This document has been
Rescinded and is located
in our Archive files.

For Active files, visit
http://www.osmre.gov/directiv.htm

	U· S· DEPARTMENT OF THE INTERIOR **OFFICE OF SURFACE MINING** **RECLAMATION AND ENFORCEMENT** **DIRECTIVES SYSTEM**	**Subject Number:** OPM - 7 **Transmittal Number:** 227 **Date:** 07/26/84

Subject: Internal Controls System

Approval: J. Lisle Reed **Title:** Acting Director

1. Purpose. The directive provides policies and standards to be followed in establishing and maintaining internal controls in program and administrative activities within the Office of Surface Mining.

2. Definitions. For the purpose of this directive, the following terms are defined:

a. Internal Control. The plan of organization and all of the methods and measures of the Office of Surface Mining which are designed to prevent or detect waste, fraud, abuse, mismanagement, and other loss by assuring the safeguarding of resources; the accuracy and reliability of information; adherence to applicable laws, regulations, and policies; and promotion of operational economy and efficiency.

b. Internal Control Standards. The standards issued by the Comptroller General on June 1, 1983, for use in establishing and maintaining systems of internal control. These are applicable to all operations and administrative functions but are not intended to limit or interfere with duly granted authority related to development of legislation, rulemaking, or other discretionary policymaking in an agency.

c. Internal Control Guidelines. The guidelines issued by OMB in December 1982, entitled "Guidelines for the Evaluation and Improvement of and Reporting on Internal Control Systems in the Federal Government."

d. Material Weakness. A situation in which the designed procedures or degree of operational compliance therewith does not provide reasonable assurance that the objectives of internal control specified in the Federal Managers Financial Integrity Act are being accomplished.

e. Internal Control Documentation. Written policies, organization charts, procedural write-ups, manuals, memoranda, flow charts, decision tables, completed questionnaires, software, and related written materials used to describe the internal control methods and measures, to communicate responsibilities and authorities for operating such methods and measures, and to serve as a reference for persons reviewing the internal controls and their functioning.

f. Internal Control Coordinator. The official designated by OSM to coordinate and facilitate compliance with OMB Circular A-123, 340 DM 1 and relevant guidance issued by GAO, PFM and OIG.

g. Event Cycle (or Transaction Cycle). A recurring sequence of activities used to accomplish the objectives of a program or administrative activity through the initiation and performance of certain related functions. The creation of the necessary documentation of the performance of these functions, and the gathering and reporting of related information.

h. Event (or Transaction). A specific, discrete activity of an event cycle (or transaction cycle).

i. Internal Control System. The sum of the organization's methods and measures used to achieve the objectives of internal control.

j. Internal Control Objectives. A desired outcome for an event of an event cycle of an OSM program or administrative activity that reflects the application of the overall objectives of internal control to that event and which is designed to prevent or detect waste, fraud, abuse, mismanagement and other loss.

k. Internal Control Technique. A process and documents that are being relied on to efficiently and effectively accomplish an internal control objective and thus help safeguard an activity from waste, loss, unauthorized use, or misappropriation.

l. Evaluation (of an internal control objective or technique). A broad, overall assessment of the appropriateness and adequacy of an internal control objective or technique.

m. Testing (of an internal control technique). An examination of the actual performance of an internal control technique through a sampling of selected events, a review of the documentation of these events, and other relevant observations and inquiries.

n. Vulnerability Assessment (VA). An assessment of the susceptibility of a Department program or administrative activity to waste, fraud, abuse, mismanagement, and other loss based on findings with respect to its inherent risk, general control environment, and existing safeguards.

o. Internal Control Review (ICR). A detailed examination of the events of the event cycle(s) of a program or administrative activity to determine whether appropriate, adequate internal control objectives and techniques exist and are functioning so as to prevent or detect -- in a cost-effective manner -- waste, fraud, abuse, mismanagement, and other loss.

p. Internal Control Review Action Agenda. The agenda of programs and administrative activities scheduled to undergo ICRs during a certain two-year cycle of reviews; the selection of programs and administrative activities is based on the results of VAs, including specific findings with respect to inherent risk, general control environment, and existing safeguards.

