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FINANCIAL AUDIT

EPA's Financial
Statements for Fiscal
Years 1988 and 1987

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

Comptroller General
of the United States

B-216351

March 16, 1990

To the President of the Senate and the
Speaker of the House of Representatives

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This report presents our opinion on the Environmental Protection Agency's (EPA) consolidated financial statements for the fiscal years ended September 30, 1988 and 1987, and our reports on internal accounting controls and compliance with laws and regulations. We conducted our audits in accordance with generally accepted government auditing standards.

Our opinion discusses the financial condition of EPA's Superfund program. Considering EPA's experience to date and the limitations in its estimating methodology, we believe that the cost to pay for and oversee the cleanup of the nation's most hazardous waste sites will far exceed EPA's current \$30 billion estimate and overwhelm the remaining \$7.1 billion Superfund authorization. The information presented in this report should contribute to the upcoming congressional deliberations on the Superfund program's reauthorization.

As we reported last year, our opinion is qualified because of (1) the manner in which EPA accounted for and supported its property accounts and (2) weaknesses in the internal control system it used to control and safeguard property assets totaling over \$320 million. EPA's problems with property are not new. The agency first reported an accounting system weakness related to property for fiscal year 1983. But, as a result of our first financial statement audit for fiscal year 1987, EPA reported this problem as a material weakness in its internal control system for property assets in its fiscal year 1988 Federal Managers' Financial Integrity Act report.

Our report on EPA's internal accounting controls discloses that, while improvements have been made by EPA, the previously mentioned material weakness in its accounting for and controlling property assets continues to exist. Our report provides details on our findings and our recommendations for improvement.

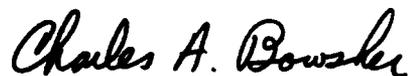
Other financial management and control problems uncovered as a result of our first financial audit in 1987 have been resolved. These include the following:

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- We identified discrepancies totaling over \$1.2 billion between EPA's general ledger and the balances appearing in the financial statements it submitted to Treasury at the end of fiscal year 1986. We also found that these reports were not supported by adequate documentation. Correcting these errors required adjustments to EPA's fiscal year 1987 consolidated financial statements totaling over \$789 million. EPA subsequently improved the quality of the documentation supporting its external reports, and we did not find similar problems in our fiscal year 1988 audit.
- We reported discrepancies totaling over \$742 million in EPA's cash, receivable, and receipt account balances. EPA management was unaware of these problems because it had not performed the periodic reconciliations necessary to identify and correct errors and omissions. As a result of our audit, EPA management has placed increased emphasis on reconciliation as an internal control technique, and similar reconciliation problems were not found in fiscal year 1988.

In 1989, while we were completing our fiscal year 1988 audit, EPA converted to a new integrated financial management system and, in the process, experienced problems. These problems have not yet been resolved and will require the full attention of EPA financial management personnel. EPA's management has taken the position that dealing with the system problems warrants its priority attention and resources. For that reason, we will not conduct a fiscal year 1989 audit. It is vital, however, that the improvements realized and corrective actions underway to improve control over property not be lost while the problems with the new system are being addressed. In order to continue the progress begun with our audits, we will monitor EPA's efforts to improve its system and work with the agency to determine when to resume financial audits.

We are sending copies of this report to the Director of the Office of Management and Budget, the Secretary of the Treasury, and the Administrator of the Environmental Protection Agency.



Charles A. Bowsher
Comptroller General
of the United States

Contents

Letter		1
Opinion Letter		6
Report on Internal Accounting Controls		12
	Property Assets Are Not Adequately Accounted For and Controlled	14
	Conclusions	18
	Recommendations	19
	Other Opportunities for Improvement	19
	Comments of Cognizant Officials	20
Report on Compliance With Laws and Regulations		21
Financial Statements		22
	Consolidated Statement of Financial Position	22
	Consolidated Statement of Operations	23
	Consolidated Statement of Changes in Financial Position and Reconciliation to Budget	24
	Notes to Financial Statements	25
Supplemental Schedules		37
	Schedule of Financial Position by Fund Activity	37
	Schedule of Operations by Fund Activity	38
	Schedule of Changes in Financial Position and Reconciliation to Budget by Fund Activity	39

Contents

Abbreviations

CERCLA	Comprehensive Environmental Response, Compensation, and Liability Act of 1980
EPA	Environmental Protection Agency
FMFIA	Federal Managers' Financial Integrity Act
GAAP	generally accepted accounting principles
NPL	National Priorities List

**Comptroller General
of the United States**

B-216351

To the Administrator
Environmental Protection Agency

We have audited the accompanying consolidated statements of financial position of the Environmental Protection Agency (EPA) as of September 30, 1988 and 1987, and the related consolidated statements of operations and changes in financial position and reconciliation to budget for the fiscal years then ended. These consolidated financial statements are the responsibility of EPA's management. Our responsibility is to express an opinion on these statements based on our audits. In addition to this report on our audits of EPA's fiscal years 1988 and 1987 consolidated financial statements, we are also reporting on our consideration of EPA's system of internal accounting controls and compliance with laws and regulations.

We conducted our audits in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. Our audits included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. Because EPA's principal financial activities consist of grants and contracts, our audits examined, on a test basis, internal controls over the award and disbursement process related to grant and contract agreements. Financial and compliance audits of the amounts charged to these agreements by grantees and contractors are performed by other auditors under provisions of federal laws and regulations. Our audits also included evaluating the overall presentation of the financial statements as well as assessing the accounting principles used and significant estimates made by management in its development of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

As we stated in our report on EPA's fiscal year 1987 consolidated statement of financial position (GAO/AFMD-89-24), fiscal year 1987 was the first year that EPA prepared consolidated financial statements in accordance with generally accepted accounting principles. Because our audit did not commence until July 1987, it was not practical to perform various auditing procedures to determine whether, as of the beginning of fiscal year 1987, assets, liabilities, equity, and related revenues and expenses were recorded in the proper accounting period. Accordingly, we do not express an opinion on the consolidated statements of operations and changes in financial position and reconciliation to budget for the fiscal year ended September 30, 1987.

Our opinion on the fiscal year 1987 consolidated statement of financial position was qualified because of (1) the manner in which EPA accounted for and supported its equipment, buildings, and library accounts and (2) weaknesses in the internal control system EPA utilized to control and safeguard these assets. Supporting records did not provide the cost and depreciation data needed to account for property assets in accordance with generally accepted accounting principles. In addition, related account balances were neither supported by adequate documentation nor subject to periodic reconciliations to subsidiary records. Our audit of the fiscal year 1988 financial statements disclosed that these conditions continued to exist. Accordingly, we determined, as we did in our fiscal year 1987 audit, that it was not practical to perform, nor did we perform, auditing procedures necessary to satisfy ourselves as to the fair presentation of the equipment, buildings, and library accounts and related expenses in EPA's consolidated financial statements for the fiscal years ended September 30, 1988 and 1987.

In our opinion, except for the effects of adjustments, if any, that might have been necessary had we been able to satisfy ourselves as to the fair presentation of EPA's equipment, buildings, and library accounts and related expenses, as discussed in paragraph four above, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Environmental Protection Agency as of September 30, 1988 and 1987, the results of its operations, and its changes in financial position and reconciliation to budget for the fiscal year ended September 30, 1988, in conformity with generally accepted accounting principles. Our audits were made for the purpose of forming an opinion on the consolidated financial statements taken as a whole. The supplemental schedules by fund activity as of and for the fiscal year ended September 30, 1988, are presented for the purpose of additional analysis and are not required as part of the financial statements. This information has been subjected to the same auditing procedures that were applied in our audit of the consolidated financial statements. In our opinion, except for the effects, if any, of the matters discussed in paragraph four above, the information in the supplemental schedules is fairly stated in all material respects in relation to the consolidated financial statements taken as a whole.

