



U.S. Department of Agriculture



Office of Inspector General  
Great Plains Region

## **Audit Report**

### **Natural Resources Conservation Service Compliance with the Improper Payments Information Act of 2002**

Report No. 10601-0003-KC  
January 2005

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UNITED STATES DEPARTMENT OF AGRICULTURE



OFFICE OF INSPECTOR GENERAL

WASHINGTON, D.C. 20250

DATE: January 10, 2005

REPLY TO

ATTN OF: 10601-0003-KC

SUBJECT: Natural Resources Conservation Service Compliance with the Improper Payments Information Act of 2002

TO: Bruce I. Knight  
Chief  
Natural Resources Conservation Service

ATTN: Steven A. Probst  
Acting Management Control Officer  
Operations Management and Oversight Division

This report presents the results of our audit of Natural Resources Conservation Service (NRCS) compliance with the Improper Payments Information Act (IPIA) of 2002,<sup>1</sup> and the requirements and implementing guidance issued by the Office of Management and Budget (OMB) and the Office of the Chief Financial Officer (OCFO). The audit was conducted as part of a Department-wide audit of USDA's implementation of the IPIA. Our review disclosed that NRCS had not taken sufficient action to comply with the IPIA and the provisions set forth by OMB and OCFO.

## **BACKGROUND**

The IPIA requires the head of each agency to annually review all programs and activities the agency administers to identify those that may be susceptible to significant improper payments. OMB issued guidance for implementing the IPIA on May 21, 2003. This guidance required each agency to report the results of its estimates for improper payments and corrective actions in the Management Discussion and Analysis section of USDA's Performance and Accountability Report for fiscal years ending on or after September 30, 2004. OMB also defined significant improper payments<sup>2</sup> and specified that if programs or activities exceeded this threshold, agencies must develop a statistically valid estimate to report to Congress. Finally, OMB required agencies to submit their implementation plans by November 30, 2003.

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<sup>1</sup> Public Law (P.L.) 107-300, November 26, 2002.

<sup>2</sup> OMB defined significant improper payments as annual erroneous payments exceeding both 2.5 percent of program payments and \$10 million. See OMB Memorandum M-03-13, dated May 21, 2003.

The OCFO, designated as the lead agency for coordinating and reporting the Department's efforts to implement the IPIA, provided instructions to agencies in August and October 2003. The August memorandum transmitted Departmental policy and instructions for implementing program reviews to identify erroneous payments. The instructions included the detailed guidance from OMB regarding implementation and requirements for the IPIA.<sup>3</sup> The guidance from OMB provided that agencies examine the risk of erroneous payments in all programs and activities they administer. In a memorandum, dated October 9, 2003, OCFO provided additional guidance to NRCS on implementing the requirements of the IPIA and requested that all agencies provide an IPIA implementation status report.<sup>4</sup> The memorandum required that all programs with outlays of \$10 million or more annually must undergo a risk assessment to determine if there is significant risk of erroneous payments. The memorandum also requested: (1) A chart detailing dates for risk assessments that have been completed; (2) planned dates for completion of remediation plans for programs with significant erroneous payments; and (3) planned dates when the agency will have determined its baseline plus improvement targets for the next 3 fiscal years (FY).

NRCS identified seven program categories with outlays of over \$2.3 billion that met the threshold for performing risk assessments. These program categories included Conservation Technical Assistance, Farm Bill Technical Assistance, Watershed and Flood Prevention Operations, Resource Conservation and Development, Farm Security and Rural Investment Programs, Conservation Operations, and All Other Conservation Programs.

## **OBJECTIVE**

The objective of the audit was to evaluate the actions taken by NRCS to assess the susceptibility of its programs to improper payments in accordance with the IPIA and the implementing guidance of OMB and OCFO.

## **SCOPE AND METHODOLOGY**

We performed our audit at NRCS Headquarters in Washington, D.C. To accomplish our audit objective, we:

- Reviewed the requirements and guidance issued by OMB and OCFO regarding improper payments;
- Reviewed Office of Inspector General (OIG) audit reports of NRCS programs and operations from January 1999 through February 2004, and internal reviews conducted by NRCS from FY 2000 through FY 2002;
- Interviewed NRCS officials and examined documentation to determine what they had done to implement the IPIA; and
- Reviewed NRCS' FMFIA Reports for 2002 and 2003.