3. Policy/Procedures

a. General. The basic authority for establishing and maintaining agency internal controls is vested in the Budget and Auditing Act of 1950, as amended by the Federal Managers Financial Integrity Act (FMFIA) and the Antideficiency Act (31 U.S.C. 1341). Section 113 of the Budget and Auditing Act of 1950 (31 U.S.C. 3512) requires the head of each agency to establish and maintain systems of accounting and internal controls. The Act also provides that accounting systems should conform to the principles, standards, and related requirements prescribed by the Comptroller General of the United States. The general guidance for developing systems requirements is set forth in the General Accounting Office Policy and Procedures Manual for Guidance of Federal Agencies.

It is Departmental and OSM policy that bureaus and offices establish and maintain effective systems of control including management, program, accounting and administrative. These systems should constitute the full range of internal controls necessary to protect and use government resources effectively and efficiently. All levels of management within OSM should ensure that adequate controls are in place to safeguard agency resources, to maintain the accuracy of data, to promote efficient management, and to comply with prescribed laws, regulations and policies.

b. Scope. The provisions of this directive apply to all operational units within OSM.

c. Responsibilities. Responsibilities for internal control system are as follows:

(1) The Assistant Secretary - Policy, Budget and Administration (PBA)

(a) Managing Departmental compliance with A-123 and the FMFIA.

(2) The Office of Financial Management - PBA (PFM)

(a) Providing oversight and guidance to the bureaus and offices concerning the review, evaluation, and maintenance of effective internal controls.

(b) Managing, directing, and evaluating the Department's reporting under the Circular and the FMFIA.

(3) Other PBA Offices

(a) Other PBA offices also have significant Departmentwide A-123 responsibilities. The Office of Acquisition and Property Management, Office of Information Resources Management, Office of Administrative Services, Office of Personnel, and Office of Budget will develop internal control guidelines for identified administrative functional areas for which they exercise Departmental oversight responsibility and report periodically to the Secretary on the adequacy of such controls within bureaus and offices.

(4) The Inspector General (IG)

(a) Provide guidance and technical assistance to Departmental management in their efforts to evaluate and improve internal controls.

(b) Evaluate bureau and office compliance with the Circular and the FMFIA, and provide the Secretary with a statement on the adequacy of annual assurance statements provided to the Secretary by the Department's senior management officials.

(c) Audit internal control systems, including their related practices and procedures, for adequacy and safeguard of reliability that can be placed in such controls to protect and safeguard the efficient and effective use of Government resources.

(d) Determine whether the policies and standards established as a result of the Circular and the FMFIA are being properly implemented and adhered to.

(5) Director/Deputy Director

(a) Ensure that adequate systems of internal control have been implemented within OSM.

(b) Review internal control evaluations and promptly take appropriate corrective actions.

(c) Promote a control conscious environment within OSM that keeps managers constantly aware of the need to establish systematic controls, monitor their application, and periodically review their effectiveness.

(d) Ensure that adequate resources are devoted to the Internal Control Review Program.

(6) Internal Control Coordinator/Program Evaluation Staff, Office of the Director

(a) Develop standards and procedures, guidelines and reporting requirements necessary to establish and maintain effective internal controls.

(b) Establish a review plan to ensure that all agency operations are periodically asssessed for vulnerability to fraud, abuse and waste.

(c) Provide guidance and assistance to OSM organizational components in the conduct of vulnerability assessments and internal control reviews.

(d) Inform the Director/Deputy Director of significant problems associated with internal control reviews and recommend corrective action.

(e) Act as liaison in coordinating OSM's reporting on vulnerability assessments and internal control reviews to the Assistant Secretary, Land and Minerals Management, the Office of Financial Management and the Office of Inspector General.

(7) Assistant Directors, Heads of Director's Staff Offices

(a) Ensure compliance with this directive and establish adequate internal controls within organizational units under their direction.