Financial Condition of EPA's Superfund Program

The current authorization for EPA's Superfund program expires in October 1991. While approximately \$7 billion in authorized funds remain, EPA estimates that it will need \$30 billion to pay for and oversee the cleanup of approximately 1,200 of the nation's most hazardous waste sites. However, because of EPA's experience to date and certain limitations in its estimating methodology, we believe that the \$30 billion figure is low. As the Congress begins its deliberations on reauthorizing this important environmental statute, we believe the following financial information on the program's operations and funding mechanism will be helpful to the discussion.

Superfund Authorization

The Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA), as amended by the Superfund Amendments and Reauthorization Act of 1986, authorized EPA to respond to releases of hazardous substances which threaten human health and the environment. In total, the Congress has authorized \$10.1 billion to be made available in annual appropriations through fiscal year 1991. To finance these appropriations, the statutes authorized the creation of the Hazardous Substance Superfund, a trust fund managed and maintained by the Department of the Treasury. The current financing for the trust fund is derived from (1) an environmental tax on corporations, (2) taxes on petroleum and chemicals, (3) appropriations from the general fund of the U.S. Treasury, (4) costs recovered from responsible parties, and (5) fines, penalties, and interest earned on invested funds. The portion of the trust fund balance made available through appropriations is under EPA's control and accounted for in its financial statements. For fiscal years 1981 through 1988, EPA has been appropriated approximately \$4.4 billion of the \$10.1 billion authorized.

Superfund Program Activity

As authorized by CERCLA and its amendments, EPA's Superfund program is responsible for identifying and prioritizing waste sites and seeing that the nation's most hazardous sites are cleaned up. Once potential waste sites have been identified, EPA begins a process of evaluating the extent and nature of the threat they pose to public health and the environment. This process includes a preliminary site assessment and a site inspection. Those sites posing the most serious threat are placed on the National Priorities List (NPL). NPL sites receive priority cleanup attention and are generally eligible for Superfund-financed remedial action.

As of September 30, 1988, EPA had identified over 30,000 sites, including more than 2,000 which were added during fiscal year 1988. Of the identified sites, EPA had completed preliminary assessments at over 26,000 and inspections at over 9,000. EPA had determined that over 11,000 sites showed no evidence that further EPA action would be required. Through the end of fiscal year 1988, EPA had proposed approximately 1,200 sites for inclusion on the NPL. While determining the eventual number of sites that will be added to the NPL is difficult, it is important to recognize that the size of the NPL is increasing because new sites are being added to it faster than existing sites are being removed.

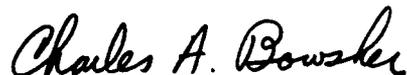
At the end of fiscal year 1988, cleanup work had begun at 201 of the 1,200 sites and had been completed at 27. EPA had spent approximately \$3.0 billion (68 percent) of the \$4.4 billion appropriated for Superfund program activities. This represents approximately 30 percent of the total \$10.1 billion authorized. EPA estimates that about half of the \$3.0 billion spent on Superfund has been used for specific site cleanup activities, while the other half has been used for various program support activities.

EPA currently estimates that it will need \$30 billion to pay for and oversee the cleanup of the approximately 1,200 sites on the NPL as of September 30, 1988. However, several aspects of EPA's methodology for estimating the \$30 billion figure lead us to believe that it is low. First, the estimate uses a current average cleanup cost figure which does not include the potential impact of inflation, even though EPA's cleanup efforts are expected to stretch well into the next century. Second, as recently reported in EPA's Management Review of the Superfund Program, there is every reason to believe that the average cleanup cost figure will likely increase as cleanup work begins at some of the more complex hazardous waste sites. In addition, EPA's \$30 billion estimate relates only to the 1,200 sites presently on the NPL and makes no provision for future sites that will be added. Based only on its inventory of sites under evaluation, which makes no provision for sites that will be identified in the future, EPA expects that 900 more sites will be added to the NPL by the year 2000. Considering EPA's experience to date and the limitations in its estimating methodology, we believe that the cost to pay for and oversee the cleanup of the nation's most hazardous waste sites will far exceed EPA's current \$30 billion estimate.

EPA's New Integrated Financial Management System

During fiscal year 1989, EPA began operating a new Integrated Financial Management System. EPA experienced problems with converting data from its old system to its new system, as well as problems with certain transactions being incorrectly recorded in the new system. As a result, during fiscal year 1989, EPA could not obtain cumulative trial balances or perform automated month-end and year-end reporting from the general ledger account balances. For fiscal year 1989, the new system's reporting features did not provide accounting information in a manner that satisfied agency needs. In addition, EPA could not reconcile, on a timely basis, its general ledger and external Treasury reports because reports at the necessary level of detail were not yet available.

EPA management has recognized these system problems. The new system software is reported as an area of concern in EPA's fiscal year 1989 report to the President required by the Federal Managers' Financial Integrity Act. We concur with the assessment of EPA management that these problems warrant its priority attention and resources.



Charles A. Bowsher
Comptroller General
of the United States

July 5, 1989

Report on Internal Accounting Controls

We have audited the consolidated financial statements of the Environmental Protection Agency (EPA) for the fiscal years ended September 30, 1988 and 1987, and have issued our opinion thereon. This report pertains only to our study and evaluation of EPA's system of internal accounting controls for the fiscal year ended September 30, 1988. Our report on our study and evaluation of EPA's system of internal accounting controls for the fiscal year ended September 30, 1987, is presented in GAO/AFMD-89-24, dated February 9, 1989.

As part of our audit, we made a study and evaluation of EPA's system of internal accounting controls to the extent we considered necessary to evaluate the system as required by generally accepted government auditing standards. The purpose of our study and evaluation was to determine the nature, timing, and extent of the auditing procedures necessary for expressing an opinion on the agency's consolidated financial statements. For purposes of this report, we have classified the significant internal accounting controls into the following categories:

- obligations,
- disbursements,
- grants,
- payroll,
- property,
- receivables and receipts, and
- financial reporting.

Our study and evaluation included all of the categories listed above. However, we did not evaluate the internal accounting controls over all functions within each category because it was more efficient to expand our substantive audit tests.

In planning the timing and extent of our work, we considered the internal control testing performed by Leonard G. Birnbaum and Company, Certified Public Accountants, as part of its financial and compliance audit of EPA's fiscal year 1988 obligations and disbursements charged to the Superfund appropriations. We reviewed and evaluated its internal control testing and concluded that we could rely on the testing and results to augment our work. Accordingly, we have incorporated its findings and recommendations in our report, where appropriate.

EPA's management is responsible for establishing and maintaining a system of internal accounting controls in accordance with the Accounting and Auditing Act of 1950 and the Federal Managers' Financial Integrity

Act of 1982 (FMFIA). In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control procedures. The objectives of a system of internal accounting controls are to provide management with reasonable assurance that (1) obligations and costs are in compliance with applicable laws and regulations, (2) funds, property, and other assets are safeguarded against waste, loss, and unauthorized use or misappropriation, and (3) assets, liabilities, revenues, and expenditures applicable to agency operations are properly recorded and accounted for to permit the preparation of reliable financial and statistical reports and to maintain accountability over agency assets. Because of the inherent limitations in any system of internal accounting controls, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the system to future periods is subject to the risk that the procedures may become inadequate because of changes in conditions or that the degree of compliance with procedures may deteriorate.

In accordance with FMFIA, EPA reviewed and reported on its system of internal accounting controls for fiscal year 1988. We reviewed the report and considered its findings in determining the nature, timing, and extent of our internal control tests.