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<sup>3</sup> OCFO Guidance, Requirements for Implementing IPIA, August 11, 2003.

<sup>4</sup> OCFO Guidance, Update on Requirements for Implementing the IPIA, Public Law 107-300, dated October 9, 2003.

The audit was initially conducted during the period March through May 2004. Subsequently, NRCS performed risk assessments and we evaluated those actions during August and September 2004.

The audit was performed in accordance with Government Auditing Standards.

## **FINDING AND RECOMMENDATION**

### **NRCS Was Not in Compliance With the Improper Payments Information Act**

Our audit disclosed that NRCS initially took only limited action to implement the requirements to comply with the IPIA's provisions. NRCS grouped similar programs into seven categories such as the category, Farm Security and Rural Investment Programs, which consisted of: the Wetland Reserve Program (WRP), Klamath Basin, Farmland Protection Program, Environmental Quality Incentives Program (EQIP), Wildlife Habitat Incentives Program, Conservation Security Program, Grasslands Reserve Program, Ground and Surface Water Conservation, Farm Security and Rural Investment Program (technical assistance), Agriculture Management Assistance (AMA), and Farm Service Agency Administrative Cost (technical assistance). In lieu of conducting detailed risk assessments, NRCS officials informed us that the decision to report that none of NRCS' programs were susceptible to significant improper payments was based on discussions with program managers, reviews of Federal Managers' Financial Integrity Act reports, reviews of various audit reports, and general program knowledge. However, we found no supporting documentation of any discussions held or of any reviews performed or prepared to support NRCS' assertion that its programs were not susceptible to significant improper payments.

Although OCFO provided guidance to NRCS for implementing the IPIA (which included guidance from OMB), we found that NRCS had not taken sufficient steps to implement the IPIA. NRCS officials stated that risk assessments were not completed because they did not have the time or personnel to perform them. Despite the absence of any evidence of the conduct of risk assessments, on November 25, 2003, NRCS reported to OCFO that none of their seven program categories, totaling over \$2.3 billion and ranging from \$14 million to over \$1 billion, were subject to significant risk of erroneous payments. OCFO, in turn, reported to OMB on December 1, 2003, in its Implementation Plan that NRCS programs were not susceptible to improper payments.

During the course of our review, OCFO informed us that OMB wanted NRCS to reconsider its assessment of the Farm Security and Rural Investment Programs, because these programs, which totaled over \$1 billion in outlays, were potentially of high risk. In response, NRCS managers initiated risk assessments for AMA, EQIP, and WRP.<sup>5</sup> NRCS informed us that the milestone date for completing the risk assessments was August 2004.

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<sup>5</sup> EQIP, Wetland Reserve Program, and AMA are individual programs that are funded under the Farm Security and Rural Investment Programs.

Accordingly, we suspended our fieldwork until these assessments were completed. Our review of the assessments, once completed, disclosed that the process that had been undertaken employed a matrix of risk factors, as suggested in OCFO guidance, a rating of the risk (high, medium, and low), an explanation of the rating, and a reference to an attached source document supporting the explanation. We found the process was inadequate because the “explanation” afforded to justify the risk rating was generally not a description of internal controls, designed to mitigate risk, but a statement of the operational procedure in place to implement the program requirement. Additionally, the justification and support for the final ratings were not described (e.g., EQIP was scored as having “medium” risk; the other assessments had not yet been finalized when we completed our work). As a result, no assurance or understanding could be gained as to the estimated dollar value of improper payments because an error rate had not been determined. Further, we were unable to readily trace the justification of the risk rating to the source document, though we abandoned the effort when we determined that the references were of limited or no utility.

NRCS officials also informed us that they had reduced assurance its controls over program activities were functioning as prescribed, because reviews of the State offices had not been performed in 2002 and 2003. However, subsequent to the end of fieldwork, NRCS officials informed us that the Financial Management Division had reinstated its reviews of State offices and completed three reviews in the June through August period of 2004. Further, they stated that they intend to expand upon their scheduled reviews. In addition, they informed us that they have aggressively worked to overcome staffing shortages by adding full-time and contractor personnel specifically for addressing issues such as improper payments. NRCS officials also informed us that they have initiated or have plans to strengthen the agency’s overall internal control posture.