(b) Ensure that vulnerability assessments and internal control reviews are conducted in accordance with the overall plan.

(c) Inform the Director/Deputy Director, through the Program Evaluation Officer, of major instances of fraud, abuse and waste.

(d) Promote a control conscious environment and ensure compliance by exacting employee accountability through appropriate program objectives, goals and performance standards.

(e) Ensure that adequate resources are devoted to the Internal Control Review Program.

(f) Develop corrective action plans to correct reported internal control weaknesses.

(g) Ensure that corrective actions are implemented as scheduled.

(h) Ensure that reports on the status of corrective actions are prepared by the responsible officials in accordance with guidance provided by the Internal Controls Coordinator.

(8) Procedures

(1) General Procedure for Establishing a System for Internal Control

(a) The process for establishing and maintaining adequate internal controls is a continuous five-phase process that involves:

1 conducting vulnerability assessments to determine the susceptibility of programs to fraud, abuse and waste and rating each program as either a high, medium or low risk;

2 developing a plan for conducting internal control reviews based on the results of the vulnerability assessments;

3 conducting internal control reviews in accordance with the overall plan to determine if adequate procedures exist to detect fraud, abuse and waste in a cost effective manner;

4 reporting the results of internal control reviews to OSM management, the Assistant Secretary, Land and Minerals Management, the Office of Inspector General, and the Assistant Secretary for Policy, Budget and Administration (PBA); and

5 determining cost effective corrective actions and promptly implementing those actions to re-enforce OSM's internal control system.

(2) Guidance - Vulnerability Assessments

(a) General. The process for establishing and maintaining adequate internal controls is an ongoing process. The determination of when to conduct an internal control review is based primarily on the results of vulnerability assessments. OSM will conduct vulnerability assessments as prescribed in the Circular and according to supplemental PFM guidance. In addition, follow-up assessments are to be conducted at least biennially. The Department has established a two-year cycle, starting with each even numbered year and ending with each odd numbered year, for bureaus and offices to follow. The even numbered years are designated as the years in which vulnerability assessments will be normally conducted. Based on the results of the vulnerability assessments, OSM will schedule and perform internal control reviews for the components requiring an evaluation. All components should be reviewed within 4 cycles (8 years) with the scheduling of the reviews determined by the results of the vulnerability assessements and the discretion of the internal control coordinator. In order to meet the vulnerability assessment requirement, OSM offices are required to:

1 identify and maintain an accurate inventory of all components,

2 prepare and execute a plan to conduct vulnerability assessments at least biennially for all components, and

3 conduct and properly document vulnerability assessments as prescribed by PFM and prepare a Component Inventory, Vulnerability Assessment Results, and Inventory Control Plan.

The completed Component Inventory, Vulnerability Assessment Results, and Inventory Control Plan must be approved by the Director and the Assistant Secretary, Land and Minerals Management. Copies of the approved document, along with the completed vulnerability assessments, must be submitted, as required, to PFM and OIG.

(b) Performance of Vulnerability Assessments. Vulnerability assessments consists of three phases that are necessary to adequately assess a program. The phases are briefly described in the following:

Phase I - The first phase of a vulnerability assessment is the development of general background information to provide the reviewer with sufficient background to complete the other phases of the assessment. Items that should be considered in this phase include:

1 Analysis of the General Control Environment. The general control environment is management's attitude and discipline concerning internal controls. The purpose of analyzing the general control environment is to determine if management's attitude is conducive to a strong internal control system. Since the control environment is an indication of top management's control consciousness, it could have a major impact on the effectiveness of internal controls. The major factors that influence the general control environment are: organization; delegation of authority; policies and procedures; personnel; planning, programming, and budgeting; and reporting and monitoring. A subjective analysis of the adequacy of these factors will lead the reviewer to a conclusion of the general control environment.