Our study and evaluation of EPA's system of internal accounting controls, made for the limited purpose described in the second paragraph, would not necessarily disclose all weaknesses in the system. Accordingly, we do not express an opinion on EPA's system of internal accounting controls taken as a whole or on any of the categories of controls identified in the second paragraph. However, our study and evaluation of internal accounting controls disclosed conditions which we believe pose a high degree of risk that material errors or irregularities may occur and not be promptly detected. These conditions relate to the inadequacies in EPA's accounting for and controlling property assets which we observed during the fiscal year 1988 audit. We reported these same conditions as a material weakness in our fiscal year 1987 internal control report (GAO/AFMD-89-24, dated February 9, 1989). In that report, we observed that EPA's property management records, which serve as the subsidiary accounting system for capital assets, (1) do not provide information needed to account for capital assets and (2) are not subject to adequate internal controls. In addition, EPA was unable to provide the supporting documentation needed to audit the fair presentation of its buildings and library account balances. As a result, we qualified our opinion on EPA's statement of financial position for fiscal year 1988, as it

was not practical to perform auditing procedures necessary to satisfy ourselves as to the fair presentation of EPA's property balances.

Other financial management and control problems uncovered as a result of our first financial audit in 1987 have been resolved. These include the following:

- We identified discrepancies totaling over \$1.2 billion between EPA's general ledger and the balances appearing in the financial statements it submitted to Treasury at the end of fiscal year 1986. We also found that these reports were not supported by adequate documentation. Correcting these errors required adjustments to EPA's fiscal year 1987 consolidated financial statements totaling over \$789 million. EPA subsequently improved the quality of the documentation supporting its external reports, and we did not find similar problems in our fiscal year 1988 audit.
- We reported discrepancies totaling over \$742 million in EPA's cash, receivable, and receipt account balances. EPA management was unaware of these problems because it had not performed the periodic reconciliations necessary to identify and correct errors and omissions. As a result of our audit, EPA management has placed increased emphasis on reconciliation as an internal control technique, and similar reconciliation problems were not found in fiscal year 1988.

Property Assets Are Not Adequately Accounted For and Controlled

Our review of EPA's property-related general ledger balances for fiscal year 1988 (totaling \$354.4 million) disclosed that the internal control problems in property management we reported on for fiscal year 1987 had not been corrected. The material weaknesses we identified included (1) the inability of the property management records to provide financial information, such as cost and depreciation data, needed to account for personal property in accordance with generally accepted accounting principles (GAAP),¹ (2) ineffective control over EPA's personal property assets, and (3) the lack of supporting documentation for EPA's libraries and buildings.

Both GAAP and the Office of Management and Budget's Financial Management and Accounting Objectives require that property records provide accountability for assets by maintaining financial information needed to account for and control property. Property records should

¹GAO's Policy and Procedures Manual for Guidance of Federal Agencies, Title 2, "Accounting Principles and Standards."

provide financial information, such as type of asset, date of acquisition, cost, estimated useful life, applicable depreciation data, physical location, and identity of custodial officers. Without reliable property management records, it is extremely difficult for EPA to manage and maintain accountability for property assets. In addition, accounting information must be accurate in order to maximize its usefulness to agency management in making decisions regarding agency programs and operations.

We identified the following material weaknesses in EPA's ability to account for and report personal property financial information:

- The Personal Property Accounting System, which serves as the property control system as well as the subsidiary accounting system for the general ledger personal property account, does not provide the data needed to account for assets, including cost, estimated useful life, and applicable depreciation data.
- Instead of capitalizing personal property when it is purchased and placed into service, as required by GAAP, all disbursements for property are charged to the operating expense account. At fiscal year-end, a manual general ledger adjustment is made to reduce expenses and increase the personal property account balance by the amount of capitalized personal property purchased during the year. The resulting personal property general ledger balance is compared to the balance in the property control system, and any difference is written off without investigating the origin of the difference.
- For fiscal year 1988, EPA did not reconcile personal property disbursements recorded in the general ledger with related acquisitions recorded in the property control system. As a result, EPA was unable to identify the cause of the \$15.3 million difference in the personal property balance between the two systems at the end of fiscal year 1988. This was due, in part, to the fact that EPA's general ledger and property control system are not integrated and do not have a common data element(s) or interface(s) to facilitate a reconciliation.
- During fiscal year 1988, physical inventories were not conducted in 221 of 800 custodial areas (28 percent) we reviewed. Of the 579 inventories that were conducted, 212 (37 percent) were not reconciled to the property control system to determine the reasons for identified differences.
- There were often delays of up to 6 months between the time property was acquired and the time it was recorded in the property control system. At the end of fiscal year 1988, personal property totaling at least \$10.3 million had been acquired by EPA but was not yet recorded in the

control system. These delays increase the risk that the property will be lost or misappropriated.

- Controls governing the recording of property transactions in the property control system are not effective. Instead of property acquisitions being recorded at the actual cost, as required by EPA policy (EAAP), property was recorded in the property control system at the amount obligated. Amounts recorded do not reflect the effect of other factors, such as discounts, installation charges, and trade-ins. We also found many input errors. For example, in EPA's Cincinnati office, a filing cabinet costing \$133 was erroneously recorded at \$7.6 million. This error was not detected in time to prevent a misstatement of EPA's unaudited Financial Statements reported to the Department of the Treasury for fiscal year 1988. Overall, 41 of 76 items we tested (54 percent) reflected differences between the invoices and the amounts recorded in the property control system, resulting in a net property overstatement of \$10.7 million (21.3 percent of total capital property acquisitions during fiscal year 1988).

EPA officials informed us that changes are underway to improve the property control system and address the serious weaknesses in personal property management. These initiatives include (1) performance and reconciliation of physical inventories of all personal property, (2) additional edit checks to prevent the input of erroneous data, and (3) the addition of data elements compatible with the general ledger to facilitate reconciliation. These efforts, if successful, should bring about significant improvements in EPA's ability to account for and control personal property. However, many of these initiatives were not begun until fiscal year 1989, and EPA officials do not expect their effects to be realized until fiscal year 1990. Consequently, personal property balances appearing in fiscal year 1989 financial reports will, in all likelihood, be as unreliable as they were in fiscal year 1988. In addition, since the close of fiscal year 1988, EPA has implemented a new Integrated Financial Management System, which replaced the existing Financial Management System. However, implementation of the property module, originally scheduled for completion by the end of fiscal year 1990, has been postponed until at least fiscal year 1991. As a result, EPA will continue to rely heavily on the property control system for the foreseeable future.

In its Independent Auditor's Report on Internal Accounting Controls for the fiscal year ended September 30, 1988 (issued September 22, 1989), Leonard G. Birnbaum and Company, the Superfund auditor, reported material weaknesses in EPA's accounting for and controlling personal property. The property weaknesses noted by the Superfund auditor are

similar to those found in prior audits of Superfund obligations and disbursements. As noted earlier, we utilized its control testing to augment ours. We concur with its findings and recommendations related to personal property. The Superfund auditor's findings can be summarized as follows:

- Property was not always recorded in the property control records. In a test of 786 property items, 276 (35 percent) were not recorded. One reason for this was that receiving documents were not always sent to the property accountability officers when property was ordered or received.
- Required physical inventories were not always performed and reconciled to the general ledger, and proper transfer documents were not maintained.
- Property and equipment were not capitalized when purchased or placed in service, as required by GAAP. Instead, it was charged to operating expenses. EPA's Financial Management System does not have the transaction codes necessary to capitalize property at the time of disbursement. EPA officials indicated that the new system will correct this weakness.
- Custodial officers did not accept responsibility for the care and protection of property assigned to them.

The Superfund auditor's recommendations can be summarized as follows:

- Property accountable officers should certify that unrecorded property items identified by the audit have been recorded in the property control system.
- EPA should ensure that procedures have been established to properly record capitalized property and equipment in the accounting records.
- EPA should establish an interim policy requiring the reconciliation of the property and accounting records.
- EPA should emphasize to the appropriate property accountable officers the importance of complying with EPA policies for physical inventories and accepting custodial duties.

