275</td>
<td>$198,116</td>
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<td>Combined Policy and Administration and Bureauwide programs as percent of total Bureau budget</td>
<td>17.4</td>
<td>18.0</td>
<td>20.9</td>
<td>21.6</td>
<td>24.1</td>
<td>21.0</td>
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<td>Total Bureau budget authority</td>
<td>$796,182</td>
<td>$898,569</td>
<td>$799,923</td>
<td>$792,637</td>
<td>$814,962</td>
<td>$943,457</td>
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Appendix IV

GAO Contact and Staff Acknowledgments

<table>
<thead>
<tr>
<th>GAO Contact</th>
<th>Rob Martin, (202) 512-6131</th>
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Acknowledgments

In addition to the individual named above, Brian Eddington and Larry Feltz made key contributions to this report.
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