2 Analysis of Inherent Risk. Risk is a type of unwanted occurrence such as loss, error, fraud, or mismanagement that might occur because internal controls are not adopted or implemented. Inherent risk, as defined by OMB's "Guidelines for the Evaluation and Improvement of and Reporting on Internal Control Systems in the Federal Government," is "the inherent potential for waste, loss, unauthorized use, or misappropriation due to the nature of an activity itself." The purpose of analyzing the inherent risk is to get an indication of the scope of the component and the degree of control necessary to prevent the risks from occurring. The major factors that affect the inherent risks of a component are: size of budget, life of component, component administration, results of audits and other studies, responsiveness to recommendations, component's impact outside the Department, and special concerns. The analysis of inherent risk is more objective than the analysis of the general control environment.

OSM management officials who direct or control resources are required to identify defined levels of acceptable risks. These levels are the point beyond which management officials are not willing to:

(1) tolerate potential loss of assets and revenues,

(2) accept a margin of error in reports and information,

(3) permit departures from established procedures, or

(4) sustain adverse public opinion.

The identification of acceptable levels of risks within OSM's components provides a basis for applying ranking criteria to the major factors in the risk analysis process.

Phase II - The second phase is to determine if appropriate safeguards exists through the completion of a preliminary evaluation of safeguards. This step calls for a subjective evaluation of the existence and adequacy of controls that exist in a component. The evaluation must exercise professional judgment based on his/her knowledge and experience with the component. In reaching a judgment, the evaluator is expected to consider what internal control standards are necessary to effect the proper controls.

Phase III - The final phase is documentation of the results of the assessment. PFM has outlined a process for assigning numerical ranking criteria to factors evaluated in a component. Where the vulnerability assessment numerical ranking for a component is "medium" or "low" and management is aware of specific circumstances such as audit findings that could alter the ranking, management should override the numerical ranking and rank the component at the appropriate level dictated by the circumstance.

(c) Assistant Directors and Heads of the Director's Staff Offices will, in cooperation with the Internal Controls Coordinator, assess the vulnerability of programs in accordance with the approved assessment plan.

(d) It is the responsibility of Assistant Directors to ensure that assessments are conducted. In order to comply with the assessment requirement, Assistant Directors shall appoint a staff member and alternate in Headquarters, State Offices and Technical Service Centers to perform the actual vulnerability assessment. In some cases, it will be inappropriate for a staff member to conduct a vulnerability analysis within his/her directorate. Consequently, it may be necessary for a staff member to cross organizational lines in order to perform the vulnerability analysis. The Internal Controls Coordinator will coordinate all assessment activity and make the final determination in cases where potential conflict exists.

(e) Completed vulnerability assessments will be submitted to the Internal Controls Coordinator for review and, if necessary, submitted to the Director/Deputy Director. Future plans for assessments will be developed by the Internal Controls Coordinator with cooperation from the affected program areas. When consolidated and reviewed, future plans will be submitted by the Internal Controls Coordinator through the Director to the Assistant Secretary, Land and Minerals Management for review and approval.

(f) The Program Evaluation Staff will be available to provide additional guidance and assistance in conducting vulnerability assessments.

(3) Guidance - Internal Control Reviews

(a) General. After completing the vulnerability assessment process and prioritizing programs according to vulnerability, internal control reviews will be planned for and conducted as part of a continuous cycle. Initial reviews will be conducted for all those components identified as "high" during the vulnerability assessment. The Internal

Controls Coordinator in conjunction with each AD will develop an internal control review plan that sets forth the specific components and controls to be reviewed, the review procedures, schedule of reviews, and the reviewers. This plan will be forwarded to PFM and the Office of Inspector General.

(b) There are three types of internal control reviews that can be conducted. Each is discussed in the following:

1 Functional Reviews - Certain functional components (such as space, printing, debt collection, cash management, etc.) are identified at the department level and specific guidelines (generally in the form of questionnaires) are issued by responsible PBA offices for bureau/office use in conducting ICRs.