EPA's accounting system problems with property are not new. As required by FMFIA, agencies annually review and report on the adequacy of their systems of internal controls (section 2) as well as their accounting system (section 4). In its initial report covering fiscal year 1983, EPA identified the need for an accounting system enhancement to integrate its accounting and property management systems. EPA's fiscal year 1988 report indicated that little progress had been made in the intervening

years. In response to our fiscal year 1987 audit results, EPA expanded its FMFIA recognition of its property weaknesses by reporting, for the first time, a material weakness in internal controls over property. Under section 2, EPA reported that the property control system and the Financial Management System are not integrated. Under section 4, EPA reported that property management and accounting records are not subject to adequate controls to ensure accurate data. Our review of EPA's property accounting for fiscal year 1988, together with the results reported by the Superfund auditor, confirms the continuing existence of material weaknesses in both EPA's accounting system for property and the internal control system over property.

Finally, we were unable to perform audit procedures necessary to test the fair presentation of EPA's \$84 million in buildings and libraries because we were unable to obtain supporting documentation. EPA's subsidiary support for buildings consists of files maintained by the Facilities Management and Services Division. Division representatives were unable to provide documentation necessary to establish the ownership, age, and cost of buildings. In addition, we found that EPA does not record depreciation on building assets. EPA officials informed us that initiatives are underway to reconstruct building records; they expect this effort to be completed in fiscal year 1990.

EPA records library books as capital assets although the acquisition costs of these assets do not meet the minimum capitalization criteria specified in GAAP. However, EPA does not maintain a subsidiary record of library books, nor does it record related depreciation. Records of library inventory are maintained by the Information Management and Services Division. Each quarter, EPA adds the obligation amount of volumes purchased to the total already recorded. This addition is not adjusted to reflect average cost, as required by EPA policy. In addition, the library inventory balance is not always adjusted to reflect dispositions or losses and was not subject to a physical inventory during fiscal year 1988.

Conclusions

EPA's subsidiary accounting system for property and related internal controls did not adequately account for or maintain control over these assets. EPA's ongoing efforts to correct its property weaknesses provide the opportunity to improve accountability for and control over personal property. Additional actions are needed to improve the accuracy and reliability of accounting data maintained by the subsidiary records as well as the internal control environment over property assets. The current property management system did not provide management with

reasonable assurance that (1) agency assets are safeguarded against waste, loss, and unauthorized use or misappropriation and (2) property-related information appearing in financial statements reported to the Department of the Treasury is fairly stated.

Recommendations

To improve EPA's accounting for and control over all property assets, we recommend that the Administrator of the Environmental Protection Agency

- ensure that the new accounting system and the property control system (1) provide accurate and reliable financial and management control records (including the type of asset, date of acquisition, cost, estimated useful life, applicable depreciation data, physical location, and identity of custodial officers) to account for and control property assets and (2) contain a common data element(s) or interface(s) to permit the reconciliation of accounting and property systems data and
- address the property-related findings and implement the recommendations reported by the Superfund auditor in its fiscal year 1988 audit report dated September 22, 1989.

Except for the property weakness identified by GAO in this report, by EPA in its FMFIA report, and by Leonard G. Birnbaum and Company in its Independent Auditor's Report on Internal Accounting Controls, our study and evaluation disclosed no other conditions which we consider to be material to the consolidated financial statements taken as a whole. While several GAO and EPA reports disclose, in our judgment, internal control weaknesses of a financial and/or programmatic nature, we believe these matters do not have a material effect on EPA's fiscal year 1988 consolidated financial statements. We considered these weaknesses in determining the nature, timing, and extent of our audit tests. Except for the inadequacies of the accounting system and internal controls related to property which caused us to qualify our opinion on the agency's consolidated financial statements for the fiscal year ended September 30, 1988, the weaknesses identified do not affect that opinion.

Other Opportunities for Improvement

During the course of our examination, we identified a number of other weaknesses in internal accounting controls which will be reported separately to the Environmental Protection Agency. These weaknesses included problems with (1) overtime and leave usage, (2) payroll control procedures, (3) invoice payments, (4) controls over cash and checks,

(5) accounts receivable, and (6) financial reporting. Although we did not consider these weaknesses to be material to the fair presentation of the consolidated financial statements, they nonetheless merit management's attention.

During the last half of 1989, EPA conducted an assessment of its internal controls and audit follow-up. This effort, performed as part of a special review of government management and integrity at the request of the Director of the Office of Management and Budget, identified several areas which need to be improved and strengthened. The areas identified were the Superfund program, contract and property management, the new Integrated Financial Management System, audit follow-up, the enforcement program, and scientific equipment and facilities. The results of this assessment and our audit offer EPA management the opportunity to focus its attention on pursuing actions needed to reduce risk by strengthening EPA management control practices.

Comments of Cognizant Officials

Although we did not obtain official agency comments from EPA, we discussed a draft of this report with the Director and Deputy Director of EPA's Financial Management Division and representatives of EPA's Facilities Management and Services Division. We have incorporated their views where appropriate. They agreed with our property accounting and control findings, conclusions, and recommendations and with our decision to qualify our opinion due to the agency's property-related weaknesses. In addition, they stated that corrective actions and/or system improvements were either in process or planned and would, in their opinion, resolve the agency's property weaknesses over time. These actions included completion of an agencywide physical inventory during fiscal year 1990; testing of a manual interface between the Integrated Financial Management System and the property control system data, which would for the first time permit a manual reconciliation of new acquisitions; and the planned installation of the automated property module for the new financial management system after the end of fiscal year 1990.

Report on Compliance With Laws and Regulations

We have audited the consolidated financial statements of the Environmental Protection Agency (EPA) for the fiscal years ended September 30, 1988 and 1987, and have issued our opinion thereon. Our audit was made in accordance with generally accepted government auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures, including tests of compliance with laws and regulations, as we considered necessary in the circumstances. This report pertains only to our consideration of EPA's compliance with laws and regulations for the year ended September 30, 1988. Our report on compliance with laws and regulations for the year ended September 30, 1987, is presented in GAO/AFMD-89-24, dated February 9, 1989.

The management of EPA is responsible for compliance with laws and regulations applicable to EPA. As part of obtaining reasonable assurance as to whether the consolidated financial statements were free of material misstatement, we selectively tested EPA's compliance with certain provisions of the following laws and their implementing regulations:

- Federal Managers' Financial Integrity Act (31 U.S.C. 3512 (b, c));
- Anti-Deficiency Act (31 U.S.C. 1341);
- Debt Collection Act of 1982 (31 U.S.C. 3717);
- Prompt Payment Act (31 U.S.C. 3902, 3903, and 3905);
- U.S. Treasury reporting standards (31 U.S.C. 3513 (a));
- Accounting and Auditing Act of 1950 (31 U.S.C. 3512 (a) (3));
- Supplemental Appropriations Act of 1955 (Section 1311 (a) of Public Law 83-663, 31 U.S.C. 1501, 1502)); and
- U.S. Treasury cash custodianship standards (31 U.S.C. 3302 (e), 3305).

Because of the limited purpose for which our tests of compliance were made, the laws and regulations tested did not cover all legal requirements with which EPA has to comply.

The results of our tests for fiscal year 1988 indicate that, with respect to the items tested, EPA complied in all material respects with the provisions of laws and regulations that could have a material effect on its consolidated financial statements. With respect to transactions not tested, nothing came to our attention that caused us to believe that EPA had not complied, in all material respects, with those provisions. Our testing disclosed certain compliance matters which, while not material, nevertheless warrant EPA management's attention. These matters will be reported separately to EPA.