Agencies have been required for over 20 years to assess the internal controls in their programs and financial management activities pursuant to the Federal Managers’ Financial Integrity Act (FMFIA) of 1982 and other legislative and administrative initiatives. The FMFIA requires ongoing evaluations of the adequacy of the systems of internal accounting and administrative control of each agency and requires the head of each agency to issue an annual report that discloses material weaknesses identified through the assessment process and the actions planned to correct those weaknesses. With this knowledge and experience, agencies should be able to assess their programs and activities for improper payments, determine those that are susceptible to significant improper payments, and meet the reporting requirements imposed by the IPFA.

In order to provide the insights needed to evaluate a program’s susceptibility to improper payments, NRCS needed to conduct a risk assessment employing a methodology such as:

- Identification of program risk factors,
- Identification of the control measures prescribed to mitigate those risks and an evaluation as to their adequacy, and
- Compliance testing to ensure the controls are functioning as prescribed; the results of this examination would yield the estimated error rate.

In summary, NRCS had not identified the control measures in place to preclude, or detect in a timely manner, improper payments nor did it know if the controls were in operation. Accordingly, in our view, NRCS was not in the position to rate its programs as to the susceptibility to improper payments nor complete the remainder of the requirements set forth in that regard, and thus it had not sufficiently complied with the guidance provided by OMB and OCFO nor met the requirements of the IPIA.

At the exit conference, NRCS officials informed us that they take the improper payment initiative very seriously but had misinterpreted the guidance regarding what they needed to do. As a result of our evaluation of the implementation of the OCFO guidance by NRCS and the other agencies included within our overall scope, we concluded that the requirements and instructions issued by the Department need to be made more prescriptive, detailed, and clarified. We have made a recommendation to that effect to OCFO in our rollup report to the Department.

### **RECOMMENDATION**

Conduct more thorough risk assessments of all programs with outlays of \$10 million or more and develop an estimated error rate by: developing criteria to identify program vulnerabilities, determining acceptable risk levels, ranking the risk factors, and establishing controls to ensure their timely and accurate completion.

### **AGENCY POSITION**

NRCS agreed to conduct more thorough risk assessments of all programs with outlays of \$10 million or more in their response, dated December 16, 2004 (see Exhibit A). NRCS will develop an estimated error rate by developing criteria to identify program vulnerabilities, determining acceptable risk levels, ranking the risk factors, and establishing controls to ensure their timely and accurate completion. NRCS stated these actions will be completed by April 30, 2005.

### **OIG POSITION**

We concur with the management decision. To achieve final action, NRCS needs to comply with the effective OCFO guidance and complete corrective action in accordance with the specified timeframes.

Please follow your agency's internal procedures in forwarding documentation for final action. Final action on the management decision should be completed within 1 year of the date of the management decisions to preclude being listed in the Department's annual Performance and Accountability Report.

Bruce I. Knight

6

We appreciate the courtesies and cooperation extended to our staff during this review.

/s/

ROBERT W. YOUNG  
Assistant Inspector General  
for Audit

# EXHIBIT A-AGENCY RESPONSE

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United States Department of Agriculture



Natural Resources Conservation Service  
P.O. Box 2890  
Washington, D.C. 20013

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DEC 16 2004

**SUBJECT:** Natural Resources Conservation Service (NRCS) Compliance with the  
Improper Payment Information Act of 2002

**TO:** Robert W. Young  
Assistant Inspector General for Audit

The NRCS' response to the Official Draft is as follows:

NRCS will conduct more thorough risk assessments of all programs with outlays of \$10 million or more. NRCS will develop an estimated error rate by developing criteria to identify program vulnerabilities, determining acceptable risk levels, ranking the risk factors, and establishing controls to ensure their timely and accurate completion. These actions will be completed by April 30, 2005.

NRCS is already participating with the OCFO IPIA effort and will plan to work diligently to resolve all concerns. If you have specific questions with this response, contact me at 202-720-9135.

A handwritten signature in black ink, appearing to read "S. Probst", written over a horizontal line.

STEVEN A. PROBST  
Acting Management Control Officer

cc:  
Katherine C. Gugulis, Deputy Chief, Strategic Planning and Accountability  
P. Dwight Holman, Deputy Chief, Management  
Joseph Oleska, Director, Financial Management Division



Informational copies of this report have been distributed to:

Chief, NRCS	
Attn: Agency Liaison Officer	(10)
Office of the Chief Financial Officer	
Director, Planning and Accountability Division	(1)
Government Accountability Office	(1)
Office of Management and Budget	(1)