2 Alternative ICRs - This approach provides for an efficient use of resources by allowing prompt corrective actions to be taken on known problems without immediately conducting a full ICR. Alternative ICRs may be performed only on those components where you know the cause of the problem and can take immediate corrective action. However, since alternative reviews only focus on limited aspects of a component's system of internal control, you must conduct a full ICR in the following year on those aspects of the component not covered in the alternative ICR.

3 Full ICRs - This encompasses a detailed examination of events and event cycle(s) of an OSM program or administrative activity to determine if appropriate, adequate internal control objectives and techniques exist to prevent or detail waste, fraud, abuse and mismanagement. Full ICRs must be conducted in accordance with the Department's Guideline for Conducting Internal Control Reviews.

(c) The Department has mandated that at a minimum, internal control reviews should be conducted on 25% of all components each cycle. Therefore, if 25% of OSM's components are not rated as "high" during a particular cycle, internal control reviews will be conducted on some components that are rated "medium" or "low". The Internal Control Coordinator will make the final decision on what components will be reviewed during a particular review cycle.

(4) Conducting Internal Control Reviews

(a) General. The unique attributes of OSM's program functions do not lend themselves to a single evaluation method, therefore, the procedures developed for each internal control review will vary considerably. However, in general terms, each internal control review will have to ensure that OSM programs meet the following general standards:

1 Internal Control Objectives - Specific internal control objectives -- developed and tailored for each event cycle -- are to be appropriate, logical, and complete (as defined in the following) with respect to the accomplishment of the cycle's operation.

a Appropriate - applicable and relevant to the specific event cycle involved and cognizant of any inherent limitations or constraints imposed.

b Logical - coherent and meaningful and derived from the overall objectives of internal control.

c Complete - covering all operations performed within a specific event cycle, yet flexible and avoiding duplication.

2 Internal Control Techniques - Specific internal control techniques -- developed and tailored to achieve the event cycle's internal control objectives -- are to be efficient, effective, comprehensive, and consistent (as defined in the following):

a Efficient - achieving desired results within the constraints of cost, benefit, and risk. [Efficiency is enhanced if one technique can be applied to help achieve two or more internal control objectives.]

b Effective - fulfilling the desired internal control objective, providing the desired coverage, and being operative at appropriate times.

c Comprehensive - organized, interrelated, and arranged in proper sequence to give reasonable assurance of achieving the desired internal control objective.

d Consistent - uniformly efficient, effective, and comprehensive over extended periods of time.

(b) Internal Control Standards. Internal control objectives and techniques are to be evaluated on their ability to contribute to the attainment of standards for internal control systems prescribed by GAO in the following:

1 Reasonable Assurance - reasonable, but not absolute, assurance that the overall objectives of the internal control system will be accomplished (recognizing that the cost of an internal control should not exceed the derived benefits, and that the benefits consist of a reduction in the risk of failing to accomplish the system's overall objectives).

2 Attitude - managers and employees, at all times, maintain and demonstrate a positive and supportive attitude toward internal control.

3 Supervision - qualified and continuous supervision is provided to assure that approved procedures are followed; lines of personal responsibility and accountability are clear.

4 Competent Personnel - managers and employees have high standards of integrity; are competent by education, experience, and/or training to accomplish their assigned duties; and possess adequate knowledge of internal control.

5 Separation of Duties - key duties (such as authorizing, approving, and recording transactions; issuing or receiving assets; making payments; and reviewing or auditing) are assigned to separate individuals to minimize the risk of loss; no one individual controls all phases of an activity or transaction such that errors or irregularities are permitted or go undetected.

6 Access to Resources - access to resources is limited to authorizing personnel (access includes both direct physical access and indirect access through the preparation or processing of documents that authorize the use or disposition of resources); periodic comparisons of resources with recorded accountability is made.

7 Execution of Transactions - independent evidence is maintained that authorizations are issued by persons acting within the scope of their authority, and transactions conform with the terms of the authorization.

8 Recording of Transactions - transactions are recorded as executed and when executed, and are properly classified.

9 Documentation - internal control systems (i.e., internal control objectives and techniques), the accountability for resources, and all transactions and other events are clearly documented, and the documentation is readily available.