Financial Statements

Consolidated Statement of Financial Position

AS OF SEPTEMBER 30, 1988
(DOLLARS IN THOUSANDS)

ASSETS	1988	1987 (RESTATED)
Funds with U.S. Treasury (Note 1)	\$10,348,722	\$10,279,970
Advance to the Trust Fund	733,955	848,000
Other Advances, Accounts and Loans Receivable, Net (Notes 1, 3)	114,890	93,633
Land, Buildings, and Equipment, Net of Accumulated Depreciation (Notes 1, 4)	142,385	128,622
Future Financing Sources	40,864	38,170
TOTAL ASSETS	<u>11,380,816</u>	<u>11,388,395</u>
LIABILITIES AND EQUITY		
LIABILITIES		
Repayable Advance From Treasury	733,955	848,000
Accounts Payable and Accruals:		
To the Public	365,395	246,724
To Other Federal Agencies	201,836	80,152
Other Advances: (Note 1)		
From Other Federal Agencies	22,306	35,672
From The Public	24,034	11,925
Amounts Due to Treasury	99,243	76,472
Accrued Payroll and Leave	79,852	67,782
Superfund Claims	20,500	0
TOTAL LIABILITIES	<u>1,547,121</u>	<u>1,366,727</u>
Commitments and Contingencies (Note 6)		
EQUITY OF THE U.S. GOVERNMENT		
Unexpended Appropriations: (Note 1)		
Unobligated Balances	1,254,313	1,913,682
Unliquidated Obligations:		
Grants and Other Assistance	7,416,903	7,179,701
Contracts and Other	1,151,442	915,158
Invested Capital (Note 1)	214,304	179,919
Cumulative Results of Operations	(203,267)	(166,792)
TOTAL EQUITY	<u>9,833,695</u>	<u>10,021,668</u>
TOTAL LIABILITIES AND EQUITY	<u>\$11,380,816</u>	<u>\$11,388,395</u>

The accompanying notes are an integral part of these statements.

Financial Statements

Consolidated Statement of Operations

FOR THE FISCAL YEAR ENDED SEPTEMBER 30, 1988
(DOLLARS IN THOUSANDS)

EXPENSES	1988	1987 (RESTATED)
Grants and Other Assistance (Note 7)	\$3,063,727	\$3,353,538
Contractual Services	1,194,544	796,675
Personnel Compensation and Fringe Benefits	624,299	553,933
Rent, Utilities, and Telephone	120,290	98,944
Travel, Printing, Supplies and Other Expenses	136,052	127,440
Depreciation (Note 1)	21,101	18,838
TOTAL EXPENSES	<u>5,160,013</u>	<u>4,949,368</u>
FINANCING SOURCES (Note 1)		
Appropriations Expended	5,108,491	4,898,914
Depreciation and Other	21,101	20,039
Appropriations to be Provided	2,694	3,324
TOTAL FINANCING SOURCES	<u>5,132,286</u>	<u>4,922,277</u>
NET RESULTS OF OPERATIONS	<u>(\$27,727)</u>	<u>(\$27,091)</u>

The accompanying notes are an integral part of these statements.

Financial Statements

Consolidated Statement of Changes in Financial Position and Reconciliation to Budget

FOR THE FISCAL YEAR ENDED SEPTEMBER 30, 1988
(DOLLARS IN THOUSANDS)

RESOURCES USED:	1988	1987 (RESTATED)
Operating Uses:		
Operating Expenses	\$5,160,013	\$4,949,368
Items (Providing) Requiring Funds:		
Depreciation (Notes 1, 4)	(21,101)	(18,838)
Loss on Property	(15,340)	(8,897)
Unfunded Annual Leave	(2,694)	(3,324)
Superfund Claims	(20,500)	0
Increase (Decrease) in Other Advances, Accounts and Loans Receivable, Net	21,257	(19,408)
Decrease (Increase) in Accounts Payable and Accruals	(271,245)	10,555
Funds Used by Operations	<u>4,850,390</u>	<u>4,909,456</u>
Non-Operating Uses:		
Acquisitions of Property (Note 1)	50,204	24,348
Net Transfers Out	125,055	650,000
Funds Transactions Included in Outlays	(8,521)	(27,099)
NET RESOURCES USED (BUDGETARY OUTLAYS)	<u>5,017,128</u>	<u>5,556,705</u>
RESOURCES PROVIDED:		
Current Year Appropriation	5,027,457	5,364,187
Net Transfers In and Other	58,423	590,664
NET RESOURCES PROVIDED	<u>5,085,880</u>	<u>5,954,851</u>
INCREASE IN U.S. TREASURY FUNDS	<u>68,752</u>	<u>398,146</u>
U.S. TREASURY FUNDS; BEGINNING OF YEAR	10,279,970	9,881,824
U.S. TREASURY FUNDS; END OF YEAR	<u>\$10,348,722</u>	<u>\$10,279,970</u>

The accompanying notes are an integral part of these statements.

Notes to Financial Statements

Note 1: Significant Accounting Policies

Entity

EPA was created in 1970 by executive reorganization from various components of other agencies in order to better marshal and coordinate federal pollution control efforts. The Agency is generally organized around the media and substances it regulates --air, water, hazardous waste, pesticides, and toxic substances. A major mechanism for achieving the Agency's pollution prevention goals is the provision of financial assistance (grants and cooperative agreements) to states, local government, universities and other qualified recipients. A major focus of EPA's activities is the Superfund program, to clean up hazardous waste sites.

Basis of Consolidation

EPA's consolidated financial statements are prepared in conformity with generally accepted accounting principles as contained in the Federal Accounting Standards of the General Accounting Office's (GAO) Policy and Procedures Manual for Guidance of Federal Agencies.

The accompanying consolidated financial statements of EPA include all accounts under EPA's control which have been established and maintained to account for the resources entrusted to the Agency's management. EPA's consolidated financial statements do not include the unappropriated portion of the "Hazardous Substance Superfund" trust fund. The financial statements are prepared on the accrual basis of accounting.

Revenue Recognition and Expended Appropriations

Financing sources are principally provided through Congressional appropriations on an annual, multi-year, and no-year basis. Appropriations may be used to finance operating expenses as well as capital expenditures for land, equipment, and other assets as specified by law. Additional revenue is recognized from services related to the revolving fund operations.

The current budgetary process does not distinguish between capital and operating expenditures. For budgetary purposes, both are recognized as a use of budgetary resources (outlays) as paid. However, for financial reporting purposes under accrual accounting, operating expenses are recognized when incurred, while advances, reimbursements, and expenditures for capital and other assets are recognized when consumed, or collected, in EPA operations. Financing sources for these expenses, which are derived both from current and prior-year appropriations, are recognized on the same basis. Appropriations for current operating expenses are recorded as a financing source when expended. Unexpended appropriations are recorded as equity of the U.S. government.

Future financing sources represent future appropriations to be provided to finance annual leave accrued as earned but not taken. The current year change in the accrual is recognized as an operating expense with a corresponding recognition as current revenue in the form of an Appropriation to be Provided. The recognition of the current period revenue results in a corresponding increase over the prior year balance in the future financing source asset account.

The statement of changes in financial position and reconciliation to budget presents a reconciliation of operating expenses on an accrual basis with cash basis budgetary expenditures.

Advances

Repayable advance from the U.S. Treasury represents the liability of EPA's general fund for advances received by the Superfund Trust Fund. In fiscal years 1988 and 1987, the repayable advance balance was \$734.0 million and \$848.0 million, respectively. The repayment of \$114.0 million, during fiscal year 1988, is excluded from EPA's Statement of Revenues and Expenses. The remaining balance is repayable by December 31, 1991. Repayments are made to the U.S. Treasury's general fund after consultation with the U.S. Treasury and Office of Management and Budget.

Advances receivable represent funds paid to employees (such as travel advances), other federal agencies, contractors, and grantees for goods or services; amounts advanced for goods and services which have not been received; or unspent funds which have not been returned. These advances include an accrual of \$2.4 million and \$6.7 million for fiscal years 1988 and 1987, respectively, representing EPA's estimate of drawdowns by letter-of-credit recipients for which costs have not yet been incurred. Advances payable represent funds paid to EPA by other federal agencies and grantees to purchase goods and services on their behalf and prior to EPA providing the goods and/or services.

