



**Department of Homeland Security – US Coast Guard
Notification of Findings and Recommendations (NFR)
Fiscal Year Ended September 30, 2005**

Location/Office: Headquarters	Finding number: CG 05-15
Audit Area: Environmental Liabilities	W/P Reference: N-30, N-206
Date Provided to Management: August 10, 2005	Date Response Due: August 17, 2005
Title: Shore Facilities Environmental Liability - Re-issuance of PY NFR	Severity: 3 (Low 1 – High 5)

Background: During the FY 2004 DHS Coast Guard segment financial statement audit, KPMG submitted findings and recommendations to the management of the Coast Guard regarding deficiencies in its process to calculate the environmental liability related to shore facility projects (NFR CG-04-0010).

At June 30, 2005, Coast Guard's estimate of the FY 2005 environmental liability was \$117 million. Approximately \$107.5 million or 92 percent was associated with 220 shore facility projects.

Condition: Coast Guard's process for calculating its environmental liability associated with shore facilities was not fully effective. Specifically:

- The Coast Guard did not consistently apply the escalation index factor to the project estimates. Of the 20 projects reviewed, 1 project did not escalate the estimated amount, six projects used an index other than 5 percent, and four projects were incorrectly escalated to a year other than 2005. The estimate appears to be overstated by approximately \$39,000 related to the application of the escalation factor for an incorrect year.
- The Coast Guard did not consistently apply a contingency factor to similar cost estimates. The estimates for the 20 projects reviewed appear to be underestimated by approximately \$107,000.
- Of 20 project estimates reviewed, eight project estimates contained errors or insufficient documentation to support the estimated liability amount. Four of the eight project estimates did not include all remediation costs, resulting in an underestimate of approximately \$448,000. The remaining four projects, in the amount of \$1.3 million, were not supported by sufficient documentation. These errors and inconsistencies were not fully resolved prior to the recording of the overall environmental liability amount as of June 30, 2005.

Criteria: Statement of Federal Financial Accounting Standards (SFFAS) Number 6, *Accounting for Property, Plant, and Equipment*, paragraph 85 defines environmental cleanup costs as those costs for removing, containing, and/or disposing of (1) hazardous waste from property, or (2) material and/or property that consists of hazardous waste at permanent or temporary closure or shutdown of associated PP&E. Paragraph 88 states that these cleanup costs meet the definition of liability provided in SFFAS number 5, *Accounting for Liabilities of the Federal Government*. In addition, SFFAS number 6 paragraph 96 states that remediation estimates shall be revised periodically to account for material changes due to inflation or deflation and changes in regulations, plans and/or technology. New remediation cost estimates should be provided if there is evidence that material changes have occurred; otherwise estimates may be revised through indexing.



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Chapter 7, Section E.3 of the Financial Resources Management Manual (COMDTINST M7100.3C) requires that “cleanup estimates shall be revised periodically to reflect material changes due to inflation or deflation and changes in regulations, places, and/or technology. New cost estimates shall be developed if there is evidence that material changes have occurred; otherwise, estimates may be revised through indexing. The effect of the estimate changes shall be recognized as expense and the liability adjusted in the period the change occurs.” Further, this policy states that “documentation shall be maintained by the appropriation manager, which explains the cleanup plan and the related methodology used in computing the cleanup liability. This information shall be retained for 6 years after the close of the reported year.”

Cause: Lack of detailed policies and procedures, or failure to follow stated policies and procedures, resulted in varying approaches by the Civil Engineering Units (CEUs) in calculating the shore facility environmental liability estimates.

Effect: The environmental liability associated with shore facilities could be potentially misstated.

Recommendations: We recommend that the Coast Guard:

1. Establish uniform standards for defining, estimating, and managing the specific types of shore facility environmental liabilities and provide training to the Coast Guard estimators on the application of those standards.
2. Determine an appropriate escalation index factor to consistently apply to the shore project estimates. Develop and implement policies and procedures to facilitate the consistent application of the escalation index factor.
3. Develop a standard form to identify general cost estimating expectations, such as the date of the estimate, the base year dollars used, estimating approach, contingency factor used, etc.
4. Develop and implement policies and procedures to maintain project folders with readily-available documentation to support assumptions, calculations, the estimate date, site conditions, and fiscal year dollars presented.

Management Response:

KPMG policy requires that we obtain your response to this notification of finding and recommendation in writing. As such, please indicate your response by checking the appropriate box below and providing the appropriate supporting documentation to KPMG within five business days from the date of this notification. Your written response will be considered when preparing the draft consolidated audit report.

- Management concurs with the Notification of Finding and Recommendation and has provided a corrective action plan, with milestone dates, developed to address the condition in the space provided below or as an attachment to this document. (Note: Responses should not be delayed until plans are finalized. If plans are not complete, specify a completion date when forwarding your responses.)

Management does not concur with the Notification of Finding and Recommendation and provided further detail supporting our position in the space provided below or as an attachment to this document.

Corrective action will be taken and completed in current fiscal year (check box if “yes”).



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General Comments

CG-443 will implement the recommendations.

Corrective Action Planned:

1. CG-443 will establish uniform methods for defining, estimating, and managing the specific types of shore facility environmental liabilities. CG-443 has tentatively scheduled a training and policy briefing for CEU project managers (those who certify estimates) for January 06.
2. CG-443 will develop and implement policies and procedures to facilitate the consistent application of the Department of Labor, Bureau of Labor Statistics Producer Price Index as the escalation index factor for all liability estimates when indexing is appropriate.
3. General cost estimating expectations, such as the date of the estimate, the base year dollars used, estimating approach, contingency factor used, etc will be added to Shore Facility Environmental Liability Estimate Sheet.
4. The CEU project manager's will be directed to maintain project folders with readily-available documentation to support assumptions, calculations, the estimate date, site conditions, and fiscal year dollars presented. CG-443 will develop minimum folder content requirements.


CAPT Anthony Reynolds
Chief, Office of Logistics (CG-44)
16 AUG 05

KPMG Response, if Necessary: *(See GAGAS paragraph 5.30)*

1. _____
Bruce Antiporowich
Senior Manager, KPMG LLP

2. _____
CAPT David Hill
Chief, Office of Financial Policy

Date Provided to Management

Date Response Received from Management



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General Comments

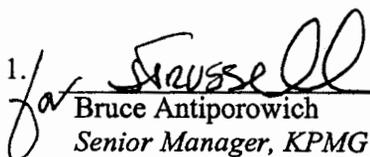
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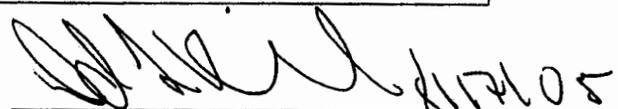
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CAPT Anthony Reynolds
Chief, Office of Logistics (CG-44)
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KPMG Response, if Necessary: (See GAGAS paragraph 5.30)

1. 
Bruce Antiporowich
Senior Manager, KPMG LLP

2. 
CAPT David Hill
Chief, Office of Financial Policy

Date Provided to Management

8/17/05

Date Response Received from Management