(c) Internal Control Testing. A control test is the examination of available evidence that one or more of the agency's internal control techniques are operating as described during some period. Contol testing is an intergral part of the review of internal controls. Effective internal control testing should include a plan for testing a component's controls before the ICR is started. Typically, the plan should set forth the test objectives, test methodology, documentation to be reviewed, sampling method, test period, sample size, and the acceptable and nonacceptable error conditions. The testing procedures should be directed at the control techniques employed to accomplish the control objectives for the component. Tests should be limited to that necessary to ensure reasonableness of the controls and to determine whether they are functioning as intended.

Internal control testing should include as appropriate:

1 Interviewing persons that exercise control functions;

2 Observing control procedures;

3 Examining documentation that shows evidence of control techniques;

4 Performing control procedures on live transactions and comparing results; and

5 Direct testing of computer-based control mechanisms by use of dummy transactions.

(5) Internal Control Review Reporting

(a) Internal control reviews performed in Assistant Directorates will be documented by written reports signed by the appropriate Assistant Director. Such reviews should include an evaluation of the controls and their effectiveness, identification of control weaknesses, planned corrective action, and plans for follow-up reviews.

(b) The individual designated as the responsible official (generally a Division Chief) has the responsibility for reviewing the Internal Control Reviews for adherence to internal control criteria established by OSM and the Department of Interior.

(c) Assistant Directors prior to sign-off will review the reports to ensure that adequate testing and documentation are contained in the reports and to evaluate the reasonableness of the report based on the relationship to other audit reports, internal memoranda, and a general knowledge of the subject area.

(d) Draft reports will be submitted to the Internal Control Coordinator for review and comment prior to finalization. If in the view of the Internal Control Coordinator, appropiate criteria has not been satisfactorily addressed, the report will be returned to the Assistant Director for correction.

(e) Finalized reports will be signed by the Director/Deputy Director and submitted to the Assistant Secretary, Land and Minerals Management for approval. Final reports should also be submitted to the Office of Inspector General and the Office of Financial Management within 10 days of being finalized.

(f) Based on the internal control reports, audits of internal controls performed by the Inspector General, the General Accounting Office and other pertinent management evaluation reports, the Director will submit an annual statement to the Secretary attesting to the adequacy of OSM's internal controls. OSM's statement will form a part of the basis for the annual Departmental statement/report which is submitted by the Secretary to the President and Congress.

(g) A copy of internal control weaknesses identified during the internal control reviews will be submitted to the Assistant Secretary, Land and Minerals Management with a copy to the OIG and PFM within 30 days after completion or by the specified due dates if earlier. PFM will provide a copy of the internal control reviews for specified administrative functional areas to the appropriate PBA office. In addition, the Chief, Division of Financial Management is responsible for conducting an evaluation

of the accounting system each fiscal year to detemine whether it conforms to the principles, standards, and related requirements prescibed by the Comptroller General and after concurrence by the Director, report the results of such evaluation to the Assistant Secretary, Land and Minerals Management with a copy to the OIG and PFM within 30 days after completion or after the end of the fiscal year for which the system was evaluated, whichever time comes sooner.

4. Reporting Requirements. In addition to those requirements set forth in the preceding paragraphs, OSM must maintain an Internal Control Improvement Tracking System (ICITS) to record and monitor internal control weaknesses, planned corrective actions and scheduled completion dates. Data gathering and report distribution for the ICITS is centralized with the internal control coordinator in the Program Evaluation Staff. The ICITS will monitor all components for which internal control weaknesses have been identified.

5. References.

a. Office of Management and Budget Circular A-123

b. Departmental Manual Part 340, Internal Control System

6. Effect on Other Documents. Supercedes OSM Directive OPM-7, Internal Control Systems, dated June 3, 1982.

7. Effective Date. Upon issuance.

8. Contact. Program Evaluation Staff, Office of the Director, (202) 343-4781.