Land, Buildings, and Equipment

Land, buildings, and equipment with a cost greater than \$5,000 and a useful life of 2 years or greater are capitalized. Library volumes are capitalized without regard to dollar value minimum. The Agency's procedure is not to calculate depreciation on buildings or library volumes; on equipment, it is calculated on a straight-line basis over an estimated useful life of 5 years.

Annual, Sick, and Other Types of Leave

Employee's annual leave is accrued as it is earned, and the accrual is reduced as leave is taken. At least once per year, the balance in the accrued leave account is adjusted to reflect current pay rates of cumulative annual leave earned but not taken. Senior

Executive Service employees may carry forward an unlimited amount of annual leave from one year to the next. Most other employees may carry forward up to 240 hours. Any excess hours not taken are forfeited unless special approval is granted. Sick and other types of leave are expensed as taken.

Cost Allocation

Certain Agency support costs (such as leases, utilities, mail operations, etc.) are initially charged to a carrier account established under the Agency's Salaries and Expense (S & E) appropriation. During the year these support costs are allocated respectively to the S & E appropriation and the Superfund appropriation based on a ratio of direct labor hours, using budgeted or actual full-time equivalent personnel, charged to these appropriations to the total of all direct labor hours. Agency support costs charged to Superfund may not exceed the ceiling established in the Superfund appropriation.

Funds with U.S. Treasury

This total represents all unexpended balances of accounts under EPA's control with the U.S. Treasury.

Invested Capital

Invested capital represents the book value of land, buildings, and equipment (note 4) and the principal amount of loans receivable outstanding (note 3).

Note 2 : Intragovernmental Financial Activities

EPA's financial activities are affected by, and are dependent upon, those of the federal government as a whole. Thus, EPA's financial statements do not reflect the results of all financial decisions and activities applicable to EPA operations, as if it were a stand-alone entity.

- . The U.S. Treasury receives, disburses, and holds moneys on behalf of EPA for 54 different account titles or fund types for which EPA has management responsibilities.
- . EPA's consolidated financial statements are not intended to report the Agency's proportional share of the federal deficit or of public borrowing, including interest thereon.
- . Financing for major construction projects was provided through appropriations. To the extent this financing was obtained through public borrowing by the U.S. Treasury, no interest has been capitalized, since such borrowings are recorded in total by the U.S. Treasury and are not allocated to individual departments and agencies.
- . During fiscal year 1988, the majority of EPA's employees

participated in the Civil Service Retirement System (CSRS). Contributions to the plan are based on 7 percent of the employees' gross pay, to which EPA made a matching contribution. EPA pension contributions for the years ending September 30, 1988 and 1987, totaled approximately \$25.7 million and \$27 million, respectively.

On January 1, 1987, the Federal Employees' Retirement System (FERS) was implemented, pursuant to Public Law 99-335. This is a defined contribution retirement plan and is comprised of a Social Security Benefits Plan, a Basic Benefit Plan, and a Savings Plan. Generally, it is mandatory for all employees hired on or after January 1, 1984. Employees hired before January 1, 1984, had the option until December 31, 1987, to elect to transfer coverage from CSRS (extended to June 30, 1988, for extenuating circumstances). Contributions to the plans are based on a percentage of the employees' gross pay. Under the Thrift Savings Plan, employees can also elect additional contributions between 1 and 10 percent of their gross pay and EPA will match up to 4 percent of the employee-elected contribution. EPA also pays 1 percent of the employees' salary into the Thrift Savings Plan. FERS and Thrift Savings employer contributions for the years ended September 30, 1988 and 1987, totaled approximately \$19.5 million and \$10.7 million, respectively.

EPA matches the employees' FICA and Medicare contributions. FICA and Medicare employer's contributions for the years ended September 30, 1988 and 1987, totaled approximately \$17.3 million and \$12.5 million, respectively.

EPA does not report CSRS or FERS assets, actuarial present value of accumulated plan benefits, or unfunded liabilities applicable to its employees, since this data is maintained by the Office of Personnel Management and is not allocated to individual departments and agencies.

- . The General Services Administration (GSA) provides many services to the EPA, such as procurement and telecommunications, which are charged through interagency billings as goods are shipped or services are rendered.
- . The EPA contracts for a wide range of goods and services through interagency agreements with other federal agencies and units of state and local governments (reimbursable only) which, for the fiscal years ended September 30, 1988 and 1987, amounted to approximately \$108.9 million and \$102.9 million in expenditures and \$33.9 million and \$31 million in reimbursements, respectively.
- . The U.S. Treasury accounts for and reports the financial activity of the Hazardous Substance Response Trust Fund, which receives funds from taxes on petroleum and chemicals, an environmental tax on corporations, congressional

appropriations, costs recovered from responsible parties, fines, penalties and interest earned on investments in U.S. obligations. The Congress annually appropriates a portion of the fund balance to finance EPA's Superfund program activities.

- . As authorized by the Congress, EPA appropriations for Superfund program activities include certain amounts which are transferred to other federal agencies for authorized activities in support of the Superfund program. The uses of these transfer appropriations are not reported in EPA's financial statements as part of EPA's Superfund program activities, rather they are reported by the specific agencies that receive the transfer amount.
- . Under the Federal Tort Claims Act, any award, compromise, or settlement in excess of \$2,500 is paid from the Claims, Judgements, and Relief Acts Fund maintained by the Department of the Treasury, while those of \$2,500 or less are paid by EPA. Payments during fiscal year 1988 and 1987 for awards, compromises, and settlements resulting from such legal actions amounted to \$1,008,593 and \$25,000 from the Treasury's Claims, Judgements, and Relief Acts Fund, and \$13,706 and \$9,568 from EPA, respectively.

Financial Statements

Note 3: Receivables

Receivables, as of September 30, 1988 and 1987, respectively, consisted of the following:

	September 30, 1988	September 30, 1987
	(Dollars in thousands)	
Advances		
Other federal agencies	\$ 9,948	\$ 4,898
The public	4,923	11,611
EPA employees	<u>777</u>	<u>653</u>
Total Net Advances	<u>15,648</u>	<u>17,162</u>
Accounts Receivable		
Other federal agencies	3,431	2,303
The public	87,805	84,309
Less: Allowance for doubtful accounts	<u>(63,913)</u>	<u>(61,798)</u>
Total Net Accounts Receivable	<u>27,323</u>	<u>24,814</u>
Loans Receivable (A, B)		
Due through July 31, 2008, at interest rates of up to 6.125 percent	71,643	51,297
Interest on loans receivable	<u>276</u>	<u>360</u>
Total Loans Receivable (including interest)	<u>71,919</u>	<u>51,657</u>
Total Net Receivables	<u>\$114,890</u>	<u>\$93,633</u>

A. The Asbestos School Loans

The Asbestos School Hazard Abatement Act of 1984 (ASHAA), as amended by the Asbestos Hazard Emergency Response Act of 1986 (AHERA), gives EPA the lead responsibility to compile technical information on asbestos, to develop procedures and standards for both public and private local educational agencies (LEAs) to use in abating asbestos hazards, and to provide financial assistance to LEAs on a school-by-school basis to carry out abatement

projects. This financial assistance includes both grants and loans to the LEAs. In addition, AHERA provides authority for the issuance of grants in 1988 and 1989 to states or LEAs to carry out inspections for asbestos-containing material in school buildings and preparation of management plans for school buildings as defined by this Act. Not more than 10 percent of the 1988 and 1989 amounts available under ASHAA may be used for these purposes. Due to the recent nature of loans extended under ASHAA and AHERA, the related collection history was not sufficient to make possible the establishment of a meaningful allowance for doubtful loans receivable. As of September 30, 1988 and 1987, there were outstanding loans under this Act of \$67,179,352 and \$46,812,306 respectively.

AHERA also established a trust fund in the U.S. Treasury, known as the "Asbestos Trust Fund." Repayments of loans must be made to EPA for deposit in the General Fund of the U.S. Treasury. Repayments of Asbestos School Loans totaled \$2,440,780 and \$846,184 for the fiscal years ended September 30, 1988 and 1987 respectively.

B. Puerto Rico Loans

EPA, pursuant to Public Law 97-357 (October 1982), has loaned funds to the Commonwealth of Puerto Rico in the amount of \$16,720,039. These loans were granted as a result of special congressional action to allow certain construction grant unobligated balances to be used as loans to enable the Commonwealth of Puerto Rico to fund five specific regional wastewater treatment systems. These funds may be used by the Commonwealth of Puerto Rico to fund the nonfederal share of the costs of such projects. Interest for these loans is recorded monthly, based on the U.S. Treasury rate established for this loan program. An allowance for doubtful loans receivable was not established for these loans due to the large amount of collections and probability that the remaining balance will be collected. As of September 30, 1988 and 1987, there were outstanding loans for this program in the amount of \$4,463,851 and \$4,484,984, respectively.

Note 4: Land, Buildings, and Equipment

Property and equipment, as of September 30, 1988 and 1987, respectively, consisted of the following:

	<u>September 30, 1988</u>	<u>September 30, 1987</u>
	(Dollars in thousands)	
Land:		
Cost	\$ <u>2,676</u>	\$ <u>2,668</u>
Building:		
Cost	70,584	64,443
Accumulated Depreciation	<u>0</u>	<u>0</u>
Book Value	<u>70,584</u>	<u>64,443</u>
Equipment:		
Cost	267,208	239,038
Accumulated Depreciation	<u>(211,979)</u>	<u>(190,878)</u>
Book Value	<u>55,229</u>	<u>48,160</u>
Library Volumes:		
Cost	13,896	13,351
Accumulated Depreciation	<u>0</u>	<u>0</u>
Book Value	<u>13,896</u>	<u>13,351</u>
Property and Equipment	<u>\$142,385</u>	<u>\$128,622</u>

Note 5: Leases

The Agency leases office and laboratory space, copiers and computers from GSA and from commercial sources. All leases are considered to be operating leases rather than capital leases; some may be cancelled without penalty cost and expire at variable intervals. Lease payments during fiscal year 1988 and 1987 totaled \$83.2 million and \$94.7 million, respectively.

The majority of EPA's office space is leased through GSA, while the majority of the leased laboratory space is leased directly from commercial sources. Rates charged to EPA by commercial sources are based upon appraisals of comparable space, while GSA's rates are approximations based upon appraisals. During fiscal year 1988, EPA did not cancel any leases. EPA does not foresee any termination of leases in the near future.

Future minimum real estate lease payments at September 30, 1988, for operating leases are as follows:

Fiscal Year

(Dollars in thousands)

1989	\$ 5,502
1990	6,017
1991	2,872
1992	1,268
1993	<u>0</u>
	\$15,659

Note 6: Commitments and Contingencies

Under the Federal Insecticide, Fungicide, and Rodenticide Act (FIFRA), as amended at 7 U.S.C. 136m, EPA is authorized to suspend and cancel registration of pesticides determined to be hazardous. Prior to the 1988 FIFRA Amendments, under certain conditions, EPA made indemnity payments to eligible owners who incurred losses as a result of cancellations or suspensions of pesticides. The Federal Government has also paid millions of dollars from the Treasury Department's Judgement Fund in claims by holders of the cancelled EDB, 2,4,5-T/Silvex and Dinoseb. Additional claims by holders of Dinoseb are projected to cost millions of dollars more. The 1988 FIFRA Amendments provide that indemnification claims will not be paid from EPA appropriations unless Congress provides a special appropriation for this purpose. As of September 30, 1988 and 1987, EPA had actual outstanding indemnification claims for two chemicals totaling approximately \$16.8 million and \$12.5 million, respectively. The total amount of claims could be as high as \$40.0 million.

Both the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA) and the Superfund Amendments and Reauthorization Act (SARA) provide for cost-recovery of funds. (See note 7). Cost recovery expenditures are expensed because there is no assurance that these funds will be recovered. EPA establishes an account receivable when there is a sum certain due from the responsible party(ies). This occurs when a judgment, consent order, or other binding agreement is made for payment. As of September 30, 1988 and 1987, the balance of accounts receivable was \$ 9.6 million and \$6.5 million, respectively. Since the inception of Superfund through fiscal year 1988, EPA has collected approximately \$104.2 million in cost-recovery.

Under Section 119 of CERCLA, as amended by SARA, EPA has authority to indemnify response action contractors and certain other persons for negligent releases arising out of response action activities. Indemnity claims will be paid out of available balances in the Hazardous Substance Superfund. The indemnification process is not subject to the provisions of the Anti-Deficiency Act. If

sufficient funds are unavailable to make such payments, the Agency has authority to request special appropriations for such purposes. The Agency has indemnified approximately 1,000 contractors and subcontractors. Because of the newness of this program, and the lack of an actuarial base, the potential financial liability of the Agency is indeterminate at this time.

EPA is a party in various administrative proceedings, legal actions, and claims brought by, or against, it. These include:

- * Various personnel actions, suits or claims brought against the Agency by employees and others.
- * Various contract, assistance, and program claims and counterclaims brought against the Agency by vendors, grantees, and others. Outstanding claims totaled in excess of \$29.2 million and \$17.4 million as of September 30, 1988 and 1987, respectively.
- * The legal recovery of EPA's Superfund costs incurred for pollution cleanup of specific sites, to include the collection of fines and penalties from responsible parties.
- * Claims against recipients for improperly spent assistance funds, which may be settled by a reduction of future EPA funding to the grantee or the provision of additional grantee matching funds. As of September 30, 1988 and 1987, approximately \$32.2 billion and \$33.7 billion respectively, of EPA payments to units of state and local governments for construction of wastewater treatment facilities are awaiting audit. EPA believes that recovery of any improperly spent costs will not be material to its financial statements.

In the opinion of EPA's management and General Counsel, the ultimate resolution of legal actions still pending will not materially affect EPA's operations or financial position.

Note 7: Major Activities

Superfund Program Activities

On December 11, 1980, Congress passed the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA), commonly referred to as "Superfund." This Act created the Hazardous Substance Response Trust Fund and authorized \$1.6 billion over the period FY 1981-1985. The Trust Fund, administered by the U.S. Treasury, was established to provide money to respond to actual or threatened releases of hazardous substances, pollutants, or contaminants that may endanger public health or the environment. This Act authorizes funding for liability, compensation, cleanup, and emergency response for hazardous substances released into the environment from uncontrolled and abandoned hazardous waste sites.

The Superfund Amendments and Reauthorization Act (SARA) was enacted October 17, 1986. SARA reauthorized CERCLA for \$8.5 billion to be appropriated over a 5-year period (FY 1987-1991) for the continuation of the program launched by CERCLA to clean up hazardous waste sites, strengthen and expand the cleanup program, and change the tax structure for financing the Fund.

Grants and Other Assistance

The Agency, in fulfilling its responsibilities for protecting and enhancing the quality of the environment, provides financial assistance to various public, private, and state recipients in the form of grants and cooperative agreements. The Agency provides assistance for many different Agency media functions, i.e. air pollution, water pollution, toxic substances, hazardous waste, construction grants for wastewater treatment (which is a significant amount of the funds the Agency provides for assistance). Assistance also represents the most significant portion of the Agency's appropriation. In fiscal years 1988 and 1987, the Agency obligated \$3.5 billion and \$2.6 billion, respectively, for recipients.

At the expiration of an Assistance Agreement, unused or improperly applied funds are either collected from the recipients or appropriately adjusted by an offset, or otherwise utilized in accordance with the conditions of the Assistance Agreement. Arrangements are made for the disposition of property purchased through the Assistance Agreements according to Federal regulations.

The Construction Grant program, a federally funded multi-billion dollar activity, has begun a period of transition. In 1987 Congressional legislation, the Water Quality Act of 1987 (PL 100-4), created the State Water Pollution Control Revolving Funds (SRF). SRF is a capitalization grant program, intended to facilitate the establishment of permanent institutions in each State that will provide continuing sources of financing needed to maintain water quality. From the SRF, States can provide loans and other types of financial assistance, but not grants, to communities and intermunicipal and interstate agencies for the construction of publicly-owned wastewater treatment facilities. The funds may also be used for implementation of nonpoint source management programs and development and implementation of plans under the new estuary protection program. The intent of the SRF program is to eventually bring to an end the Federal government role in funding municipal wastewater plants by making grants to States on a matching basis. Under the SRF program, States will have control of the proceeds of the loans which they collect from the cities. The proceeds of these loans are to be used by States as a revolving fund to make additional loans. Implementation of this program has the potential for making a significant impact on the Agency's financial statements, as it will decrease the grants portion of the Agency's expenditures.

NOTE 8: RESTATEMENT OF FISCAL YEAR 1987 FINANCIAL STATEMENTS

The fiscal year 1987 consolidated statements of financial position, revenues and expenses, and changes in financial position and reconciliation to budget have been restated to correct identified errors in the application of generally accepted accounting principles. In total, these changes increased assets by \$844.7 million, increased liabilities by \$910.2 million, decreased equity by \$65.5 million and decreased net results of operations by \$28.3 million.

SUPPLEMENTAL SCHEDULES

The following supplemental schedules provide, by major fund activity, further detail of assets, liabilities, and U.S. government equity; revenue, financing sources, and expenses; sources and uses of funds; and budgeted and actual outlays.

General fund accounts are used to record financial transactions arising under congressional appropriations or other authorizations to spend general revenues. EPA is managing 49 general fund accounts, of which 6 are funded by current-year appropriations, 11 have unobligated balance carryovers from previous fiscal years, and 18 cannot incur new obligations. The remaining 14 are suspense, receipt, and deposit accounts. In addition, the general fund has been combined with a small certification revolving fund and the GSA Building Fund for financial reporting purposes.

Superfund accounts are used to record transactions arising from the fulfillment of EPA's responsibilities under CERCLA and SARA. (See note 7.) The Superfund program activity has been combined with two smaller program activities covering the Leaking Underground Storage Tanks Trust Fund and the Miscellaneous Contributed Funds.

Supplemental Schedules

Schedule of Financial Position by Fund Activity

AS OF SEPTEMBER 30, 1988
(DOLLARS IN THOUSANDS)

	GENERAL FUND APPROPRIATIONS	SUPER FUND APPROPRIATIONS	CONSOLIDATED BALANCES
ASSETS			
Funds with U.S. Treasury	\$8,687,269	\$1,661,453	\$10,348,722
Advance to the Trust Fund	733,955	0	733,955
Other Advances, Accounts and Loans Receivable, Net	98,585	16,305	114,890
Land, Buildings, and Equipment, Net of Accumulated Depreciation	130,444	11,941	142,385
Future Financing Sources	35,502	5,362	40,864
TOTAL ASSETS	<u>9,685,755</u>	<u>1,695,061</u>	<u>11,380,816</u>
LIABILITIES AND EQUITY			
LIABILITIES			
Repayable Advance From Treasury	733,955	0	733,955
Accounts Payable and Accruals:			
To the Public	275,949	89,446	365,395
To Other Federal Agencies	47,644	154,192	201,836
Other Advances:			
From Other Federal Agencies	8,902	13,404	22,306
From The Public	3,786	20,248	24,034
Amounts Due to Treasury	83,831	15,412	99,243
Accrued Payroll and Leave	67,686	12,166	79,852
Superfund Claims	0	20,500	20,500
TOTAL LIABILITIES	<u>1,221,753</u>	<u>325,368</u>	<u>1,547,121</u>
EQUITY OF THE U.S. GOVERNMENT			
Unexpended Appropriations:			
Unobligated Balances	1,129,729	124,584	1,254,313
Unliquidated Obligations:			
Grants and Other Assistance	6,996,997	418,906	7,416,903
Contracts and Other	291,804	859,638	1,151,442
Invested Capital	202,363	11,941	214,304
Cumulative Results of Operations	(156,891)	(46,376)	(203,267)
TOTAL EQUITY	<u>8,464,002</u>	<u>1,369,693</u>	<u>9,833,695</u>
TOTAL LIABILITIES AND EQUITY	<u>\$9,685,755</u>	<u>\$1,695,061</u>	<u>\$11,380,816</u>

Supplemental Schedules

Schedule of Operations by Fund Activity

FOR THE FISCAL YEAR ENDED SEPTEMBER 30, 1988
(DOLLARS IN THOUSANDS)

	GENERAL FUND APPROPRIATIONS	SUPER FUND APPROPRIATIONS	CONSOLIDATED BALANCES
EXPENSES			
Grants and Other Assistance	\$2,986,229	\$77,498	\$3,063,727
Contractual Services	468,848	725,696	1,194,544
Personnel Compensation and Fringe Benefits	511,712	112,587	624,299
Rent, Utilities, and Telephone	101,903	18,387	120,290
Travel, Printing, Supplies and Other Expenses	90,399	45,653	136,052
Depreciation	17,261	3,840	21,101
TOTAL EXPENSES	4,176,352	983,661	5,160,013
FINANCING SOURCES			
Appropriations Expended	4,135,544	972,947	5,108,491
Depreciation	17,261	3,840	21,101
Appropriations to be Provided	1,979	715	2,694
TOTAL FINANCING SOURCES	4,154,784	977,502	5,132,286
NET RESULTS OF OPERATIONS	(\$21,568)	(\$6,159)	(\$27,727)
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Supplemental Schedules

Schedule of Changes in Financial Position and Reconciliation to Budget by Fund Activity

FOR THE FISCAL YEAR ENDED SEPTEMBER 30, 1988
(DOLLARS IN THOUSANDS)

RESOURCES USED:	GENERAL FUND APPROPRIATIONS	SUPER FUND APPROPRIATIONS	CONSOLIDATED BALANCES
Operating Uses:			
Operating Expenses	\$4,176,352	\$983,661	\$5,160,013
Items (Providing) Requiring Funds:			
Depreciation	(17,261)	(3,840)	(21,101)
Loss on Property	(8,862)	(6,478)	(15,340)
Unfunded Annual Leave	(1,979)	(715)	(2,694)
Superfund Claims	0	(20,500)	(20,500)
Increase in Other Advances, Accounts and Loans Receivable, Net	14,720	6,537	21,257
Increase in Accounts Payable and Accruals	(93,885)	(177,360)	(271,245)
Funds Used by Operations	<u>4,069,085</u>	<u>781,305</u>	<u>4,850,390</u>
Non-Operating Uses:			
Acquisitions of Property	36,787	13,417	50,204
Net Transfers Out	125,055	0	125,055
Funds Transactions Included In Outlays	(5,638)	(2,883)	(8,521)
NET RESOURCES USED (BUDGETARY OUTLAYS)	<u>4,225,289</u>	<u>791,839</u>	<u>5,017,128</u>
RESOURCES PROVIDED:			
Current Year Appropriation	3,885,042	1,142,415	5,027,457
Net Transfers In and Other	108,595	(50,172)	58,423
NET RESOURCES PROVIDED	<u>3,993,637</u>	<u>1,092,243</u>	<u>5,085,880</u>
INCREASE (DECREASE) IN U.S. TREASURY FUNDS	<u>(231,652)</u>	<u>300,404</u>	<u>68,752</u>
U.S. TREASURY FUNDS; BEGINNING OF YEAR	8,918,921	1,361,049	10,279,970
U.S. TREASURY FUNDS; END OF YEAR	<u>\$8,687,269</u>	<u>\$1,661,453</u>	<u>\$10,348,722</u>
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